



## Fiscal Illusion and Defining Factors of Capital Expenditure (Study on Undeveloped Areas in West Nusa Tenggara)

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### ABSTRACT

The purpose of this study is to verify and find empirical proof on the influence of local revenue, general allocation funds, special allocation funds and profit-sharing funds on capital expenditures. And to detect the occurrence of fiscal illusions on capital expenditure financing. The population is the form of local government financial report of fiscal year 2012 until 2016 of all districts included in undeveloped areas in NTB according to Presidential Regulation No. 131 of 2015. This study takes the entire population as the subject of research (census study). Data analysis technique used is descriptive statistics and F test, t test and R<sup>2</sup> test to test the hypothesis by first doing the classical assumption test. The result of classical assumption test shows that normal distributed data, no multicollinearity problem, no autocorrelation, and free data from heteroskedasticity problem. The results show that local revenue, special allocation funds and profit-sharing funds have a positive effect on capital expenditure. While for variable of general allocation fund have negative effect to capital expenditure. There has been a fiscal illusion on capital expenditure financing since there is a variable of general allocation receipt which has a negative correlation with the spending of local government capital expenditures.

**Keywords:** Local Government, Capital Expenditure, Fiscal Illusion

**JEL Classifications:** D24, G3

### 1. INTRODUCTION

Regional autonomy is a government program for sustainable development and minimizes the gap between one region and another. The implementation of regional autonomy provides an opportunity for local governments to manage their natural resources effectively and efficiently and develop regional potentials to increase local revenue (Irawan, 2016). The success of Local Government in carrying out regional development and improving people's welfare can not be separated from the success of managing APBD effectively and efficiently. The problem that arises is when local governments are confronted with small amounts of local revenue but must bear the great need. On the other hand, each region has unequal financial capability in funding its activities, which creates fiscal imbalances between one region and another. To address this fiscal imbalance, the government allocates funds sourced from APBN to fund regional needs in decentralization implementation. At the same time, the amount of regional revenue increases (both from local revenue and transfer

funds), but regional spending has not been able to optimally improve the condition of infrastructure in the area (Rusydi, 2010). The greatest challenge in infrastructure development in all local governments in Indonesia is the allocation of APBD for capital expenditure which has been absorbed for relatively less productive routine expenditure. The allocation of resources into the capital expenditure budget is actually intended to meet the public need for public facilities and infrastructure provided by the local government, both for the smooth implementation of government tasks and for public facilities.

Based on data from the Regional Finance and Asset Management Board (BPKAD) of NTB Province in 2016, the Provincial Government Expenditure of NTB only accounts for 21% of total regional expenditure. While the realization of capital expenditure to total regional government expenditure in NTB during 2012-2016 only able to meet the average proportion of capital expenditure by 20% compared with the total regional expenditure in the same year. Referring to the national medium-term development

plan (RPJMN) for 2010-2014 and the National Medium-Term Development Plan (RPJMN) 2015-2019 Central Government gives the average target of local government capital expenditures in the range of 26-30% of total regional expenditure. This condition indicates that the lack of attention from local government to encourage economic growth, because the proportion of capital expenditure budgeted is still low (Widiasih and Gayatri, 2017).

In line with that, president Jokowi has set 8 districts in NTB province as lagging regions 2015-2019. Determination was stipulated in the presidential regulation (perpres) No. 131 of 2015 on the determination of disadvantaged regions 2015-2019. In the perpres mentioned, the disadvantaged regions are districts whose regions and communities are less developed compared to other regions on a national scale. Establishment of all districts in NTB province as disadvantaged areas indicates that local governments are required to be more independent in managing local recipients intended for the restructuring process of regional development. Local governments are required to optimize their potential revenue and one of them by providing larger portion of regional expenditure for productive sectors (Wandira, 2013). Problems related to the allocation of expenditure, which is currently the local government allocates more of its revenues to operational needs so that the allocation of capital expenditure for the needs of public services felt not adequate (Irawan, 2016). Based on data from the Regional Finance and Asset Management Board (BPKAD) of NTB province, the operational expenditure of NTB provincial government reached 78.69% of the total regional expenditure. While the realization of operational expenditure for district of disadvantaged area in NTB reach 75% from total expenditure area. This value is dominated by the amount of personnel expenditure that reached 47% of total regional expenditure. If this condition is allowed to drag on, then it is feared that bankruptcy will threaten the region soon, because its APBD is only used to finance employees (Detiknews, 2017).

The sources of funds used to finance regional expenditures, especially capital expenditures, according to Law No. 33 of 2004 on the financial balance between the central government and local government are from the Pendapatan Asli Daerah (PAD) and balanced fund consisting of the general allocation fund (DAU), special allocation fund (Dana Alokasi Khusus [DAK]) and DBH (Wandira, 2013). Increased local revenues from both PAD and balancing funds are expected to increase investment in local government capital expenditure so that the quality of public services is better but what happens is an increase in PAD and balancing fund is not followed by a significant increase in capital expenditures, this is because the revenue of the area many are sucked in to finance other less productive spending. Based on data from the regional finance and asset management board (BPKAD) of the provincial Government of West Nusa Tenggara, regional revenue from local revenue sources (PAD), which until 2016 shows the realization of revenue of Rp. 1.3 trillion or 34% of the total regional income proclaimed in APBD. While the amount of funds transferred from the Central Government of Rp. 2.5 trillion or 65% of the total Regional Income. Transfer revenues received by all district of disadvantaged areas in NTB averaged 85% of the total regional revenue. Similarly, the transfer revenue received by

the district of disadvantaged areas in NTB which reaches 85% of the total regional revenue. This means that most of the regional income is sourced from the transfer fund. During the period of 5 years from 2012 until 2016, the regional government in NTB placed the DAU as the biggest contributor of regional income with percentage reaching 58%, then DAK 11%, PAD 9.7%, DBH 5.9% and others -other legitimate regional income 4%. This shows that transfer funds from the central government still dominate regional revenue.

The high level of regional spending dependence on funding of transfer funds, indicates the high dependence of regional finance on central government funding. This condition shows an indication of less seriousness of the region in optimizing its potential. Local governments are increasingly relying on balancing funds rather than seeking to increase local revenues (PAD). This phenomenon is also called fiscal illusion where there is an asymmetric relationship between revenue (income) and expenditure (spending) (Priyo, 2009). Rusydi (2010) emphasized that when the central government provided assistance through transfers to regions to increase local spending, there was speculation that local government spending responded to the transfer changes asymmetrically. Logically, any government revenue must have an impact on the amount of spending and in turn the greater the government's expenditure, the government should benefit by increasing government revenues in the future. This means there is a symmetrical relationship between the revenue and government spending. If the reality is the opposite (an asymmetric relationship) then it can be said that there is a fiscal illusion, because the central government or the community is not aware that they are contributing (transfer funds and taxes/retributions) greater than what is required by the local government.

The issuance of presidential regulation (Perpres) No. 131 of 2015 above motivates this research. In addition, the phenomenon of capital expenditure realization in NTB during the last 5 years from 2012 to 2016 which is still below the national average target. Differences in the results of research on factors affecting capital expenditure. Also, the indication of fiscal illusion in funding of capital expenditure in local government, especially on local government in NTB province becomes an interesting research opportunity to be researched.

## 2. LITERATURE REVIEW AND HYPOTHESIS

### 2.1. Capital Expenditure

Capital expenditure under government accounting standards in government regulation No. 71 of 2010, represents budgetary expenditures for the acquisition of property and equipment and other assets that benefit more than one accounting period. Indicators of capital expenditure variables include: Ground shopping, equipment and machinery shopping, building and building expenses, road shopping, irrigation and networks, other asset expenditures (Yovita, 2011). The capital expenditure in this study is measured using the capital expenditure realization figures in regional expenditure items in the budget realization report of the 2012-2016 budget year.

## 2.2. Local Original Revenue (PAD)

Local revenue by Law no. 32 years 2004 Article 1 is income obtained by area collected according to local regulations in accordance with laws and regulations. PAD indicators include: local taxes, regional levies, the result of separated regional wealth management, other legitimate local revenue (Yovita, 2011). PAD can be measured using the realization figures of PAD in regional revenue items in the budget realization report of the 2012-2016 budget year.

## 2.3. General Allocation Fund (DAU)

General allocation funds according to Law no. 33 of 2004 on fiscal balance between central government and local government Article 1 is one of the central government fund transfers to local governments derived from APBN revenues, allocated for the purpose of equitable inter-regional financial capacity to fund regional needs in the context of decentralization implementation. DAU in this study was measured using DAU realization figures on balancing fund items in the budget realization report of the 2012-2016 budget year.

## 2.4. Special Allocation Fund (DAK)

Special allocation funds are funds sourced from APBN allocated to certain regions with the aim of assisting in funding special activities which are regional affairs and in accordance with national priorities. The DAK in this study is measured using the DAK realization figures in the balancing fund item in the budget realization report of the 2012-2016 budget year.

## 2.5. Revenue Sharing Fund (DBH)

DBH is a fund sourced from APBN revenues allocated to NTB provincial governments based on percentage figures to fund regional needs in the context of decentralization implementation. DBH in this study was measured using the DBH realization figures (profit sharing+non-tax) on balancing fund positions in the budget realization report of budget year 2012-2016.

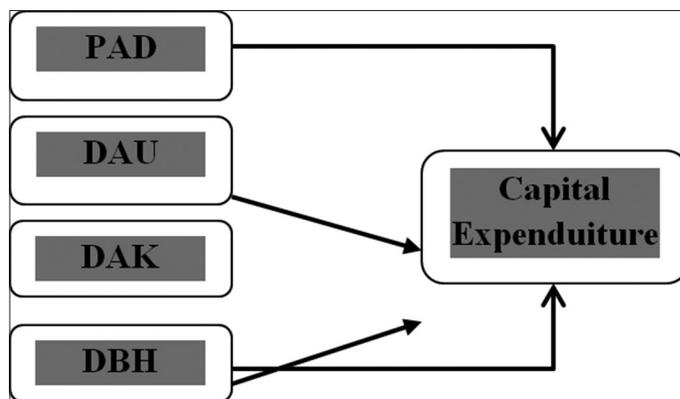
## 2.6. Fiscal Illusion

According to Priyo (2009), the increase in the amount of revenue component should have a positive relationship with expenditure, but if the opposite occurs then indicated fiscal illusion. Thus, the requirement for the occurrence of fiscal illusion through revenue measurement (income enhancement) in this study is that there are income variables namely PAD or balancing fund (DAU, DAK and DBH) which are negatively related to the variable of capital expenditure.

## 2.7. Research Framework

This study aims to examine and find empirical evidence of the effect of PAD and balancing fund consisting of general allocation fund (DAU), special allocation fund (DAK) and profit sharing fund (DBH) to capital expenditure as well as the detection of fiscal illusion (fiscal illusion) on capital expenditure financing which caused 8 districts in West Nusa Tenggara included in the criteria of disadvantaged areas based on presidential regulation No. 131/2015 on the determination of disadvantaged regions 2015-2019. Based on the description above conceptual framework of this study can be seen in the following Figure 1.

Figure 1: Research framework



Based on Law no. 32 of 2004 which has been revised into Law no. 23 year 2014, one source of local revenue is the local revenue (PAD) consisting of local taxes, the results of regional retribution, the result of separated regional wealth management and other legitimate PAD. So far, PAD has a role to finance the implementation of regional autonomy in order to achieve the main goal of regional autonomy that wants to improve public services and promote the regional economy (Mardiasmo, 2002. p. 46). Starting from the desire to realize that expectation, local government do various ways in improving public service, one of them by doing expenditure for investment interest realized through capital expenditure.

In accordance with PP. 58 of 2005 on the management of regional finances which states that the APBD is prepared according to the needs of governance and local revenue capability. That is, in every APBD drafting, if the local government will allocate capital expenditure then it should be fully adjusted to the needs of the region by considering the received revenue. The size of capital expenditure will be determined from the size of PAD. So if the local government wants to improve public services and public welfare by increasing capital expenditures, the local government must strive to dig the PAD as big as possible so that the needs and welfare of the region can be fulfilled. In research conducted by Febriana dan Praptoyo, 2015; Anjani and Akram 2015; Saefudin dan sari, 2016; Fiona et al., 2016; Widiasih and Gayatri, 2017) PAD has a positive and significant impact on capital expenditure. Thus, the first hypothesis can be expressed as follows:

$H_1$ : Local original revenue has a positive effect on capital expenditure.

Based on Law no. 33 of 2004 on fiscal balance between the central government and local government and PP. 55 year 2005 concerning balancing fund, DAU is a block grant which means that the freedom of use is given to regional heads that are adjusted to the priorities and regional needs in order to improve public services in the context of the implementation of regional autonomy. The results of stated that there is a positive and significant relationship between DAU and capital expenditure. Empirical research conducted by (Putranto, 2017, Febriana and Praptoyo, 2015; states that there is a link between transfer funds from the central government and capital expenditures. Saifudin

and Sari (2016) obtained empirical evidence that the amount of capital expenditure is affected by DAU funds received from the central government. They found that regional independence did not get better, even what happened was the opposite of the local government's dependence on central government transfers (DAU) to be higher. This gives a strong indication that the behavior of regional expenditures, especially capital expenditures will be greatly influenced by DAU revenues. From the above description can be concluded the higher the DAU then the allocation of capital expenditure also increased. This is because of the large revenue-generating regions (DAU), the allocation for regional budgets including capital expenditures will increase. Thus, the second hypothesis can be expressed as follows:

H<sub>2</sub>: General allocation fund (DAU) has a positive effect on capital expenditure.

DAK or specific purpose grant is a fund derived from APBN allocated to selected regions to assist in financing activities of a special nature which is the territory of the regional authority but in accordance with national priorities, especially in the effort to fulfill the need for basic public service facilities and infrastructure. Such special activities shall be determined by the central government by prioritizing development activities and/or procurement and/or improvement and/or improvement of physical facilities and infrastructure to perform basic public services with long economic life, including the provision of supporting physical facilities. Research conducted by Tuasikal (2008) which examined 326 districts/cities in Indonesia in 2005, in line with research (Wandira, 2013, Sugiyanta, 2016) a positive influence between DAK on capital expenditures. The results are in line with the objectives of DAK allocation for equity and to improve the condition of physical infrastructure that is considered a national priority. Thus, the third hypothesis can be expressed as follows:

H<sub>3</sub>: Special allocation fund (DAK) have a positive effect on capital expenditure.

Revenue sharing fund is a fund sourced from APBN revenues allocated to the region based on percentage figures to fund the needs of the region in the context of implementation of decentralization. The revenue-sharing fund consists of taxes and natural resources. The nature of the DBH is almost the same as the DAU which is a block grant. Where in the use of this DBH, local governments are given flexibility in the use of expenditure on the allocation of DBH. Although there are some allocations that have been set by the central government. DBH is a determinant of capital expenditure allocation, this is in accordance with research conducted by Wandira 2013, Fiona et al., 2016; Irawan, 2016) which found out that DBH has a positive influence to capital expenditure allocation. The allocation of capital expenditures is influenced by the amount of DBH transfers, indicating that DBH is one of the potential sources of local revenue to fund development in areas other than PAD, DAU and DAK. Thus, the fourth hypothesis can be expressed as follows:

H<sub>4</sub>: DBH has a positive effect on capital expenditure.

Dollery and Andrew (1999) gives an illustration of the fiscal illusion into a model diagram. The model explains that local governments make a lower tax revenue budget than the realizable tax revenues that can be obtained. Consequently, fiscal illusions may occur where the central government allocates the general allocation fund (DAU) to meet spending needs that are inconsistent with local needs. This resulted in the excess of tax revenues from budgeted by the local government (misappropriation of tax revenues) and the central government allocated a larger DAU than required by local governments. The results of the study from Gemmell et al. (1998) also showed similar results, namely a significant increase in central government transfers, but not offset by self-revenue. Research conducted by Logan (1986) shows the existence of information asymmetry. Local governments benefit from an emerging perception that government assistance is being used to improve tax services to increase PAD. The increasing role of DAU in financing as Priyo (2009) finds an indication of fiscal illusion. Thus, the fourth hypothesis can be expressed as follows:

H<sub>5</sub>: There was a fiscal illusion on capital expenditure.

### 3. RESEARCH METHODS

#### 3.1. Population and Sample

The population in this study is all districts included in undeveloped areas in NTB according to presidential regulation no. 131 of 2015. This study takes the entire population as the subject of research so that this research is a census study. This research data is secondary data in the form of budget realization report of budget year 2012 until 2016. Data obtained from official document of NTB provincial government, website of directorate general of fiscal balance and other website supporting this research.

#### 3.2. Data Analysis Method

Data analysis method used in this research is descriptive statistic and inferential statistisk. Descriptive statistics are statistics that are used to analyze data by describing or delineating the collected data as they are without intending to make general conclusions or generalizations. Meanwhile, inferential statistics are statistical techniques used to analyze sample data and the results are applied to the population (Sugiyono, 2016. p. 148). In this study the analysis of inferential statistical data used is multiple regression analysis starting from simultaneous test (F test), coefficient determination test (R<sup>2</sup>) and partial test (t test) for hypothesis testing. Regression testing must meet the requirements of passing the classical assumption test, which includes: First, the normality test is a test of the normal distribution of data. Data that is normally distributed means that data will follow the normal distribution form. The data is said to be normal distribution when significance > alpha = 0.05. Second, the autocorrelation test aims to test whether in the linear regression model there is a correlation between the error of the tampering pata period t with the intruder error in period t-1. Autocorrelation test can be done with Durbin-Watson test, which is used to determine the existence of autocorrelation or not. Durbin-Watson value is a criterion not the occurrence of autocorrelation, where the comparison of Durbin-Watson value with the value in the table by using the value of significance, the number of samples and the number of independent variables.

Third, multicollinearity test has a purpose to test whether in the regression model found the existence of correlation between independent or independent variables. To detect the presence or absence of multicollinearity in the regression model can be seen from the tolerance value and the opposite value of variance inflation factor (VIF). No multicollinearity is a VIF <10 and has a tolerance value > 0.1. Fourth, heteroscedasticity test aims to test whether in the regression method there is a variant inequality of the residual one observation to another observation. To detect the presence or absence of heteroscedasticity symptom, the Glejser method is used by regressing the residual absolute value of the model estimated against the independent variable.

Model suitability test is conducted to find out whether this research model has fulfilled the model conformity test. This research can be said to meet the fit model if the value of regression significance is <5% (significance <0.05). The coefficient of determination is used to measure how big the independent variable is able to explain the change of the dependent variable. The value of  $R^2$  is between 0 and 1. If  $R^2 = 1$ , then 100% of the total variation of the dependent variable can be explained by the independent variable. However if  $R^2 = 0$ , then there is no total variation of the dependent variable which can be explained by the variation of the independent variable. Hypothesis testing is done to measure how far the influence of each independent variable partially in explain variation of dependent variable.

## 4. RESULTS AND DISCUSSION

### 4.1. Descriptive Statistics Analysis Results

Descriptive statistics aim to provide information on the characteristics of research variables consisting of the number of observations, minimum values, maximum values, mean values, and standard deviation (Ghozali, 2013. p. 19). Descriptive statistical results are presented in Table 1.

Average original regional revenue in the disadvantaged regions in NTB province for the period 2012-2016 amounted to 101,357,575,680 rupiahs, a minimum of 2,629,7196,957 rupiah, and a maximum of 236,147,475,251 rupiah. The average general allocation funds in the disadvantaged regions in NTB province for the period 2012-2016 amounted to 647,451,017,375 rupiahs, a minimum of 259,334,022,000 rupiah, and a maximum of 1,162,763,206,000 rupiah. The average special allocation fund for disadvantaged areas in NTB province for the period 2012-2016 amounts to 125,726,401,686 rupiahs, a minimum of 28,651,770,000 rupiah, and a maximum of 465,783,119,252 rupiah. Average revenue sharing funds in disadvantaged areas in NTB province for the period 2012-2016 amounted to

**Table 1: Descriptive statistical analysis**

Variable	N	Minimum	Maximum	Mean±SD
Y	40	1.E11	4.E11	2.17E11±7.903E10
x1	40	26297196957	2.E11	1.01E11±5.506E10
x2	40	3.E11	1.E12	6.47E11±2.423E11
x3	40	28651770000	5.E11	1.26E11±1.045E11
x4	40	15801782446	5.E11	6.54E10±6.884E10

SD: Standard deviation, Source: Secondary data processed (2017)

65,409,714,338 rupiahs, minimum of 15,801,782,446 rupiahs, and a maximum of 455,854,715,420 rupiah. Average capital expenditure in the disadvantaged regions in NTB province for the period 2012-2016 amounted to 217,011,270,311 rupiahs, a minimum of 109,555,971,230 rupiahs, and a maximum of 421,798,287,025 rupiah.

Before the regression model is used to test the hypothesis, firstly testing the accuracy of the research model in the form of classical assumption test. The classical assumption test is performed to determine whether there is any deviation from the classical assumption of the multiple linear regression equation used. The test results shall show that the data satisfy various criteria of classical assumption testing, ie normal distributed data, no multicollinearity problem, no autocorrelation, and free data from heterokedastisity problem.

Normality test aims to test whether in the regression model, residual variables have a normal or abnormal distribution. Research data is said to be normal distribution if Asump value significance (2-tailed) >0.05. Normality test results show that Asump value. Significance (2-tailed) model equations tested of 0.513 >0.05. This shows the data from the regression model in this study is normally distributed.

Multicollinearity test has a purpose to test whether in the regression model found the existence of correlation between independent or independent variables. Multicollinearity test results show that the tolerance value >0.1 or VIF value is smaller than 10. So it can be concluded that did not experience multicoleniaritas gejala in this study.

The autocorrelation test aims to test whether in the linear regression model there is a correlation between a period t with the previous t period. The results of the autocorrelation test indicate that the Durbin-Watson value of 1.684, in the Durbin-Watson table with n = 40 and k = 45% significance level shows the value  $dL = 1.2848$  and  $du = 1.7209$ . The DW value of 1.684 lies between the value of  $dL = 1.2848$  and  $du = 1.7209$  so there is no definite conclusion about whether or not the autocorrelation symptoms of the data. To solve the problem of the above data, then the steps that must be done is by test run test. The result of the test run test shows that Asym significance (2-tailed) value of 0.873 is >0.05 it can be concluded that there is no symptoms or autocorrelation problem. Thus, the problem of autocorrelation that can not be resolved with Durbin Watson can be resolved through the test run test so that linear regression analysis can proceed.

Heteroskedasticity test aims to test whether in the regression method there is a variant inequality of the residual one observation to another observation. The result of heteroscedasticity test shows that the level of significance of the local original income, general allocation fund, special allocation fund and sharing fund is >0.05 so it can be concluded there is no problem of heteroskedastisitas in this research data.

### 4.2. Inferential Statistics Test Results

The method used is multiple linear regression. It is intended to test the content of PAD, DAU, DAK, and DBH against BM by

looking at the strength of the relationship between BM and PAD, DAU, DAK, and DBH. The following is the result of regression analysis test (Table 2).

Based on Table 2, it can be arranged the following regression equation:

$$Y = 87530793700.662 + 0.733 \text{ PAD} - 0.003 \text{ DAU} + 0.247 \text{ DAK} + 0.398 \text{ DBH} + e$$

1. Constant value = 87530793700,662 is positive. Indicates capital expenditure of 87530793700,662 with the provisions of the variables in this study not included in the regression equation or constant value (0).
2. The value of regression coefficient of local revenue variable (PAD) (b1) positive equal to 0.733. Indicates if the local revenue (PAD) is increased by 1 unit it will raise capital expenditure (BM) by 0.733, with the other constant (0).
3. The value of regression coefficient variable of general allocation fund (DAU) (b2) negative is -0.003. Indicates if the general allocation fund (DAU) is increased by 1 unit it will decrease capital expenditure (BM) by -0.003, provided that other variables are constant (0).
4. The value of variable regression coefficient of special allocation fund (DAK) (b3) positive is 0.247. Indicates if the special allocation fund (DAK) is increased by 1 unit it will raise capital expenditure (BM) by 0.247, provided that other variables are constant (0).
5. The value of regression coefficient of profit sharing (DBH) (b4) positive is 0.398. Indicates if DBH is increased by 1 unit, it will raise capital expenditure (BM) by 0,398, provided that other variable is constant (0).

4.2.1. F test (simultaneous test)

Model feasibility test or F test is an early stage to identify the effect of independent variables on the dependent variable.

Based on Table 3, the test results obtained by prob. F arithmetic (significance) value is 0.000 smaller than the 0.05 significance level so it can be concluded that the estimated linear regression model is appropriate to explain the effect of PAD, DAU, DAK and DBH on capital expenditure variable. The result of statistic test F in Table 3 above to test the effect of PAD, DAU, DAK and DBH having F-count of 25.872 with significance value 0.000 this means significance level <5% ( $\alpha = 0.05$ ) and F-count equal to 25.872 > F-table of 2.64 which means that PAD, DAU, DAK and DBH simultaneously have a significant effect on capital expenditure.

4.2.2. T test (parsial test)

Regression coefficient test (t-test) in multiple linear regression is intended to test whether the parameters (regression coefficients and constants) suspected to estimate multiple linear regression equations/models are parameters capable of explaining the behavior of independent variables in influencing the dependent variable. The t test is used to determine the effect of independent variables on the dependent variable and t test is used to see the effect one by one or partially. Partial test results can be seen in Table 2 so it can be concluded that:

1. The result of t test for the variable of original revenue (PAD) obtained t value equal to 3.641 with significance equal to 0.001, because t count bigger than t-table (3.641 > 2.13185) or value significance <0.05 0.001 is smaller than 0.05), then  $H_1$  is accepted, meaning that PAD variable has a positive effect on capital expenditure.
2. The result of t test for variable of general allocation fund (DAU) obtained t value equal to -0.063 with significance equal to 0.950, because t count smaller than t table (-0.063 < -2.13185) or value significance above 0, 05 (0.950 is >0.05), then  $H_{2a}$  is rejected, it means that general allocation fund (DAU) variable has no positive effect on capital expenditure.
3. The result of t test for the variable of special allocation fund (DAK) obtained t value 2.779 with significance equal to 0.009, because t count bigger than t table (2.779 bigger than 2.13185) or significance value below 0.05 0.009 <0.05), then  $H_{2b}$  accepted means the variable special allocation fund (DAK) has a positive effect on capital expenditure.
4. The result of t test for the DBH variable is obtained t value equal to 3.871 with significance equal to 0.000, because t count bigger than t table (3.871 bigger than 2.13185) or significance value below 0.05 0.000 <0.05), then  $H_{2c}$  is accepted meaning the DBH has positive effect on capital expenditure.

4.2.3. Determination coefficient analysis (R<sup>2</sup>)

Determination coefficient analysis describes the variation of the influence of independent variables on the dependent variable. Determination coefficient analysis can be measured by the value of R<sup>2</sup> or adjusted R<sup>2</sup>.

Table 4 shows the Adjusted R<sup>2</sup> number is 0.718 indicating 71.8% of government expenditure can be explained by the variable of original revenue, general allocation fund, special allocation fund and profit sharing fund. While 28.2% is explained by other variables. The standard error of the estimate (41937907919.746) is smaller than the government expenditure standard deviation (79028169107.406), then the regression model is better at acting as

Table 2: Regression analysis

Coefficients <sup>a</sup>							
Model	Unstandardized coefficients		Standardized coefficients	t	Significance	Collinearity statistics	
	B	Standard error				Beta	Tolerance
1							
(Constant)	8.753E10	2.088E10		4.191	0.000		
x1	0.733	0.201	0.511	30.641	0.001	0.366	2.729
x2	-0.003	0.046	-0.009	-0.063	0.950	0.362	2.766
x3	0.247	0.089	0.326	2.779	0.009	0.525	1.906
x4	0.398	0.103	0.347	3,871	0.000	0.900	1.111

Source: Secondary data processed (2017)

a predictor of government spending than the average government expenditure itself. The role of all variables is very influential, considering that the variable is a source of funding used to finance government spending. The results of the research indicate that the original revenue, special allocation fund and revenue sharing fund have a positive relationship with government expenditure. While the general allocation fund has a negative relationship. Indigenous revenue variables, special allocation funds and revenue-sharing funds have significant influence because the significance value is <0.05. However, the variable of general allocation fund has no significant effect because its significance value >0.05.

**4.3. Hypothesis Test Results**

**4.3.1. Effect of PAD on capital expenditure**

Based on hypothesis test result (Table 2) found that PAD have positive effect to capital expenditure. Revenue original (PAD) is revenue obtained by the region and levied according to local regulations in accordance with legislation. The higher (PAD) earned then reflects the performance of good local government, so with the high (PAD) obtained then the higher also allocated for capital expenditure. In this study, PAD in all districts under disadvantaged regions during the period 2012-2016 averages only contributes 10% of total regional revenues, but the amount of small local revenue (PAD) is still small will still affect the capital expenditures due to the revenue region (PAD) is the main source of revenue of local governments. The sources of finance derived from local revenues in the implementation of regional autonomy are more important than sources other than local revenues, since local revenues can be used in accordance with local initiatives and initiatives whereas the form of government

grant (non-PAD) is more binding. This finding may indicate that the magnitude of PAD becomes one of the decisive factors in determining capital expenditure. This is in accordance with government regulation no. 58 of 2005 which states that APBD is prepared in accordance with the needs of the government and the ability of regions to generate income. Each APBD preparation, capital expenditure allocation must be adjusted to the needs of the region by considering the received revenue. So if the local government wants to increase capital expenditure for public services and public welfare, then the local government should dig as much PAD. The results of this study are in accordance with research conducted by (Sumarmi, 2010; Khadafi, 2013; Meianto et al., 2015; Nugroho, 2015; Febriana and Praptoyo, 2015; Anjani and Akram 2015; Fiona et al., 2016; Widiasih and Gayatri, 2017; Keswando et al., 2016; local own revenue (PAD) has a positive and significant impact on capital expenditure. But sometimes the increase in PAD is not always followed by an increase in capital expenditure budget because PAD is widely absorbed to finance other expenditures. Research conducted by Irawan (2016) found a low correlation between PAD and capital expenditures due to PAD is more used to finance other expenditures, such as routine expenditure/operational expenditure rather than to finance capital expenditure. In line with this, the Yovita (2011), Wandira (2013), found PAD has no effect on capital expenditure realization in a number of local governments in Indonesia.

**4.3.2. Effects of DAU on capital expenditures**

Based on hypothesis test results (Table 2) it is found that DAU has no positive effect on capital expenditure. This is because local governments pay less attention to the proportion of general allocation funds allocated to capital expenditures. However, the larger public allocated fund is used to finance other expenditures such as personnel expenditure, goods expenditure, grant expenditure, social assistance expenditure, financial aid expenditure. In this study, the average of operational expenditures of disadvantaged areas shows a ratio of 75% of total regional expenditure. This value is dominated by the amount of personnel expenditure that reaches 47% of the total regional expenditure. This is not in accordance with the mandate of presidential regulation of

**Table 3: F test**

ANOVA <sup>b</sup>					
Model	Sum of squares	df	Mean square	F	Significance
1					
Regression	1.820E23	4	4.550E22	25.872	0.000
Residual	6.156E22	35	1.759E21		
Total	2.436E23	39			

Source: Secondary data processed (2017)

**Table 4: Determination coefficient analysis**

Model summary <sup>b</sup>					
Model	R	R <sup>2</sup>	Adjusted R <sup>2</sup>	Standard error of the estimate	Durbin-Watson
1	0.864	0.747	0.718	4.194E10	1.684

Source: Secondary Data Processed (2017)

**Table 5: Detecting fiscal illusion with revenue measurement**

Coefficients <sup>a</sup>					
Model	Unstandardized coefficients		t	Significance	Conclusion
	B	Standard. error			
1					
(Constant)	8.753E10	2.088E10	4.191	0.000	
x1	0.733	0.201	3.641	0.001	There is no fiscal illusion
x2	-0.003	0.046	-0.063	0.950	There is a fiscal illusion
x3	0.247	0.089	2.779	0.009	There is no fiscal illusion
x4	0.398	0.103	3.871	0.000	There is no fiscal illusion

Source: Secondary data processed (2017)

the Republic of Indonesia number 2 year 2015 on RPJMN year 2015-2019, where the target average percentage of district/city employee expenditures maximum of 35% of regional expenditure. The high proportion of personnel expenditure at the central and regional levels is not separated from the existence of various employee policies so far. Remuneration proven not to reduce the behavior of bureaucratic corruption, 13<sup>th</sup> salary, continuous recruitment of civil servants regardless of budget constraints, as well as policies that implicate the burden of personnel expenditure such as the appointment of Sekdes to civil servants resulted in regions, especially districts, have a larger portrait of APBD. This is evidenced by the amount of DAU allocation to local government in NTB during 2012-2016 has placed DAU as the biggest contributor of regional revenue with percentage reaching 58%, almost entirely used for personnel expenditure and operational expenditure. The results of this study are in accordance with the study of Lestari et al. (2016) found that general allocation funds have no effect on capital expenditures, research results (Yovita, 2011; Wandira, 2013; Irawan, 2016) further strengthens the empirical evidence. While Sugiyanta (2016) found that DAU has significant effect in the opposite direction because of the nature of the transfer fund which is a block grant in which the regional head is given full flexibility in using the transfer funds.

#### *4.3.3. Effect of DAK on capital expenditures*

Based on the result of hypothesis testing (Table 2) found that special allocation fund has positive effect to capital expenditure. The special allocation fund (DAK) is a fund sourced from APBN revenues allocated to certain regions with the aim of assisting in funding specific activities which are regional affairs and according to national priorities. So in this case if the special allocation fund (DAK) is not used for special activities and national priorities then the special allocation fund can be used for capital expenditure, the greater the special allocation fund (DAK) will be used for capital expenditure. DAK is the second largest contributor after DAU for regional revenue to local governments in NTB during the period 2012-2016. The average proportion of DAK is 11% of total regional revenue over the last 5 years. This means that DAK is one of the determinants of capital expenditures on disadvantaged local governments in NTB. The results of this study are in line with research (Wandira, 2013, Sugiyanta, 2016) stating that there is a positive influence between DAK on capital expenditures. The results are in line with the proportion of special allocation funds allocated to capital expenditures. The results are in line with the objective of DAK allocation to fund national government programs in the regions, where one of the programs is related to capital expenditure. But the results of research conducted by Jannah et al. (2017) found that there was a significant negative effect between DAK and capital expenditure, indicating that local governments should pay more attention to the proportion of special allocation funds allocated to capital expenditures.

#### *4.3.4. Effect of DBH on capital expenditure*

Based on hypothesis test results (Table 2) found that DBH has positive effect on capital expenditure. This is because the region is a producer and manager of the wealth of the area itself that is used to build and prosper the region. These developments and other expenditures related to the management of local wealth

will affect the amount of capital expenditure, so the greater the DBH will affect the greater capital expenditure. Over the past 5 years DBH averages accounted for 5.9% of local revenue for local governments in NTB. This means DBH is also one of the potential sources of income used by local governments to finance capital expenditures. Research (Wandira 2013; Irawan, 2016) found out that DBH has a positive effect on capital expenditure allocation. On the other hand, studies conducted by Sugiyanta, 2016, Widiasih and Gayatri, 2017) do not find the effect of DBH on capital expenditure spending. This means that both DBH Tax and DBH SDA in most districts/cities in Indonesia is not a source of potential revenue for regional financing.

#### *4.3.5. Fiscal illusion on capital expenditure*

The results of this study indicate that there has been a fiscal illusion on capital expenditure financing. This is because the variables that have negative correlation with government expenditure with significant value, namely general allocation fund (DAU) used to finance personnel expenditures and routine expenditures are relatively less productive. The results of this study are not in line with the findings of Holtz-Eakin et al. (1994) which indicates a close bond between central government transfers and regional expenditures. Reality suggests otherwise that local governments are not optimal in spending allocations for DAU revenues. This is in line with the theory put forward by Gemmell et al. (1998) which states that if there are variables that have a negative relationship with government spending, then indicated the existence of fiscal illusion. The results of this study are also in line with research conducted by Gemmell et al. (1998) who found fiscal illusions through a negative relationship between government spending and revenue from general allocation funds used for expenditure (Table 5).

## **5. CONCLUSIONS AND RECOMMENDATIONS**

Based on the analysis and discussion conducted, it can be deduced conclusions original revenue, special allocation funds, and revenue-sharing funds positively affect the capital expenditure of disadvantaged areas in NTB. While general allocation funds, no effect on capital expenditure of disadvantaged areas in NTB. And it is detected that there is fiscal illusion in the funding of disbursed capital expenditure in the period 2012-2016 in NTB.

The results of this study are expected to provide information and consideration to local governments on effective and efficient APBD management, especially the allocation of capital expenditure budget for the development of public needs of public infrastructure facilities in an effort to improve the quality of public services and the acceleration of development of disadvantaged areas. In addition, it can be taken into consideration for the stakeholders in policy making and regulations related to capital expenditure.

Good regulation on the utilization of local potency that can increase local revenue (PAD) to be allocated in capital expenditure, also regulation about minimum portion of capital expenditure that must be budgeted by local government in regional budget

in accordance with RPJMN, to reduce government dependency region to the central government.

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