

CHAPTER EIGHT

APBD MANAGEMENT UNDER THE CURRENT BUDGETING POLICY: AN ANALYSIS

8.1. Introduction

Along with the implementation of the local autonomy policy beginning in 2001, the Indonesian authorities have obligated local governments to apply a new paradigm of budgeting system that consists of such approaches as the Performance-Based Budgeting System (PBBS), the Medium-Term Expenditure Framework (MTEF), Integrated Budgeting, and the Accrual Based Accounting System. As well as this, the government has issued many policies to ensure that the APBD budgetary events run under professional and technocratic processes. These policies also promote the implementation of a bottom-up and participatory approach in the budgeting process.

To what extent have the new approaches of budgeting been implemented? What are the achievements of, and constraints faced by, local government officers in implementing these systems? Is the budgeting process considered as a managerial or political event? Is the intention to manage the APBD using a bottom-up approach successfully implemented? Has the local community enjoyed more local budget funds under the new budgeting system? Why? This chapter will clarify these critical questions, particularly in relation to the operation of the new budgetary approaches. The chapter also analyses the controversy about the issue of managerial and political influence in the budgetary events. In addition, the chapter examines the bottom-up

method adopted in the budgeting process.

This chapter consists of four sections. The first section elucidates and analyses the adoption of four new budgeting approaches, and the next section clarifies the budgeting process, whether it is a managerial or political event. The third section analyses the efficacy of *Musrenbang* as a major device to apply a bottom-up approach in the budgeting process, then the final section examines whether or not the local community enjoys more local budget funds under the new budgeting system.

8.2. Adoption of New Budgeting Approaches

Since governance reform in 2000, Indonesia has been applying the ‘new paradigm of budgeting system’ (Mardiasmo, 2002, p. 131) by adopting such budgeting principles as a Performance Based Budgeting System (PBBS). Implementation of the PBBS is then followed by the introduction of some supporting approaches, such as a Medium-Term Expenditure Framework (MTEF), integrated budgeting, and an accrual-based accounting system. This section analyses the achievements and challenges of the execution of these four approaches in the study areas.

8.2.1. Performance-Based Budgeting System (PBBS)

One of the most important points in relation to Indonesia’s governance reform is the reform of public finance and budgeting. In view of this, the government has issued a range of laws and guidelines¹ requiring government institutions to implement

¹ In the early phase of budgeting reform, provisions requiring government institutions to apply a Performance-Based Budgeting System (PBBS) can be found in the PP (*Peraturan Pemerintah/ Government Regulation*) 105 of 2000 regarding Local Finance Management and *Keppmendagri* (*Keputusan Menteri Dalam Negeri/ Decree of Minister of Home Affairs*) 29 of 2002 concerning Guidelines of Formulation, Management, and Accountability of the annual local budget (APBD).

the Performance-Based Budgeting System (PBBS). According to the OECD (2003b, p. 7), performance budgeting is a form of budgeting that relates funds allocated to measurable results. Meanwhile the GAO (1993, p. 4) points out that performance budgeting links performance information with the budget. Along with introduction of PBBS in Indonesia, government institutions have been encouraged to gradually make a transition away from the traditional budgeting system, as this method (which applies incremental and line-item budgeting) is not able to manage government finances economically, efficiently, or effectively.

As found at the research sites, the intensity of local governments in implementing the PBBS varies. This means that, while a particular local government may have adopted the PBBS in an ideal manner as required in the guidelines, other local governments still appear to struggle to apply this approach perfectly. Even though the local governments in the research locations apply the PPBS in various ways, it can be assessed that they generally execute the PBBS through four main steps.

The first phase is the preparation of the strategic plan (*Renstra*). The strategic plan consists of the institutional vision and mission, the objectives, and the target. Additionally, the *Renstra* also elaborates upon the strategies needed to realise the objectives and targets of the institution.

The second phase involves the creation of an annual performance plan (*Rencana Kinerja Tahunan*). In the current budgeting process, the annual

The requirement to implement the PBBS became more urgent with the issuance of Law 17 of 2003 on Public Finance, as this statute strictly obligates government bodies to apply the PBBS in managing the institutional budget. Subsequently, the requirement to implement PBBS was detailed in the PP 54 of 2005 (this PP replaces PP 105 of 2000) and PERMENDAGRI 13/2006 (this replaces KEPMENDAGRI 29 of 2002).

performance plan is known as the work plan of local government units (*Rencana Kerja Satuan Kerja Perangkat Daerah/ Renja-SKPD*). The annual performance plan is basically the elaboration of the strategic plan (*Renstra*) in the form of programmes, projects, and activities that will be executed by local government units in a particular financial year. In general, the performance plan consists of three components: (1) the targets intended to be achieved in a fiscal year; (2) performance indicators which contain the five factors of input, output, outcome, benefit, and impact²; and (3) programmes, projects, activities, and an operational plan to execute them.

The third stage is the setting up of the ‘determination of performance’ (*Penetapan Kinerja*). The determination of performance is the declaration of the operating officials who are in charge to implement the established programmes and activities. In this context, the determination of performance is prepared by the heads of local government units (*SKPD/ Satuan Kerja Perangkat Daerah*) to be presented to the head of the local government (*Bupati/ Walikota*). The determination of performance contains two main elements, the declaration of determined performance and the appendix, consisting of targets that have to be achieved by an institution during the financial year. Along with this process, local governments prepare the Expenditure Standard Analysis (*Analisa Standar Belanja/ ASB*) that will be used as a reference to set up the cost and input of programmes/ activities. Informants of local officials stated that all local government units have to refer to this standard (*ASB*)

² In this context, input consists of any resources/ materials (such as human resources, funds, materials, time, technology, and so on) needed to produce output;

Output is any product (in the form of goods/ services) arising from programmes/ activities;

Outcome reflects the function of output;

Benefit is any advantages (either directly or indirectly) obtained by the community, particularly to improve their lives;

Impact is the impact of programmes/ activities on the socio-economic condition of the community.

upon allocating a budget for any local spending, because these allocated costs will be more rational and accountable. Therefore, the implementation of programmes/ activities will be more economical, efficient, and effective.

The fourth step is the preparation of the measurement of performance. The measurement of performance is used to assess whether or not the execution of programmes/ activities has been undertaken successfully. Performance measurement is conducted using performance indicators that have been previously set up and determined based on data collected from internal and external parties. The collection of performance data for the indicators of input, output, and outcome, is undertaken during the ongoing process of programmes/ activities, while the collection of performance data for indicators of benefit and impact is carried out once the execution of the programmes/ activities has been completed³. As seen at the research sites, local government officials measure the performance of programmes/ activities by using the following formula:

$$\text{Performance of Achievement} = \frac{\text{Realisation}}{\text{Target}} \times 100\%$$

Subsequently, the results of the performance measurement are evaluated by top-level officials. This evaluation aims to analyse the supporting and constraining factors involved in programme/ activity implementation. The evaluation also intends to minimise the obstacles that may arise during the execution of the programmes/

³ This performance measurement aims to provide an understanding of the efficiency, effectiveness, frugality, and quality of target achievement of programmes/ activities implemented by local government institutions. It also intends to analyse the costs and benefits as well as the obstacles emerging in the execution process of programmes/ activities.

activities in order to be able improve the quality of performance in the future.

The stages elucidated above is in line with contention of Harrison (2003) who specifies three components of performance budgeting, including the result (the end outcome), the strategy (ways to achieve the end outcome), and activity/ outputs (what is actually done in order to achieve the end outcome). Performance budgeting establishes a link between the rationales for specific activities and the end outcome. This information enables policymakers to determine which activities are cost-effective in reaching their end outcome

As mentioned earlier, all local bodies have implemented the principles of PBBS in managing the APBD (local budget) although not necessarily perfectly at this point. It can be seen from the process of arranging programmes and projects that local staff members always apply the performance indicators (input, output, outcome, benefit, and impact indicators) to set up a plan for the programmes and projects. Moreover, as Gianakis & McCue (1999, p. 25) point out, in PBBS, resources are allocated to specific activities that produce immediate outputs, rather than to the line-items that indicate the materials consumed in the production process

The informants for the local executives and legislatures admit that this phenomenon has a positive impact, as the performance and achievement of programmes and projects executed by local governments becomes more tangible and measurable as a result. Moreover, some local governments such as the Regency of Trenggalek and the City of Surabaya have created standard guidelines to determine the price of any goods and services procured by local government entities. Additionally, local authorities in the research areas also seem to put in serious efforts to continuously improve the implementation of the PBBS.

Nonetheless, the reality indicates that Surabaya City, Batu City, and Trenggalek Regency face significant constraints in the ideal implementation of the PBBS. The first challenge is the limited budget. Local officials frequently complain that they have often ideally formulated the work programmes and performance indicators. Unfortunately, they cannot implement the plan properly as the budget is very limited. Consequently, local authorities repeatedly have to change the established programmes in order to match them with the available funds.

The second problem is the poor quality of human resources. Most local staff members in the research areas do not have adequate skills and knowledge about the planning and budgeting system. As a result, they are not able to create the work programmes and performance indicators accordingly. They primarily ‘copy and paste’ the work programmes and performance indicators from the previous year’s work programmes.

Thirdly, there is a conflict of interest among local executives and legislatures. As seen in the study areas, once the authorities of the local legislature and the executive discuss the development plan and budget, the members of the legislature tend to review the proposed programmes from a political perspective (for example, to what extent the programme will have a positive impact on their constituents and the political party). On the other hand, local executives place a greater focus on reviewing the details of the programmes and performance indicators such as inputs, outputs, outcomes, benefits, and impacts of the programmes. This different point of view often leads to prolonged debate among these two bodies, and as a result, the finalisation of the formulation and validation process of the APBD is frequently delayed. In this connection, Robinson & Brumby (2005, pp. 15-16) note that, in its

most extreme form, the argument is that budgeting is inherently political rather than rational, and that politics will always win, thus the construction of the objective to prioritise rational expenditure is largely an illusion.

Moreover, the legislature members in the study areas appear to be quite reluctant, and some of them even appear apathetic, in responding to the implementation of the PBBS. They argue that it was very easy to review the budget proposals (proposed by executives); however, presently the budget proposals are elaborated in a complex way, therefore they have to consider lots of indicators (input, output, outcome, benefit, and impact) once reviewing the proposals. Consequently the APBD validation process in parliament takes more time, even often finishes untimely.

Another legislator explained that most legislature members are not interested in mastering the details of the new system (PBBS) or other new approaches such as the MTEF, integrated budgeting, the accrual accounting system, and so forth. They are not motivated to do this because learning these new systems is time-consuming. Moreover, they argue that there is no guarantee that they will be re-elected (as a legislator) at the next election; hence, it would be pointless to have learnt the new system without any longer holding a position as a legislator. This circumstance confirms the statement of Harrison (2003) that performance budgeting requires a change in the legislature's perspective on the budget, because the character of the legislature is one that tends to resist the measurement of performance and accountability. Further, Wendland (2003, cited in Harrison, 2003) details the reasons that cause legislative members to prefer the incremental approach, and therefore to reject performance based budgeting, because: (1) it is easy to calculate; (2) the present activities are tied to a known past rather than to an unknown future; (3)

traditional budgeting does not require analysis of policy. Line-item budgets are policy-neutral, thereby lessening conflict; (4) traditional budgeting lives on because it is easier, simpler and reduces conflict; (5) many portions of the current budget cannot be altered; and (6) the cost of auditing performance reports can be very high.

Finally, the standards of costs and minimal services cannot be comprehensively determined. The reality shows that the standards of costs and minimal services have not been comprehensively established to support the implementation of the PPBS. Some local agencies still struggle to set up the price standards for each programme and activity. This situation is caused by the absence of a reliable database and a good accounting and planning system. This situation further triggers many of the difficulties faced by local staff members in creating the actual performance indicators and targets, including to determine: (a) how much input is needed to execute a project, (b) the kind of output that would be generated, (c) the quality of the outcome, (d) the benefits for the community, and (e) the improvement of community life. As a result, the efficiency of programmes and activities becomes difficult to be accurately measured and evaluated.

The discussion above clearly indicates that the Performance-Based Budgeting System (PBBS) is more advantageous than traditional budgeting. Nevertheless, it needs to be implemented very carefully otherwise this system is unlikely to produce optimal results as expected. In light of this, Joyce & Sieg (2000) suggest - at least - four prerequisites in order for the PBB to be successfully implemented, including that: (a) public entities need to know what they are supposed to accomplish; (b) valid measures of performance; (c) accurate measures of cost; and (d) cost and performance information needs to be brought together for budgeting decisions.

8.2.2. Medium-Term Expenditure Framework (MTEF)

In accordance with the budgeting reform initiative, the government encourages government institutions to implement the Medium-Term Expenditure Framework (MTEF) to manage local government budgets and finances. The authorities argue that the implementation of the MTEF is urgent as the budgets developed and executed on an annual basis have certain limitations. This is because there is no definite linkage between the implemented policies and the annual budgetary expenditures due to inconsistencies in the timing. As Armenia (2013, pp. 4-6) states, planning of medium-term public expenditure is an ongoing process and, in essence, represents a complete logical chain of “policy formulation – planning – budgeting”. This enables the adjustment of possible inconsistencies between the available resources and expenditure needs, as well as enabling the making of changes in public expenditures equivalent to the policy changes in different sectors.

The statement above is in line with the provision mentioned in Law 17 of 2003 regarding Public Finance, Law 25 of 2004 on the National Development Planning System, and *Permendagri* 13 of 2006 concerning the guidelines for local finance management. These regulations state that the implementation of the MTEF aims to reduce the obscurity of the linkages between policy, planning, and budgeting. Furthermore, the regulations are also intended to improve the quality of public services and fiscal discipline. The main point of the MTEF, in the Indonesian context, is to implement budget management through a multi-year perspective (more than one financial year) because, as Armenia (2013) emphasise, budgets developed and executed on an annual basis have certain limitations as they are based on short-term macroeconomic forecasts, and there is no definite linkage between the implemented

policies and the annual budgetary expenditures due to inconsistency in the timing. Moreover, budgetary decisions have to be based not only on relative needs as they are today, but also on forecasts of what the needs will be tomorrow, next year, or in the next decade (Lewis, 1952, cited by Gianakis & McCue, 1999, p. 19)

As seen at the research sites, particular local government units that have implemented the MTEF have generally arranged the implementation of the MTEF in five main steps, as follows:

- (1) Preparation of the projection and plan of macro-economics for the medium-term period. In this step, the DPPKAD (*Dinas Pendapatan dan Pengelolaan Keuangan dan Aset Daerah/ Service of Revenue Affairs and Management of Finance and Assets*) and the BAPPEDA (*Badan Perencanaan Pembangunan Daerah/ Local Government Body for Development Planning*), and other related local government bodies, prepare the medium-term macro-economic plan and projections. These projections are generally made for a period of 3 to 5 years;
- (2) The DPPKAD, BAPPEDA, and other related institutions, arrange the medium-term projections and targets of the fiscal conditions, such as taxes, the surplus/ deficit ratio, the ratio of government income to debt, and other projections;
- (3) The DPPKAD and the BAPPEDA then invite local government units (SKPD/ *Satuan Kerja Perangkat Daerah*) that have medium-term programmes/ projects/ activities to jointly create the medium-term budget framework (including projections of revenue, expenditure, and finance). These projections are then referred to in the setting up of the total allocations of medium-term local government expenditures;
- (4) Once the allocation of medium-term government expenditure has been

determined, the DPPKAD and the BAPPEDA distribute budget allocations to each local government unit that has mid-term projects/ activities. This allocation indicates the maximum amount of the budget allowed to be spent by the local institutions in executing medium-term projects/ activities;

(5) Each local government unit (SKPD) elaborates the allocated expenditure budget into medium-term programmes/ projects/ activities that will be executed by those institutions.

In short, the MTEF arrangements involve two crucial activities, namely, arranging of policy priorities⁴ and creating of forward estimations⁵. As found in the study areas, the local authorities are generally able to create policy priorities as the first activity of the MTEF. Nonetheless, many of them tend to struggle to create the forward estimations precisely enough (to follow up the policy priorities) as the situations and conditions in Indonesia frequently change very rapidly. This is also caused, as the informants explain, by fiscal instability and the uncertainty of financial capacity of local governments. Furthermore, the lack of human resource capacity contributes significantly in hampering the success of MTEF execution. In correlation with this fact, implementation of MTEF must be executed extra prudently. Otherwise, as warned by Levy (2007), it can be a great consumer of time and resources and may distract attention from the immediate need for improving the annual budget and the budgetary execution process.

⁴ Arranging the policy priorities is an activity to set policy priorities that will be implemented by local government bodies, therefore local authorities enable the calculation of funds needed to implement the policies which can then be adjusted to the available budget.

⁵ Arranging the forward estimations is the calculation of the funds required for the next financial year, therefore the local authorities can ensure the sustainability of programmes and activities. This calculation will also be referred to in the formulation of the budget for the next financial year.

The informants explain that the implementation of the MTEF is not a simple matter because it also needs a special MoU (memorandum of understanding) within the local executives and legislatures, so the preparation of long-term projects may take longer than annual projects/activities. Moreover, the normative guidelines do not allow local governments to implement the MTEF if there is a change of local government head in that particular financial year. As happened in Batu City, an Office Block development in Batu City municipality - which was set up as a multi-year project with a duration of 5 years - was delayed in 2013 because there was a local election to elect the City Mayor and Vice-Mayor that took place at the beginning of 2013. Consequently, any development activities for this office had to be stopped during the 2013 financial year, which would be continued in the 2014 financial year⁶. In practice, the implementation of the MTEF is simultaneously combined with the principle of integrated budgeting⁷.

Despite its popularity, the MTEF has been effective in only a few countries. Schick (2008) affirms that it is mostly a technical exercise which is institutionally and procedurally separate from the annual budgeting process. As a result, resource decisions are still made on an annual basis and the budget remains input-based and incremental. Challenge of implementing the MTEF is about considering the right timing based on an objective assessment of conditions and a clear understanding of its benefits and limitations. Failure to do this may devalue the MTEF which then becomes meaningless term associated with unfulfilled expectations of public sector reform. In view of this, Kasek & Webber (2009, pp. 39-40) further suggest a number

⁶ <http://mitrafm.com/2012/12/19/proyek-block-office-batal-anggaran-multiyears/> - Dec 19th, 2012

⁷ Unified Budgeting is the formulation of a yearly financial plan implemented integrally for all kinds of expenditure; therefore it will be able to execute government activities efficiently.

of practical considerations which need to be understood in deciding whether or not to undertake a MTEF, including: integration with existing budgeting systems and classifications; deployment of the MTEF process; leadership of the process; and linkages between the MTEF and national planning (Kasek & Webber, 2009, p. 40).

As introduction of the MTEF is not a simple task, therefore it needs proper preconditions. The IMF (Levy, 2008) suggests some preconditions that ought to be in place before the implementation of the MTEF, among others, are: (a) reliable macroeconomic projections, linked to fiscal targets in a stable economic environment; (b) a satisfactory budget classification and accurate and timely accounting; (c) technical capacity and disciplined policy decision-making, including budgetary discipline; and (d) political discipline for fiscal management. Furthermore, Kasek & Webber (2009, pp. 39-40) further recommend a number of practical considerations in deciding whether or not to undertake MTEF approach, being: integration with existing budgeting systems and classifications; deployment of the MTEF process; leadership of the process; and linkages between the MTEF and national planning.

In connection with implementation of the Performance-Based Budgeting and the Mid-Term Expenditure Framework (MTEF), it is also required to apply the integrated budgeting (*pengangguran terpadu*) system as the PBBS and the MTEF will not work well without applying integrated budgeting. In terms of budget structure, integrated budgeting is implemented by integrating the routine and the capital budgets as well as by applying the I-account format to replace T-account which was implemented during pre-reform era.

The findings indicate that the T-account suffers from a number of weaknesses.

The T-account format of the APBD was not able to provide clear, real, or valid financial information, particularly in controlling deficits and enhancing transparency. This is in line with the statement of Mardiasmo (2002) that the implementation of the integrated budgeting and I-account format is good for all stakeholders as they would know whether the projection of APBD performance is in deficit or surplus. This also boosts the local authorities to work hard in managing the local budget in order to meet with the APBD projections.

In the light of this issue, therefore, since the fiscal year 2001, the APBD was changed to the I-account format. The prototype of the I-account APBD structure has been displayed in Chapter Three of this thesis, while the APBD structure in the T-account format is briefly illustrated below:

Table 8.1. The Old Structure of APBD (Pre-Reform Period) in the T-account Format

Account Number	Local Government Revenue	Amount	Account Number	Local Government Expenditure	Amount
Routine Budget					
Routine Revenue			Routine Expenditure		
	Own-Source Revenue			Salary, subsidy, donation	
	Local tax			Retirement and veteran	
	Local Levy			Public Affairs	
			General Work	
	Transfer from central govt.			Public Health	
	Subsidy			Culture and Education	
	Financial Assistance			Deficit of previous year	
			Social Housing & labour	
	Remaining fund of	
	
Development Budget					
Development Revenue			Development Expenditure		
	Own-Source Revenue			Programs	
	
	Transfer from central govt.			Projects	
	
	Remaining fund of				
	T o t a l			T o t a l	

Source: *Makuda* (Manual of Local Government Finance)

The main purposes of integrating the budget, among others, are: (1) to avoid duplication in the allocation of funds (from either the capital or the operational budget); (2) to place each local government unit (SKPD) as the accounting entity in charge of managing institutional assets and finances; (3) to reduce the uncertainty of local financial management; (4) to promote responsibility of the local governments in managing the local budget; (5) to simplify the analysis, monitoring, and control of the management of the APBD; (6) to ease the calculation of the real surplus or deficit of the APBD within the current financial year; (7) to encourage transparency in the formulation and execution of the APBD; and (8) to ensure that every account of the local government budget is set up for specific transactions, and thereby duplication and overlapping in the recording of budget transactions can be avoided (Bastian, 2006; Halim, 2008; Mardiasmo, 2002). Unfortunately, after more than 10 years of the introduction of the new APBD format, the ideal objectives as mentioned above, have not been fully realized in the research areas.

Even though the process is still far from ideal, local officials from the study areas admit that the present situation is better than during the early days of the implementation of the new system. A number of essential constraints have been eliminated or significantly lessened. In view of such positive trends, local government officials expect the central government not to rush to introduce the new policy regulating the process of the APBD, as this would give them time to master the existing policy; otherwise they will have to learn the newer system, and may even possibly be trapped in further confusion.

8.2.3. Accrual-Based Accounting System

To support the application of performance-based budgeting, the Indonesian government bolsters local government units to apply the accrual-based accounting system instead of the cash basis because the accrual basis is able to provide better, accurate, and well-informed financial reports (Tudor and Mutiu, 1990, p. 8; Gianakis & McCue, 1999, p. 43). Before the implementation of the local autonomy policy, local government institutions in Indonesia applied the cash-based accounting system. In conjunction with the implementation of the local autonomy initiative, starting in 2001, the Indonesian authorities encouraged local units to apply the accrual basis accounting system instead of the cash-based system, because the cash-based accounting has disadvantages such as the income statement and balance sheet cannot display an overall picture of recent activity and conditions (Tudor and Mutiu, 1990, pp. 7-8).

In view of the change of accounting systems, the data exhibit that, in the 2005-2010 period, local governments in the study areas applied a transitional accounting system called the ‘cash basis toward accrual’ system⁸. This strategy is consistent with a tactic recommended by Diamond (2002, pp. 18-21) namely ‘from-cash-to-accrual’ transition. In this accounting system, local government entities applied a cash basis accounting system to record revenue, expenditure, and financing in the realisation report of the budget, while at the same time using accrual basis accounting to record assets, obligations, and equity on the balance sheet. The change of government accounting system from cash basis to accrual basis was undertaken gradually because this strategy eases the change process and reduces the resistance

⁸ The implementation of the transitional accounting system is based on PP (*Peraturan Pemerintah/ Government Regulation*) 24 of 2005 concerning the Standard of Government Accounting.

that may arise from stakeholders.

As PP (*Peraturan Pemerintah/ Government Regulation*) 71 of 2010⁹ stipulates, the Indonesian authorities have instructed the institutions of central and local government to fully apply the accrual basis accounting system by 2015 at the latest. This means that local governments - since the issuance of PP 71/2010 - have a transition time of five years to implement the policy.

In anticipating this requirement, during the five year period, the local governments in the study locations have arranged the timelines as follows: in 2010, local government develops a framework for the accrual basis accounting system. Local governments also conduct dissemination of the policy to all government staff. In 2011, local governments prepare the code of conduct and technical guidance for the accrual system policy. Moreover, local governments also expand the IT-based accounting system. Along with this process, the local authorities develop the human resources capacity.

In the following year, the main agenda is basically the continuation of the expanding of the IT-based accounting system and development of the human resource capacity. In 2013, the local authorities set up a number of selected local government units to act as the pilot project for the implementation of the accrual basis accounting system. Additionally, local elites review, evaluate, and perfect the proposed system. To support this process, local governments also continue to develop the human resource capacity. Furthermore, in 2014, all local government bodies are expected to start implementing the accrual basis accounting system. Along with this process, the

⁹ PP (*Peraturan Pemerintah/Government Regulation*) 71 of 2010 on Government Accounting System is a formal regulation which requires and guides government agencies in applying the accounting system. This PP replaced the old law which was PP 24 of 2005 regarding the Standard of Government Accounting.

activity of review, evaluation, and perfection, and the ongoing development of the human resource capacity will be continued in this year. Finally, all local government institutions should apply the full version of the accrual basis accounting system in 2015. Starting in this financial year, all government entities are not permitted to apply the method of 'cash basis toward accrual' anymore. In the light of this, local governments also undertake sustainable development of their human resource capacity, aiming to support the implementation of the policy.

The transition elaborated above is similar to the suggestion of Diamond (2002, pp. 18-21) recommending the transitional strategy 'from-cash-to-accrual' which consists of steps as follows: stage one, get cash accounting to work well; stage two, integrate operating accounts and financial asset and liability accounts to move to modified accrual; stage three, introduce more elements of accrual recording and move to a partial accrual presentation in ex-post reporting; stage four, recognize nonfinancial assets as the final stage for accrual accounting; and stage five, move from accrual accounting to accrual accounting and budgeting.

The national officials affirm that if the accrual accounting system is implemented perfectly, it will bring significant advantages to the management of local government finances. It is because by adopting the accrual system, as Tudor & Mutiu (1990) claim, the actual costs of development and public service as well as the real amount of local government income can be accurately calculated. Therefore, it will help local government officers to analyse the efficiency and effectiveness of local government financial management. The accrual system also significantly contributes to improve the quality of financial report and evaluation, hence it will be easier to measure and evaluate the financial performance of institutions (Diamond,

2002). Other than this, as normative guidance stipulates, the implementation of the accrual accounting system is crucial as the system of PBB (Performance Based Budgeting) and MTEF (Mid-Term Expenditure Framework) cannot work properly if it is not accompanied by the application of the accrual-based accounting system.

In respect of implementing the accrual basis accounting system, local bodies in the study locations have experienced some problems, particularly in association with the IT-based accounting system. Ideally, this system requires information technology support to produce the best results. Nevertheless, not all local bodies have had support for the IT-based accounting system. The data show that local government units located in urban areas, such as Surabaya City, have not had many problems in applying the IT-based system. On the contrary, some of the local bodies in the sub-urban and rural areas, such as in Batu City and the Trenggalek Regency, generally still struggle to implement the computer-based accounting system because the number of local staff members who comprehend the IT-based accounting system is very limited. This circumstance confirms the argument of Barton (1999) and Mellett (2002) that implementation of the accrual accounting requires complex system and technology which brings consequence where governments frequently lack of capable personnel who are able to manage this accounting system. As well, adoption of accrual accounting in some public sectors has caused confusing financial statements (Barton, 1999; Mellett, 2002) and lead to the roles of managerial and political in governmental environment become vague (Liguori et al., 2009).

According to Ezzamel et al. (2005), operation of accrual accounting is not simple and costly; therefore the costs to implement accrual-based accounting may reduce the advantages of this method itself (Jones & Puglisi, 1997). This contention is

in line with the fact found in the fields whereby implementation of the accrual system has increased the burden on local governments to provide financial reports. Under the previous system (cash accounting), local governments had to prepare only four reports, however the accrual method currently applied requires local officials to create seven financial reports¹⁰. The informants state that this change does not only impact on the government accounting system but also increases the budget allocated for creating these reports. Consequently, local officials need more time to complete the reports. Also, this may prolong the entire APBD budgeting process.

Furthermore, local government elites do not appear to wholeheartedly support the change of system as the majority of them do not understand the technical aspects of the accrual basis and IT-based accounting system. This condition also often triggers resistance to system change from local staff members as they already feel familiar and comfortable with the old system. Nevertheless, the officials in Batu City and Trenggalek Regency declare that they are optimistic about dealing with the problem and confident that they will be able to comprehensively implement the accrual-based accounting system by 2015.

8.3. The Budgeting Process: Managerial or Political?

Budgeting is essentially a process aimed at maximizing the benefits of public spending that is funded through available resources (Ljungman, 2009, p. 3). In general, there are two perspectives on budgeting (Alexander, 1999). The first viewpoint expresses budgeting as a technical exercise (Gianakis & McCue, 1999;

¹⁰ Under PP 24/2005 regarding government accounting, every year local governments must provide four financial reports include a budget realisation report, financial balance, cash flow report, and notes of financial statements. Nonetheless, as stipulated in PP 71 of 2010 that replaced PP 24/2005, every financial year local officials should create seven financial reports including a budget realisation report, report of the changes to the rest of budget, financial balance, report of operations, report of equity changes, cash flow report, and notes of financial statements.

Evans & Wamsley, 1995) and also an instrument for allocation, reallocation, redistribution, and an accountability mechanism (Fubb, 1999), while the second angle stresses the political influence on the budgetary process (Wildavsky, 1964; Agrawal, et al., 1999; Unger, 1987). This section analyses the nature of the budgeting process at the local government level to clarify whether it is a managerial or political event.

As explained in the previous chapters, the present budgeting system at the local level encourages local members of parliament to get involved in almost every substantial phase of the APBD process. This strategy intends to give local legislators a greater chance to propose initiatives to be accommodated into the APBD. This is also intended to avoid prolonged debate in the APBD validation process as local legislators have been involved since the early stages of the process. More importantly, this aims to minimise political bias in the budgeting process, therefore the budget can be managed rationally and professionally. Additionally, to position the APBD budgeting process as a rational and technocratic process, the central government has issued comprehensive guidelines to assist local governments in executing the complicated APBD procedures.

The reality seen in the study areas confirms that local legislators seem not quite enthusiastic about maximising their role in the APBD formulation process. They also tend to be more passive in the various events in the APBD formulation and surrender to the local executives. The local legislators behave so because they mostly lack skill and knowledge about the details of the complex budgeting process. On the other hand, most local government officials are also still struggling to apply the new regulations and guidelines issued by the central government. This is because the central government has frequently changed many regulations in a relatively short

space of time. Moreover, those regulations often overlap or do not complement each other.

As guided by the formal guidelines, the APBD must accommodate only programmes and activities proposed through the *Musrenbang* (Discussion of Development Planning). However, due to political intervention, it has frequently been found that ‘new projects’ have been included in the APBD, not through the proper procedural channels, as such projects were not proposed by any of the *Musrenbang* participants. The projects listed through the non-procedural way are generally proposed by powerful parties such as political party elites, legislators, NGO activists, financiers, and other pressure groups. This political brokering practice stimulates the emergence of an illegal category of projects known as *proyek titipan* (by-order projects) and *proyek fiktif* (fictitious projects).

Budgeting is inherently political rather than rational, and politics will always win, thus the objective to prioritise rational expenditure is largely an illusion. In this context, politics and rationality are highly antithetical (Robinson & Brumby, 2005, pp. 15-16). This point of view conforms to the reality discovered in the field. The facts denote that intervention from powerful parties in the process of project procurement and execution often results in prolonged debate and negotiation between the local executives and legislators. To hasten the deal with legislators, local officials often apply a strategy of giving special funds allocated to parliamentary members in the form of a discretion fund, *Dana Hibah* (grants), *Bantuan Sosial* (social assistance), *Dana Aspirasi* (aspiration fund), or other project funds which can be utilised under the full discretion of local legislators. This political nuance strongly influences the process of budgeting and defeats the rational process of the APBD.

Political conflict between the local government officials and the local parliament members is one of the prominent distortions in the APBD budgeting process. The legislator-executive conflicts appear because the local officials and legislators scramble the 'APBD cake'. They also have a different orientation in utilising the APBD funds. In this case, the local executives claim that they intend to ensure that every programme funded by the APBD fits in with the strategic planning of local government. On the other hand, the DPRD members require every programme to meet with the preferences of the community (their constituents). However, in fact the conflict is actually due to individual interest, in which each of the local officials and legislators seems to prioritise their own intention to gain personal benefit, either in tangible or intangible form. This reality leads to a situation as described by Wildavsky (1964) whereby resource allocation cannot be decided rationally because of budgetary politics. Further, the characterization of the politics of budgeting is often simplified as "who gets what, when and how" (Unger, 1987, p. 145).

As typically happens in political institutions, rivalry among factions appears to be a common phenomenon. Nevertheless, the facts disclosed in the local parliaments in the field show a unique and different tendency. Local legislators tend to treat their colleagues, both from the same and other political parties, as mutual partners. They are inclined to avoid rivalry and political conflict among the factions. They build collegial relationships not only with peers from the same political party, but also with those representing other parties. They apply this strategy to strengthen their political position once they confront the local executives in the budget sessions.

The study indicates that most practical budgeting stages take place in a grey

area between politics and rationality. Every formal phase of the APBD validation process operates as guided by laws and regulations. Nonetheless, in fact, these events appear to be only a formality. The real process of APBD validation is primarily conducted 'behind' the formal sessions through various political compromises and bargaining processes. The political compromises on the budgeting process frequently lead to hidden conspiracies to misuse the public budget, aiming to use it for the interests of the local elites and their cronies instead of the public interest. As indicated in the study sites, various issues mentioned earlier have caused delays in local development execution, thus the time available to execute local development projects is very limited. Furthermore, this circumstance leads to unutilized funds and a high number of unfinished development projects. The phenomena above are consistent with finding of Seymour & Turner (2002, pp. 40-44) that local autonomy in Indonesia faces numerous challenges including: (1) inappropriate levels of autonomy; (2) no improvement in the real fiscal autonomy; (3) lack of finance; (4) the central government treats local governments unequally; (5) 'grey areas' in central-local government control; and (6) issues with human resource capabilities.

All in all, it can be concluded that APBD is not managed in an ideal manner through a rational and technocratic process. Conversely, the APBD is mostly trapped in the political conspiracy designed by local legislators, local executives, interest groups and other political powers. In consequence, the local budget seems to fail to optimally contribute to improving the local community livelihoods. This is largely due to a disjuncture between formal and legal democracy, which presupposes a rational bureaucracy, and the politicised nature of government (Schick, 1978; Wildavsky, 1964). Consequently, most efforts to make public budgeting better as a

technical and managerial instrument have failed to meet expectations (Timney, 1995).

8.4. Bottom-Up vs Top-Down Approach to Budgeting

One of the most fundamental points in the budget formulation is how the budget is formulated: whether through a top-down or a bottom-up approach. According to Ljungman (2009, p. 4), a top-down budget process means that a binding decision on budget aggregates is taken *before* allocating expenditure in detail. On the other hand, a *bottom-up* approach indicates that total expenditure is determined residually in a process of discussing and establishing the details of the budget, whereby there is no point of reference in terms of an expenditure limit for each sector. Another crucial point of the bottom-up method is that input from the public is seriously considered in the budgetary process.

The Indonesian government promotes the view that government units should apply bottom-up and participatory approaches in managing public budgets. It is because, as Çağatay et al, (2000) assert, applying a participatory approach may encourage people-centered development and may also meet the stated needs of the citizenry. The main way to implement this approach is by conducting a participatory forum called the *Musrenbang*. This section examines whether the bottom-up budgeting approach is successfully applied through the *Musrenbang* or whether the APBD continues to be managed under the top-down process.

The *Musrenbang* is a citizens' forum aiming to collect aspirations from the local people about desired developments and activities proposed to be financed by APBD funds. The *Musrenbang* takes place in five stages namely: (a) *Musrenbang Desa/ Kelurahan* (*Musrenbang* at the village level); (b) *Musrenbang Kecamatan*

(*Musrenbang* at the Sub-regency level); (c) *Forum SKPD* (Joint Forum of the local bodies/SKPD); (d) *Musrenbang Kabupaten/Kota* (*Musrenbang* at the Regency/ City level); and (e) *Pasca Musrenbang Kabupaten/Kota* (Post-Regency/City-level *Musrenbang*). Details of each stage of the *Musrenbang* are elaborated below:

Table 8.2. Details of *Musrenbang*

Name/Level of Musrenbang	Timing	Organiser	Participants	Main Agenda
<i>Musrenbang</i> at the Village Level	Week three of January	a committee set up by head of the village government	elites from village government, local figures, and representatives of professional and interest groups	discussing the proposals and priorities for development activities that will be proposed at the Sub-Regency-Level
<i>Musrenbang</i> at the Sub-regency level	Beginning of February	a committee established by the head of the sub-regency (<i>Camat</i>)	the head and officials of the sub-regency (<i>Kecamatan</i>) government, the heads and officials of the village government, representatives of the local community, local NGOs, and others	to discuss the proposals put forward by the villages (the results of the village-level <i>Musrenbang</i>) and to set the development activities proposed to the higher level <i>Musrenbang</i> called the SKPD Forum (the Joint Forum of Local Bodies/ SKPD)
Joint Forum of local bodies/ SKPD	Mid-February	a team established by the head of BAPPEDA	The heads and officials of Bappeda, local bodies (SKPD), <i>Kecamatan</i> , and other invited parties	to synchronise the development priorities put forward through the sub-regency <i>Musrenbang</i> and the draft of the local bodies work plan (<i>Renja-SKPD/ Rencana Kerja Satuan Kerja Pemerintah Daerah</i>) set up earlier by the local bodies themselves
<i>Musrenbang</i> at the Regency/ City level	March	a committee set up by the head of BAPPEDA	key officials of local government and local agencies (SKPD) and delegations of sub-regency <i>Musrenbang</i> and the SKPD Forum	to collect inputs from all stakeholders of local development, so that local government has reliable information to improve the initial draft of the RKPD (<i>Rencana Kerja Pemerintah Daerah/ Work Plan of Local Government</i>) as well as to create the initial draft of the Budget and Work Plan of Local Bodies (RKA-SKPD/ <i>Rencana Kerja dan Anggaran Satuan Kerja Pemerintah Daerah</i>)
Post-Regency/City-level <i>Musrenbang</i>	April	a committee set up by the head of BAPPEDA	delegations from the regency/ city-level <i>Musrenbang</i> and also key officials of local government bodies	a final draft of the RKPD and the policy direction, strategy, and margins of the APBD (annual local budget)

Source: guidelines of *Musrenbang* jointly issued by the *Bappenas* Chief and Minister of Home Affairs number 0008/M.PPN/01 - 050/264A/SJ of 2007 and primary data

The government policy to promote a bottom-up budgeting system contradicts the views of a number of scholars who declare that the top-down approach is more beneficial than the bottom-up system (Ljungman, 2009; Hagen, 1992; Ehrhart et al., 2006). Even though most scholars tend to recommend the application of the top-down approach in formulating budgets, Indonesian authorities insist on applying a bottom-up and participatory budgeting which is implemented through the *Musrenbang*. Indonesia prefers to do so because they want to reduce the stigma of centralistic and authoritarian governments attached to the administration of the *Orde Baru* regime. They also believe that this system can link public demands with development projects and programmes set up by governments, therefore those projects and programmes will adequately meet the public needs and interests. This intention is consistent with the statement of Beal (2005) contending that participatory approach in the budgeting process intends to achieve three objectives. The first is administrative, where the participatory budget is seen as a way of improving the efficiency of public administration; the second is social, where it is expected that the participatory budget would invert investment priorities; and the third is political, where the goal of the participatory budget is to democratise development process.

Moreover, Berner (2001) mentions at least two main purposes of involving the public in decision-making processes: (1) to inform the public of government decisions; and (2) to involve the public in government decision-making. In addition, citizen input is generally viewed as a way to reduce the level of citizen distrust in government, and to educate people about government activities (Berman 1997, cited in Ebdon & Franklin 2004).

The facts show that participatory forums of *Musrenbangs* are implemented regularly and on a timely basis as stipulated in the formal guidelines. The *Musrenbang* can be accessed by all people regardless of their socioeconomic status. Furthermore, the *Musrenbang* provides a great chance to accommodate the community's interests as all programmes and projects which are intended to be funded by the APBD should be proposed through the *Musrenbang*. Nevertheless, the implementation of the *Musrenbang* still experiences a number of problems, some of which are clarified below.

8.4.1. Lack of Education and Knowledge leads to passive participants

The existing situation shows that many of the residents involved in the *Musrenbang*, particularly those in the rural areas, have low levels of education and generally have limited knowledge about the budgeting system of the APBD, hence, they do not really comprehend the material discussed at the forum. Even the participants living in urban areas, such as in Surabaya City, who have better knowledge and higher levels of education, also often struggle to comprehensively understand the material debated at the *Musrenbang*. This happens because the budgeting system of the APBD is very complicated and involves many complex technical terms. Also, local officials do not disseminate in advance the material to be discussed at the *Musrenbang*, because of very limited time. Due to this circumstance, the majority of local people attending the *Musrenbang* cannot make a significant contribution and tend only to be passive participants.

As found in the sites, the lack of education and knowledge of the people participating at budgeting forum commonly leads to only passive participation.

Public participation is made difficult by constraints such as lack of time, citizen apathy, and public perceptions that their opinions are unwanted. Also, the attendances at public meetings are often low and may not represent the whole community, as well as the participants having insufficient understanding for effective input. This fact conforms the claim of Yao (2006, p.19) that public meeting to discuss planning process often contains significant scientific, technical and legal information; nevertheless residents mostly do not have sufficient technical knowledge, so that it can be difficult for the average citizen to understand. Moreover, residents are perceived as unenthusiastic and have poor knowledge, skills, and time for public participation; therefore citizen must have expertise if they intend to get directly involved at the planning process (Callahan, 2007).

8.4.2. Time Constraints and Apathy of the Local Community

As seen in the study locations, the participatory forum which directly involves local residents is the village-level *Musrenbang*. This event is primarily conducted through public hearings that usually take place on weekdays between 10.00 a.m. to 1.00 p.m. Members of the local community often complain as they are generally busy working at these times. For economic reasons, people have to work harder and smarter to fulfill or increase their living standards. Residents think that it is not worth spending their time attending these meetings because, for the rural community, this means leaving their farming activities; and for people living in urban areas, they generally struggle to get permission from their workplace to attend the *Musrenbang*.

Due to the complaints about the timing of the *Musrenbang*, local officials in some rural areas occasionally conduct village-level *Musrenbang* in the evening

because people usually have free time at this time of day. However, this strategy does not work well either. Thus the public has little opportunity to influence results. According to Hetifah (2007), some technical problems in accessing citizen participation also contribute to more restricted official channels for citizen participation. As the leading actor in promoting citizen participation, the government apparatus often lacks the capacity to do so effectively.

The enthusiasm of the local community to take part in the *Musrenbang* remains low because communities are reluctant to spend their time at the *Musrenbang*, as they doubt whether their proposals would be seriously followed up. They are also pessimistic that the *Musrenbang* will significantly impact on their life. This fact is in line with the concern of Frisby & Bowman (1996) warning that participation is possibly hampered by a lack of knowledge, citizen apathy, lack of time, and also public perceptions that their opinions are unwanted. Local officials, on the other hand, are not overly worried about this phenomenon because a number of notable people and leaders of the local community consistently attend the *Musrenbang*. Therefore, local government authorities argue that local people are represented by the attendance of these local elites.

However the representativeness of public in this circumstance is still debatable as these groups may not represent whole public (Dola & Mijan, 2006). Yao (2006) points out that even though many interest groups claim as the representative of residents; nonetheless in practice the public is generally not satisfactorily represented. This point is supported by Eccleston (2000) contending that one of the primary barriers of public engagement is the matter of representativeness because the representations attending the meeting are usually more educated and

sophisticated than the common public and in fact they tend to prioritise their own interests. As well, Berman (1997); Schooley (2008); and Yang & Callahan (2007) declare that people who participate at citizen forums are often critiqued for their self-interest and lack of commitment for the greater society. This atmosphere could lead to three implications: first, the public is always satisfied and believed in the proposal; second, the public do not feel that participation is necessary and third, they do not understand the plan and do not know their rights (Dola & Mijan, 2006)

8.4.3. Elitist Representation and Mobilisation, Instead of Genuine Participation

Even though all local residents have an equal opportunity to participate in the *Musrenbang*, nonetheless, the participants attending the village-level *Musrenbang* are mostly the elites of the local community. This happens because the invitation to attend *Musrenbang* does not get circulated thoroughly, but is only addressed to certain local public figures and elites. As most participants are local elites, they tend to propose programmes and projects that suit their interests and may provide advantages for themselves. Consequently, the interests of people with low socioeconomic status tend to be ignored. This tendency can be seen in the empowerment programs and projects funded through the APBD in the local governments of the study areas, which are often not targeted at less fortunate people.

Additionally, some *Musrenbang* participants seem to get paid for their attendance at the *Musrenbang*. In the light of this, local officials clarify that local governments do not intend to pay the *Musrenbang* participants, however they do provide transport fees amounting to around thirty thousand to fifty thousand Rupiah as participants have to travel long distances to get to the *Musrenbang* venue. Some

participants quite frankly admit that their attendance at the *Musrenbang* is not for the purpose of actively participating by contributing constructive ideas, but instead, to get the fee from the *Musrenbang* committee. Further, they state that they would possibly not attend the *Musrenbang* if there was no fee for their attendance.

This condition leads to criticism from non-government parties, contending that the *Musrenbang* is basically a kind of mobilisation rather than a participatory budgeting forum. The local authorities do 'pay' participants apparently to ensure that local people attend the *Musrenbang*, as local officials will be judged to have failed if the *Musrenbang* has a few local attendance. Even though the majority of local officials reject this accusation, some *Bappeda* staff members admit that they implement the *Musrenbang* for 'just doing obligations' (*menggugurkan kewajiban*) stipulated by the laws, so that they look as if they are appropriately delivering on their duty to implement the rules.

Public administrators play strategic role to articulate and facilitate public interests to be accommodated in the policy agenda (Frederickson, 1982). In view of this, capable public administrators are required to encourage and manage effective public engagement (Callahan, 2007). However, as also seen in the research areas, officials often lack expertise and capability to execute these tasks, hence they seem failed to develop effective and successful public participation (King et al., 1998; Yang & Callahan, 2007).

8.4.4. Formalistic and Top-Down Planning and Budgeting

The study finds that the *Musrenbang* is always initiated and facilitated by local government officials. The operation of the *Musrenbang* is very formal and is

held at limited times. As such local people do not feel free to express their ideas and proposals. Moreover, the draft of the programmes and projects proposed by village governments have often been previously arranged by village government elites, therefore the (village-level) *Musrenbang* is apparently held only to formalise proposals created by village government elites.

The local officials claim that they are not happy about involving too many parties, particularly local people, in formulating the development plan because this is both time- and money-consuming as a wide range of ideas has to be accommodated. As seen in the study sites, the development programmes and projects commonly have already been created at an earlier time -- when the local authorities create the RKPD (*Rencana Kerja Pemerintah Daerah/ Work Plan of Local Government*) -- which is undertaken before the *Musrenbang*. Therefore, the *Musrenbang* is basically a formalistic event.

In most public hearings, the materials and results of the meeting have been constructed earlier. Besides, there is no warranty that the public's voice will be seriously considered as (Denhardt & Glaser, 1999). The local budgeting process, which is dominated by the budget authorities, leads to a tendency for top-down budgeting because it tends to prioritise initiatives coming from government institutions instead of prioritising input from the community. As well, nobody can guarantee that the input or the proposals from the public will be accommodated and then financed through APBD funds. The local residents also seem, almost always, to struggle to monitor whether or not their proposals have actually been accommodated.

The data show that in the final phase of APBD formulation, proposals from local people often get eliminated because these are over-ridden by programmes and

projects proposed by local government units (SKPD). For example, in the 2011 *Musrenbang*, the fishermen community of Trenggalek regency put forward a proposal for cold storage as they need to store their fish so that they last longer in a fresh condition, without worrying about them rotting. Nevertheless, the local authorities preferred to finance road maintenance in these areas as they argue that this project had already been set up in the annual work plan of local government (RKPD). A similar tendency is also found in Batu City. On many occasions, for instance, the farming community put forward proposals for financial and technical assistance to rejuvenate their apple trees, as many of them are old and no longer productive. However, the local authorities generally prefer to finance infrastructure development and maintenance such as roads, bridges, drainage, irrigation channels, and other such projects. The *Bappeda* officials confirm this tendency, as these types of developments have been previously set up by the municipality officials in the RKPD.

Local officials argue that it is not efficient to involve residents in every stage of planning process as allocated time is very limited. This phenomenon is in line with contentions of some scholars contending that public participation is stigmatized as mostly time consuming, costly, and generally inefficient (Doelle & Sinclair, 2006; Dola & Mijan (2006). Magnusson (2003, p.229) and Dietz & Stern (2008, p.3) also argue that public participation might not provide any positive effects that justify extra cost. Further, Charnley & Engelbert (2005, p.170) emphasise that direct involvement of people in the planning process might increase conflict between public and government institutions. Other than that, public participation may reduce efficiency and contradicts the idea of representative democracy (Berman, 1997; Schooley, 2008; Yang & Callahan, 2007). Direct participation is also seen pointless. It is therefore

strongly insisted to completely ignore common people from any arena of policy making process (Rohr & Chandler, 1984; Stivers, 1990).

8.4.5. Improper placement of the *Musrenbang* stage in the APBD formulation process?

As previously mentioned, the execution of the *Musrenbang* in the field is performed on a timely basis as stipulated in the guidelines. Every year, local governments conduct *Musrenbang* at the village level starting in mid-January, which is finalised by the post-regency/city-level *Musrenbang* held in April. However, the timely process of running the *Musrenbang* is often not very useful to accommodate the aspirations of local residents, because once a *Musrenbang* is being conducted, at the same time, local governments have already created the work plan which has been formalised earlier through the RKPD (Work Plan of Local Government) and the *Renstra*-SKPD (Strategic Plan of the SKPD).

As stated in the formal guidelines, when formulating programmes and projects, local authorities have to refer to the existing RKPD and *Renstra* - SKPD. Furthermore, local officials are not allowed to make programmes and projects which are not in line with the RKPD and *Renstra* - SKPD set up earlier. This provision is frequently used by local officials to reject proposals put forward by local people in the *Musrenbang*, by using the excuse that these proposals are not considered to be in line with the RKPD. Most *Musrenbang* participants are already familiar with the rejection of their proposals due to reasons of incompatibility with existing work plans (RKPD). In fact, local officials often behave unfairly in selecting project proposals. Evidently, even though they repeatedly reject proposals from the local community, those bureaucrats mostly accommodate programmes and projects proposed or

initiated by the local officials themselves.

In this connection, local officials argue that they prefer to do so (rejecting proposals from the community but accommodating their own proposals) because they are bound by the regulations stipulating that local officials are only allowed to accommodate programmes and projects which are in line with the RKPD and the *Renstra* - SKPD. This means that they are authorised to reject any initiatives (proposed by local people through the *Musrenbang*) which are considered to be inconsistent with the RKPD and/or the RENSTRA-SKPD. Additionally, local officials clarify that the rejection of residents' proposals (due to incompatibility with the RKPD) is not because of any intention to ignore the aspirations of local residents, but only because they want to comply with the rules.

Based on this fact, it can therefore be concluded that the execution of the *Musrenbang* is timely in terms of stipulation, but it is improperly placed in the stages of the APBD formulation process, because, before the *Musrenbang* being run, local governments have already created a work plan and a strategic plan (RKPD and *Renstra* - SKPD) that have to be referred to in formulating local programmes and projects. As a result, the aspirations of, and proposals by, the local community often cannot be accommodated because these are mostly inconsistent with the RKPD and the *Renstra* - SKPD formalised earlier.

As often occurs, public hearings usually take place late in the process, thus the public has little opportunity to influence the results (Berner, 2001). To anticipate this situation, Ebdon & Franklin (2004) advise government officers to gather input earlier in the hearing process. Ideally, the *Musrenbang* should be run before the finalisation of the RKPD and the RENSTRA-SKPD, thereby being able to capture the aspirations

of the community so that they can be optimally accommodated. In addition, the *Musrenbang* is held only during the formulation stage of the budgeting process. Therefore, local people are only involved at the early stage of the APBD budgeting process. As a result, public participation is absent during the other stages, particularly at the validation, execution, and supervision and accountability phases of the APBD.

Hetifah (2007) have determined some requirements to make bottom-up and participatory budgeting work ideally. Those requirements, among others, are small population, well educated people, a low-activity and non-busy community, and a homogeneous society. Unfortunately these assumptions are absent in Indonesia. Indonesia deals with a huge population, which leads to complex activities and heterogeneities. Also, there are high numbers of un-educated and unemployed people, who have to work harder for their living. Thus, they do not have plenty of time and adequate capacity to participate in policy making processes.

The issues and challenges elaborated above do not only occur in the study locations; these are common at the local government level across Indonesia. As reported in the mass media, the *Musrenbang* was found to be ineffective in the City of Padang (Harian Haluan¹¹), Pandeglang (Radar Nusantara¹²), Banten Province (Banten Pos¹³), Sintang (Antara News¹⁴), Bandung Regency (Inilah Koran¹⁵), North

¹¹ Harian Haluan, 27 December 2010, http://www.harianhaluan.com/index.php?option=com_content&view=article&id=74%3Amusrenbang-dinilai-tak-penting-lagi&Itemid=89

¹² Radar Nusantara, 14 February 2012, <http://www.radarnusantara.com/2012/02/h-aan-awaludin-kades-sukamanah.html>

¹³ Banten Pos, 30 April 2013, <http://www.bantenposnews.com/berita-991-musrenbang-harus-jadi-solusi.html#.UwukXawr18E>

¹⁴ Antara News, 23 July 2010, <http://www.antaraneews.com/berita/212989/musrenbang-yang-beriharapan-kosong>

¹⁵ Inilah Koran, 25 February 2014, <http://www.inilahkoran.com/read/detail/1950550/musrenbang-kabupaten-bandung-tidak-efektif>

Sumatra (Medan Bisnis¹⁶), Capital Special Territory of Jakarta (Jurnal Nasional¹⁷), and other local government areas.

To optimise the benefits and to minimise the distortions of public participation events, Ebdon & Franklin (2004) suggest several precondition the encouragement of public participation, such as: (a) input is representative of the community; (b) opportunity is available for large numbers of citizens to participate; (c) input occurs early in the process; (d) sincere preference/ willingness to pay is revealed; (e) participation includes two-way communication between the public and city officials; and (f) input is considered in decisions.

8.5. Local Financial Management under the Current Policy

Fiscal decentralisation could lead to positive and negative impacts on financial management at the central and local governments (Liu, 2007, pp. 11-17). Positive impacts on fiscal decentralisation, among others, are improvements in economic efficiency (Oates, 1972); development of economic performance through strengthening governance (Inman & Rubinfeld, 1997); and promotion of economic performance by enhancing macroeconomic stability (Fukasaku & DeMello, 1998). On the other side, a government may suffer from disadvantageous impacts from fiscal decentralisation, due to inhibition of economic performance (Prud'homme, 1995), conflict between fiscal decentralisation and macroeconomic policy (Musgrave, 1959), as well as national-local government policy conflict. This may lead to a national debt crisis as fiscal decentralisation provides a strong incentive for sub-

¹⁶ Medan Bisnis, 06 April 2012, http://www.medanbisnisdaily.com/news/arsip/read/2012/04/06/75375/musrenbang_kawasan_mp3ei_tidak_efektif/#.UwxZW6wr18E

¹⁷ Jurnal Nasional, 29 November 2013, <http://demo.jurnas.com/halaman/32/2013-11-29/276481>

national governments to make loans (Prud'homme, 1995). This section examines whether the local governments in Indonesia have enjoyed the benefits of the current fiscal decentralisation policy, or, conversely, whether they are suffering from the obstacles of this policy.

Indonesia has been consistently developing the implementation of the fiscal decentralisation policy since the governance reforms in 2000. This policy was later followed up by the budgeting reforms at both central and local government levels. Indonesian authorities have undertaken these policies because they believe, as stated in some laws and regulations¹⁸, that fiscal decentralisation and budgetary reform can be greatly beneficial in improving financial management and accountability, promoting the efficiency and effectiveness of resource allocation, improving the internal operation of the governmental institutions, and developing budget deliberation processes.

Indonesia's budgeting reform is not only intended to modify the budget structure, but also to change the budgeting process. As found in the study sites, crucial steps in the APBD budgeting process have been changed to make the process more efficient and effective. These changes also aim to equalise the role of local government, local parliament (DPRD), and the society as a whole in the APBD budgeting process. Local governments have adopted some new budgeting approaches such as the Performance-Based Budgeting System (PBBS), integrated budgeting, the Medium-Term Expenditure Framework (MTEF), and accrual-based accounting to convert the traditional and unintegrated budgeting system, annual expenditure

¹⁸ This stipulation can be found at Law 17 of 2003 concerning Public Finance, Law 32 of 2004 about Local Government, Law 33 of 2004 regarding Financial Balance between the Central and Local Governments, Law 58 of 2005 on Management of Local Government Finance, *Permendagri* 13 of 2006 concerning Guidelines of Local Government Financial Management, and other regulations.

framework, and cash-based accounting system. Moreover, the process and management of local budgets are currently showing the potential to improve transparency, public participation, and accountability.

Nevertheless, the linkage between reform and changing budgetary outcomes is uncertain (Rubin, 1993). Several empirical studies have shown that rational budget reforms do not improve resource allocation in governmental agencies and/or development projects and programmes (Connelly & Tompkins, 1989; Harkin, 1982; Joyce, 1996; Lauth, 1985; Schick, 1978). As the study has found, local financial management and budget reform are still far away from the expected level. Efforts to equalise the roles of related parties in the budgetary events are apparently unsuccessful. The facts show that local executives remain highly dominant in the budgeting process; while the local legislators – who are granted high political authority – find it difficult to maximise their roles due to lack of competence and knowledge. Also, the legislators are presumed to lack commitment in actualising the public interest as they often only prioritise their own interests.

Despite their dominant role, local government officials habitually struggle to maintain data validity and to sustain coordination and synchronisation among local institutions. They are also unable to accurately link the master plan of development with budgeting aspects. As well, the development projects and programmes usually do not meet the community needs, as those are mostly created based on the preferences of local government elites instead of those of the community. Consequently, local people cannot obtain the optimal benefits of local development. Development projects and programmes often overlap with each other. This is simply because the governance reform was not well prepared and was often illustrated as a

'big bang' transformation (Hofman & Kaiser, 2002; Bennet, 2010). In addition to this, fiscal decentralisation and budgeting reform in Indonesia has not been done perfectly because of a chronic problem in the form of sectoral egoism and lack of connection between planning and budgeting (Dendi & Roesman, 2005).

As discovered in the field, the APBD budgetary process cannot be rationally managed and carried out in a timely fashion due to political conflicts or disagreements between the local government and the parliamentary authorities. This reality is aggravated by the lack of capability and skill of the local officers, who commonly face such difficulties in implementing a large number of new rules issued as an integral part of budgetary reform. In addition, fiscal decentralisation policy, which grants a great discretion to the local officials to independently manage local finance, has not significantly contributed to the growth of local revenue. Data show that the volume of the collected PAD (own-source revenue) remains low. Consequently, local governments mostly rely on funds transferred from the central government. This is due to several factors, including the poor design of the PAD collection; the lack of reliable data; inadequate training for, and the irrelevant qualifications of, local finance officers; and the disincentive policy inherent in the DAU (General Allocation Fund). Furthermore, the centralised nature of tax assignment also considerably hampers the optimisation of PAD accumulation as potential sources of revenue are mainly collected by the central government. This reality fits to the findings of a study conducted by Smoke & Lewis (1996) that the problems of decentralisation found in Indonesia include: (a) lack of coordination among central government agencies; (b) central-local government conflicts; (c) poor government performance incentives; and (d) counterproductive donor organization

behaviours.

Fiscal decentralisation and budgeting reform also have not shown constructive impacts on the project procurement and execution system. In respect of the project procurement system, particularly in selecting a project executor, local officials prefer to conduct either a direct appointment or a simple auction instead of an open tender. They favour these methods because manipulation and collusion with potential contractors can be easily carried out. In this case, to avoid the obligation for an open tender, local officials apply a strategy of splitting projects, hence the value of each project becomes small and eligible for not being openly tendered.

Various unlawful practices to abuse APBD funds constantly arise because internal controls and audit systems in Indonesia work quite poorly. This leads to pervasive corruption, inefficient cash management, and collusive actions (Yilmaz, et al., 2010, p. 283). Even though the quality of APBD supervision is currently better compared to the pre-reform era, except for the KPK (Corruption Eradication Commission), the existing supervisory agencies are unable to optimize their roles in supervising the APBD management. This is due largely to problems which include (1) the lack of capacity of the human resources; (2) political powerlessness of supervisory officers; (3) vagueness and overlapping of authority; and (4) involvement of the supervisory officers in illegitimate actions and rent-seeking practices organised together with executive officials.

Furthermore, law enforcement in the study areas, except for that conducted by the KPK, generally reflects the stigma of 'sharp downward yet blunt upward'. Also, law enforcement activities lead to a phenomenon of the 'ATM machine', as labelled by the local government officials, in which the bureaucrats must provide large

amounts of money for auditors and law enforcement officers to maintain ‘good relationships’ between them. If they do not offer money for the officers, then the auditors will apply stricter procedures in auditing the local officials. Consequently, once the officials make any mistakes in managing the local budget, they will be seriously investigated and then reported to the law enforcement units. The suspected staff, therefore, might face legal prosecution.

Along with the implementation of fiscal decentralisation and budgeting reform, Indonesia has issued numerous policies to guide the local apparatus in managing local finance and budgets. As a result, the existing policies regarding local finance and budget management look much better, compared to the pre-reform period. Nevertheless, since it is interfered with by the political conflicts of the legislatures and executives and administrative misconduct, management of the local finance and budget cannot be executed properly as stipulated in the formal regulations. This reality supports the argument that rational budget reforms do not always successfully improve resource allocation either at local or national level (Connelly & Tompkins, 1988; Harkin, 1982; Joyce, 1996; Lauth, 1985; Schick, 1978). As seen in the study locations, this fact is also aggravated by the poor performance of law enforcement officers which leads to massive corruption and manipulation practices¹⁹. This condition is indicated by a great deal of local government heads (318 out of 524²⁰) and thousands local legislators²¹ that have been

¹⁹ The tendency towards manipulation and corruption demonstrated by local bureaucrats and legislators is primarily led by the high costs of democracy which forces local elites to spend a great deal of money to obtain a strategic position in the local government or parliament. Therefore, once they have gained an occupation, they attempt to collect as much money as possible (both legally and illegally) to recoup their spent funds.

²⁰ Indopos (JPNN Group), 15 February 2014, <http://www.jpnn.com/read/2014/02/15/216728/318-Kepala-Daerah-Terjerat-Korupsi->

²¹ Tribun News, 4 August 2014, <http://www.tribunnews.com/nasional/2010/08/04/anggota-dewan->

found guilty because of corrupting and abusing the APBD funds. As a result, until now, Indonesia has not adequately enjoyed the benefits of the policy concerning fiscal decentralisation and budgetary reform.

8.6. Summary

This chapter reveals that all local institutions have now applied the PBBS approach. Nevertheless, the adoption of the PBBS has not been perfected yet, as local officials face a number of issues in doing so, such as limited budgets, the poor quality of human resources, conflicts of interest between local executives and legislatures, as well as the fact that the standards of costs and minimal services cannot be comprehensively determined.

In addition, local officers appear to have not perfectly implemented the principle of the MTEF, because they are generally still struggling to arrange forward estimations as local situations change rapidly. On the other hand, the integrated budgeting approach was introduced simultaneously with the implementation of the I-account system which replaced the T-account system of accounting. Even though local officers have not struggled with the implementation of the integrated budgeting approach, they have not yet witnessed any dramatic positive impacts from, or benefits of, the implementation of the I-account system. Furthermore, the implementation of the accrual accounting system has not resulted in satisfactory achievements because the local governments mostly face a number of problems in conjunction with the lack of availability of an IT-based accounting system; the limited number of local staff who understand IT-based accounting systems; the lack of commitment of local elites

to accelerate change and resistance from local staff as they are already familiar with the old system.

The intention of promoting a bottom-up budgeting system is apparently not in line, as expected, because the *Musrenbang* does not work properly. This circumstance is created by a number of obstacles coming from the local community and local officers themselves. The current governance system also seems failed to manage the APBD in an ideal manner through a rational and technocratic process. On the contrary, the APBD is mostly snared in the political collusion set up by local legislators, local executives, interest groups and other political powers. After more than a decade of governance reform, Indonesia has not yet satisfactorily enjoyed the advantages of the fiscal decentralisation and budgetary reform policy.