

Conference Paper

Earmarking Tax Policy on Local Taxation in Indonesia: Towards Pro Fiscal Legitimacy and Budget Flexibility Policy

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Abstract

Earmarking tax, the concept of specific expenditure allocated from particular taxes, has been debatable. In Indonesia, the policy of earmarking tax is regulated in the Law of 28/ 2009 concerning Local Tax and Local Charges for Motor Vehicle Tax, Cigarette Tax and Street Lighting Tax. This study discusses the urgency, implementation, and theoretical reconstruction of earmarking tax on Local Tax in relation to fiscal legitimacy and budget flexibility. Theoretical reconstruction is made since there are only a few studies accommodating the three concepts in a single study, although there have been a number of studies on earmarking tax and fiscal legitimacy or earmarking tax and budget flexibility. This research uses constructivist paradigm with qualitative approach and an illustrative method for qualitative data analysis. Research was conducted in Daerah Istimewa Yogyakarta Province and Batu City, East Java. Results of the study reveals three urgencies of earmarking tax policy: accommodation of benefit principle in the policy of local tax and expenditure, fund's availability for particular spending, and promoting local government's expenditure accountability. The implementation of earmarking tax policy has frequently faced up dilemma between the desire to promote government's fiscal legitimacy and the necessity to maintain budget flexibility. This study initiated dual pro earmarking tax that accommodating the concepts of fiscal legitimacy and budget flexibility at the same time. Therefore, earmarking tax can serve as an instrument to improve tax compliance as well as welfare of taxpayers.

Keywords: earmarking tax, budget flexibility, fiscal legitimacy, dual pro earmarking tax.

1. Introduction

Disconnection between the tax collected by government and the benefits directly received by the taxpayers is conceptually reflected in the definition of tax stating that "tax is obligatory paid, but the benefits may not be directly observed" (James,

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1996; Sommerfeld, Anderson & Brock, 1981; Soemitro, 1987, Hyman, 2011). On the one hand, this characteristic provides flexibility for the government to utilize tax revenue to meet their high priority expenditure. However, at the same time, this situation also confirms tax payer's weak bargaining power to allocate tax revenue in the provision of public goods and services. Tax is frequently associated with any attempt to divide tax based on taxpayers' ability to pay. There is lack of discussion about benefit principle or benefit received by taxpayers from government's spending. In the perspective of benefit principle, equity is ensured when the tax burden is equivalent to the benefits received by the people (Jung and Bird, 2005; Musgrave, 1984; Musgrave and Musgrave, 1984; 1990; Neil, 2000).

The government is often in the dilemmatic position of either increasing the tax rate or expanding tax basis to finance the increasing of government's expenditure, or to cut the tax rate that will reduce public expenditure. Mulgan and Murray (1993) revealed that the paradox of increasing government expenditure and government's low legitimacy to collect tax has resulted in taxation crisis in several countries in the form of tax revolution, resistance to tax, or refusal to pay the tax.

The refusal to pay tax is associated with several factors such as public perception of government legitimacy to collect taxes. Trandafir and Ristea (2013) revealed the urgency of legitimacy to support efficient fiscal policy. Without collective revenue based on government regulation on tax collection, the government will have no authority to collect a tax. This condition will make the government difficult to allocate the resource to finance public needs. Legitimacy depends on government ability to solve the problems efficiently and provides public goods and services needed by the society (Scharpf, 1999). In this perspective, legitimacy is associated with allocation in fiscal policy [14], or government's expenditure quality. The benefits of government expenditure financed by tax income is a component to strengthen tax obedience (Feld and Frey, 2007; Palil, 2010) as well as to improve *tax morale* for better tax obedience [1].

Fiscal legitimacy reflects public trust to government's good performance in tax collection and expenditure. The Government may strengthen *fiscal legitimacy* among others by improving the quality of public expenditure to be more equitable and suitable for interests of taxpayers (OECD, 2007, 2009, 2010). *Fiscal legitimacy* can be understood by the perspective of *Fiscal Contractual Theory*, viewing the relation between taxpayers and the government as a contract between the two parties of which is obliged to either pay tax or provide public services [6]. In Indonesia, fiscal legitimacy came up

to respond the appeal of the National Congress of NU in 2012 to boycott tax payment since the government has abused the tax (<http://www.tempo.co/read/>).

In this context, earmarking tax stressing about a relation between the collected tax and the benefits received by the people specifically from government expenditure is a crucial issue. However, the earmarking tax is also debatable. The proponents of *earmarking tax* suggest that it secures fund availability to provide particular public services or to improve the accountability of the use of tax revenue [4, 5, 12, 15]. Politically, *earmarking tax* has some advantages in ensuring reliable and predictable fund availability to carry out government programs and improve support to the government in fundraising [9, 12]. However, one of the criticisms to earmarking tax is the lower budget flexibility since part of the budget allocation has been determined in advance so that the government would find it difficult to reallocate the expenditure deriving from tax revenue (Musgrave, 1989; Wilkinson, 1994). A flexible budget is necessary for the government to anticipate the changing environment [2].

In the implementation, *earmarking* seems to be more successful in the context of local government since there is a closer relation between the benefit recipients and taxpayers and public service users can more easily express their preference through political voting (Perroni and Dellon, 2000) and therefore improve *tax morale* [7]. In Indonesia, earmarking tax policy is regulated in Law of 28 / 2009 concerning Local Tax and Local Charges (Local Tax and Charges Law/2009). The tax types earmarked include Motor Vehicle Tax and Cigarette Tax in Province and Street Illumination Tax in regency/ city while not reserving the possibility for local governments to add the types of *earmarked tax* when it is deemed necessary. As the implementation of Law of PDRD / 2009, including in DIY Province and Batu City nearly all regions in Indonesia has accommodated earmarking tax policy. DIY Province regulates *earmarked tax* for Motor Vehicle Tax, Motor Vehicle Fuel Tax, Cigarette Tax, and Surface Water Tax in the Regulation of 3 / 2011 concerning Local Tax. DIY Province is one of the regions with the largest *earmarked taxes* in Java. Meanwhile, on the contrary to DIY Province, Batu City has not regulated *earmarked tax* in its local regulation. Although it is not the only city/regency in Indonesia, the phenomenon of Batu City describes more comprehensively to complete research concerning *earmarking tax* in the local tax.

The aim of this research is to evaluate earmarking tax policy in local tax in Indonesia to strengthen the *fiscal legitimacy* and provide a recommendation to design earmarking tax policy that is able to sustain the balance between *fiscal legitimacy* and *budget flexibility* (*dual pro earmarking tax*). This study also attempts to discuss the theoretical

reconstruction of *earmarking tax* accommodating the concepts of *fiscal legitimacy* and *budget flexibility*.

2. Method

The paradigm used in this research is constructivist with a qualitative approach. The study was conducted in DIY Province and Kota Batu, East Java, which have different *earmarking tax* regulations. DIY Province has more regulations of *earmarking tax* than other provinces in Indonesia and has the largest number of regulations in Java Island, while Kota Batu has no regulation concerning *earmarking tax* on their local tax regulation. Meanwhile, according to the Law of PDRD / 2009, each regency/ city minimally has Street Illumination Tax as an *earmarked tax*. Qualitative data was collected through in-depth interview with informants involved in the implementation of earmarking tax policy (*stakeholders*) in DIY Province and Kota Batu as well as the academicians. The data was analyzed with *an illustrative method*. The interview was performed in the period of October 2014 to April 2015. Meanwhile, secondary data was obtained from the relevant literary study and documentary study that includes laws and local regulations concerning the *earmarking tax*.

3. Results and Discussion

Some literature has revealed the advantages and disadvantages of *Earmarking tax for the government and the people*. Theoretical debate over *earmarking tax* includes three approaches to *traditional public finance*, *public choice* and *unorthodox approach* each of which has the different perspective on *earmarking* [15]. The proponents of *traditional public finance* generally perceive *earmarking tax* as reducing the flexibility and efficiency of a budget. *Public choice* relates *earmarking tax* to public preference to particular types of public goods or services provided by the government. *Unorthodox approach* relates *earmarking tax* to such issues as *fiscal legitimacy* and *tax morale*. However, regardless of the disadvantages, results of the study have shown that earmarking is necessary to strengthen fiscal legitimacy through improvement of local government expenditure accountability. In the context of local government, Perroni and Dellon (2000) also assured that earmarking tax policy might improve accountability.

As previously described, earmarked local tax in Indonesia include Motor Vehicle Tax and Cigarette Tax (Province) and Street Illumination Tax (regency /city). The minimal allocation is 10% of Motor Vehicle Tax for road infrastructure rehabilitation and the

transportation mode, 50% of Cigarette Tax for health and law enforcement, and part of the revenue from Street Illumination Tax for illumination facilities of roads and public streets. The regulation is expected to explain or inform the public about the use of local tax fund that they have paid.

Assurance for the effective expenditure of the revenue deriving from local tax in Indonesia is very crucial since at present time, the allocated budget is mostly spent on employment salary and the only small portion is for capital expenditure. DIY Province also has the highest ratio of employee salary to total expenditure in Indonesia (56.11%) and lowest ratio of allocation for capital expenditure (12.59%) to total expenditure in Indonesia (DJPK, 2013). Capital expenditure has a significant effect on local economic growth and has the *multiplier effect* in improving the local economy and public welfare.

Earmarking tax policy has also ensured certainty in the budgeting of expenditure allocation from the tax revenue involving the government and the local parliament or Dewan Perwakilan Rakyat Daerah (DPRD). This process is very important since decentralization of fiscal in Indonesia tend to stress on *expenditure assignment* characterized by a distribution of management at different levels of governments that will have an impact on the structure and portion of the local government budget. In the case of Kota Batu, the process of budgeting is a crucial point since there are institutional problems of less optimal commission in the process of budget development and relatively dysfunctional *check and balance* function between local government and DPRD. The problems seem to derive from political constellation and dynamics in the process of local policy formulation, including the process of local expenditure policy formulation (in-depth interview, 2014).

Accountability in local government expenditure is an important point in improving obedience of tax payers that will lead to improve tax revenue (Feld and Frey, 2007; Palil, 2010, Mulgan and Murray, 1993) needed by local governments due to the relatively low local tax contribution to total local revenue at province or regency/city levels (DJPK, 2013). In DIY Province, in 2013 local tax contributed to 41.2% (local budget of Province of DIY 2013) while in Batu City, local tax contributed 7,56% to total local revenue in the same period (Data from Tax Service Agency Batu City, 2015). This indicates the necessity for local government, particularly the government of Batu City to increase tax revenue through awareness rising among the people to pay tax.

Besides improving the process of budgeting, *earmarking tax* may also simplify public monitoring to the allocation of government budget since there has been a regulation on extent and percentage for particular types of expenditure as the reference for local

government. However, of course, public monitoring is only possible when local governments provide adequate and easily accessed information for the people. On the other hand, the public will have to have clear information about *earmarking tax*. Therefore, the people as the taxpayers feel sure that the government has the commitment to provide an output equivalent to tax revenue. However, in practice, public monitoring may be absent due to the lack of information about *earmarking tax* regulation and inadequate information on the relation between particular tax types and government's expenditure allocation (in-depth interview, 2014).

Currently, policy and regulation on of *earmarking tax* in local tax in DIY Province and East Java Province as the reference of *earmarking tax* regulation in Batu City can be seen on Table 1.

TABLE 1: Allocation and Classification of *Earmarking tax*.

No	Tax type	Expenditure type	Percentage	Characteristics*
1	Motor Vehicle Tax	Development and/or maintenance of road and improvement of public transportation mode and facilities	20% (DIY) 10% (UU PDRD)	Specific – Loose – (Rationale) Benefit (Type B) : Type B has clear relation between revenue and usage. However, the relation between revenue and expenditure is loose, which means that the amount spent will not necessarily increase along with the increase of revenue, and vice versa.
2	Motor Vehicle Fuel Tax	Mitigation to air pollution and environmental damage	10%	Specific – Loose – (Rationale) Benefit (Type B)
3	Surface water tax	Conservation and Tree Planting	10%	Broad – Loose – (Rationale) Benefit (Type D) : Type D is analogous to type B. There is a clear relation between paid tax and beneficiaries, but the relation between the collected tax and expenditure is in a loose area.
4	Cigarette Tax	Public health services and law enforcement by the authority.	50%	Broad – Loose – (Rationale) Benefit (Type D)
5	Street Illumination Tax	Road illumination services	Partial	Specific – Loose – (Rationale) Benefit (Type B)

Source: Law of 28 / 2009, Local Regulation of DIY Province of 3 / 2011 and Local Regulation of East Java Province of 9 / 2011, processed.

* Characteristics based on Bird and Jun (*Earmarking in Theory and Korean Practice* June, 2005 Richard M Bird & Joosung Jun, p.41)

In general, referring to Bird and Jun's criteria the *earmarking tax* in local tax in DIY Province and Batu City is *loose*. It implies that the extent of revenue of *earmarked*

tax does not necessarily influence the extent of a specific expenditure. This is so because most of the fund derives from the *general fund* (in-depth interview, 2014). This condition has obscured the relation between collected tax and specific expenditure of local government. Consequently, the people do not feel the benefit from the paid tax (*earmarked tax*) (in-depth interview, 2014).

Based on the table, *the earmarking tax* may be classified into *fixed* and *flexible*, in addition to *little* and *moderate*. *Fixed* refers to a particular percentage specifically determined by the law and local regulation. This includes Motor Vehicle Tax, Cigarette Tax, Surface Water Tax and Motor Vehicle Fuel Tax. Meanwhile, *flexibility* refers to the allocation not specified in any law or local regulations as in Street Illumination Tax.

Fixed tax has advantages since it specifies clearly the allocation extent. Therefore, there is no doubt in the implementation of *earmarking tax*. However, *fixed earmarking tax* has also disadvantage since it potentially decreases the flexibility of local government to formulate the policy based on the priority scale or public need. Moreover, in such cases, the allocation extent is *moderate* or *large* (50% or higher of tax revenue). This issue deserves attention since it is related to the concept and policy of decentralization in Indonesia. Strict regulation of *earmarking tax* for *fixed-type* with a relatively large percentage at central government level potentially results in the problem at local government level in the implementation of the policy due to the potential *mismatch* between the specified expenditure allocation and real need of government. This will result in difficult allocation through *earmarking tax*.

Meanwhile, the *flexible type* has advantages since it provides large flexibility to local government to arrange their own expenditure budget based on their own priority scale, vision-mission of *the* local head and public aspiration or need (in-depth interview, 2014). Therefore, it is expected that expenditure allocation will meet the principles of efficiency, effectiveness, and decentralization while considering public aspiration (*local voice*) and public choice (*local choice*) (Norton, 1994). However, in practice, the *flexible* type has disadvantages too. Regulation by a local government such as in regulation of Street Illumination Tax in Kota Batu has not clearly regulated *earmarking tax*. This is common in other regency/city.

Lack of regulation on the allocation extent of *earmarking tax* has made the position of *earmarking tax* weak. There is no clear difference between *earmarked tax* and *non-earmarked tax*. In addition, the position of *benefit principle* in *earmarking tax* is not clear since there is no clear relation between tax payment and benefits received by the taxpayers. This position has diminished the support of *earmarking tax* to the strengthening of fiscal legitimacy. The strong relation between tax and government

expenditure reflects *fiscal contract* between the people and the government in the form of *fiscal exchange*. *The Fiscal contract* will positively contribute to the obedience of taxpayers to increase *revenue productivity*.

Referring the previous discussion, the alternative form of *earmarking tax* that may strengthen fiscal legitimacy in local tax in Indonesia is *flexible* type at central government level to provide flexibility to local government in the design of earmarking tax policy suitable to local public needs. However, the extent has to be *fixed* at local government level to ensure that the substance of *earmarking* is accommodated in local government policy. However, caution is necessary for designing the allocation of *earmarking tax* to avoid inefficiency and ineffectiveness of budgeting. Therefore, the allocation extent should be between *little* to *moderate* to maintain budget flexibility in local government.

This dissertation will analyze the concept and policy of earmarking tax in attempt to support *fiscal legitimacy* and *budget flexibility* named *Dual Pro Earmarking tax*:

TABLE 2: Concept of *Dual Pro Earmarking tax*.

<i>Pro Fiscal legitimacy</i>	<i>Pro Budget flexibility</i>
Benefit Principle (Mugrave, 1984) : tax is correlated to the benefits received by the people from the government or there is a connection between tax payment and government expenditure (Mulgan and Murray, 1993)	Allocation of <i>earmarking tax</i> may not decrease the ability of the government to minimize the effect of decreased revenue and meet the objective or function of budgeting tin <i>resources</i> allocation expenditure control [2]
Expenditure allocation has to be accountable and easily monitored by the people (OECD, 2011) through public participation (OECD, 1994)	
There is assurance that particular expenditure will not end due to government funding problem [9]	moderate allocation (OECD, 2010)
<i>Earmarking tax</i> is a formal form of contract between the people and the government or exchange between tax payment and public goods and services by the government (OECD, 2010; D’Arcy (2011)	
Source : Processed from different sources, the author, 2015	

Based on the concept presented in table 2, *Dual Pro Earmarking tax* is introduced by considering three criteria:

1. *Substantive Earmarking Tax Policy* developed from the concept of *benefit principle*, *fiscal contractual* and *tax bargain* as the part of policy;
2. *Better Earmarking Tax Process* as a *Political and social aspect* developed from accountability principle being the part of *good governance*;

3. *Moderate Allocation and Proper Tax Base as Financial aspect* as the attempt to maintain *budget flexibility*;

The criteria of *Substantive Earmarking Tax Policy* as the policy aspect imply that the design of substantive earmarking tax policy has to be based on the concepts that support *earmarking tax* to enhance *fiscal legitimacy*, which is the focus of *unorthodox approach*. *Dual pro earmarking tax* is based on *benefit principle* by considering the relation between the paid tax and received benefit. *Benefit taxation* put tax in the position that resembles to price in private transaction. Implementation of this concept will put resource allocation as the direct response to public needs as public service consumers, instead of mere voters (Musgrave, 1984). Clarity of the benefit received from the paid tax will increase public obedience to pay tax (In-depth interview, 2014). Beside that, clarity of relation between tax revenue and benefits will increase public trust to the government to collect tax. *Earmarking tax* is an attempt to assure the taxpayers about the availability of fund for the provision of public goods and services, as well as responding the public doubt and distrust to the implementation of *public expenditure*. (In-depth interview, 2014).

In *substantive earmarking policy*, the preferred expenditure type has to be specific or *narrow* in order that the relation between paid tax and expenditure is clearly identified. In addition, the benefit will have to be directly enjoyed by the public being the tax payers in order that the public can clearly identify the benefits received from tax. This clarity will increase accountability of government's expenditure since the people can get clear and accurate information concerning government's economically rational expenditure (in-depth interview, 2014).

In designing the *earmarking tax* in local tax, particularly in heterogeneous community, central government will have to clarify the expenditure types and expenditure allocation percentage. This is first, more suitable with the local autonomy substance that accommodates *local wisdom*, and *local choice* and *local voice*. Flexible design of earmarking tax policy may accommodate heterogeneity of public characteristics, whether it is *rural* or *urban*, and allocated expenditure and thus it will be effective in meeting the public needs. Second, this will keep from mismatch between expenditure allocation and local public needs. It will accordingly support efficiency and effectiveness in the provision of public goods or services.

In *dual pro earmarking tax*, one way to strengthen the policy of government's expenditure to *fiscal legitimacy* is by accommodating the participation, socialization and communication in the process of determination and reporting of government's expenditure for better accountability. Better *earmarking tax* is a social aspect and political aspect

of the criteria of *dual pro earmarking tax*. Process is the important key word in *dual pro earmarking tax* since this process will compensate the extent of expenditure allocation of *earmarking tax* in order that it does not compromise *budget flexibility*.

Participation refers to public participation to be directly involved in the process of determination of government expenditure from *earmarking tax*. This involvement is important since it makes people believe that the tax revenue will result in public benefit. Participation will also help the process of identification of the expenditure types financed by particular tax revenue. In this process, the people involved will learn that the paid tax will result in public benefits instead of individual benefits. Therefore, horizontal participation may strengthen the horizontal aspect of *fiscal contractual* [6].

Participation may increase public trust to the government, and therefore, it will improve the taxation performance in local government. This view is in line with the study concerning local tax conducted by Bahiigwa *et al.* (2004) and Ssewakirinyanga (2004) in Uganda (OECD, 2010) revealing that the key challenge to improve local taxation is reconstructing public trust through enhanced explicit relation between tax collection and public expenditure.

As a political strategy, *earmarking* is effective since it has impact on government accountability, transparency, and public monitoring through public participation. Therefore, *earmarking tax* may serve the interest of political participation (OECD, 2010). Participation is a beneficial political process that enhances democratization and transparency in the determination of government's expenditure, as well as strengthens *fiscal legitimacy*. Participation in the determination of expenditure is also an instrument to socialize transparency and democracy in the society. Participation is necessary in local tax collection and expenditure since the relation between government and the people is direct. This is also in line with the spirit of local autonomy oriented to local public aspiration.

In the context of *earmarking tax* in local tax, participation is an important instrument to obtain public aspiration, which is in line with local autonomy's objective of providing public services based on local needs. Besides that, allocation of *earmarking tax* has to consider public characteristics, whether it is *rural* or *urban* for effective allocation of expenditure (in-depth interview, 2014).

Communication refers to the government's communication to explain tax revenue and expenditure type specifically financed by particular tax. It is necessary to have good political communication from the government to support *fiscal legitimacy* by providing the relevant data or information. Accurate and accessible data and information is very important to increase transparency and accountability in the management of

government's revenue and expenditure at national and local levels. Government will have to seek the methods suitable with the situation, condition, and culture in the communication about policy of expenditure to the public (in-depth interview, 2014).

One of the criticisms to *earmarking tax* is that it results in lower budget flexibility since the budget has been allocated for particular types of expenditure determined in earmarking tax policy (Gwilliam and Shazili, 1999, Wilkinson 1994, Musgrave and Musgrave, 1984). Low budget flexibility may result in two conditions. They are too large allocation and/ or too many tax types including in the scheme of *earmarking tax*. To avoid this problem, we propose at least two proposals.

First, allocation of *earmarking tax* is not in total or in whole, but rather in part (*partial earmarking tax*). Local government allocates the extent of allocation of *earmarking tax* by considering the total tax revenue and the predicted and projected expenditure. Again, local expenditure allocation may help accurately project the extent of expenditure. Partial allocation will be able to reserve the government's interest to have relatively flexible budget so that the government will be able to relocate the budget as necessary. Allocation should be *fixed-little* or *fixed moderate* (maximally 50%) to prevent from inefficiency in government's expenditure or budget inflexibility. However, evaluation is needed to ensure periodical efficiency and effectiveness of expenditure.

Second, alternative tax types of *earmarking tax* must be limited to only the tax types meeting such criteria as *immobile* and large number of taxpayers and equitable distribution throughout the region. Criteria of *immobile* is important as revealed by a number of studies that *earmarking tax* is more ideal when it is implemented in local tax and *immobile* is one of the most important criteria in local tax. Besides minimizing potential *dispute among* the regions, immobile tax objects has clear relation to the provision of public goods and services by the government.

Results of this research show that fiscal decentralization has stronger effect on tax obedience. Results of the research also show that *tax morale* is higher when the government provides public goods based on region or locality since the development of the region or satisfaction of the public needs [7].

A tax type that meets the criteria of *earmarking tax* is property tax, particularly *tax on land and building*. An important fact concerning property tax commonly ignored is that in the determination of property tax may involve taxpayers in political dialogue with the government. By doing so, the government may grow *fiscal contract*. Property tax has extensive and visible reach. Therefore, principally it is a good alternative to empower the people. Property tax has a specific relation to location and such public

expenditure as infrastructure. Allocation of tax with relatively clear relation to expenditure will have good management through public empowerment and public trust development when the government meets their commitment (in-depth interview, 2014).

The selection of appropriate tax type such as Property Tax or other type with similar criteria will be advantageous for local government in the form of increased public trust. Increased public trust will contribute to the stronger *fiscal legitimacy* on the one hand, while maintaining *budget flexibility* on the other hand since moderate or partial allocation of *earmarking tax* will grow public trust about the relatedness between the paid tax and government's expenditure.

Substantive earmarking tax policy should maintain local government flexibility in designing the earmarking tax policy. Local governments are in charge of designing the types of local tax and expenditure regulated in local regulation and local head's regulation in compliance with public aspiration and local priority scale. Clear regulation is important to provide clarity to the public about government's expenditure financed by *earmarking tax*. Flexibility in designing the *earmarking tax* gives opportunity to local government to accommodate public aspiration being the taxpayers and avoid mismatched allocation of *earmarking tax*. Periodical evaluation is needed to keep the match between expenditure type and public needs. When public need for expenditure types change, local government will have to change or relocate the expenditure from *earmarking tax* (in-depth interview, 2014). In other words, dynamic expenditure allocation in *earmarking tax* is advisable.

4. Conclusion

To improve fiscal legitimacy and budget flexibility this research suggests the application of *Dual Pro Earmarking tax*. This concept of substantive *earmarking tax* encourages public participation and improves communication concerning tax and expenditure between government and the public. *Fixed-little* or *fixed moderate* allocation is advisable to keep budget flexibility and appropriate *tax base*. This paper suggest narrow expenditure type to accommodate local public needs and flexible national regulation yet *fixed-little* or *fixed moderate* local regulation to ensure improved accountability on local government's expenditure.

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