ABSTRACT

This study examines the effects of the lagged Fiscal Independence Index, Fiscal Balance Transfers, and Local Own-Source Revenue on Regional Expenditure and identifies indications of a flypaper effect among regencies and municipalities in Java. It also compares the estimation patterns between metropolitan and nonmetropolitan areas. This study uses panel data from 113 regencies and municipalities covering 2017–2024. Based on the applicable spatial-planning regulations, the sample is classified into 27 metropolitan and 86 nonmetropolitan local governments. The use of a one-period lag for the Fiscal Independence Index results in an effective estimation period of 2018–2024 with 791 observations. The data were analyzed using a Two-Way Fixed Effects Model with local-government and year fixed effects and cluster-robust standard errors.

The results show that the lagged Fiscal Independence Index has a negative and significant effect on Regional Expenditure in the full and metropolitan samples but is insignificant in nonmetropolitan areas. Fiscal Balance Transfers have positive and significant effects in the full and nonmetropolitan samples but are insignificant in metropolitan areas. Local Own-Source Revenue has a positive and significant effect across all estimations, whereas Gross Regional Domestic Product and population are insignificant. The Local Own-Source Revenue coefficient exceeds the Fiscal Balance Transfer coefficient in all estimations; therefore, no indication of a flypaper effect is found. These findings suggest that Regional Expenditure is more responsive to locally generated revenue, although transfers remain important for financing expenditure, particularly in nonmetropolitan areas. Differences between metropolitan and nonmetropolitan estimates are interpreted descriptively because no formal structural-difference test was conducted.

Keywords: *Fiscal Independence Index; Fiscal Balance Transfers; Local Own-Source Revenue; Regional Expenditure; Flypaper Effect.*