REVENUE COLLECTION IN NON-EXTRACTIVE NATURAL RESOURCE SECTORS IN INDONESIA

BRIEF: POTENTIAL STATE REVENUE FROM THE REGIONAL AGRICULTUTRAL SECTOR AND ITS PROBLEMS

BRIEF FACTS

In 2015, 37.8 - 38.3 million Indonesians worked in the agricultural sector

An estimated 56.1 – 56.9 million Indonesians depend on agriculture for their livelihoods

In 2013, households engaged in agriculture had an average income of IDR 26.6 million with IDR 12.4 million of that coming from agricultural activities

Households engaged in agriculture worked an average of 8.926 m^2 of land in 2013

Land owners and landless farmers: 25,751,267

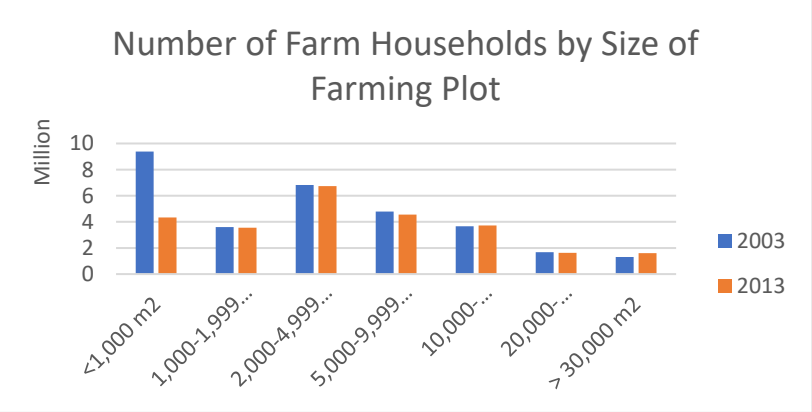
Smallholder and landless farmers: 14,248,864 farmers

The agriculture and forestry sectors contributed 7.5 percent of total state revenue in 2014

There were 4,209 legal businesses in the agriculture sector in 2013

INDONESIA'S AGRICULTURAL SECTOR

Tens of millions of Indonesians depend on the agricultural sector for their livelihoods. The sector is dominated by individuals and small scale and informal businesses and statistical data shows that most Indonesian farmers work less than 0.5 hectares of land.



The agricultural sector is governed through several regulations which, in principal, are permitted through the government. However, these regulations are restricted to businesses that employ more than 10 workers or encompass an area of more than 25 hectares (Article 7 of Law 18/2010) and less than 10,000 hectares (Article 8 paragraph (2) of Law 18/2010). Businesses employing fewer than 10 workers or below the size thresholds are regulated by local/regional government. In addition, all farmers using facilities and/or services provided by the government are required to pay Non-Tax State Revenues.

"Farmers whose net income reaches 1.2 billion per year but are not in possession of a TIN are practically 'invisible' to the state, and do not pay any taxes.''

FINDINGS

This study: 1) provides an overview of the management structure for regional agricultual state revenues; 2) estimates the amount of revenue that the state could potentially collect based on the size of the sector in various locales (defined as "potential state revenues"); 3) estimates the possible loss of revenue attributable to

manipulation (define as potential revenue “leakage”); 4) identifies the actors involved in the loss of revenues; and 5) discusses governance issues in the agricultural sector.

The sector is dominated by small farms, self-employed farmers, and those with fewer than 10 workers. Most farmers have assets, other than land, of less than IDR 2.5 billion. Tax and non-tax revenues (PNBP) from the licensing of agricutlural activities are almost non-existent. While the majority of farmers manage a small amount of land, others manage up to tens or even hundreds of hectares. These large farms also employ up to hundreds of people, who work informally. The income of these farmers can reach tens or even hundreds of millions of rupiah per month. There is a potential revenue loss associated with larger farmers that fail to register with the government and obtain a tax identification number (NPWP). In one of the districts of Jawa Timur, for example, a farmer with a net income of IDR 1.2 billion per year was found. At this income level, he could be expected to owe about 297 million rupiahs per year. However, he paid nothing because he did not have a NPWP and was therefore essentially "invisible" to the state.

Potential revenues from the agricultural sector come from land and building taxes (PBB-P2). Often times, the government fails to collect all potential revenues. In District X in Lampung Province, for example, when the target was IDR 3.96 billion, actual collections reached IDR 4.96 billion. This indicates that something is wrong with the tax estimation and planning processes.

In addition, there are other potential revenue sources that have not been explored, such as groundwater taxes. In one of the districts in Lampung, for example, there is one company with 100 points of boreholes, but one of them is not licensed. This results in a potential tax leakage of up to IDR 400 million per year. But because it operates illegally, and there is no proper supervision of government officials, the revenue is not collected and the company continues to operate the illegal well.

The problems associated with state revenue collections from the agricultural sector are fairly simple, since relatively little activity is subject to tax. Agricultural operations employing fewer than 10 people, managing less than 25 hectares of land, with less than IDR 2.5 billion in assets, or sales of less than IDR 4.8 billion are exempt from taxation.

The most significant problem facing the sector is the high rate of conversion of small farms to non-agricultural uses, such as residential or commerical activities. Conversion is common on plots of less than 1,000 m^2 and the number of households that work on farms of this size decreased significantly between 2003 and 2013.

Land conversion is triggered by low levels of tax revenue generation, among other problems. This problem results from the fact that UN-P2 is subject to the authority, and is the source, of regional income. Regional governments have been steadfastly trying to increase the assessed value of land for tax purposes in order to raise property tax (PBB-P2) revenues. This can make it difficult for farmers to maintain agricultural land and agricultural activities. If potential tax collections are deemed to be too high in comparison to income from agricultural activities, farmers will choose to sell their land or change the designation of the land to other more profitable uses. This problem is exacerbated by the lack of up-to-date data on remaining farmlands.

Illegal payments are still present. Illegal payments are usually taken by government officials in small amounts, but frequently. These payments are not directly related to agricultural production processes, but are, instead, related to the provision of government assistance to the sector, such as assistance with infrastructure for rice production, guidance, and other services. Officials argue that these payments are used to cover the cost of transportation and to make up for their low salaries, among other reasons.

IMPLICATIONS

What are the implications of the findings discussed above for state revenues, public well-being, and resource sustainability? The agricultural sector provides livelihoods for a large share of the population, is subject to a decline in average farm size, and is under pressure by conversion and other economic factors. Because of this, it should not be seen as a source of significant state revenues. Instead, the government should find ways to make this sector grow and provide dependable incomes for farm households.

Photo: Hamidah

Researcher Contact

Email: yutaa89011@gmail.com

Perkumpulan Inisiatif
Jl. Suryalaya XVIII No.23, Kelurahan Cijagra, Kecamatan Lengkong, Bandung 40265, Jawa Barat, Indonesia
Phone/Fax: +62 22- 733 1105
inisiatif@inisiatif.org
www.inisiatif.org

Sekretariat Nasional
Forum Indonesia untuk Transparansi Anggaran (FITRA)
Mampang Prapatan IV, Jl. K No. 37 Rt. 006 Rw. 04 Jakarta Selatan 12790, Po Box: 7244, Ph. (021) 7947608, Fax. (021) 7985432

Even if the agricultural sector contributes little to the country's income, it can provide viable livelihoods. Efforts to increase revenue collections in the agricultural sector should focus on the handful of farmers who employ many people and control a large amount of land. However, governments should also assess whether it is economical to collect taxes and non-tax revenues from these farmers.

Currently, the economic well-being of most farmers is low and efforts to increase state revenues can easily reduce their income. Government programs aimed at empowering farmers, such as training and aid for agricultural production infrastructure, such as rice production, often becomes an oportunity for corruption. The loss of revenue from these practices cannot be estimated as the community value system does not consider paying less than the amount owed to be an illegal or corrupt act.

Improving the well-being of farmers creates a dilemma. A minimum level of land is needed in order for farming to make economic sense. However, many farmers lack sufficient land to meet this threshhold. In light of the limits on land suitable for production, it may be desirable to reduce the number of farmers so that the remaining farms are of sufficient size to reach a profiltable scale.

The sustainability of the agricultural sector is threatened from two sides, namely the lack of young farmers and the difficulty in reaching the scale needed to attain profitability. As noted above, the number of farm households has declined. In addition, a large number of farmers have reached, or are past, their productive age.

CONCLUSION

A number of challenges complicate efforts to ensure that the agricultural sector improves the public well-being, increases state revenue collections, and fosters the sustainable use of renewable resources. However, the nature of this sector and its reliance on small scale farming, constrains its revenue generating potential. Because of these constraints, this study recommends that sectoral reforms should prioritize improving the welfare of farmers that work the land, rather than maximizing state revenue collections. Policymakers should reduce pressure on the sector and those that depend on it for their livelihoods by addressing structural issues such as high assessed value for property tax purposes, land conversions, permitting, and law enforcement, among others, as well as economic pressure from high production costs, low commodity prices, and other factors.

Jean Ross prepared this brief as a consultant to the International Budget Partnership in October 2018