CLIMATE
POLICY
INITIATIVE

Indonesia's Village Fund: An Important Lever for Better Land Use and Economic Growth at the Local Level

Guntur Sutiyono
Saeful Muluk
Tiza Mafira
Randy Rakhmadi

March 2018

A CPI Report

Acknowledgements

Our analysis benefited from close interaction with national and regional governments in Indonesia. We would like to express our gratitude to Government of Central Kalimantan Province, Government of Kotawaringin Timur and Katingan Districts in Central Kalimantan, and Government of Berau District in East Kalimantan which facilitated us in series of discussion, interviews, and data collecting. We would like to thank Joko Tri Haryanto from Fiscal Policy Agency, Ministry of Finance, Christy Desta Pratama from Conservation Strategy Fund, Alief Aulia Rezza from World Bank for their review.

We would like to thank our CPI colleagues: Caroline Dreyer, Tim Varga, and Elysha Davila for their review and communications support, Suzanty Sitorus for her overall guidance, Darianus Tarigan and Lidya Jalius for their logistical support. We thank Dr. Yusurum Jagau and Ari Hidayat Alda from Yayasan PILAR for their role in building communication and engagement with governments in Central Kalimantan. This study was funded by the David and Lucille Packard Foundation.

Descriptors

Sector	Land use
Region	Indonesia
Keywords	Village Fund, land use, deforestation, fiscal policy
Contact	Suzanty Sitorus suzanty.sitorus@cpiclimatefinance.org

About CPI

With deep expertise in policy and finance, CPI works to improve the most important energy and land use practices around the world. Our mission is to help governments, businesses, and financial institutions drive growth while addressing climate risk. CPI works in places that provide the most potential for policy impact including Brazil, Europe, India, Indonesia, and the United States.

Executive Summary

Background

In keeping with its goals for sustainable economic growth and an inclusive and equitable economy, Indonesia is committed to avoiding deforestation. As the drivers of deforestation often originate from activities outside of forest borders, it is not enough to solve deforestation by conducting segregated actions targeted to specific forest areas. Indonesia must also work to strengthen the rural economy and improve regional collaboration by working across various administrative jurisdictions that encompass forest governance. To ensure the success of this jurisdictional approach, improved economic power and village governance are key.

In recent years, the Government of Indonesia has made numerous fiscal policy changes to enhance its rural economy, most notably the Village Fund instrument, which has been in effect since 2015. These efforts are in line with the government's mission to develop Indonesia "from the periphery," President Joko Widodo's signature phrase to emphasize his priorities on marginalized and less developed regions.

Study Approach

This study provides recommendations on how the Village Fund can be used more effectively for stronger rural economic development, underpinned by sustainable resources management. We looked at national-level data on Village Fund usage and priorities, and we also collected fiscal data on villages in three districts: Katingan and Kotawaringin Timur in Central Kalimantan, and Berau in East Kalimantan.

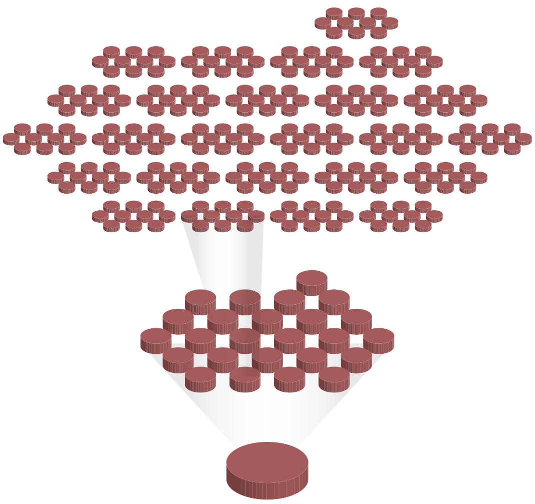
Findings

Overall, we found five major challenges limiting the Village Fund's potential to encourage sustainable village practices, and have identified opportunities to address these challenges. These opportunities exist across jurisdictions, beginning with interventions that are implementable within villages, and progressing to those that will require the involvement of the central government.

1. Districts include "sustainability" as a component of their development planning, but this is often not harmonized with village plans. Integrating village priorities into district planning will create better sustainability planning and fund allocation from district to villages.

The Village Fund is a relatively new fiscal instrument that, in many ways, lies outside of what has traditionally been considered central-to-regional fiscal transfers. The process of accessing district funds and village funds are completely different, and have no perceptible influence on one another. Consequently, the preparation of village development plans do not need to take into account the larger goals set by the district government, which often include environmental goals.

The Government of Indonesia has issued Ministry of Home Affairs (MoHA) Regulation Number 114/2014 on Village Development Guidelines, which aims to synchronize development planning between village and district. However, while village development planning is governed by this regulation of the Minister of Home Affairs, the Village Fund use is governed by a regulation of the Minister of Villages. The two regulations are not



Village level: 1. **Integrate village priorities** into district planning

District level: 2. **Maximize the Village Empowerment Office**

3. **Create village guidelines** for sustainable land use activities

4. **Focus on negative-list** for village fund spending

National level: 5. **Add sustainability variable to village fund formula** in sync with each other. This may explain why, from the districts we observed, synchronization has not been fully complied with in all villages yet.

To alleviate this discord, regional governments can develop brief guidelines to integrate the two regulations in a simpler and comprehensive way.

We found two examples where districts are attempting to synchronize village planning and Village Fund utilization. Both examples are in Java, and used a two-step method. First, they synchronized the District Mid-Term Development Plans (RPJMD) with the Village Mid Term Development Plans (RPJM Desa). Second, they synchronized the Village Work Plans (RKP Desa) with the District Work Plans (RKPD).

Streamlining the Village Fund into district planning would remove unnecessary bureaucratic processes, and help to develop better coordination between the district government and the village government.

The synergy between district and village planning could be also improved by gradually giving the district governments discretion to distribute the Village Fund according to each village's condition, and in accordance with district sustainability goals. In order for such a policy change to happen, the district-to-village allocation must be standardized by a District Regulation and a Head of District Regulation in order to minimize the risk of misuse.

2. Village Fund administration is prohibitively complicated for villages. In order to improve, more resources should be put into maximizing the role of the Village and Community Empowerment Office.

The main village authority with influence over Village Fund management is the Village and Community Empowerment Office (*Dinas Pemberdayaan Masyarakat dan Desa*), under the District Government's authority. However, according to our interviewees, the role of the Village and Community Empowerment Office has been limited to administrative facilitation, despite having authority to tackle matters of substance. In practice, they have not been involved in much substantive decision-making, nor have they been empowered to provide guidance on which programs the village could spend its Fund on.

Village governments' technical capacity and planning experience is a significant factor in determining whether sustainable land use activities are included in the village development plan, including how the Village Fund is being utilized to support these activities. Our interviewees described the Village Fund paperwork as burdensome for an already limited number of village officials. Meanwhile, village officials, including the Village and Community Empowerment Office, often lack sufficient planning and budgeting skills.

Villages face particular challenges in planning and budgeting when they start to incorporate more elaborate programs, such as in economic development, community empowerment, and natural resource management, including land use and environmental protection (e.g., forest fire prevention and suppression).

The Village and Community Empowerment Office, as the main village authority to provide facilitation and support to village development planning and program implementation, holds promise in this regard. Their role should be fulfilled to its maximum potential by empowering them to provide substantive technical assistance in planning, budgeting, and financial reporting. They also hold authority to guide and facilitate the creation of more village programs on sustainable development and environmental protection.

3. Spending on environmental management is allowed, but not encouraged explicitly enough. Guidelines on how the Village Fund can be spent on sustainability should be created.

Village Development activities, including improvements to roads, bridges, irrigation systems, ports, etc., represent the largest use of the Village Fund, committing 82.2% in 2015 and 89.8% in 2016. However, much less is spent on Community Empowerment, despite also being a priority.

By law, the Village Fund can be allocated towards resource management, economic development, and/or environmental protection. But, so far, the Village Fund has mostly been used for infrastructure development. In the villages we observed within the scope of this study, however, the Village Fund has not been spent on infrastructure for environmental conservation, infrastructure for agro-industry, or supporting conditions for environmental conservation.

Village governments tend to focus Fund spending on a limited number of activities that utilize large amounts of financial resources (e.g. infrastructure development), rather than spreading the allocation into more activities that are less capital-intensive (e.g. environmental protection, agricultural productivity improvement, etc.).

Table ES1. Uses of Village Fund

PROGRAM	ELIGIBLE ACTIVITIES BY VILLAGE MINISTRY REGULATION	AVG. SHARE IN OBSERVED VILLAGES (NATIONAL AVG, 2015-2016)	EXAMPLES OF USES IN OBSERVED VILLAGES:
I. VILLAGE ADMINISTRATION NON-PRIORITY	Unregulated	**5.5%** (5%)	salary and operations
II. VILLAGE DEVELOPMENT PRIORITY	Infrastructure development for: 1. settlement environment 2. transportation 3. energy 4. information and communication 5. basic community health 6. basic education 7. agro-industry 8. disaster management 9. environmental conservation 10. other village infrastructure	**89%** (89%)	75% access road to village port and casting of retaining wall, development and improvement of village road 14% water supply
III. COMMUNITY DEVELOPMENT NON-PRIORITY	Unregulated	**-** (7%)	
IV. COMMUNITY EMPOWERMENT PRIORITY	Community empowerment activities, including: 1. participatory village development 2. capacity development 3. community resilience 4. village information systems 5. support for basic social services 6. support for environmental conservation 7. support for disaster management 8. village enterprise development (BUMDES) 9. community economic development 10. village partnerships 11. other community empowerment activities	**5.5%** (3%)	5.5% capital investment to BUMDES

Source: Directorate General of Fiscal Balance, Ministry of Finance, 2016.

Detailed guidelines for government officials on Village Fund spending decisions will help create confidence when spending on activities that support sustainable land use. The guidelines can be developed in the form of district-level regulations, which can then serve as a basis for the village government to make planning and spending decisions.

4. Villages are rigid in interpreting how the Village Fund can be used, limiting their scope to innovate. Creating a negative-list, instead of a list of allowable spending categories, will enable villages to create sustainable programs based on their own local needs.

We found that the existing rules relating to the priorities of the Village Fund are seen by village officials as limitations that do not allow room for innovation.

Instead of having a long list of allowed activities, which is often perceived literally by the villages, the Ministry of Finance, together with the Ministry of Villages, should create a '*negative list*' consisting of the few activities that are absolutely prohibited when using the Village Fund. This practice has been done in successfully Berau and could be replicated elsewhere.

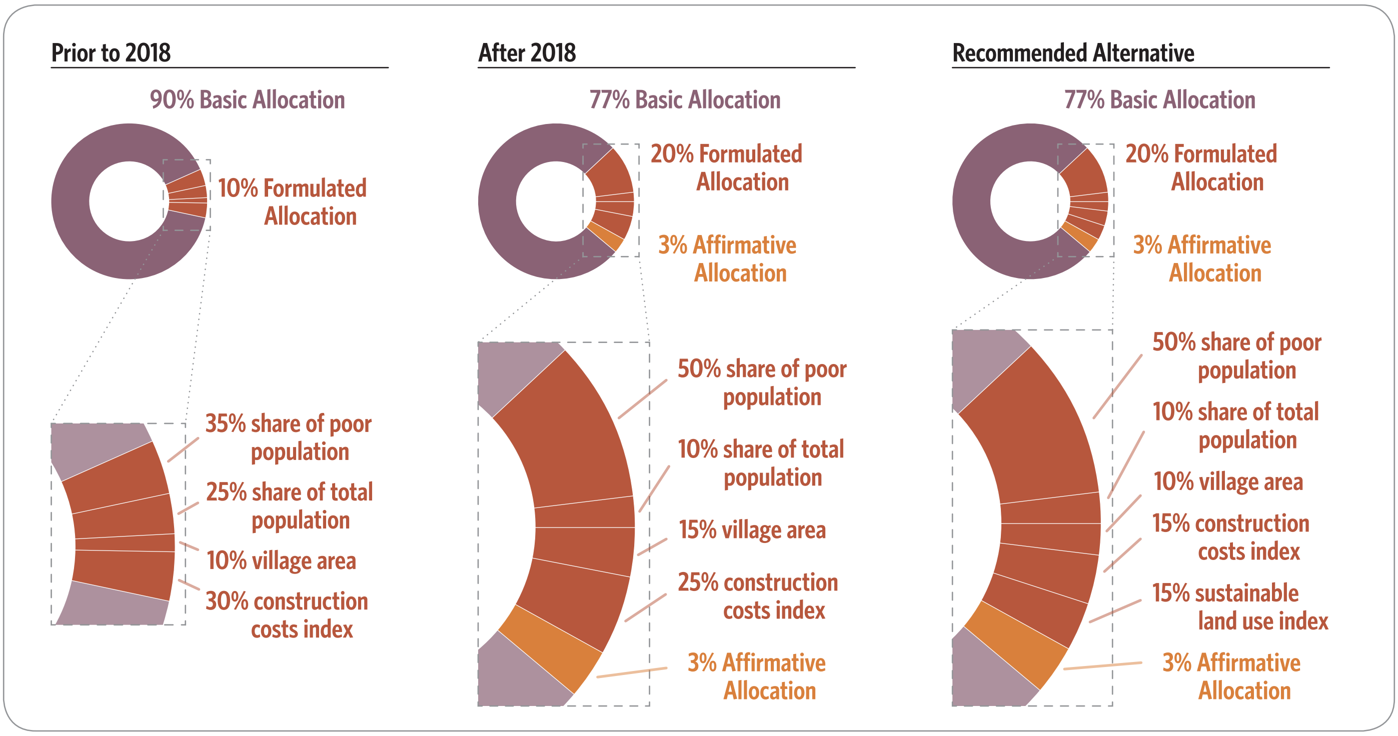
The '*negative list*' could help reduce the misinterpretation that usually occurs during process planning, and provide freedom for villages to design the most needed or best-suited programs in their own village.

5. The Village Fund formula has recently been modified to put more effort into poverty alleviation. With this as precedent, the formula could also be modified to encourage sustainability.

The Village Fund formula has been changed recently to improve its potential to achieve government priorities, which currently is to close the gap between the poorest and more well-off villages. This provides an important precedent, as it shows the Village Fund may be able to accommodate a new sustainability variable in its formula, should the government wish to prioritize environmentally sustainable villages.

The challenge with this is that there is not yet any defined indicator for sustainable land use. Unlike welfare indicators, such as the percentage of a population below the poverty line, sustainability indicators can consist of many things, and may even differ from one village to the next.

The possibilities of having a specific indicator, or perhaps even an index, that can be inserted into the Village Fund formula to push villages towards sustainable land use practices, are possibilities that merit further study. CPI will be exploring this in more detail in follow-up studies.



Contents

1. Introduction

1.1 Fiscal transfers are an essential part of the jurisdictional approach to better land use

Indonesia is committed to improving sustainable and equitable land use governance in order to fulfill the needs of present development while ensuring that the needs of future generations are preserved. As such, the Indonesian Ministry of Finance has made this a top priority, calling for an inclusive and equitable economy to support sustainable economic growth (Sri Mulyani 2017).

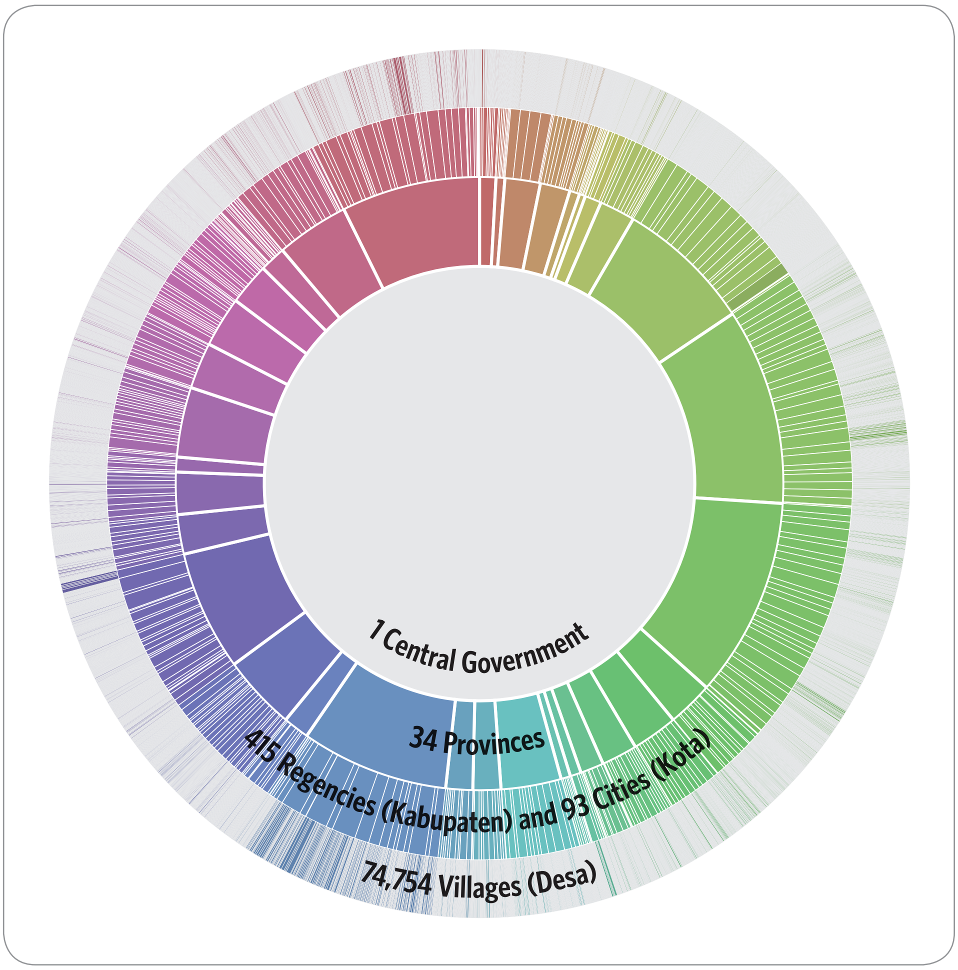
Improving sustainable land use requires a better mapping of natural resource potentials, better land planning, and better fiscal management. Forests and natural resources, which protect the livelihoods for both current and future generations, must be conserved, while still ensuring that the economy can grow and thrive. As the drivers of deforestation are often economic activities that originate from outside the borders of a forest (e.g. urban spread, agricultural industrialization, smallholder encroachment), it is not enough to solve deforestation by conducting segregated actions targeted to specific forest areas. The entire administrative jurisdiction encompassing the forest, whose decisions affect the forest directly or indirectly, need to be involved. Therefore, civil society organizations have advocated for a jurisdictional approach to land use management that directly engages with the multiple stakeholders involved in making decisions around land utilization.

To ensure the success of the jurisdictional approach, improved economic power and village governance are key. This is also in line with the government's mission to develop Indonesia "from the periphery," President Joko Widodo's signature phrase to emphasize his priorities on marginalized and less developed regions. As such, this study provides recommendations on how fiscal instruments, particularly the Village Fund, can be used more effectively for stronger rural economic development, underpinned by sustainable resources management.

Under Indonesia's decentralized governance regime, decisions over resources and land management are largely made at sub-national government levels (e.g. province and district/city levels). Such decisions are based on various motives, often political, but rarely take fiscal implications into account.

In fact, decisions over land use have a major impact on government revenue, and, conversely, fiscal decisions have an impact on land use. For instance, policies to source revenue streams from production taxes may be spurning private companies away from investing in downstream processing. In the context of the palm oil industry, the existing fiscal system provides no reward for sustainable agricultural practices and, instead, encourages sub-national governments to expand licensing for new plantations. This ultimately puts greater

Figure 1: Indonesia's administrative governance levels and scale



pressure on areas with high conservation value (Mafira and Sutiyono, 2015).

The fiscal system is a key component of any jurisdictional approach to sustainable and equitable land use. A sound fiscal policy framework at the national level should provide encouragement to sub-national governments to sustainably manage their resources. This fiscal policy framework should also be felt by the smallest unit of governance: the village.

1.2 Approach

This paper analyzes whether the existing fiscal system in Indonesia encourages sustainable land use and resource management at the village level. Specifically, it looks at fiscal instruments that enable revenue in a village, particularly the recently implemented Village Fund, which will be emphasized in this study due to the following factors:

1. It is a current policy priority for villages as they seek to better understand how to utilize and absorb the Fund;
2. It is in its early stages of implementation, and, therefore, provides greater opportunity to support contemporary policy innovations;
3. It empowers village governments' role in allocating the funds, while allowing for strong coordinating support from the district government; and
4. It has grown in monetary significance over the past few years, and is still set to increase.

This analysis will focus on answering the following questions:

- What is the Village Fund's role in overall fiscal policies on central-to-regional fiscal transfers?
- How is the Village Fund governed and who has authority to make decisions on its utilization?
- What are the challenges and opportunities in utilizing the Village Fund to support sustainable resource management and environmental protection?

For this study, we conducted a desktop analysis of regulations relevant to the Village Fund, including presidential and ministerial regulations from the Ministry of Finance, Ministry of Home Affairs, and Ministry of Villages, Underdeveloped Regions, and Transmigration (Ministry of Villages). This research benefits from the publications of the Ministry of Finance and Ministry of Villages that collect fiscal transfer data as well as information from the Village Development Index.

The study team also collected primary district-level data through a series of focus group discussions and interviews with relevant provincial and sub-district officials in two districts in Central Kalimantan, Katingan and Kotawaringin Timur, and one district in East Kalimantan, Berau. Data collecting in these districts allowed us to collect samples of regional regulations and village budgets, providing valuable insight into Village Fund planning, budgeting, initiatives, uses, and challenges.

1.3 Report Structure

This paper provides recommendations targeted to district-level policy makers and civil society organizations on how to avoid pitfalls when utilizing the Village Fund and also how to maximize its strengths to meet sustainability goals. Following an overview of fiscal policy and transfer systems, including recent fiscal policy reform trends purported by the Indonesian government, we will provide an introduction into the Village Fund as Indonesia's newest fiscal instrument, touching on its purpose and formulation. We will then discuss the Village Fund governance, and identify key actors and challenges in its implementation, from planning and management to disbursement and reporting. Finally, we will provide conclusions and recommendations based on the needed areas of improvement identified through this research.

2. Recent Fiscal Policy Changes focus on Regional Development

In the last three years of President Joko Widodo's administration, national fiscal policy has focused on optimizing the role of the state budget in accelerating inclusive growth and Indonesia's competitiveness in the global market. This has been done by reallocating consumptive spending into productive spending, starting with the politically sensitive fossil fuel subsidy reform in 2015. From the reform, the Government was able to save USD 15.5 billion, or more than 9% of total Government expenditure. Half of these savings went into infrastructure spending, which saw a significant increase from USD 15 billion in 2015 to USD 23 billion in 2017 (IISD 2015). Central-to-regional fiscal transfers also saw increases in both their structure and amount.

2.1 Structural changes in the fiscal transfers

The Government's decentralized fiscal policy shows an increased focus on regional empowerment, implemented through the restructuring, reformulation, and reallocation of a number of transfer instruments. Decentralization laws underwent a major reform with the enactment of Law Number 23 of Year 2014 on Regional Government, and Law Number 6 of Year 2014 on Village Governance.[1] Among the changes is the emergence of a new nomenclature on the national budget structure since fiscal year 2015, namely the Regional Transfer and the Village Fund.

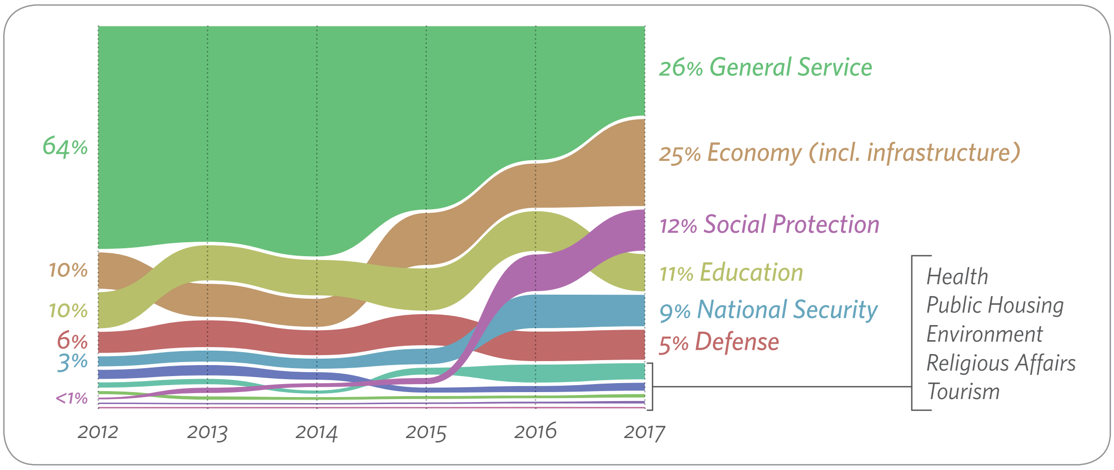
In 2016, as part of new Regional Transfer instruments, the previously singular Special Allocation Fund (SAF) has now been divided into two distinct categories: Infrastructure SAF and Non-infrastructure SAF. Infrastructure SAF is a continuation of SAF instruments that existed in the previous year, and non-infrastructure SAF is a new placeholder for transfer instruments previously used in Adjustment Fund posts, such as Teacher Professional Allowances and School Operational Assistance Fund.[2] The change is significant as it elevates the previously ad hoc funds under Adjustment Funds into a more permanent fiscal transfer instrument under SAF.

These changes led to the creation of the Village Fund. 10% of the total central-to-regional transfers received by districts is mandatorily allocated to the villages and named the Village Fund. These changes are intended to increase the size of the district's budget allocation to the villages.

2.2 More allocation for fiscal transfers to the regions

The Government of Indonesia intends to show its commitment to support regional development by increasing its central-to-regional fiscal transfers significantly over the current medium-term development plan (2014-2019). The current administration is allocating fiscal transfers more than ever before, from 32% of their total expenditure in 2015 to 37% in 2017. Total transfers in 2017 equals USD 59 billion, which is 15% higher than in 2015. Several transfers experienced a sharp increase: at USD 4.6 billion, the Village Fund almost tripled in 2017,

Figure 2. Ranked share of Indonesian central government spending by function, 2012-2017



Source: Nota Keuangan APBN 2017, Ministry of Finance
General Service is spending for bureaucracy, including travels. National Security includes spending for detention facility, intelligence, and counter-terrorism. Economy includes, agriculture, industry, trade, and infrastructure. Social Protection includes spending for Universal Health Care Program, Conditional Cash Transfer Program, and disability allowance.

1 Law No. 23/2014 on Regional Government replaces the previous Law No. 32/2004. It regulates the jurisdictional and financial authority of local governments across sectors such as education, health, infrastructure, forestry, and land use.

2 Also called Tunjangan Profesi Guru and Bantuan Operasional Sekolah in Indonesian terms.

meanwhile the Regional Incentive Fund was almost four times larger than in 2015, at USD 577 million.

Despite being relatively smaller than other transfer instruments, the increase in these Village and Incentive Funds is in line with the Government's stipulated policy of incentivizing good performance at the sub-national level and encouraging bottom-up development from the villages.

2.3 Boosting infrastructure spending is a key part of subnational growth strategy

In terms of spending, significant changes to expenditure priorities have been made since 2015. Prior to 2015, General Service expenditure, which is mostly spent on civil servant salaries and government office operations, made up two-thirds of total government expenditure. Today the government has reduced the General Service expenditure to less than one-third at 26% of total expenditure.

Prior to 2015, infrastructure contributed to no more than 10% of expenditures. Now it has gradually increased from 14% in 2015 to 18.6% in 2017. This includes the Government's equity participation in infrastructure-related State-Owned Enterprises amounting to approximately USD 2.2 billion in 2015 and USD 3 billion in 2016. Portions of this have been allocated to upgrade or build 13 new airports and 61 seaports, all of which are in subnational regions.

These policies have contributed to maintaining Indonesia's economic growth by 5% in 2016, despite the decreasing growth of domestic retail consumption. The Government's commitment to building infrastructure has boosted spending and growth.[3] GDP from tax revenue and the air transportation sub-sector recorded double-digit growth of 19% and 13%, respectively, in 2016, which is triple and double growth compared to 2014. The shift of funds to infrastructure is also consistent with a strong government focus on developing subnational regions.

3 Infrastructure spending is categorized under the Economy Function, and is mostly spent on transportation but also includes infrastructure in agriculture and public facilities.

3. Village Fund Governance and its Challenges

3.1 Overview of Fiscal Transfers in Indonesia

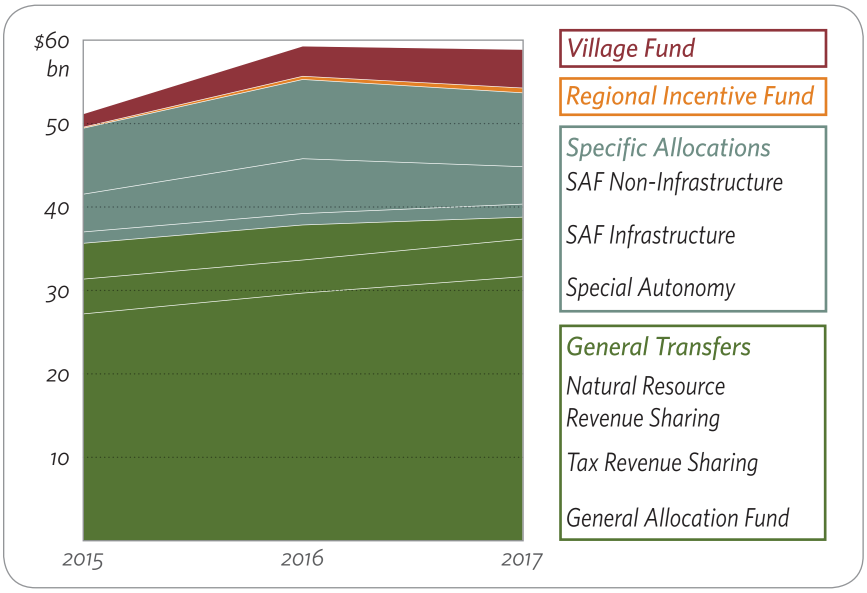
There are four major instruments in Indonesia's central-to-regional transfer mechanism:

1. General Transfer Fund
2. Specific Transfer Fund
3. Regional Incentive Fund
4. Village Fund

The General Transfer Fund, consisting of the General Allocation Fund and Revenue Sharing, is the most important transfer instrument, accounting for 66% of total regional transfers. The Specific Transfer Fund, called the Specific Allocation Fund (SAF) prior to 2016, consists of an Infrastructure SAF and a Non-infrastructure SAF. The Non-infrastructure SAF is actually a set of several transfers that used to be categorized under Adjustment Funds. Adjustment Funds are a collection of ad hoc annual fund transfers that were created to pursue specific government priorities like education or infrastructure development, and have great flexibility over its use or allocation (Mafira and Sutiyono, 2015).

The Regional Incentive Fund is a performance-based transfer that rewards subnational governments for their financial performance, compliance, as well as improvement of socio-economic indicators. It was established in 2011 and categorized under Adjustment Funds, before finally being upgraded into its own category in 2017. The allocated amount has increased from USD 106 million in 2011 to USD 654 million in 2017. In 2018, the Ministry of Finance is planning to improve the performance criteria used in Regional Incentive Fund allocation, and loosen the constraints in its use (Haryanto 2017).

Figure 3. Central Government's fiscal transfer



Source: Nota Keuangan APBN 2017 and LKPP 2016, Ministry of Finance

3.2 Overview of Village Fund

The formation of the Village Fund is the central government's way of recognizing villages as units in society that each have broad diversity, unique cultures, customary rights, individual resources, varying levels of social and economic development. The Village Fund intends to support villages in their development in order to lessen the welfare gap.[4]

The Village Fund represents a significant portion of village revenue

Fully enacted in 2015, the Fund amount allocated to each village is equal to a maximum of 10% of the total transfer to the region. Allocation in 2017 equaled 7.8% of the total transfer, USD 4.6 billion. District governments have a key role in governing the Village Fund, particularly in guiding its strategic allocation and monitoring its spending.

A village has three main categories of revenue source, i.e. Village Own Source Revenue (OSR), Transferred Revenue, and Other Revenues. Own Source Revenues come from village dividends, asset management interest, non-government sourced funds, social participation, and others. The category of Other Revenues can consist of grants, donations, and third-party partnerships.

More than 90% of villages' revenue comes from transfers from a higher-level government, and the Village Fund alone contributes more than 50% of their total revenue. Other sources of transferred revenue are:

• Village-Allocated Fund, which is taken from a minimum of 10% of the district's share of General Transfer.

4Law No. 6/2014 page 41.

This contributes to 20%-40% of village revenue.[5]

- Revenue sharing from the district government, which is taken from 10% of the district's tax and levy revenue. This contributes to less than 5% of village revenue.
- Financial assistance from the district or province governments. The amount and occurrence of financial assistance is ad-hoc, and comprises less than 3% of village revenue.

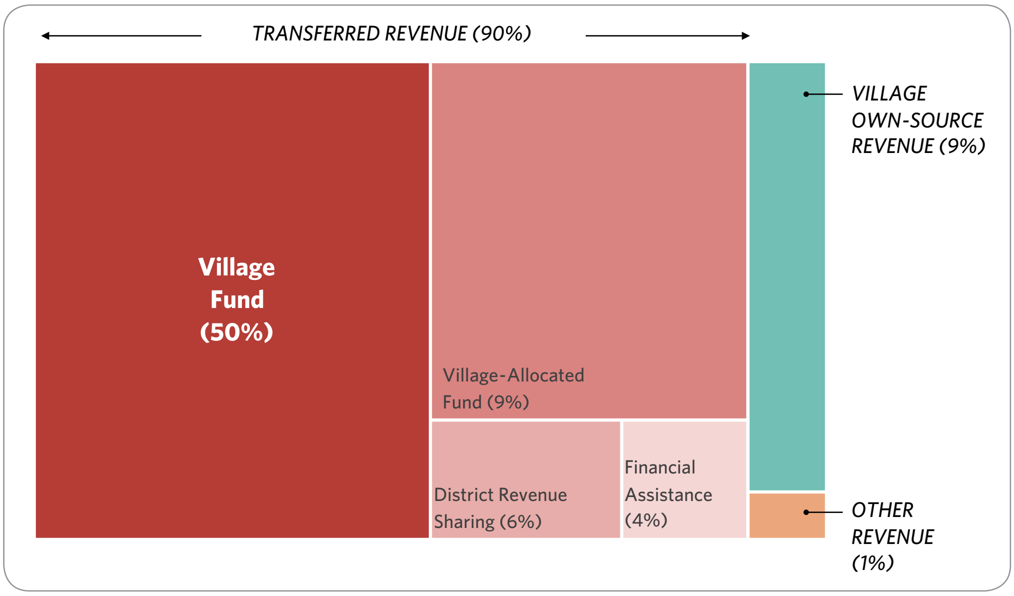


Table 1. Sources of village's revenue from central government transfers

TRANSFERRED REVENUE IN VILLAGE BUDGET (APBDES)	SOURCE	% TO VILLAGE REVENUE
TOTAL REVENUE FROM TRANSFER		> 90%
Village Fund	Maximum of 10% of total central-to regional fiscal transfer	> 50%
Village-Allocated Fund	Minimum of 10% of General Transfer (Revenue Sharing + GAF) received by the districts	20 - 40%
District Revenue Sharing	10% of district's tax and levy revenue	< 5%
Financial Assistance from district or province	Ad-hoc, depends on the district or province	<3%

The Village Fund allocation formula is designed to achieve equity and equality, with a current focus on poverty alleviation.

The Village Fund is distributed based on a formula meant to fulfill the principles of equity and equality. Figure 4 describes the Village Fund formula.

The total amount of the Village Fund is calculated as 10% of the aggregate central-to-regional fiscal transfers comprising of General Transfers, Specific Transfers, and the Regional Incentive Fund. The 10% is given on top of, instead of taken from, the central-to-regional transfer allocation. The Government is still working towards fulfilling this goal of 10%, having recently managed to reach 8.3%. This amount is then divided into two categories: the Basic Allocation and the Formulated Allocation.

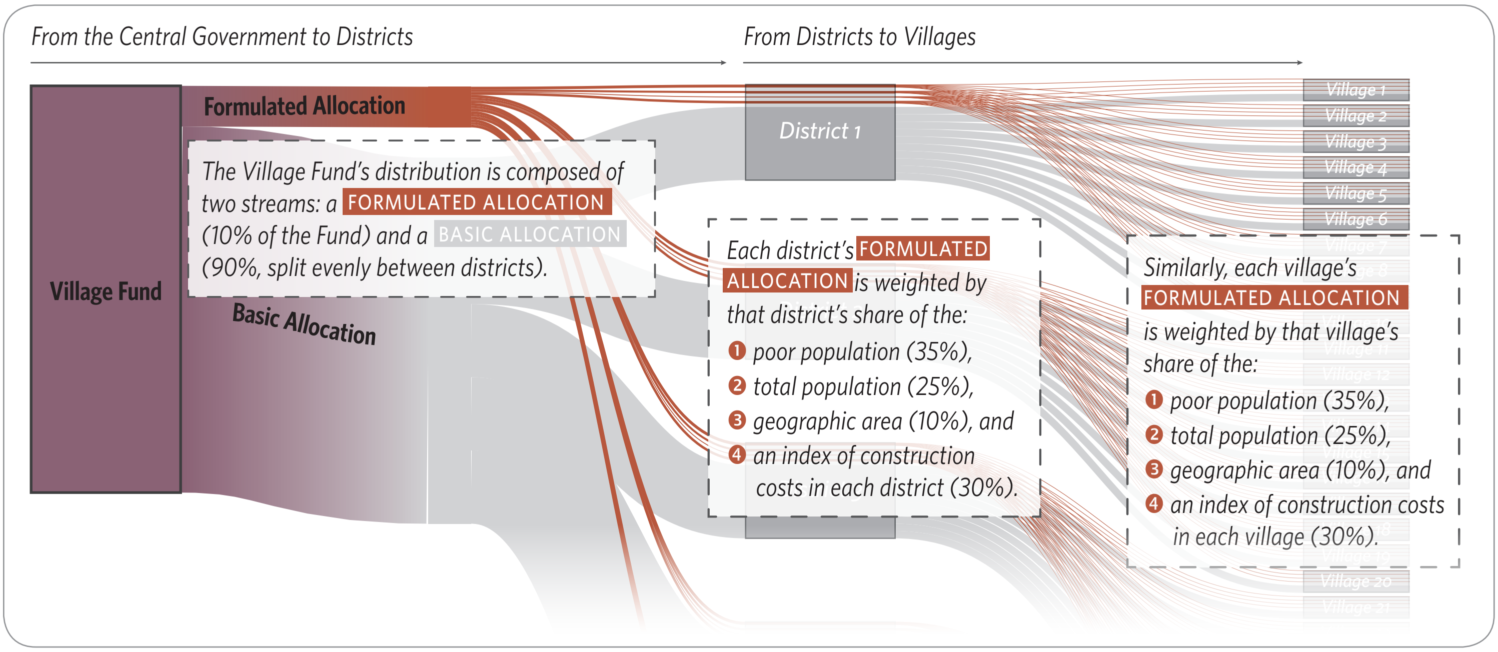
The Basic Allocation currently equals 90% of the Village Fund and is given in equal amounts to all villages nationally, based on a principle of equality. The remaining 10% is the Formulated Allocation, which is distributed based on weighing several unique characteristics of each particular village: population (0.25 weighted), percentage of people living in poverty (0.35), size of the area (0.1), and construction cost index (0.3). This formula is mandated under the equity principal to reduce the development gap between the weakest and the strongest village recipients.

The composition of Basic Allocation and Formulated Allocation can be revised by the Ministry of Finance, to be implemented in the following fiscal year, but the basic principles remain the same.[6] In fact, the Ministry of Finance has recently issued a regulation changing the Village Fund formula starting in 2018. The changes can be seen in Figure 5.

5 Village-Allocated Fund or Alokasi Dana Desa has a similar name to the Village Fund or Dana Desa, yet they are different: VF is calculated from a maximum 10% of the total national fiscal transfer and allocated by specific formula to the villages through districts. The VAF is calculated from a minimum 10% of district's share of General Transfer (Revenue Sharing plus General Allocation Fund). In VAF, the Revenue Sharing and GAF are given to the districts first using their own formula, districts then retain the authority in determining the allocation to the villages.

6 In 2018, Ministry of Finance is planning to change the Village Fund composition by adding Affirmative Allocation (3%) for the lagging regions and enlarging the Formulated Allocation to 20%, while reducing the Basic Allocation to 77%. There is also a plan to change the weight used in the Formulated Allocation so that it may reward more funds to villages with large number of poor populations.

Figure 4. Village Fund Formula



These changes are made effective through amendment by the Ministry of Finance, and it shows that the Village Fund can be quite responsive to adjustments in order to better achieve the fund's goals.

In this case, the main reason for the formula change is to hasten poverty eradication in the poorest villages. The Ministry of Villages recorded that 46% of villages (approximately 33,000 villages) are still categorized as "lagging," and that 18% (approximately 13,000 villages) are categorized as "extremely lagging." These villages are mostly found in Papua and/or West Papua provinces, with indications that they may need a larger Village Fund allocation before they can improve their economy.[7]

The new formula now has a stronger focus on poverty eradication, as can be seen from the new allocation of a 3% "Affirmative Allocation" exclusively for lagging villages, and the increased strength of the "poor population" variable from 35% to 50%.

The formula prior to 2018 yielded a disbursement of Village Funds with a distribution ratio of 1:4, meaning that the recipient getting the largest share of funds received four times more than the recipient getting the smallest share of funds. After the formula change, villages most in need received a noticeable preferential gain at a ratio of 1:2 and 1:4. This means that lagging villages received two times more, and extremely lagging villages received four times more, than villages receiving the smallest share of funds.

The Village Fund is accessed from bottom-up and disbursed from top-down

The process of accessing the Village Fund typically occurs through a bottom-up approach, with administrative requirements flowing from village to district, district to central government.

In order to be eligible to access the Village Fund, village governments must submit their annual village budget for the first disbursement cycle at the beginning of the calendar year, and then submit quarterly progress reports on Village Fund spending for subsequent disbursement cycles within the year.

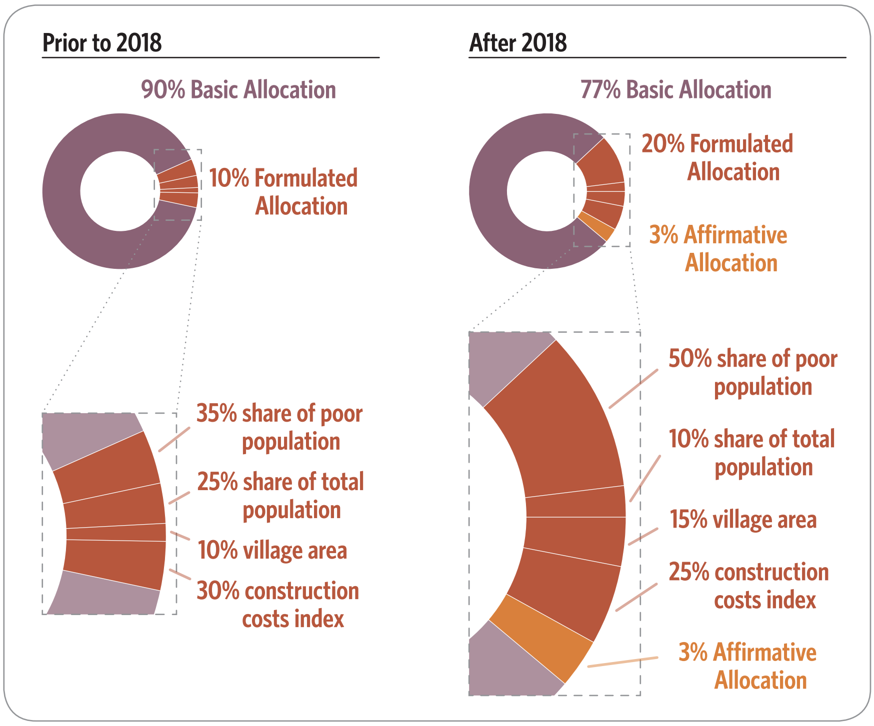
The district government then consolidates the reports and budgets from every village under its jurisdiction and submits them to the central government to obtain allocation for the Village Fund.

After being cleared, the Village Fund is disbursed top-down, from the central government to the district government every three to four months, which, in turn, makes the transfer to the villages.

7 Ministry of Villages classifies villages in Indonesia into 5 categories; Developed, Progressing, Developing, Lagging, Extremely Lagging. The classification is based on Village Development Index established by the Ministry. The Index is composed from three sub-index; Social Resilience, Economic Resilience, and Environmental Resilience. The indicators used to build the Index is taken from Village Potential Survey conducted by government agency, Statistics Indonesia. Lagging and Extremely Lagging Villages usually have very low Economic Resilience sub-index.

Transfer of the Village Fund from the national budget to the district budget reached 100% and 91.9% in 2015 and 2016, respectively. Despite the high rate of transfers, the process of mobilizing funds from the central government to the village governments often face significant delays. An evaluation carried out by the Ministry of Finance suggested that the delays are mostly related to difficulties in consolidating financial reporting at the district level, and delays in ratifying the Village Budget at the village level. Delays might be improved over time as officials become more accustomed to reporting requirements, or better support is provided to train officials at financial reporting.

Figure 5. Village Fund Formula Changes in 2018



3.3 Village Fund: Priorities and Usage

For the purpose of this study, we observed the national average of village fund distribution, as well as the degree to which the Village Fund is utilized at the sub-national level, specifically in three districts: Katingan and Kotawaringin Timur in Central Kalimantan province, and Berau in East Kalimantan province.

The budget allocation for Village Fund continues to increase

Since becoming operational, the fund's budget has almost tripled in size, from IDR 20.7 trillion in 2015 to IDR 60 trillion in 2017, and is expected to increase even further in the coming years, as it has yet to reach the mandated allocation of 10%.

In the three districts we observed for this study, the villages in Berau—and East Kalimantan in general—received slightly above the average across all years. The district has discretion to provide a larger proportion of village transfers in general.

Each of the three districts has hundreds of villages, which would explain why each village receives approximately 1% of the total Village Fund received by the District Government. Although the percentage seems small, the amount represents a significant source of funding for villages. When the Village Fund was established in 2015 it provided 36% of village revenue (with a national average of USD 21,500). Now, in 2017, the amount has increased three-fold to USD 59,692, contributing 55% to village revenue. Given the importance and strategic position of the Village Fund, it is vital that the Central and District Government enact a good structure to ensure effective utilization and timely delivery of the Fund, as well as to impose accountability for all stakeholders involved.

The Village Fund is mostly spent on infrastructure, though opportunities exist to spend it on environmental management

The main categories of Village Fund utilization are to support village administration, village development, community development, and community empowerment. Currently, the Government is encouraging village officials to prioritize Village Fund spending for village development and community empowerment.

Table 2. Increasing Budget for Village Fund

YEAR	AMOUNT (USD BILLION)	% TO TOTAL TRANSFER	NUMBER OF VILLAGES	AVERAGE RECEIVED BY VILLAGE (USD)
2015	1.6	3.4%	74,093	21,538
2016	3.6	7.0%	74,754	48,000
2017	4.5*	8.3%	74,910	59,692
2018	4.6**	7.9%	74,958	61,538

*) Outlook 2017, **) RAPBN 2018. Source: Nota Keuangan RAPBN 2018

Table 4. Increasing Village Fund allocated to villages located in the three observed Districts (IDR billion)

DESCRIPTION	2015	2016	2017
TOTAL VILLAGE FUND ALLOCATED TO DISTRICT			
KATINGAN	42.7	95.7	121.7
KOTAWARINGIN TIMUR	46.9	105.0	133.8
BERAU	28.7	66.0	84.1
AVERAGE FUND RECEIVED PER VILLAGE			
KATINGAN	0.28	0.62	0.79
KOTAWARINGIN TIMUR	0.28	0.63	0.80
BERAU	0.29	0.66	0.84

Village Development activities, including improvements to roads, bridges, irrigation systems, ports, etc., represent the largest use of the Village Fund, committing 82.2% in 2015 and 89.8% in 2016. Despite also being a priority, not as much has been spent on Community Empowerment.

By law, the Village Fund can be allocated towards resource management, economic development, and/or environmental protection. But in reality, the Village Fund has mostly been used for infrastructure development so far.

The table below shows that by law, the four major categories of Village Fund priorities are actually divided into many items of eligible activities, which include a wide range of resource management, economic development, and environmental protection items. Despite this, the Village Fund has almost exclusively been used for transportation infrastructure so far.

Most noticeably, in the villages we have observed within the scope of this study, the Village Fund has not been used forinfrastructure for environmental conservation, infrastructure for agro-industry, nor supporting conditions for environmental conservation.

The high percentage of Village Fund utilization on transportation, compared to other potential uses, is not unexpected. Problems with road connectivity, or the lack thereof, in many regions in Indonesia, specifically those outside of Java, often hamper regional economic development. However, high spending on transportation is expected to plateau over time as public facility needs are met and villages will likely shift focus to other kinds of development.

Infrastructure is also a relatively tangible expenditure compared to community empowerment. There are no detailed guidelines from the central government on the processes that village governments can follow in allocating and prioritizing its village fund resources. These factors may explain why most village governments prioritize spending on infrastructure development.

As we will discuss in the next chapter, a lack of technical guidelines and challenges in understanding the Village Fund allowed utilization hampers initiatives to use it for environmental protection or natural resource management.

3.4 Challenges in Supporting Sustainable Land Use

Our findings indicate that there are various challenges in supporting sustainable land use effectively, including capacity problems, limited guidelines, and a lack of cohesion regarding Village Fund use within district planning.

Planning and Fund management challenges at the village level

Village governments are responsible for preparing and executing development plans every five years. During this process, village governments have a high degree of flexibility and independence in determining the most appropriate activities that should be included in the plan. Village development plans directly impact how the Fund is prepared, allocated, and spent.

The main village authority with influence over Village Fund management is the Village and Community Empowerment Office (Dinas Pemberdayaan Masyarakat dan Desa). Its role is to provide guidance, coordination, facilitation, and recommend technical policies to implement village development programs. Their role can support all kinds of village development program sectors, including economic empowerment, natural resource and technology utilitzation, community participation, and others.

However, according to our interviewees, the role of the Village and Community Empowerment Office has been limited to administrative facilitation. In practice they have not been involved much in substantive decision-making, let alone providing guidance on what kind of programs the village could its Fund on.

Table 3. Uses of Village Fund

PROGRAM	ELIGIBLE ACTIVITIES BY VILLAGE MINISTRY REGULATION	AVG. SHARE IN OBSERVED VILLAGES (NATIONAL AVG, 2015-2016)	EXAMPLES OF USES IN OBSERVED VILLAGES:
I. VILLAGE ADMINISTRATION NON-PRIORITY	Unregulated	**5.5%** (5%)	salary and operations
II. VILLAGE DEVELOPMENT PRIORITY	Infrastructure development for: 1. settlement environment 2. transportation 3. energy 4. information and communication 5. basic community health 6. basic education 7. agro-industry 8. disaster management 9. environmental conservation 10. other village infrastructure	**89%** (89%)	75% access road to village port and casting of retaining wall, development and improvement of village road (2. transportation) 14% water supply (5. basic community health)
III. COMMUNITY DEVELOPMENT NON-PRIORITY	Unregulated	**-** (7%)	
IV. COMMUNITY EMPOWERMENT PRIORITY	Community empowerment activities, including: 1. participatory village development 2. capacity development 3. community resilience 4. village information systems 5. support for basic social services 6. support for environmental conservation 7. support for disaster management 8. village enterprise development (BUMDES) 9. community economic development 10. village partnerships 11. other community empowerment activities	**5.5%** (3%)	5.5% capital investment to BUMDES (8. village enterprise development)

Source: Directorate General of Fiscal Balance, Ministry of Finance, 2016.

Lack of capacity and capability

Our observations indicate that village governments' technical capacity and planning experience is a significant factor in determining whether sustainable land use activities are included in the village development plan, and Village Fund utilization. Interviewees described the Village Fund paperwork as burdensome for an already limited number of village officials. Meanwhile, village officials often lack sufficient planning and budgeting skills.

In addition to capacity problems, human resource availability to support village governments is often inadequate to perform the high workload associated with managing the Village Fund. For example, on average, villages in Katingan are supported by only four or five village officials, and while technical assistance was available for certain villages, it was mostly related to performing administrative tasks, rather than planning and fund management.

Hesitant to break out of the mold

Because the governance system currently lacks human resource capacity and experience, village governments tend to focus Fund spending on a limited number of activities that utilize large amounts of financial resources (i.e. infrastructure development), rather than spreading the allocation into more activities that are less capital-intensive (i.e. environmental protection, agricultural productivity improvement, etc.).

As such, Fund support for environmental protection activities is not significant in portion. Our interviewees described the use of the Fund for environmental protection in limited cases only, mostly focused on forest fire suppression. However, even in these instances, the activities carried out are often to control small fire incidents before they spread to forest areas, rather than preventative measures, such as re-wetting peatland.

Limited regulatory basis and technical guidelines on the use of Village Fund

One role of district government in deploying the Village Fund is to translate the policies and directions provided to the village government by the national government.

However, in the three districts we observed, we found no detailed guidelines or regulatory basis for village governments to perform the allocation, planning, and disbursement of the Village Fund. This means village governments often have no reference to whether certain activities are eligible to be included in the planning and budgeting for the Village Fund, and consequently, are unable to fund these activities, many of which are related to sustainable land use.

The lack of technical guidelines was found to be a particular problem in Kotawaringin Timur. Historically, the Village Fund in that district was used to finance infrastructure development such as roads, bridges, irrigation facilities, and safety equipment. Recently, activities to support economic development through alternative income activity, such as agricultural productivity and waste management, are beginning to emerge. However, many villages are hesitant to scale-up these types of activities as they are not specifically backed by any regulation or technical guidelines.

Village Fund priorities are not always in harmony with district planning

In all of the observed districts, our analysis suggests that Village Fund utilization priorities are not always in harmony with priorities set during district-level planning, which has more comprehensive objectives and targets, including those of environmental concerns.

There are a couple of factors contributing to misaligned priorities between the Village Fund and district planning.

First, the Village Fund is a relatively new fiscal instrument that in many ways lies outside of what has traditionally been considered central-to-regional fiscal transfers. The process of accessing district funds and village funds are completely different, completely separate, and, therefore, has no perceptible influence on one another.

The district's mid-term development plans (*Rencana Pembangunan Jangka Menengah Daerah* or "**RPJMD**") are comprised of goals and targets that are more comprehensive than the village mid-term development plans (*Rencana Pembangunan Jangka Menengah Desa* or "**RPJM Desa**"), or its derivative village development work plans (*Rencana Kerja Pembangunan Desa* or "**RKP Desa**"). In the districts we observed, these village planning documents are often not harmonized with the district level planning documents. Literature studies reveal that some villages have started to harmonize their plans with the district's plans, but, again, most of these villages are in Java.

Consequently, the preparation of village development plans do not need to take into account the larger goals set by the district government, which may include environmental goals. Inversely, the process of carrying out, planning, and preparing a budget at the district level also does not take into account the plans and budget prepared by the villages. It is also plausible that certain items in the district budget are identical to those found in the Village Fund budget, yet the central government still allocates funds for both. Second, we also found that there is a lack of coordination between the village government and district government when it comes to planning, monitoring, and evaluating the process of the Village Fund implementation. For example, our observation suggests that the District Planning Office of Katingan plays a limited support role in village planning activities. This means that the Planning Office has little opportunity to provide input and guidelines, as well as to ensure that the critical aspects in the district planning, which often include environmental protection aspects, are properly translated into action plans at the village level. This problem is exacerbated by the District Planning Office's limited presence in the monitoring and evaluation process of the Village Fund implementation, further hampering any opportunity to improve the effectiveness of spending.

Regulatory support for budgeting more advanced programs is lacking

As part of this study, the Center for Climate Finance and Multilateral Policy of The Ministry of Finance (PKPPIM), supported by Climate Policy Initiative (CPI) led a workshop that discussed the latest challenges in using the Village Fund to support environmental protection and natural resources, including land management. The workshop included the Directorate General of Fiscal Balance of the Ministry of Finance, Civil Society Organizations, donors, and research institutes working on the Village Fund.

The Ministry acknowledged that while it is entirely possible to allocate the Village Fund to support sustainability, there is a lack of regulatory support in clarifying the use of the Village Fund for sustainable development purposes, or even for some economic development programs.[8]

PKPPIM also identified that village officials might find it difficult to report which category of spending their activities fall under, when they move into more advanced programming in using the Village Fund. This reflects an overall challenge, which is that budget reporting requires a level of experience that villages may not be well-equipped to handle yet. In order to address this issue, the Ministry of Finance anticipates the need to involve not only the Ministry of Villages, but also the Ministry of Home Affairs as the main authority in ensuring budget reporting lines are kept up to date with the types of activities conducted by villages, and that villages are aware of how to use them.

8 CPI and Rare found similar desire from villages in using Village Fund to control price volatility in agriculture and fishery produces, especially during harvesting season. However, these initiatives are not yet applied due to lack of confidence over the legal basis.

4. Opportunities for Village Fund governance to support sustainable land use

Our analysis finds that there are opportunities to strengthen the Village Fund governance to support sustainable land use activities. These opportunities exist on a sliding scale, beginning with interventions that are implementable within the village jurisdiction, and progressing to those that will require the involvement of the central government.

1. Integrate Village Fund priorities into district planning

The Government of Indonesia has issued Ministry of Home Affairs (MoHA) Regulation No. 114/2014 on Village Development Guidelines, which aims to synchronize development planning between village and district.

However, while village development planning is governed by this regulation of the Minister of Home Affairs, the Village Fund use is governed by a regulation of the Minister of Villages. The two regulations are not in sync with each other.

To alleviate the discord, regional governments can develop brief guidelines to integrate the two regulations in a simpler and more comprehensive way.

The main authority that could lead such a task is the Regional Planning and Development Body (*Badan Perencanaan Pembangunan Daerah* or "**Bappeda**"). The Bappeda as the main regional planning authority needs to be more involved in improving how the Village Fund can be used to achieve district and village development goals.

We found two examples where districts are attempting to synchronize village planning and Village Fund utilization, however both examples are in Java. The Governments of Gunung Kidul District in Yogyakarta and Kebumen District of Central Java, assisted its village governments' annual planning process in accordance to District's annual planning (Zamroni et.al. 2015). A more prominent example is the Magelang District Government in Central Java, which worked to synchronize villages' medium-term development plan with the District's medium-term development plan.[9]

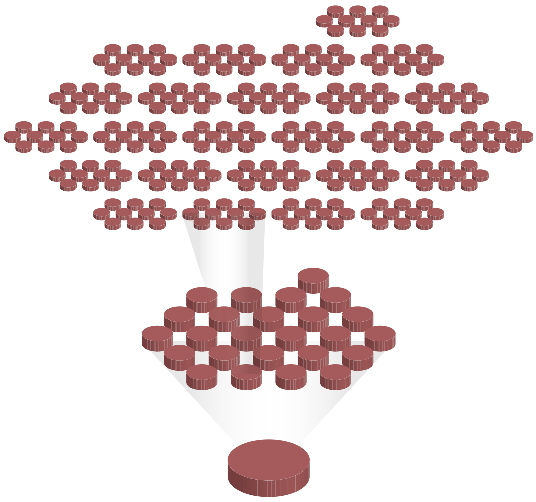
There are two things that these villages in Java did. First, they synchronized the District Mid-Term Development Plans (RPJMD) with the Village Mid Term Development Plans (RPJM Desa). Second, they synchronized the Village Work Plans (RKP Desa) with the District Work Plans (RKPD). Our analysis suggests that integrating the Village Fund plan into district development plans would provide significant benefits to improve the Village Fund's effectiveness. This integration would ensure that Village Fund spending priorities are always aligned with the sustainable development goals and priorities set by the district. In addition, this would ensure budget efficiencies by avoiding double allocation of funds for identical activities covered separately in the village and district plan. Of course, there will still need to be safeguards to ensure that villages retain their autonomy and independence in utilizing the funds.

Streamlining the Village Fund into district planning would also help to develop better bureaucratic coordination between the district government and the village government. This means that the preparation of the district plan will have to be slightly altered, as it needs to consider and consolidate the Village Fund spending plan. Consequently, this must lead to a process where the districts' planning office and other technical offices collaborate, providing inputs to one another, and coordinating each office's responsibility in making sure that Village Fund planning is aligned with the district's planning. The synergy between district and village planning could also be improved by gradually giving the district governments discretion to distribute the Village Fund according to each village's condition. In order for such a policy change to happen, the district-to-village allocation must be standardized by a District Regulation and a Head of District Regulation in order to minimize the risk of misuse. Such practice has already been implemented for the Village-Allocated Fund, and therefore can reasonably be replicated for the Village Fund.

2. Optimizing the role of Village and Community Empowerment Office

We found that the limited technical capacity of village government officials is a recurring problem in the implementation of the Village Fund policy. This is especially true for villages in the preparation of their spending plans and regular reports, both of which are requirements to access the Village Fund. This issue could potentially become a serious threat if the Fund

9 Medium-term development plan is a five-year term planning document that becomes the basis of the government's program and budget. It is a 'must have' for all levels of government and it is the most solid planning document for a government.



Village level:	1. **Integrate village priorities** into district planning
District level:	2. **Maximize the Village Empowerment Office**
	3. **Create village guidelines** for sustainable land use activities
	4. **Focus on negative-list** for village fund spending
National level:	5. **Add sustainability variable to village fund formula**

continues to increase, and the requirements imposed for accessing it becomes more stringent.

Our analysis finds that villages face particular challenges in planning and budgeting when they start to incorporate more elaborate programs, such as in economic development, community empowerment, and natural resource management. This includes land use and environmental protection (e.g. forest fire prevention and suppression).

The Village and Community Empowerment Office, as the main village authority to provide facilitation and support to village development planning and program implementation, holds promise in this regard. Their role should be fulfilled to its maximum potential by empowering them to provide substantive technical assistance in planning, budgeting, and financial reporting. They also hold authority to guide and facilitate the creation of more village programs on sustainable development and environmental protection.

3. Create village-level guidelines to encourage sustainable land use activities

We found that, although the Village Fund provides room for spending on environmental conservation, the villages we observed are simply not utilizing the Fund for that purpose. Transportation infrastructure is dominating spending, while other important environmental management infrastructures are not prioritized. It is not enough to allow spending on environmental management, there must be specific encouragement through technical guidelines which serve as a reference when making Village Fund spending decisions. This will enable Villages to confidently spend on activities that support sustainable land use.

The guidelines used by villages do not currently provide information that is sufficient for village government to support sustainable land use activities, as they are often not explicitly mentioned in the guidelines.

Our observations in the district of Kotawaringin Timur show that the lack of technical guidelines on Village Fund utilization is contributing to the lack of activities supporting sustainable development. While infrastructure dominates the use of the Village Fund, activities to increase agricultural productivity and waste management are not getting enough funding. This is because there are no technical guidelines explicitly stating that those activities fulfill the requirement of being funded by the Village Fund.

These guidelines can be developed in the form of district-level regulations, which can then serve as a basis for the village government to make planning and spending decisions. Therefore, the guidelines should also be able to translate the policies issued by the Ministry of Villages into priorities and action points that are still consistent with the district's development objectives.

4. Create a negative-list for Village Fund spending instead of a list of allowable activities

There has been an ongoing process within the Ministry of Finance to improve the Village Fund, and, more importantly, look at how it can be used to support environmental protection. CPI found that the existing guidelines relating to the priorities of the Village Fund are seen by village officials as limitations that do not allow room for innovation in setting up programs in their village.

Example of Village Fund Negative List

The regent of Berau in 2016 issued a circular on the technical guidelines of the Village Fund in 2017. Besides providing directives to refer to the Village Fund priority programs prepared by the Ministry of Villages, the regent also added guidelines on what the Village Fund should **not** be used for, as follows:

1. Building and maintenance of village government facilities such as Village Head Office, Village Conference Facility, Village Representative Assembly Office, and other offices.
2. Building and maintenance of religious facilities.
3. Charity in the form of social, financial aid or grants directly to communities not part of a business organization.
4. Religious days or national day ceremonies.
5. Competitions or prizes.
6. Operational support items such as stationery, official travels, meeting consumption, honorariums, which are not relevant to the development and empowerment activities.
7. Activities that are supposedly covered by village operational budget such as goods/services procurement.

Instead of having a long list of allowed activities, which is often perceived literally by the villages, the Ministry of Finance, together with the Ministry of Villages, should create a '*negative list*' consisting of a few activities that are absolutely prohibited when using the Village Fund. This practice has been done in Berau and could be replicated elsewhere (see Box insert).

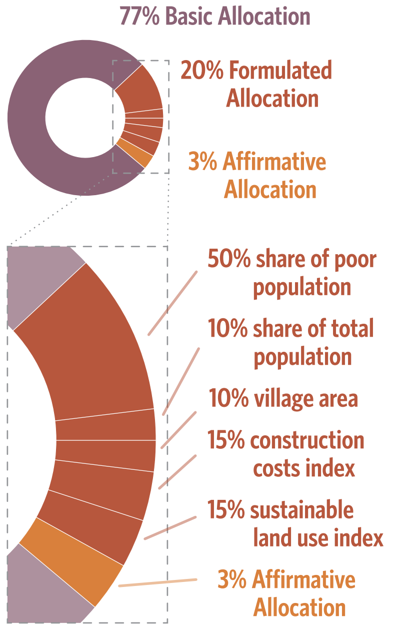
The '*negative list*' could help reduce the misinterpretation that usually occurs during process planning, and provide freedom for villages to design the most needed or best-suited programs in their own village.[10]

5. Add a sustainability variable to the Village Fund formula

The Village Fund formula has been changed recently to improve its potential to achieve government priorities, which in the current case is to close the gap between the poorest and more well-off villages. This provides an important precedent, as it shows the Village Fund may be able to accommodate a new sustainability variable in its formula, should the government wish to prioritize environmentally sustainable villages.

The challenge with this is that there is not yet any defined indicator for sustainable land use. Unlike welfare indicators, such as the percentage of population below the poverty line, sustainability indicators can be a variety of things and may even differ from one village to the next.

Recommended Alternative



10 Climate Finance Unit, Ministry of Finance expressed their preference for this recommendation, given that similar approach has been applied in other sectors, and saw its feasibility according to Ministry of Finance's jurisdiction.

For example, using "forest coverage" as a sustainability indicator may work for villages that naturally have a forest cover, but will not be applicable to villages that do not. This may be viewed as unfair to villages with a different natural resource profile. On the other hand, the recent formula change has carved out a specific percentage of the Village Fund (3%) to be allocated exclusively for villages that are still lagging. The same might be done for villages that are in dire need of protecting their forests, and do not have the resources to do so.

The possibilities of having a specific indicator, or perhaps even an index, that can be inserted into the Village Fund formula to push villages towards sustainable land use practices, are possibilities that merit further study. CPI will be exploring this in more detail in follow-up studies.

5. Conclusion

This study looks into how the Village Fund, a government transfer instrument dedicated to the village level, is governed, as well as its organization from a macroeconomic fiscal policy perspective, its allocation, and its distribution. This study also analyzes its current progress and the challenges met in utilizing the Village Fund to finance wider economic development and environmental protection programs in Indonesia's villages.

Indonesia's central government has committed to improve each regions' ability to finance their development by increasing the amount of fiscal transfer to the regional level. Over the last three years, this has been done by increasing the allocation for specific fiscal transfers or by creating new transfers, and overall, gradually increasing the allocations to regions.

The Village Fund is an important fiscal transfer for both the central government and local governments. From the central government's perspective, it is evidence of the commitment to support development in villages according to their unique characteristics, and to further reduce the welfare gap between villages. On the other hand, the Village Fund is a major source of revenue for village governments, providing more than 50% of village revenue. Most of this revenue is being spent on infrastructure development, although, from interviews and literature review, we are also seeing villages with better infrastructure, mostly in Java, use the Fund to develop agriculture and land use management in their villages.

A bottom-up process in accessing the Village Fund, and increasing the allocation of the Fund, could provide more resources and improve Village Fund implementation towards sustainable land use. However that has not been the case yet, because there are several basic challenges in implementation:

- Village governments are finding it hard to plan, budget, and report on the use of the Village Fund. Our interviewees described the Village Fund paperwork as burdensome for an already limited number of village officials. Meanwhile, village officials often lack sufficient planning and budgeting skills.
- District governments are already preoccupied with the monitoring of administrative requirements submitted by the villages, with these activities taking valuable time and technical capacity. The time spent on administration work often means that officials are then not able to spend time on planning or guiding villages on how the fund could be used more effectively.
- Village Fund priorities are not always in line with the district's planning. We found potential budget overlaps in financing development programs. The district government can play a bigger role coordinating development priorities financed by district budgets and the Village Fund.

We also saw potential for improving the Village Fund in practice, especially if the villages are planning to use it for more developed programs:

- There must be strong regulatory support from the district that details the guidelines for Village Fund utilization. This is important to minimize the lack of clarity on the part of the village government when deciding what types of activities should be prioritized, and whether certain types of activities are eligible to be financed by the Village Fund.
- Integrating the Village Fund plan into the district development plan would provide significant benefits in improving its effectiveness. This would ensure that Village Fund spending priorities are always aligned with the development goals and priorities set by the district. This would also provide more substantial interactions between district and village governments, giving districts a better understanding of village's needs and development challenges.
- The district's Village Development Office must provide more practical technical assistance on planning, budgeting, and financial reporting.

The above opportunities are simple steps essential for improving Village Fund governance. They do not necessarily need to be implemented simultaneously, but can each help to synchronize different district government agencies and village governments' development efforts. More importantly, these steps will help to optimize the use of the Village Fund for improving the rural economy, reducing deforestation, and managing land use sustainably – ultimately helping to improve land use and economic growth at the local level.

6. References

Dixon G, Hakim D. 2009. Making Indonesia's Budget Decentralization Work: The Challenge of Linking Planning and Budgeting at the Local Level. International Public Management Review Volume 10 Issue 1.

Falconer A, Glenday S, Rosenberg A, Wilkinson J. 2014. Landscape of Public Climate Finance in Indonesia. Climate Policy Initiative. Available at: https://climatepolicyinitiative.org/publication/landscape-of-public-climate-finance-in-indonesia-3/

Gatra News. 2016. Article: "Presiden Jokowi: APBN2017 Masih Ekspansif, Defisit Rp 332,8 triliun". Available at: https://www.gatra.com/ekonomi/makro/211854-presiden-jokowi-apbn-2017-masih-ekspansif-defisit-rp-332-8-triliun

Government of Magelang District. No year. Sistem Perencanaan Pembangunan Desa. Presentation slide from Magelang District Development Planning Office. Available at: http://lp3m.ummgl.ac.id/wp-content/uploads/2016/10/BAPPEDA-SISTEM-PERENC-PEMB-DESA1.pdf

Haryanto J. 2016. Reformasi Dana Insentif Daerah. Online article. Fiscal Policy Agency, Ministry of Finance. Available at: http://www.weblama.kemenkeu.go.id/Artikel/reformasi-dana-insentif-daerah

International Institute for Sustainable Development (IISD). 2015. Tinjauan Subsidi Energi di Indonesia, Terbitan 1, Vol. 2, March 2015.

Mafira and Sutiyono, 2015. Improving Land Productivity through Fiscal Policy: A Framework for Analysis. Climate Policy Initiative. Available at: https://climatepolicyinitiative.org/publication/improving-land-productivity-through-fiscal-policy/

Ministry of Finance, Republic of Indonesia. 2017a. Nota Keuangan Beserta Rancangan Anggaran Pendapatan dan Belanja Negara Perubahan Tahun Anggaran 2017. Available at: http://www.anggaran.depkeu.go.id/content/Publikasi/NK%20APBN/2017%20NK%20RAPBNP%202017.pdf

Ministry of Finance, Republic of Indonesia. 2017b. Laporan Keuangan Pemerintah Pusat Tahun 2016 Audited. Available at: https://www.kemenkeu.go.id/media/5998/lkpp-2016.pdf

Ministry of Finance. 2016. Presentation slide: "Kebijakan Pengalokasian dan Penyaluran Dana Desa Tahun 2017". Presented in Jakarta November 21-24, 2016. Available at: http://www.djpk.depkeu.go.id/wp-content/uploads/2016/11/Paparan-Kemenkeu.pdf.

Purwiyanto. 2017. Presentation slide: "Kebijakan Pengelolaan Transfer Ke Daerah dan Dana Desa". Presented in Musrenbang Provinsi Kalimantan Timur on April 3rd, 2017. Ministry of Finance. Samarinda, East Kalimantan. Available at: http://datacenter.bappedakaltim.com/data/2017/list05/6%20Bahan%20Musrenbang%20Kemenkeu.pdf

Statistics Indonesia (BPS). 2017. Online Statistics Database. Table: "[Seri 2010] Laju Pertumbuhan Kumulatif Produk Domestik Bruto Menurut Lapangan Usaha (Persen), 2014-2016". Available at: https://www.bps.go.id/linkTableDinamis/view/id/1138

The World Bank. 2017a. Indonesian Economic Quarterly June 2017 Upgraded. Available at: http://www.worldbank.org/en/country/indonesia/publication/indonesia-economic-quarterly-june-2017

The World Bank. 2017b. Indonesian Economic Quarterly January 2017. Available at: http://www.worldbank.org/en/country/indonesia/publication/indonesia-economic-quarterly-january-2017

Zamroni S, Zainal A, Mariana D. 2015. Mengintegrasikan Perencanaan Pembangunan Desa. Policy Brief. Institute for Research and Empowerment. Yogyakarta. Available at: https://ireyogya.org/uploads/PB%20Mengintegrasikan%20Perencanaan%2009012015%20FINAL%20SIAP%20CETAK-2.pdf