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Fiscal Policy Law Reform Based on Distributive Justice to Reduce Economic Disparity and Improve People's Welfare

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Abstract: Fiscal policy is the main instrument of the state in realizing the goals of the state, including protecting the nation, advancing welfare, and realizing social justice as stipulated in Article 33 paragraph (1) of the 1945 Constitution. One of the important principles in fiscal policy is distributive justice, namely the proportional distribution of burdens and benefits to reduce economic disparities. This study aims to analyze the implementation of distributive justice in Indonesia's fiscal policy and assess the need for legal reform to increase its effectiveness. The method used is normative juridical with an analysis of laws and regulations, including Law Number 17 of 2003 concerning State Finance (Articles 2 and 21), Law Number 7 of 2021 concerning Harmonization of Tax Regulations (Articles 4 and 13), and Law Number 1 of 2022 concerning Financial Relations between the Central Government and Regional Governments (Articles 5 and 12), as well as the latest State Budget. The results of the study indicate that although the fiscal legal framework has supported equity, its implementation still faces inequality in budget distribution, low tax compliance, and less than optimal fiscal transfer effectiveness. This study recommends reforming fiscal law based on social justice, strengthening progressive taxation, increasing transparency in state financial management, and optimizing fiscal transfers to achieve equitable public welfare.

Keywords: Distributive Justice, Fiscal Policy, Economic Disparity, People's Welfare

INTRODUCTION

Increasing national economic disparities indicate that the distribution of wealth and opportunity is not yet balanced in Indonesia (Handini et al., 2025). Inequality between the western and eastern regions, and between high and low income groups, is an indicator of the weak distribution of development outcomes (Sugiastuti & Pratama, 2022). The economic structure, which remains concentrated in urban areas, creates disparities in productivity and income among rural communities (Yenny et al., 2025). This situation demonstrates that implemented macroeconomic policies have not fully addressed aspects of social justice oriented toward shared prosperity (Hafizd et al., 2024). This inequality also contributes to the emergence of social problems, such as structural poverty, disguised unemployment, and limited access to public services.

Fiscal policy plays a strategic role in addressing economic inequality and realizing social justice, as mandated by Article 33, paragraph (1) and Article 34 of the 1945 Constitution of the Republic of Indonesia (Prasetyo & Rakhmadian, 2021). The state is obliged to control sectors of production that are important to the people and utilize them to the maximum for the prosperity of the community (Triningsih, 2020). This provision emphasizes that fiscal instruments, through tax management, state spending, and fiscal transfers, are the state's primary tools for regulating the fair distribution of resources (Huda et al., 2024). The principle of social justice serves as a normative orientation in every economic policy, ensuring not only growth but also the equitable distribution of development outcomes (Merdiani & Ruslina, 2025). The equitable utilization of fiscal policy will ensure that all levels of society benefit from national development.

Legal reform of fiscal policy becomes a national urgency when existing provisions do not fully reflect the principle of distributive justice (Retnani et al., 2024). Existing regulations do establish a general framework for state finances, but they do not specifically address the equitable distribution of development benefits across all regions and groups. Some norms still tend to focus on macroeconomic stability and budget efficiency, rather than equitable distribution of outcomes. Legal reform is needed so that fiscal policy can balance economic growth and equitable distribution of public welfare. Policy revisions that place distributive justice as a primary principle are expected to strengthen the moral and legal legitimacy of state fiscal implementation.

The idea of distributive justice is rooted in Aristotle's idea, which emphasizes that justice means giving everyone according to their rights and contributions (Pratama et al., 2024). Justice is not synonymous with absolute equality, but rather proportionality that takes into account the circumstances and needs of each individual. In Aristotle's view, inequality is acceptable as long as it maintains social balance and the common good (Nusantara & Harahap, 2025). This principle is highly relevant to the public finance system, as fiscal policy aims to distribute resources fairly based on the abilities and needs of citizens (Lubis, 2024). Distributive justice is a fundamental value that guides the state in establishing proportional taxation and public spending policies.

Modern thinking on distributive justice was largely developed by John Rawls, who proposed the theory of "Justice as Fairness" (Prasetyo, 2022). Rawls asserts that justice must guarantee equal basic freedoms for all, but social and economic differences can only be justified if they provide the greatest benefit to the most vulnerable groups (Arianto et al., 2025). This principle is known as the difference principle, which positions distributive justice as a tool to correct structural inequality (Narwadi et al., 2025). In the state financial system, Rawls's view emphasizes the importance of progressive fiscal policy, for example, through progressive taxation and social spending allocation so that justice is not merely formal but also substantive (Habibi & Wulandari, 2025). These values form the ethical foundation for modern fiscal law oriented towards social welfare.

The application of the theory of distributive justice in state finances explains that every fiscal policy must consider the balance between state capacity and societal needs (Arifin et al., 2024). Taxes, as the primary source of state revenue, must be designed to be not only fiscal in nature but also serve as a redistribution instrument. Similarly, state spending must be directed towards reducing income inequality and strengthening access to public services. Distributive justice requires that every fiscal policy not impose a disproportionate burden on certain groups (Wulandari & Pramukty, 2025). This principle requires the state to be responsible for ensuring economic justice through a balanced tax system and budget management.

Fiscal policy, according to Law Number 17 of 2003 concerning State Finances, is regulated through Articles 2 and 21, which emphasize the government's role in managing state revenues and expenditures efficiently and responsibly. This provision demonstrates that fiscal management is a primary function of the state in maintaining economic stability and ensuring public welfare (Putra et al., 2025). State finances are not merely a technical instrument, but also a manifestation of the government's constitutional responsibility to realize social justice (Simatupang, 2021). The principle of distributive justice dictates that every fiscal policy must strike a balance between the interests of the state and the economic rights of the people. Public financial management that promotes equity is a concrete manifestation of the implementation of the values of Pancasila and the 1945 Constitution.

Fiscal policy has three main, interrelated functions: allocation, distribution, and stabilization. The allocation function emphasizes the efficient use of public resources for the benefit of the community. The distribution function emphasizes the importance of equitable distribution of development outcomes through taxation and state spending mechanisms. The stabilization function, meanwhile, plays a role in maintaining economic balance to prevent excessive inflation or deficits. These three functions complement each other and must be implemented in a balanced manner to achieve the goal of social justice (Britania et al., 2024). When the distribution function is neglected, economic growth tends to benefit only a few parties and widens the gap in social inequality.

Distributive justice, as a principle of fiscal law, is also closely related to the concept of the welfare state, which forms the ideological foundation of the Indonesian legal system. A welfare state places the state's responsibility not only as a regulator but also as an active actor in ensuring the welfare of all citizens (Pamungkas & Hariri, 2022). Article 33, paragraph (1) of the 1945 Constitution emphasizes that the economy is structured as a joint effort based on the principle of kinship. This principle implies that fiscal policy must be oriented towards collective welfare, not the interests of particular individuals or groups. Distributive justice is a measure of the state's success in carrying out its economic functions equitably.

Integrating the principle of social justice into national fiscal law and tax regulations is a crucial step in strengthening the legitimacy of the state's financial system. Law Number 7 of 2021 concerning the Harmonization of Tax Regulations stipulates a more progressive and equitable tax structure, but implementation still needs to be strengthened to ensure its benefits are felt widely. Establishing a fiscal policy that is responsive to the needs of the poor and underdeveloped regions will strengthen the state's role as a regulator and protector of social justice. This understanding emphasizes that fiscal law not only regulates the flow of state funds but also regulates the distribution of equitable values within the nation's economic life. The principle of distributive justice must continue to be used as a guideline in designing fiscal policies that favor the welfare of the people.

METHOD

The method applied in this journal is a normative juridical method with a statutory approach and a conceptual approach. The statutory approach is used to examine various positive legal provisions governing state fiscal policy and their relationship to the principle of distributive justice. The analysis is conducted on legal norms contained in the 1945 Constitution of the Republic of Indonesia, specifically Article 23, Law Number 17 of 2003 concerning State Finance, Law Number 1 of 2022 concerning Financial Relations between the Central Government and Regional Governments, as well as implementing regulations related to fiscal policy, such as the Regulation of the Minister of Finance. This approach aims to understand the extent to which applicable legal norms provide a framework for distributive justice in the management of state fiscal resources. Meanwhile, the conceptual approach is used to examine legal and economic theories on distributive justice, including classical thought such as the theories of justice of John Rawls and Aristotle, which emphasize the balance between rights and responsibilities in the distribution of public resources. This approach helps to examine the relationship between the concept of social justice in Article 33, paragraph (4) of the 1945 Constitution, and modern fiscal policy oriented towards the welfare of the people. Through a combination of these two approaches, this study seeks to identify normative and conceptual gaps in the implementation of fiscal policy in Indonesia and to formulate recommendations for legal reforms that are based on distributive justice.

RESULT AND DISCUSSION

Regulation and Implementation of Fiscal Policy in Indonesia

Fiscal policy in Indonesia is based on the 1945 Constitution of the Republic of Indonesia, which affirms the state's role in regulating the national economy for the greatest prosperity of the people, as stipulated in Article 33 paragraph (1) and Article 34 paragraph (2). State financial regulation is intended not only to maintain macroeconomic stability but also as a means of realizing social justice. The Constitution mandates that the state control vital sectors of production and manage natural resources for the welfare of the people. This principle serves as the philosophical foundation for fiscal policy, which demands the equitable distribution of resources and income between regions and social groups.

The primary legal framework for fiscal policy is established through Law Number 17 of 2003 concerning State Finances. Article 2 explains that state finances encompass all state rights and obligations that can be valued in money, including assets managed by the central and regional governments. Meanwhile, Article 21 emphasizes that the State Budget (APBN) is prepared based on a performance approach to achieve efficiency and effectiveness in the use of public funds. These norms confirm that the function of fiscal policy is not merely a technical accounting exercise, but rather a public policy oriented towards the welfare of the people. The principles of transparency, accountability, and fairness are fundamental values in every state's fiscal decision-making process.

The enactment of Law Number 1 of 2004 concerning the State Treasury strengthens the governance of the State Budget (APBN) as a fiscal policy instrument. This regulation governs the mechanisms for budget planning, implementation, and accountability, including the position of the state treasurer and the legal responsibilities of budget-using officials. Through this regulation, fiscal policy is directed so that the budgeting process not only meets the principle of legality but also ensures the effectiveness of public spending for the benefit of the wider community. Efficient management of state finances reflects the government's constitutional responsibility to the people.

A major reform occurred with the enactment of Law Number 1 of 2022 concerning Financial Relations between the Central Government and Regional Governments (HKPD Law), which replaced the previous fiscal balance system. Article 106 of the HKPD Law emphasizes that Transfers to Regions (TKD) are an instrument to reduce fiscal disparities between regions and improve the quality of public services in the regions. This law defines several components of the Regional Revenue Sharing Fund (TKD), including the Revenue Sharing Fund (DBH), the General Allocation Fund (DAU), the Special Allocation Fund (DAK), the Special Autonomy and Privileges Fund, and the Village Fund, as outlined in Article 1, points 38–42. This new system provides a formula for calculating the DAU based on the fiscal gap (Articles 124–129), the DBH based on resource receipts and performance (Articles 110–123), and the DAK based on national priorities (Article 131). This legal structure demonstrates that fiscal policy is normatively directed to uphold the principle of distributive justice between regions.

The integration between the State Finance Law, the State Treasury Law, and the HKPD Law reflects a hierarchical and complementary state financial legal system. The State Finance

Law provides the principal basis, the Treasury Law regulates the technical implementation mechanisms, and the HKPD Law ensures fiscal balance between regions. This integration reflects the application of the principle of lex specialis derogat legi generali, where the HKPD Law serves as a special regulation that regulates central-regional fiscal relations in greater detail. This legal relationship demonstrates that fiscal policy does not stand alone but is part of the national legal system, oriented towards equitable distribution of public welfare, as mandated by Article 33 of the 1945 Constitution.

Taxes are the primary instrument of fiscal policy in realizing distributive justice. Law Number 7 of 2021 concerning the Harmonization of Tax Regulations (HPP Law) introduces several fundamental changes to the national tax system. Article 4 of the HPP Law regulates progressive Income Tax (PPh) rates by increasing the highest taxable income layer by 35% for taxpayers with incomes exceeding IDR 5 billion per year. This provision demonstrates the government's efforts to strengthen the principle of vertical equity, where citizens with greater economic capacity bear a higher tax burden. Furthermore, Article 13 of the HPP Law emphasizes tax administration reforms to improve compliance and broaden the tax base. The progressive taxation regulated by this regulation is a direct manifestation of the principle of distributive justice in fiscal law.

The second instrument is the Regional Transfer system, stipulated in Law No. 1 of 2022. Articles 124 to 129 govern the General Allocation Fund (DAU) mechanism, which aims to address the disparity in fiscal capacity between regions. The General Allocation Fund (DAU) formula is calculated based on fiscal needs and potential regional revenue. This model emphasizes the principle of proportionality in public finances, ensuring that all regions have relatively equal capacity to provide public services. Through this system, the state strives to create balanced development without compromising regional autonomy.

The next instrument is the Special Allocation Fund (DAK), as stipulated in Article 131 of the HKPD Law. DAK is provided to specific regions to support the achievement of national priorities established in the national medium-term development plan. DAK allocations are divided into physical and non-physical DAK, with physical DAK directed toward basic infrastructure development, while non-physical DAK is aimed at improving public services such as education and health. This provision emphasizes that the DAK allocation serves to address gaps in public services that cannot be covered by the DAU allocation. The primary objective of this regulation is to ensure balanced national development across Indonesia.

In addition to the DAU and DAK, Articles 110 to 123 of the HKPD Law regulate Revenue Sharing Funds (DBH) derived from tax revenues and natural resources. The Village Fund (DBH) is distributed to producing regions based on a specific proportion established by law to balance regional rights over the resources exploited within their territories. The DBH distribution mechanism aims not only to incentivize producing regions but also to strengthen the principle of horizontal equity between regions. This provision seeks to correct structural inequalities between resource-rich regions and those with less significant economic potential.

Fiscal redistribution policies are also implemented through the Village Fund, as stipulated in Article 134 of Law No. 1 of 2022. These funds are channeled directly into village accounts with the aim of supporting community-based economic development and strengthening local independence. The Village Fund scheme demonstrates the state's efforts to extend distributive justice to the lowest levels of government. This provision aligns with the spirit of Article 18B paragraph (2) of the 1945 Constitution, which guarantees recognition and respect for regional government units that are specific and local in nature.

The normative structure of Indonesia's fiscal policy reflects the spirit of distributive justice, but its implementation still faces various challenges. The realization of the General Allocation Fund (DAU) and Special Allocation Fund (DAK) often does not fully reflect the actual needs of regions due to limited data, weak planning capacity, and political interference in determining budget priorities. Although Article 106 of the Regional Allocation Fund (HKPD) Law emphasizes that the primary objective of the TKD is to reduce the fiscal gap, an evaluation of the implementation of the 2025 State Budget (APBN) shows that disparities between regions remain relatively high, particularly between provinces in Java and outside Java.

Taxpayer compliance also remains a serious obstacle to the effectiveness of fiscal policy. Although the HPP Law has strengthened the administration system and progressive tax rates, Ministry of Finance data shows that Indonesia's tax ratio remains below 11% of GDP, far below the average for developing countries. Low tax compliance limits the government's fiscal space to implement redistributive programs such as energy subsidies, social assistance, and public infrastructure development. The gap demonstrates that distributive justice in fiscal policy cannot be regulated normatively; it must be accompanied by effective implementation and strong oversight.

Another challenge arises in the effectiveness of fiscal transfers. Several regions still exhibit a high dependence on central funds and have not been able to develop their potential Regional Original Revenue (PAD) as mandated by Article 95 of the HKPD Law. This dependence creates imbalances in fiscal capacity and weakens the spirit of decentralization. The central government has responded to this situation through the Fiscal Incentive Fund policy, as stipulated in Article 108 of the HKPD Law, which rewards regions with good fiscal performance and public services. This incentive is expected to encourage efficiency and increase fiscal responsibility at the regional level.

Weaknesses in fiscal policy implementation are also evident in the low effectiveness of social spending and subsidies in reducing economic inequality. Many aid programs are not well-targeted due to inaccurate recipient data and weak inter-agency coordination. Yet, social spending plays a crucial role in upholding the principle of distributive justice mandated by Article 34, paragraph (2) of the 1945 Constitution. Budget management reforms must be directed at strengthening the poverty database, expanding the reach of productive assistance, and ensuring transparency in budget use so that the results truly impact public welfare.

Legal Analysis of Fiscal Policy Legal Reform Based on Distributive Justice

The norms in Law No. 17 of 2003 concerning State Finances contain the principle of justice and fairness in Article 3 paragraph (1), which requires the management of state finances to be orderly, in accordance with laws and regulations, efficient, economical, effective, transparent, and accountable, while taking into account a sense of justice and fairness. Although this principle is quite clear, the norm is still general and does not regulate in detail how distributive justice is realized between regions and between economic groups, especially regarding the structure of progressive tax rates, fiscal transfer mechanisms that are responsive to the needs of poor and disadvantaged regions, and minimum service standards. This limitation makes it urgent that fiscal norms in subsequent laws contain regulations that provide certainty for fair distribution. The Harmonization of Tax Regulations Law (Law on the Harmonization of Taxation Regulations No. 7/2021) introduced a progressive tax rate system (e.g., Article 17 of the Income Tax Law, which stipulates a tiered Income Tax rate for individual taxpayers) and the VAT regulation in Article 4 paragraph (2) of the Law on the Harmonization of Taxation Regulations, which increased the VAT rate from 11% to 12% no later than January 1, 2025. The policy demonstrates the intention of fiscal justice, but the VAT increase could have a regressive impact on low-income groups if not accompanied by adequate fiscal compensation or social spending policies. This gap demonstrates that norms alone are not enough; additional regulations must guarantee compensation or mitigation of the tax burden on vulnerable groups.

Law No. 1 of 2022 concerning Financial Relations between the Central Government and Regional Governments also contains articles aimed at improving fiscal distribution, but implementation challenges remain. For example, the methodology for calculating the General Allocation Fund (DAU) and Regional Revenue Sharing Funds (DBH) and the Special Allocation Fund (DAK) allocation mechanism have been updated, but their implementation in the field still shows inequality. Regional governments' ability to compile the necessary data, administrative capacity, and other technical constraints means that distribution does not always align with legal formulas. Regulations must be strengthened so that they are not merely paper norms but can be implemented accurately and fairly.

Fiscal centralization remains strong in several aspects of the central government, particularly in control of the Special Allocation Fund (DAK) spending mechanism and the allocation of development priorities. Although the Regional Development Planning Law (HKPD) grants greater autonomy to regions, the central government retains a dominant role in setting national priority programs, which often influence the allocation of physical and non-physical DAK. This imbalance between national policies and local needs creates tensions in economic equity. Moving forward, legal reforms need to clarify the division of authority so that regions have greater leeway in public budget planning based on actual needs.

Limited transparency and accountability remain major problems in Indonesia's fiscal policy. Public financial accountability reports are often late, regional public service reports are not always public, and poverty or basic needs data used in the DAU or DAK allocation formulas still vary in quality. This situation undermines the effectiveness of sound legal norms, as poorly monitored implementation can lead to abuse or biased allocations. New legal norms need to include stronger public oversight mechanisms and sanctions for failure to meet transparency standards.

The 1945 Constitution is once again the superior legal source for fiscal reform. Article 33, paragraph (1), which states that the economy is structured as a joint effort based on the principle of kinship, and Article 34, which stipulates that the poor and neglected children are cared for by the state, serve as normative anchors that fiscal law must be directed at distributing resources and development benefits to the most vulnerable groups. Statutory norms must remain consistent with and not contradict this constitutional mandate. Normative failures in laws or fiscal policies that exacerbate disparities could become constitutional issues.

The creation of new legal norms should clarify the state's obligation to distribute the budget based on actual needs and fiscal disparities between regions. For example, the Regional Government Regulation (HKPD) Law could include an article mandating the development of minimum service standards as variables in the DAU and DAK allocation formulas, rather than solely based on potential revenue and population. These norms must have strong legal authority, not merely administrative implementing regulations.

Progressive tax system reform needs to be strengthened through legislation that expands the income tax rate layer, reduces disparities in the tax burden across income groups, and introduces exemptions or lower rates for low-income groups. Article 17 of the Income Tax Law already uses a progressive rate, but regulations governing the progressivity threshold and exemptions (non-taxable income) are still needed to avoid burdening vulnerable groups. Likewise, the new VAT regulations (the HPP Law) must be balanced with exemption mechanisms, lower rates, or subsidies for commodities related to basic needs.

The integration of equity and accountability principles into national fiscal law must make public audit mechanisms, public service evaluations, and performance reporting integral components. The State Treasury Law (Law No. 1/2004) could be updated to ensure accountability for public budget use encompasses both outcomes (tangible results for public welfare) and inputs (fund allocation), ensuring accountability is not merely formal but substantive. Sanctions and reward mechanisms based on regional performance could be more clearly regulated in the law. The legal reform framework must also address the principle of inclusivity, ensuring that the voices of vulnerable communities and disadvantaged regions are included in the fiscal regulation formulation process. This right to public participation can be strengthened through laws governing public consultation in the preparation of the State Budget (APBN) and Regional Budget (APBD), the development of implementing regulations for fiscal policy, and the development of indicators for the distribution of fiscal justice. Thus, fiscal legal norms are not simply created in the name of justice, but are created collaboratively with those affected.

Optimizing the integrated implementation of Law No. 1/2022 on Regional Government Development Planning (HKPD) and Law No. 7/2021 on Regional Government Development Planning (HPP) is crucial to ensuring that tax revenue sources (regulated by the HPP Law) and fiscal transfer allocations such as the General Allocation Fund (DAU), Special Allocation Fund (DAK), Regional Revenue Sharing Funds (DBH), and Village Funds (regulated by the HKPD Law) mutually support distributive justice efforts. The HPP Law must accommodate incentives or exemptions for low-income communities if tax rates or VAT increases have a regressive impact. Implementing regulations must be effectively absorbed, and government regulations or presidential decrees must regulate mechanisms for synchronization between the central and regional governments.

Enforcement of the principles of transparency and public accountability must be strengthened in legal regulations. New or revised legislation should require the provision of open fiscal data at all levels of government in a structured manner (public, routine, and reliable), performance and financial audits involving independent institutions, and the use of audit reports as a basis for fiscal policy evaluation. Checks and balances, including public participation and legislative oversight, should also be strengthened to ensure legal norms are not merely formal.

Aligning fiscal policy with the Sustainable Development Goals (SDGs) is a mandatory recommendation. Fiscal law should incorporate targets for reducing inequality (SDG 10), inclusive welfare, and the environment in a balanced manner. Fiscal regulations, such as the allocation of Special Allocation Funds (DAK) and Regional Revenue and Expenditure Funds (DBH), must consider environmental and social impacts, not just the physical volume or number of projects, to ensure economic development does not widen social disparities or cause environmental damage.

It is crucial that implementing regulations and annual budget policies (APBN and APBD) include measurable indicators of distributive justice as part of the evaluation mechanism. For example, the law could stipulate that each APBN must include a report on inter-regional welfare balances, an analysis of the local cost of living, and the impact of tax policies on real community income. New regulations could mandate the inclusion of such public reports.

CONCLUSION

Fiscal policy plays a strategic role as the state's primary instrument in realizing social justice and public welfare, as mandated by Articles 33 and 34 of the 1945 Constitution of the Republic of Indonesia. Analysis shows that although Indonesia's fiscal legal framework, through Law No. 17 of 2003 concerning State Finances, Law No. 7 of 2021 concerning Harmonization of Tax Regulations, and Law No. 1 of 2022 concerning Financial Relations between the Central Government and Regional Governments, regulates the principles of efficiency, propriety, and transparency, its implementation does not fully reflect distributive justice. Fiscal inequality between regions, the low effectiveness of regional financial transfers, and tax policies that tend to be oriented toward state revenue interests indicate a gap between legal norms and the goal of economic equality.

The principle of distributive justice, which should underpin fiscal policy, remains declarative and has not yet become an operational norm that guarantees equitable distribution of development benefits. Therefore, fiscal law reform must be directed toward ensuring that the state's financial system distributes burdens and benefits proportionally across all levels of society. Recommendations for reforming fiscal policy law should focus on strengthening social justice through more progressive and responsive legal instruments. Strengthening progressive tax rates, establishing fiscal transfer mechanisms based on regional needs, and increasing transparency and public accountability are concrete steps toward a just and sustainable fiscal system.

The new fiscal law must include indicators of distributive justice and public participation in the formulation of budget policies to ensure that state financial management is not only administratively efficient but also substantively fair. Thus, reforming fiscal law based on distributive justice not only serves to close economic disparities but also strengthens the foundation of a welfare state that benefits all Indonesians.

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