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Management of Assets and Follow-Up the Findings of the Audit Board to Increase Financial Performance of Local Governments

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ABSTRACT

The dependence of most local governments on the central government in funding regional spending is still a problem in Indonesia. Although the regional autonomy system has been implemented, including in terms of regional financial management, local governments still have difficulty in implementing efficient regional spending. This effort is done so that the financial management of local governments can be implemented efficiently. This research aims to find out the impact of the size of local governments, audit findings and follow-up of the recommendations of The Audit Board of the Republic of Indonesia on the financial performance of local governments. This study uses a quantitative approach by testing hypotheses using multiple regression analysis methods in cross sectional data. The study used data from local government performance reports in 2019. The study analyses 406 district/city governments report in Indonesia. The results showed that: 1) There is a positive and significant influence on the size of local governments on the financial performance of local governments in Indonesia; 2) There are negative and significant influences on the findings of examination of the financial performance of local governments in Indonesia; 3) There is a positive and significant influence on follow-up recommendations of examination results on the financial performance of local governments in Indonesia. The results implication is that efficiency of local government asset and follow-up of audit findings of the Audit Board Republic of Indonesia can improve the financial performance of local governments.

Keywords:

Local Government Size, Audit Findings, Audit Recommendations Follow-up, Financial Performance of Local Governments

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1. Introduction

The Indonesian government system after the reformation era gave flexibility to the local government to organize regional autonomy. The implementation of regional autonomy refers to Law, no 22, year 1999 and updated by Law, No. 23 of 2014 on Local Government. The implications of implementing regional autonomy are the existence of fiscal decentralization as a delegation of fiscal responsibility from the central government to local

governments. It is including handing over authority for local government⁴ for local revenue and expenditure, the implementation of local government autonomy to improve public services and good governance.

Delegation of the authority from the central government to the local government is in the affairs of service to the public and regional financial management. It forms agency relations in the context of Indonesian local government to the community; delegation of authority from the community and local government; the community and the regional representative council (DPRD), and the DPRD and local government. Principal gives regulatory authority to agents to provide services that are in the principal's interest and provide resources to agents in the form of taxes and others. The community (principal) as the main stakeholder of the government wants the government (agent) to provide maximum public services while the government (agent) have resources constraint and their owned interests of itself (Monteduro & Allegrini, 2020). The local government acts as an agent in planning, implementing, and reporting on the regional budget in order to account for services to the public, and the community acts as a principal that gives authority to the legislature to oversee the performance of local governments (Boholm, 2019).

In the theory of agency, there are demands for financial performance accountability from the public (principal) that requires local governments (agents) to provide a transparency of their performance through local government financial statements (Kim, 2016). Accountability of financial performance of local government⁷ which presented in the Local Government Financial Report (namely LKPD) is then audited by the Audit Board of the Republic of Indonesia (called as BPK RI). BPK RI as a⁵ external auditor of local governments in Indonesia conducts an examination of LKPD in order to provide opinions on the fairness of financial information presented in financial statements (Fresneda Fuentes & Hernández Borreguero, 2018). This is based on agency theory on the existence of information asymmetry carried out by agents or governments to the public that allows cases of violations of internal control and compliance with laws and regulations (Mansoor, 2021). Examination of local government financial statements by BPK RI becomes one form of monitoring carried out by the public to minimize the occurrence of agency problems.

In accordance with the provisions of State Financial Examination Standard (called as SPKN), the Report of Examination Results (LHP) presents the findings of the examination as well as the recommendations from the examiner⁵. Examination findings is used as a reference in the provision of audit opinions on the results of the examination. Recommendations are then addressed to the agent so that they they can take remedial action. Recommendations can minimize the consequences resulting from irregularities in the management and financial responsibility of the local government. Therefore, recommendations need to be followed up for the improvement of local government financial performance, so that there is an occurrence of organizational learning process (Lenart-Gansiniec, 2021). Audit opinions can boost the performance of local governments. The better the BPK audit opinion obtained by the local government, it can show the improving financial performance (Raghavan & Yu, 2021) of local governments. Also, following-up BPK RI recommendations can be used as a tool to improve the performance of local governments in managing their regional asset and financial.

Factor that affects the financial performance of local governments in Indonesia is determined by the size of the local government. The performance achieved by each district or city in Indonesia is very diverse, because the size of the government in each area diverse. Regarding to the size of the different local governments, the implementation of government will also be different and produce diverse performance. In the context of government, the size of local government can be seen from the amount of ownership of a regional asset. Regional assets are an important resource for local governments. Local governments that have a large amount of assets will have a large need for funds in the implementation of regional revenue and spending authority. Therefore, it is important for local governments to be able to manage assets adequately.

Several characteristics that show local government's ability to implement regional autonomy properly are (1) the existence of regional government capabilities in terms of

exploring the potential of regional income (which is called Local Owned Source Revenue or PAD). In this case, local government acts an entrepreneur organization (Dong et al., 2022); (2) managing and using regional spending efficiently to finance the implementation of government (Wang et al., 2018); and (3) ability to decrease the dependence on central government assistance.

The purpose of the research is to examine the factors that affect the financial performance of local governments by using financial performance of local government, namely the ratio of PAD to regional spending as well as internal and external factors in local governments, including the size of local governments, the findings of examinations and the completion rate of follow-up recommendations of BPK RI examination results. Further analysis, this research purpose can be divided as follows:

- Does size of the local government increase the financial performance of local governments?
- Does the number of BPK examination findings decreases the financial performance of local governments?

Does the follow-up recommendations of BPK examination results increases the financial performance of local governments?

2. Methods

Research design uses a quantitative approach. The research uses secondary data consisting of three types of documents, namely (1) Local Government Financial Statements for Fiscal Year 2019 (audited); (2) Overview of BPK RI examination results for semesters I and II, for financial reports 2019 and 2020; and (3) district or city government data in Indonesia year 2019, which published by the Indonesian Ministry of Home Affairs. Sampling technique uses purposive sampling method. The study population was 542, and the final sample that meet the research criteria is 406. The sample selection process is presented in table 1.

Tabel 1. Sample selection process

No	Sample Criteria	Sum
1	Local government in Indonesia in 2019	542
2	Provincial Government in Indonesia in 2019	(34)
3	District/city government in Indonesia in 2019	508
4	District / city government that did not compile LKPD in 2019 and has not been audited by BPK	(1)
5	District / city government that is not included in the Overview of Examination Results of Semester I and II of year 2019 and year 2020	(0)
	Number of sample	507
	Data outlier	(101)*
	Number of final sample	406

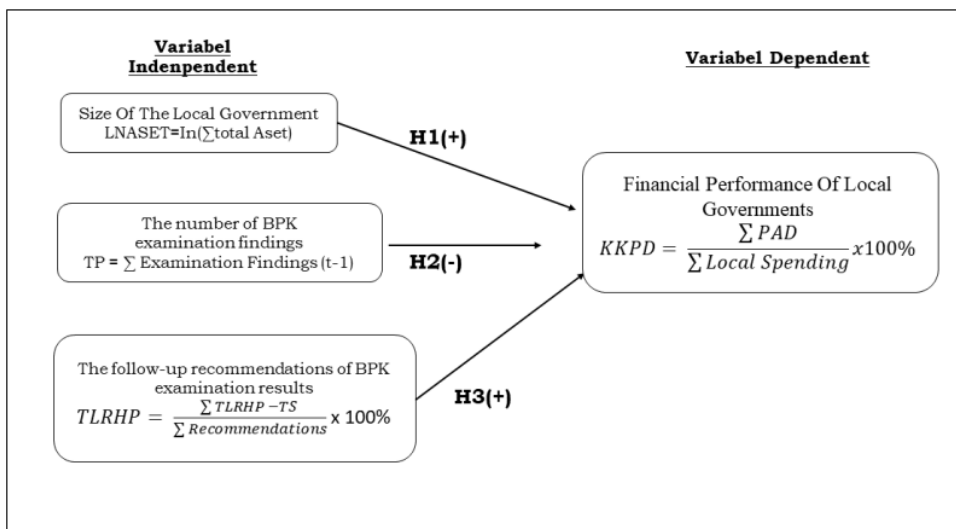
Table 1 shows that the number of local governments in 2019 is 508 based on data published by the Ministry of Home Affairs of the Republic of Indonesia. In 2019 there was one local government that did not compile LKPD and has not been audited by the BPK RI, so that the number of observations that became research samples were obtained was 507 local governments. Furthermore, there are 101 outlier data because the data deviates too far from other data (extreme data). Variables that have extreme values can distort the

approximate regression coefficient. Therefore, data of extreme value (outlier) needs to be excluded from research data with Casewise Diagnostics so that observations that become the final sample as many as 406 local governments.

The study used three independent variables and a dependent variable. Independent variable consists of the size of the local government (X1), the number of BPK examination findings (X2), and the follow-up recommendations of BPK examination results (X3). While variable dependent is the financial performance of local governments (Y). The proxy used for variable size of local government is total assets. The proxy of the number of BPK examination findings is the number of findings of the previous year. Follow-up proxy continued recommendations of BPK examination results are projected with the level of follow-up completion in accordance with the recommendations of BPK examination results.

The research framework of this research is that the larger the size of the local government projected with total assets, the higher the financial performance of local governments. The fewer the number of BPK examination findings projected with the number of findings of the previous year, the higher the financial performance of local governments. The higher the follow-up recommendations of BPK examination results that are projected with the level of follow-up completion in accordance with the recommendations of BPK examination results, the higher the financial kinerja of local governments. Research framework for this research can be seen at figure 1.

Figure 1. Research framework



3. Results

Partial significance test results (statistical t-test) showed that local government measures (LNASET) and follow-up examination recommendations (TLRHP) had significant positive p-values with coefficients of 4,389 and 0.110, respectively. These results show that the size of local governments and follow-up inspection recommendations have a positive effect on the financial performance of local governments. The examination findings (TP) have a significant p-value of -0.201, these results show that the examination findings negatively affect the financial performance of local governments as follows.

Table 2. Partial significance test results (statistical t-test)

Model	N	Expt Sign	B	t-value	Sig.
(Constant)			-119,521	-15,812	0,000 ^a
LNASET	406	+	4,389	16,071	0,000 ^a
TP	406	-	-0,201	-5,063	0,000 ^a

Source : SPSS output

H1: size of the local government on the Financial Performance of Local Governments

The local government size variable with a probability value of 0.000 which is smaller than the error rate of 1% and the coefficient value of 4.389 indicates that the size of the local government has a positive effect on the financial performance of the local government so that the first hypothesis is accepted.

H2: The number of BPK examination findings decreases the financial performance of local governments

The variable of the examination findings with a probability value of 0.000 which is smaller than the error rate of 1% and a coefficient value of -0.201 indicates that the examination findings negatively affect the financial performance of local governments so that the second hypothesis is accepted.

H3: The follow-up recommendations of BPK examination results increases the financial performance of local governments

The variable of Follow-up of examination results with a probability value of 0.000 that is smaller than the error rate of 1% and a coefficient value of 0.110 indicate that the examination findings have a positive effect on the financial performance of local governments so that the third hypothesis is accepted.

4. Discussion

Based on the theory of good governance it is stated that local governments with greater total assets will maintain and manage their assets in a transparent and accountable manner in order to realize good governance. Local governments that have large total assets will have adequate resources (Zhang et al., 2022) to further optimize Regional Income (PAD). In 2019 there are guidelines in asset management regulated in various provisions including Government Regulation No. 12 of 2019 on Regional Financial Management, Regulation of the Minister of Home Affairs No. 21 of 2011 on Regional Financial Management Guidelines and Regulation of the Minister of Home Affairs No. 19 of 2016 on Guidelines for The Management of Regional Property. The provision becomes a guideline for local governments in order to improve the financial performance of local governments.

Summary of The Results of Semester Examination (IHPS) I and II BPK RI in 2016 to 2020 showed an increase in the amount of local government assets in the Local Government Financial Report (LKPD) fiscal year 2015 to 2019. This shows the efforts of local governments in improving and optimizing regional assets through adequate regional asset management. Local governments that have large total assets can further explore the potential of regional financial income through PAD to finance spending in the administration of government (Dagiliené et al., 2021). In addition, local governments can also reduce the level of dependence on central government assistance (Reiling et al., 2021).

Based on agency theory, it is stated that the examination of the Local Government Financial Report by the BPK is one form of monitoring to minimize the occurrence of agency problems because the community (principal) demands financial performance accountability to local governments (agents) to provide a clear picture of its performance.

Summary of The Results of Semester Examination (IHPS) for semester I and II BPK in 2016 to 2020 showed a decrease in the number of financial examination findings in local governments that had an impact on increasing the achievement of opinions on the Local Government Financial Report (LKPD) fiscal year (FY) 2015 to 2019. This shows that local governments are working to improve performance in regional financial management. Thus, a growing number of examination findings show that local governments do not fully have adequate internal control and comply with the provisions of legislation in running the government.

The results of this study are in line with previous research that the greater number of BPK audit findings in a local government, the lower the performance of the local government because there are problems in accountability (Bakker et al., 2018) of regional financial management, among others, high weaknesses in internal control system and irregularities in financial governance. Factor determinants of high regional financial performance, namely the findings of BPK audit of non-compliance with laws and regulations. The impact of the audit has a significant negative effect on the performance of the local government means that the greater the number of BPK audit findings in a local government, the lower the performance of the local government.

Based on agency theory it is stated that the community that acts as principal gives authority to the DPRD to oversee the performance of local governments. Based on Law No. 15/2004 on Examination of State Financial Management and Responsibility, it is also stated that the implementation follow-up of BPK examination results is the responsibility of local governments and DPRD. Furthermore, it is known that Law No. 23/2014 on Local Government in Article 149, it is stated that the DPRD has a supervisory function in the form of supervision on the implementation of follow-up results of financial statement examination by the Audit Board (BPK). Therefore, the results of TLRHP monitoring carried out by BPK are delivered once every semester to the DPRD in the form of an Overview of Semester Examination Results (known as IHPS).

Based on the recapitulation list of local government TLHP monitoring results in the Overview of The Results of The Semester Examination (IHPS) I and II of BPK RI in 2015 to 2020 showed that the average percentage of Follow-up Recommendations of Examination Results (TLRHP) of BPK followed up by local governments amounted to 67.7% or as many as 107,882 recommendations from 159,317 recommendations. The BPK recommendation on the results of the examination has been followed up by depositing money / assets to the region or completing work / goods, administrative actions in the form of warnings, reprimands, and / or sanctions to the persons in charge and / or implementing activities. Administrative actions can also be corrective actions on regional financial management, completing evidence of liability and improvement of some or all internal control systems.

Previous research revealed that the greater the percentage of recommendations of examination results that are followed up, the financial performance of local governments in accountability of regional financial management will be better. Previous research found that follow-up audit recommendations had a significant positive effect on local government financial performance because recommendations minimized the impact of irregularities in regional financial management and responsibility that would impact the quality of local government financial statements.

5. Conclusion

The dependence of most local governments on the central government in funding regional spending is still a problem in Indonesia. There are factors that affects the financial performance of local governments in Indonesia. It is including the size of the local government, Accountability of financial performance of local government which presented in the Local Government Financial Report audited by the BPK RI, and follow-up of examination results of BPK recommendation. Based on the results of research and discussions that have been conducted, it can be concluded that (1) the size of the local

6 government has a positive effect on the financial performance of the local government; (2) the examination findings negatively affect the financial performance of local governments; (3) the examination findings have a positive effect on the financial performance of local governments.

This research provides the implication that managing regional assets is the implementation of regional autonomy in financial aspects. The efficiency of the use of regional revenues must be controlled through transparency in the use of funds presented through local government financial statements. The results of the examination of regional financial statements by the BPK provide several recommendations. And follow-up the findings of The Audit Board to increase financial performance of local governments. Thus, managing regional assets and follow-up, the findings of The Audit Board to increase financial performance of local governments

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