

The usefulness of accrual-based financial statements at local government

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ABSTRACT: Like other countries in the world, Indonesia is also undergoing public financial management reforms. This reform was marked by a change in Government Accounting Standards (SAP) from a cash basis to an accrual basis as stipulated in Government Regulation Number 71 of 2010. However, after decades of public financial management reform, this accrual accounting model has been criticized because the resulting financial information has not been able to meet the necessities of its users. But some previous research prove that accrual-based financial statements have provided usefulness for its users. The purpose this investigation is to give empirical proof regarding the usefulness of accrual basis financial statements in decision making, and factors that will improve financial reporting quality in local governments.

1 INTRODUCTION

New public management (NPM) era's or reform in financial information systems is characterized by the use of accrual-based accounting in the public sector, which previously used a traditional cash accounting system (Lapsley, 1999). In Indonesia, the adoption of accrual basis Government Accounting Standards (SAP) based on Government Regulation Number 71 of 2010, is intended to provide better usefulness for stakeholders, both users, and auditors of government financial reports. The existence of an accounting update delivers information that is accountable, transparent and useful for decision making for users of that information (Kober *et al.*, 2010). Quality financial information will be useful for internal decision-makers to be more controlled and transparent in using public resources more economically, efficiently and effectively.

However, after decades of NPM changes, this public management model has been criticized and this financial information has not been able to meet the necessities of its users (Mack and Ryan, 2006). However, some studies found the opposite, that accrual-based financial statements are more useful than cash-based financial statements, such as Andriani *et al.* (2010) in government institutions in Australia which are in line with the results of Kober *et al.* (2010), and Cohen and Karatzimas (2017) that accrual-based information is more useful for its users. Absence of awareness and readiness to accept updates (changes from cash-based accounting to accrual-based) and insufficient ability to maintain updates, will lead to the failure of these updates (Hepworth, 2003). Thus further proof is needed regarding the relationship between the quality of accrual-based financial reporting in the public sector and the benefits felt by its users for decision making.

2 RESEARCH ISSUE

The examination results of the Republic of Indonesia Supreme Audit Agency (BPK RI) show that governance, development, and implementation, as well as the operation of information

technology in local government financial reporting, have not been fully effective in supporting government financial reporting because there are still several problems (IHPS BPK RI, 2016). Local governments need a system that can produce financial information in a more comprehensive manner which includes information on the financial position of the region, financial performance conditions, and accountability of the Regional Government.

3 LITERATURE REVIEW

Organizational theory explains organizational change and reforms carried out in the public sector, both in financial management and accounting systems (Nogueira & Susana, 2015). Organizational change in the public sector is caused by the need for *New Public Management* (NPM) and *New Public Financial Management* (NPFM), which is triggered by information needed for decision making. Contingency theory in the public sector is used in the public sector to explain accounting reform and public sector management, specifically reform in reporting systems (Anessi-Pessina *et al.*, 2008; Woods, 2009). Institutional theory is used by many researchers to explain organizational change, namely how organizations respond to pressure from their institutional environment (Nogueira & Susana, 2015). Isomorphism is the tendency of organizations towards uniformity concerning the environment and their institutions (DiMaggio & Powell, 1991). Isomorphism can occur with the mechanism of Coercive, Normative, and Imitative.

As explained by International Public Sector Accounting Standard Board / IPSASB (2010), financial reporting must provide information related to the entity, which is useful for its users. In this context, benefits are valued in terms of decision making and accountability. The use of an accounting basis based on cash or accruals will affect the financial statements presented and have an impact on different decision making.

4 RESEARCH METHOD

The research method used is a survey obtained through questionnaires and interviews. Data analysis uses *structural equation modeling (SEM) Partial Least Square (PLS)*. Application of Accounting Information Systems (X) using dimension system quality, service quality, and system use (DeLone and McLane, 2008). Quality of Financial Reporting Quality (Y) using dimension relevant, reliable, comparable, understandable (Belkaoui, 2004) and Government Accounting Standards (SAP) 2010. Accrual basis Financial Statements (Z) using dimension Perceived importance and Perceived usability (Cohen, Sotirios, Karatzimas, 2017).

5 DISCUSSION

5.1 Effect of Application of Accounting Information Systems on the Quality of Financial Reporting Local Government

DeLone and Mclean (1992) states that the determining factor of success of information systems is the *System Quality, Information Quality, Service Quality, usage, user satisfaction*. O'Brien and Maracas (2010) argue that information systems with computers cause managers to obtain information quickly and provide more reports. Information technology makes it easy to manage decentralized activities and decision making. Studies by Abdallah (2013), Ramdani (2015), Sacer and Oluic (2013), provide evidence that accounting information systems affect the financial statements quality. The effectiveness of accounting information systems can help companies maintain the usefulness of accounting information and make effective decisions. Based on the literature and previous research, the following hypothesis is stated: H1: The Application of Accounting Information Systems has effect on the Financial Reporting quality in Local Governments, positively.

5.2 Effect of the Quality of Accrual basis Financial Reporting on the Usefulness of Quality Financial Reports

Financial reporting quality is information that meets the qualitative characteristics of information that is relevant, reliable, comparable, and transparent information on a timely basis. (IPSAS, 2010; Belkaoui, 2004; Gamayuni, 2018). The cash-based recording system has several weaknesses in the information generated because most accounting data are not recorded such as

assets and debt. These limitations cause cash-based accounting can not meet the objectives of decision making (Bergmann, 2012). The adoption of accrual-based accounting is intended to improve the existing cash basis accounting system. Quality financial information will be useful for internal decision-makers to be more controlled and transparent in using public resources more economically, efficiently and effectively (Cohen and Karatzimas, 2017; Kober *et al.*, 2010; Lapsley, 2009; Andriani *et al.*, 2010). Thus the following hypothesis is proposed: H2: The financial reporting quality has effect on the usefulness of financial statements in decision making, positively.

6 CONCLUSION

The fundamental contribution and the novelty of this research want to explore about the usefulness of accrual based financial statements in decision making in local governments. Quality financial reporting is expected to increase the usefulness of local government financial reporting, and to prove the characteristics of accounting information systems that can increase the financial reporting quality in local governments. The results of this study are also expected to help local governments to improve and enhance policies, to improve financial quality so that it is beneficial for the government to increase resources, efficiently, and effectively for the achievement of the community.

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