



The Quality of Financial Reporting and Internal Control System before and after the Implementation of E-budgeting in Indonesia Local Government

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Authors' contributions

This work was carried out in collaboration between both authors. The study was designed and drafted by all the authors. Both authors read and approved the final manuscript.

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ABSTRACT

This study aims to determine differences in the quality of financial reporting of local governments in Indonesia before and after implementation of the e-budgeting system and government internal control systems in the preparation and management of regional finances that are measured from the achievement of the Unqualified Opinion from the Audit Report of the Supreme Audit Board (LHP BPK) on the Local Government Financial Report (LKPD). The population of this research is all 542 local governments in Indonesia with a sample of research the local government in Indonesia that has implemented e-budgeting from 2017 until 2018. This research method is a quantitative empirical research method using secondary data with data analysis using an Independent sample T-test using SPSS 23 software.

The results of testing the hypothesis with a Independent Sample T-test using the SPSS 23 software indicate that there are significant differences between regions that have implemented e-budgeting system to the quality of its financial reporting with t value of 8.287 with 0.000 level of significance. Local governments that have implemented an e-budgeting have been able to obtain Unqualified opinions of 105 local Governments or around 96%, while the remaining 4 local governments have not been able to achieve Unqualified opinions or around 4%. While the average value of the quality of local government financial reporting that has not implemented e-budgeting with a score that is,

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1.7354 were able to obtain Unqualified opinions of 284 local Governments or around 66%, while the remaining 149 local governments were only able to obtain Non Unqualified opinions or around 34%.

The results of hypothesis testing with different T-test also showed that there was a significant difference between the average value of the quality of financial reporting of local governments that obtained Unqualified opinion with SPIP score of 2.4890, namely 367 local governments or about 92%, while the remaining 34 local governments have not been able to reach the Unqualified opinion or around 8%. While the average quality of the financial reporting of local governments that have an effective SPIP score of 1.7035 or at the SPIP pilot stage is only 22 local governments or around 16% capable of obtaining Unqualified opinion, while the remaining 119 local governments have not been able to achieve Unqualified opinion or around 84% with t value of 14,036 with 0.000 level of significance.

Keywords: E-budgeting; government internal control; quality of financial reporting.

1. INTRODUCTION

Based on Supreme Audit Board (BPK) Inspection Report (LHP) for 2017, BPK still found material findings of 6,222 findings that affected the quality of financial reporting presented by local governments which resulted in the unachieved of unqualified opinion on LKPD. Findings related to weaknesses in the control system for the implementation of the revenue and expenditure budget dominate BPK's findings by 46% and followed by weaknesses in the internal control structure by 20%. These findings have an impact on the financial reporting system that can result in losses, potential losses, lack of revenue, administrative weaknesses, inefficiencies and ineffectiveness that affect the materiality of financial reporting of local governments.

The finding of weaknesses in the implementation of the revenue and expenditure budget is due to inconsistencies between planning, drafting and realization of the budget in the programs and activities of the local government so that the aspects of the adequacy of disclosure and compliance with laws and regulations in accordance with Law Number 15 of 2004 concerning auditing are not fulfilled of the management and responsibility of state finances that affect the quality of local government financial reporting. In addition, the element of conformity with Government Accounting Standards (SAP) is not fulfilled in accordance with Government Regulation Number 71 of 2010 concerning government accounting standards, namely the principle of realization and consistency. The foregoing has the effect of not fulfilling the qualitative characteristics of financial reporting [1].

Local government financial reporting must have some qualitative characteristics that are required

to obtain an unqualified opinion from BPK. Quality financial reporting is financial reporting that produces useful information for its users, namely information that meets the qualitative characteristics of information that is relevant, reliable, comparative and understandable [2]. The financial statements presented are expected to be able to describe the real performance conditions so that they can provide quality, accountable, useful and transparent information to the community and can be useful for the decision making process by stakeholders and the optimal allocation of resources [3].

The implementation of e-budgeting is expected to reduce the number of findings related to weaknesses in the control system of the implementation of the revenue and expenditure budget, especially inconsistencies in the program components and activities of the local government in accordance with presidential instructions contained in Law No. 23 of 2014 and Permendagri No. 86 of 2017. E-budgeting is able to prevent budget markup for programs and activities and as a tool for controlling consistency between programs and public budgets. In addition, aspects of planning and budgeting are done online will be documented through digital footprint so that all stakeholders can monitor so as to minimize the occurrence of irregularities related to the realization of the budget and against the legislation. This is because in the stage e-budgeting there are consists of the Musrenbang mechanism (Development Planning Conference) which involves all parties to be involved (community, local government, and legislature) so that aspects of transparency, consistency and public accountability can be realized. In addition, in the preparation of the budget through e-budgeting, there is one step in the procedure, namely the Local Government

Work Plan (RKPD) whose output is in the form of a General Budget Policy (KUA) and a Priority Budget Ceiling (PPAS) in which there are Expenditure Standards Analysis (ASB) and Price Standards Analysis (ASH).

Regarding the results of previous studies, there are still differences in results related to the application of e-budgeting to the quality of financial reporting. Atyanta [4] argues that the weakness of the control system of the implementation of the revenue and expenditure budget becomes an obstacle in achieving the unqualified opinion. In contrast to the results of the study [5], according to him, the role of transparency in the implementation of e-budgeting in the public sector is not significant because of the exclusive nature of information and not all parties can access it.

Related to the main problems of the Government Internal Control System (SPIP) is in the process of preparing reports that are not in accordance with the provisions, recording, and documentation of assets have not been done accurately, procedures for segregation of duties and functions as well as ineffective authorization procedures and existing Standard Operating Procedures (SOP) the entity is not running optimally related to the effectiveness and efficiency of the activity program. In addition, the existing internal oversight unit is inadequate or not running optimally as indicated by not following up on the findings of the previous audit inspection [6]. This finding has the effect of not fulfilling the audit aspects of LKPD opinion, namely from the aspect of conformity to SAP and the government internal control structure in accordance with Law Number 15 of 2004 concerning auditing the management and responsibility of state finances that affect the quality of local government financial reporting. The existence of Perka BPKP NO.4 in 2016 which measures the size, nature, and complexity of local governments with the effectiveness and capability of the internal control system is able to help reduce findings related to government internal control structures. This is because the function of the government internal supervisory is more optimized in conducting supervision related to the 5 elements of the Internal Control System namely the control environment, risk assessment, control activities, information and communication, and monitoring.

Regarding the results of previous studies, differences in the results related to the

government's internal control system on the quality of financial reporting are also found. According to Bastian [7] the audit findings describe all important information relating to a particular audit problem. In reporting weaknesses in internal control over financial reporting, the examiner must identify conditions that can be reported individually or cumulatively as material weaknesses. The examiner must place the findings in a reasonable perspective in relation to providing audit opinion. However, research [8] states that the internal control system does not influence BPK's audit opinion. The results of the study [9] also stated that SPIP's weakness did not affect the disclaimer's opinion.

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

2.1 The Quality of Local Government Financial Reporting

Quality of Local Government Financial Reporting is all aspects related to the process of providing and delivering financial information for *stakeholders*. These aspects include the institutions involved (Legislative and executive), the applicable regulations including SAP, and the mechanism for delivering information in the form of financial statements. Government financial reports are a medium in the delivery of financial information and representation of the financial position of transactions carried out by the government. Local government financial reporting must have some qualitative characteristics that are required to obtain an unqualified opinion from BPK. The qualitative characteristics of local government financial statements which are normative requirements as mentioned in the Government Accounting Conceptual Framework (PP NO 71 of 2010) are relevant consisting of feedback value, prediction value, complete and timely. Reliable consists of verifiable, honest and neutral presentation, which can be understood and can be compared.

As a form of accountability to the public, local governments will report LKPD. LKPD which has been prepared based on SAP and has been reviewed will be submitted by the head of government to the Supreme Audit Agency (BPK) no later than two months after the end of the fiscal year to be audited by the BPK based on 4 evaluation criteria. The 4 criteria for examining the quality of LKPD by the BPK based on article 16 paragraph (1) of Law Number 15 of 2004 concerning audits of management and

accountability of state finances are 1). Compliance of LKPD with Government Accounting Standards (SAP). 2). Adequacy of Financial Statement Information. 3). Effectiveness of the Internal Control System. 4). Compliance with statutory regulations. After examining the financial statements, the BPK will issue an Audit Report (LHP). LHP contains an audit opinion on LKPD. BPK's opinion on LKPD is rated from 1 to 5 consisting of Disclaimer, Unqualified Opinion, Qualified Opinion, Unqualified With Explanatory Opinion, and Unqualified With Explanatory Opinion and Unqualified Opinion.

According to Mardiasmo [10] the quality of public sector financial reporting is a comprehensive information to compare the realization of revenue, expenditure, transfers, financing, assets, liabilities, equity funds, and cash flow of a reporting and financing entity with a predetermined budget by assessing financial conditions, evaluate the effectiveness and efficiency of a reporting entity and help determine compliance with laws and regulations. The quality of financial reporting in the public sector is closely related to accountability which refers to Government Accounting Standards in the form of the presentation of information that is useful for decision making and the accountability of the reporting entity for the resources entrusted to it.

LKPD is one form of embodying the theory of stewardship in public sector organizations such as government organizations. In LKPD, local governments must disclose relevant accounting data and other information in a relevant, clear and detailed manner. LKPD made by the local government will be used by various parties who need financial statements for decision making and policy evaluation. Legislative and executive parties can use LKPD to make economic decisions and various regional strategic plans. The implication of the stewardship theory for this research is how LKPD can explain the existence of local government as an institution that can be trusted to accommodate the aspirations of the community, can provide good service to the public, be able to make financial responsibilities mandated to it, so that economic objectives are met and community welfare can be achieved maximally.

Government management is required to provide services for the interests of the principal by acting as a steward. This is supported by research conducted by [11] which shows that

government management acts more as a steward because it is influenced by the type of service provided, the level of public management capacity, the types of incentives and sanctions used, and the frequency of information needed where fund managers the public is expected to work as well as possible for the interests of the principal, namely citizens and their institutions.

2.2 E-budgeting

E-Budgeting is an information system for regional financial management that is integrated with sequential stages using web-based computer application programs starting from the planning stages of budgeting to the accountability of the budget which is guided by applicable laws and regulations in order to improve the quality of spending and accountability in the management of regional finances and maintain consistency in planning and control. The stage of e-budgeting consists of the Local Government Work Plan (RKPD), the General Budget Policy (KUA) and the Provisional Budget Priority Ceiling (PPAS) which includes Expenditure Analysis Standards (ASB) and Price Standards Analysis (ASH), Budget Activity Plans (RKA)) SKPD, Regional Revenue and Expenditure Plans (RAPBD) and Budget Implementation Documents (DPA).

E-budgeting guarantees consistency and accountability between program planning and activities towards its budget. E-budgeting facilitates the process of preparing regional expenditure budgets aimed at transparency for each party as well as improving the quality of APBD in terms of compliance with the Medium-term of local government development plan (RPJMD), the accuracy of values, account codes and accountability as well as consistency between program budgets and activities towards their realization. Ritchi et al. [12] conducted a study in which the results of the study showed that there was a positive influence between the use of e-budgeting on the quality of accounting information systems and local government financial reporting. Another study by Mancini et al. [13] found that there was a positive influence in the form of flexibility, network connectivity, and data integration as well as the level of transparency of financial information on the success of the government's financial information system. Wirasedana et al. [14] states that public sector organizations facing budgeting problems in the form of significant budget deviations are likely to face a lack of clearer synchronicity between the goals set and the program which is

carried out so that it impacts on the effectiveness of development programs and activities as well as public services.

Johansson et al. [15] explains that budgeting and budget control are central in planning, controlling, and accountability in public sector organizations. An important reason for budgeting in public sector organizations is that the resources allocated must be used to improve people's welfare. The results of other studies conducted by Srivastava [16] found that the implementation of e-budgeting both in terms of government policies, public service administration, plan reports, and budget realization had a positive effect on the level of quality of financial information produced by the government so that it had an impact on increasing public confidence in terms of budget transparency. The quality of accounting information systems will produce good accounting information that is the information data generated is relevant, reliable and accurate for the decision-making process in government.

H1: There is an increase in the Quality of Local Government Financial Reporting after the implementation of E-Budgeting.

2.3 The Government Internal Control System (SPIP)

Government Internal Control System (SPIP) according to Government Regulation of the Republic of Indonesia Number 60 the Year 2008 is a system and procedure for evaluating the effectiveness of internal control of local governments to ensure the achievement of objectives through effective and efficient activities, reliability of financial reporting, securing state assets, and adherence to laws and regulations. SPIP consists of 5 elements, namely the control environment, risk assessment, control activities, information and communication, and monitoring controls.

In relation to the effectiveness of the preparation of financial statements, the merits of implementing an internal control system can affect the quality of local government financial reports. Measurement of the SPIP Variable is assessed from the score of SPIP Implementation which is derived from the inspectorate's evaluation conducted *Quality Assurance* review by BPK in the form of an assessment of the Internal Control System Elements (SPIP). The SPIP Maturity Level is a framework for assessing

the size, nature, and complexity of local governments with the effectiveness and capability of their internal control system in accordance with BPKP Regulation No.4 year 2016.

According to Zhou and Zhou [17] there is a relationship between Independent auditors and disclosure of internal control problems. Auditors are required to issue clean opinions or unqualified opinions when they do not find material problems in the company's internal control. If the SPIP weakness findings are low then the possibility of getting an unqualified opinion is high. Kawedar [18] in his research concluded that one of the causes of decreased audit opinion in Purworejo District was due to the increase in cases related to SPIP weaknesses. Furthermore [19] in the conclusion of his research stated that there were three things that caused differences in opinion on BPK Examination on LKPD of the Four Lawang Regency, namely due to the incompatibility of three elements of audit namely SPIP effectiveness, compliance with applicable laws and regulations and the presentation of financial statements with the criteria that have been established, which in this study proves that the internal control system has a positive effect on audit opinion.

According to Gamayuni [2] cases of weaknesses in the internal control system and non-compliance with laws and regulations that occur in local governments in Indonesia shows the low quality of financial reporting in Indonesia. Therefore an effective SPIP function is needed to create quality financial reporting (relevant and reliable), transparent and accountable.

H2: There is an increase in the Quality of Local Government Financial Reporting after the implementation of SPIP.

3. METHODOLOGY

3.1 Population and Research Sample

The population in this study is all Local Governments namely Provinces, Regencies / Cities in Indonesia, amounting to 542 Local Government. The sampling method with purposive sampling is that local administration in Indonesia that has implemented e-budgeting at the RKPD stage in 2017-2018. This research method is a quantitative empirical research method using secondary data with data analysis

carried out statistical tests of Independent test T-test using SPSS 23. Data used in this study are secondary data in the form of Audit Reports (LHP) of the Provincial Government Financial Reports, Regencies and Cities in Indonesia in 2017-2018 in the form of BPK Opinion, Data on the level of system implementation e-budgeting and scoring data of the Local Government's Internal Control System assessment obtained from BPKP. The sample selection was chosen from 2017 to 2018 because the President mandatory all local governments according to Permendagri No. 86 of 2017 to have started implementing e-budgeting starting in 2017.

The implementation of e-budgeting is measured by the stages of the implementation and integration of local government planning and budgeting systems using a Score of 1 to 5 based on the regulation of the Permendagri No. 86 of 2017, which is explained in the Table 1.

3.2 Government Internal Control System (SPIP)

Government Internal Control System (SPIP) variables are measured using the SPIP score of 1 to 5 based on the regulation of the Financial and Development Supervisory Agency (BPKP) Regulation No.4 year 2016.

The quality of local government financial reporting as measured by the achievements of

the unqualified Opinion Report of the financial Audit Board (BPK) on the Local Government Financial Reports (LKPD).

4. RESULTS AND DISCUSSION

To prove the differences before and after the implementation of e-budgeting to the quality of financial reporting of local governments in Indonesia, the authors conducted a series of data tests namely Independent sample T-test with SPSS 23. The Independent Samples T-test compares the means of two Independent groups in order to determine whether there is statistical evidence that the associated population means are significantly different.

Based on The table above can be explained as follows:

- 1. Independent sample T-Test E-Budgeting:**
In Table 4 it appears that the average value of the quality of financial reporting of local governments that have used e-budgeting with a score of 2.3101 is able to obtain an unqualified opinion of 105 Local Governments or around 96%, while the remaining 4 local governments have not been able to reach the unqualified opinion or around 4%. While the average value of the quality of local government financial reporting that has not implemented e-budgeting with a score that is, 1.7354 were

Table 1. The implementation stage of E-Budgeting

Category	Scoring
Not yet implemented e-planning and e-budgeting	1
Implementation of e-planning for 5 years (RPJMD and Strategic Plan)	2
Implementation of e-planning for 5 years and annually (RPJMD, Renstra, Musrenbang, RKPD, Renja)	3
Integration of e-planning, e-budgeting systems (RPJMD, Strategic Plan, ASB & SSH, Musrenbang, RKPD, Renja, KUA PPAS)	4
Integration of e-planning, e-budgeting systems with local financial management (Full Implementation) (RPJMD, Renstra, ASB & SSH, Musrenbang, RKPD, Renja, KUA PPAS, Budgeting Application, Financial Administration and Reporting)	5

Source: Regulation of the Permendagri No. 86 of 2017

Table 2. The government internal control system

SPIP	Scoring
Not Available	Less than 1.0 (0 < Score < 1.0)
Stub	1.0 to less than 2.0 (1.0 < score < 2.0)
Developing	2.0 to less than 3.0 (2.0 < score < 3.0)
Defined	3.0 to less 4.0 (3.0 < score < 4.0)
Managed and Measured	4.0 to 4.4 less (4.0 < score < 4.5)
Optimum	Between 4.5 to 5.0 (4.5 < score < 5)

Source: BPKP Regulation No.4 year 2016

Table 3. Independent sample T-test results

		Levene's test for equality of variances		t-test for equality of means							
		F	Sig.	t	df	Sig. (2-tailed)	Mean difference	Std. error difference	95% confidence interval of the difference		
										Lower	Upper
ebud	Equal variances assumed	6,920	,009	8,287	1082	,000	,57468	,06935	,43861	,71074	
	Equal variances not assumed			8,896	381,788	,000	,57468	,06460	,44766	,70170	
spip	Equal variances assumed	,449	,503	14,036	1082	,000	,78551	,05596	,67570	,89532	
	Equal variances not assumed			13,501	329,818	,000	,78551	,05818	,67106	,89997	

Table 4. Independent sampel t-test results of local governments that have and have not implemented E-budgeting

	Score of implementation	Quality of financial reporting	Number of local governments	Percentage	t	Sig. (2-tailed)
E-budgeting	2,3101	Unqualified opinion	105	96%	8,28	,000
		Non-unqualified opinion	4	4%		
Non E-Budgeting	1,7354	Unqualified opinion	284	66%	14,03	,000
		non-Unqualified Opinion	149	34%		
SPIP	2,489	Unqualified opinion	367	92%	14,03	,000
		Non-unqualified opinion	34	8%		
NON SPIP	1,7035	Unqualified opinion	22	16%		
		Non-unqualified opinion	119	84%		

able to obtain unqualified opinions of 284 Local Governments or around 66%, while the remaining 149 local governments were only able to obtain Non-unqualified opinions or around 34%. Based on Table 4 value t of 8.287 with 0.000 significance probability. So it can be concluded that there is a difference between the average LKPD that uses e-budgeting and has not applied e-budgeting to the quality of financial reporting as measured by unqualified opinion.

E-budgeting is able to reduce information asymmetry between the government and the public regarding the use of budgets and the allocation of public resources. This can reduce agency conflict in agency theory between the government and the community. Public sector accountability has a very important role in the implementation of government activities because the implementation of public sector accountability aims to provide accountability to the community because the source of funds used comes from the community, presents information useful for decision making and for the reporting entity's accountability for the resources entrusted to it. In addition, the results of this study confirm the theory of stewardship where the local government as a trustworthy institution can provide good services to the public, be able to make financial responsibilities mandated to it so that economic objectives are met and public welfare can be achieved to the maximum.

Participation and transparency in the budget process with e-budgeting provide more relevant and reliable financial information as a basis for the preparation of LKPD. These results confirm the results of previous studies conducted by [12] where the results of the study showed that there was a significant positive effect between the use of e-budgeting on the quality of accounting information systems and local government financial reporting. That is because the information becomes more reliable and easy to trace per budget item related to the accountability aspects of planning and budget management of each local government.

2. Independent sample T-Test of the Government Internal Control System: In Table 4 it is seen that the average value of

the quality of financial reporting of local governments that obtain unqualified opinion has a SPIP maturity level with a score of 2.4890 or at the developing stage of 367 local governments around 92%, while the remaining 34 local governments have not been able to reach the unqualified opinion or around 8%. While the average quality of the financial reporting of local governments that have SPIP maturity with a score of 1.7035 or at the SPIP pilot stage is only 22 local governments or around 16% capable of obtaining unqualified opinion, while the remaining 119 local governments have not been able to get an unqualified opinion or around 84%. Based on Table 4 value t of 14.036 with a significant probability of 0.000. So it can be concluded that there is a difference between the average LKPD that has a better SPIP maturity level against the quality of financial reporting as measured by the unqualified opinion.

The government internal control system is able to guarantee the reliability of local government financial reporting through a series of SOP implementations, a tiered authorization process, segregation of duties as well as documentation and recording. SPIP assists the government in carrying out control and evaluation of the responsibility for using and reporting financial resources mandated to it. The better SPIP will be able to minimize the findings of internal control system weaknesses. Effective internal control at all levels and stages in the organization ranging from the existence of policies, the formation of the organization, preparation of the budget, facilities, and infrastructure, the determination of personnel who carry out, the determination of procedures and review at all stages affect the performance in achieving effectiveness and efficiency, adherence to regulations the legislation and the reliability of the presentation of government financial statements which means better internal control structures of local governments. The better the internal control structure, the better the quality of financial reporting in LKPD. These results confirm the results of previous studies conducted by [2] that cases of weaknesses in the internal control system and non-compliance with laws and regulations that occur in local governments in Indonesia show the poor quality of financial reporting in Indonesia. Therefore an

effective SPIP function is needed to create higher quality financial reporting (relevant, reliable, understandable, comparable, accurate, complete and timely).

5. CONCLUSION

Based on the results of tests that have been carried out in this study, it can be concluded as follows: 1). The results of this study support the hypothesis that there is an increase in the quality of local government financial reporting after the implementation of the e-budgeting system in planning, drafting and realization of local government budgets. 2). The results of this study also support the hypothesis that there is an improvement in the quality of local government financial reporting after the implementation of the local government internal control systems (SPIP).

E-budgeting is able to reduce information asymmetry between the government and the public regarding the use of budgets and the allocation of public resources. E-budgeting guarantees consistency and accountability between program planning and activities towards its budget. Participation and transparency in the budget process by e-budgeting provide more relevant and reliable financial information as a basis for preparing quality local government financial reports. The results showed that the implementation of e-budgeting and SPIP influenced the opinions given that had practical implications for local governments in making improvements in regional financial management and the quality of local financial reporting. Local governments are expected to be able to increase SPIP scores and e-budgeting in order to be able to create quality, transparent and accountable financial reporting.

6. RECOMMENDATIONS

the results of this study are important so It is recommended that:

Provincial and Regency/City of local governments In Indonesia are expected to implement e-budgeting in their budget preparation because it is mandatory from the president. Besides being able to increase transparency, accountability of public funds and public control, it can also improve the quality of financial reporting of local governments. E-budgeting is able to help local governments who have not been able

to achieve unqualified opinions. In principle, the e-budgeting system automates the process of preparing and implementing the budget and also the documents will be documented through digital footprint so that all stakeholders can monitor to minimize the occurrence of irregularities related to the realization of the budget and against the legislation. The implementation of e-budgeting is able to overcome the stealth budget and budget misuse such as markups, manipulation of goods specifications and misappropriation of the use of the budget that affects the quality of local government financial reporting.

7. SUGGESTIONS FOR FURTHER STUDIES

For the next research, it can increase the number of samples and years of research objects because it is expected that all local governments in Indonesia have implemented e-budgeting. Suggestions from the authors that local governments are expected to be able to make appropriate regulations so as to optimize the use of information technology systems in the implementation of e-budgeting.

COMPETING INTERESTS

Authors have declared that no competing interests exist.

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