

# Good government governance and opinions of the audit board of Republik Indonesia

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**Abstract:** This study aims to provide an empirical evidence over the transparency and accountability of local governments of Indonesia. This research is important because local governments should be able to apply the principles of good government governance, as a ways of improving services to the public. This study used two variables as predictors of the performance of local government financial reporting, transparency and accountability. The final sample for testing the relationship of transparency on the performance of local government financial statements are as many as 461 local governments. While the sample for testing the relationship of accountability on the performance of local government financial statements is as many as 1,238 in period 2009–2011. The results of the testing of both hypotheses of this study indicate that good government governance (shown by the degree of transparency and accountability) have been associated with the performance of local government financial statements.

**Keywords:** audit board of the Republik Indonesia; transparency; accountability; opinion

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## 1 Background

Since the Audit Board of Republik of Indonesia or *Badan Pemeriksa Keuangan Republik Indonesia* (BPK-RI) enforced auditing on regional financial statements as a regional responsibility of regional financial management autonomy, the performance creation and the measurement in public sector has become the priority in Indonesia. Now, local government should perform their ability in preparing a good financial statement as compliance to the *Part 18 Act Number 15, 2004* about inspection of state financial management and responsibility.

**Table 1** The result of BPKs opinion 2006–2011

<i>LKPD</i>	<i>WTP</i>	%	<i>WDP</i>	%	<i>TW</i>	%	<i>TMP</i>	%	<i>Total</i>
2006	3	1	327	70	28	6	105	23	463
2007	4	1	283	60	59	13	123	26	469
2008	12	3	323	66	32	7	118	24	485
2009	15	3	330	65	48	10	111	22	504
2010	34	7	341	66	26	5	119	22	520
2011	66	15.5	319	75	5	1	36	8.5	426

Source: <http://www.bpk.go.id>

Up to 2012, overview of the semester audited results BPK RI has showed how slow the enhancement of local government finance report (state as *Laporan Keuangan Pemerintah Daerah – LKPD*) quality is. Table 1 shows the result of audit opinion during 2006–2011. It displays the amount of local governments that have first rank audited opinion (*Wajar Tanpa Pengecualian – WTP*), an opinion that indicates local government's adherence to the administration and financial reporting according to the procedure and the reporting standard. Table 1 describes the result of BPKs opinion period 2006–2011.

There are four levels of opinion to be given to the local government and these are; *WTP* opinion, *Wajar Dengan Pengecualian* (*WDP*) opinion, *Tidak Memberikan Pendapat* (*TMP*) opinion, and *Tidak Wajar* (*TW*) opinion. This research will group BPK-RI's opinion into two types: *WTP* and non-*WTP* (included in *WDP*, *TMP* and *TW* opinions).

This research aims to provide an empirical research related with transparency and accountability that has been carried by each local government across the country. It is important to do because local government should be able to apply the principles of good government governance; in this context are accountability and transparency. Requisites of good governance should be supported by good government performance too, so that the funds managed by the government could be accounted for (accountable) without any effort of hiding information related to the receipt, allocation and disbursement of the funds (transparent). This research is expected to provide information for local government related to BPK-RI's audit result for local government finance report from each regency/city in Indonesia.

This research finds that transparency and accountability have a positive relationship with local government finance report performance reflected in the *WTP* Opinion. These findings also indicate that a local government which can implement the disclosure of government's extensive activities relatively is a local government which has a good financial reporting performance. This condition is in accordance with the prediction in the signalling theory. The contributions of this research are divided into practical and theoretical contribution. For the theoretical contribution, this research has given confirmation for the theory of organisational change related to the regency/city and province's preparations in actualising good government governance. On the other hand (for the practical contribution), the findings of this research give recommendation to the government and society about how far the implementation of transparency and accountability in the government of the city and regency across the country. This research also gives contribution to practitioners in the government sector, related with the

condition that should be applied to support the local government's transparency and accountability.

## 2 Literature reviews and hypothesis development

### 2.1 Basic theory

Research in the public sector in Indonesia did not have strong and various basic theories. But, some of the common theories used are the agency theory and the theory of organisational change. As well as this research, both of those theories will be used as the basic theory for the theoretical framework. The agency theory explains interaction (often stated as a conflict) between the owner (principals) and the manager (agents). In the agency theory that was introduced by Jensen and Meckling (1976), there was an information asymmetry between stakeholders, who are the principals and the agents since the firm separated both of them.

In local government's responsibility issue, the agency theory explains that the governments (as the agents) should be responsible for the funds that they managed for regional development and the citizens (as the principals). There could be an information asymmetry existing in this relationship because the government has more information than the citizens. For that reason, the government's transparency and accountability are needed by the citizens.

Another theory which is quite important to be the basic assumption in this research is the theory of organisational change. The research from De Korte and van der Pijl (2009) and Boonstra (2003) have deeply discussed the theory of organisational change in a government bureaucracy. This theory became the grounded theory in the research when it was the transition period on a duty in the Dutch Audit Department (Netherlands). Because this research also uses the same setting with the research that has been done by De Korte and van der Pijl (2009), this research will use the theory of organisational change as well. This theory used to explain that a government organisation has a major change after regional autonomy, even more when the inspection was performed by one of the state supreme institution which is BPK.

The signalling theory explains in more detail the entity's information disclosure, either in private sector or in public sector. Triyono dan Hartono (2000) said that signalling theory can explain relationship between companies' profitability and financial information disclosure. In a study where the entities' information disclosure are using a website, Marston (2003) explained that there is a significant relationship between the favourable information for the company (profitability) with the company's disclosure on the website. Even, the dissemination of information was getting upgraded since 2001 (Marston, 2003). They used the signalling theory by saying that the disclosure (one of which is using a website) used by the executives of the entity who have positive information to give a positive signal to external users (including the investors).

Mohamad et al. (2004, p.72) contends that accountability appears as the answer for the information asymmetry problem. The information asymmetry theory assumes that there is a lot of information gap between the managers who have direct access to the information and the constituents or the society outside the management. Scott (2008)

explained the lifespan of an organisation is determined by the ability to create an open information, balance and is equitable for the stakeholders.

## 2.2 *Previous study and hypothesis development*

Some researchers have done studies in the area of good government governance, particularly in the local government finance report (see Mulyana, 2006; Sopanah et al., 2004; Steccolini, 2002; Mardiasmo, 2006; Anondo, 2004). Mulyana (2006) found that financial statement accessibility had a positive and significant influence to regional financial transparency and accountability. While Sopanah et al. (2004) found there was relationship between public accountability, society participation and public policy transparency with budgeting knowledge and regional financial supervisory (APBD).

Steccolini (2002) did a research about the relationship between the local government's annual report presentation and accountability: whether the local government's annual report is available to the media for accountability. The result is the annual report looks like just being used for accountability enforcement to the internal users, however, the report did not have any significant role in the communication with the external users, so that actual financial report role and the accountability degree in Italy's local government should be questioned. The study that has been done by Mardiasmo (2006) about transparency actualising and public accountability through public sector accounting found that public sector accounting which being articulated through management accounting, financial accounting and public sector auditing has really pushed the development and application as an instrument to actualise transparency and public accountability in achieving good governance. This result is related to the study by Anondo (2004). Anondo concluded that regional financial statement and the regional head's performance accountability report had a positive influence to government/ regency's public accountability.

### 2.2.1 *Public transparency in local government's financial statement*

Transparency is one of the good governance principles. Transparency is built based on a free information flow, all of the governance processes, institutions and information should be accessible by the stakeholders, and the available information should be adequate enough to be understood and monitored. The financial statement is a form of transparency which needs the supporting requirement for accountability reflected in the government's openness or public resources management activity. Transparency of information, especially financial and fiscal information should be performed in a relevant and a simple form that could be understood (Campo and Tomasi (1999); in Mardiasmo (2006)). Transparency could be performed if there is clarity in duties and authority, the availability of information to the public, an open budgeting process and integrity guarantee from the independent parties about fiscal prediction, information and the explanations [IMF (1998) in Schiavo-Campo and Tommasi (1999)]. Nowadays, the government has already had government accounting standard which is the accounting principles that should be applied in preparing and presenting a financial statement (Peraturan Pemerintah Republik Indonesia Nomor 24 Tahun 2005).

In general, according to Hood and Heald (2006), transparency is a new culture in government openness which the dimensions of it refers to management rules and focus in the information. De Korte and van der Pijl (2009) gave transparency indicator as:

"Extensive use of written documents. The hierarchical relation is regulated, including the justification". On the other side, Sopanah and Mardiasmo (2003) states that budgets which are prepared by the executive could be considered transparent if it meets the following criteria:

- 1 there is a budget policy announcement
- 2 there is an available budget document and it is accessible
- 3 there is a timely accountability report
- 4 accommodation of people's vote/suggestion
- 5 there is an information delivery system to the public.

Transparency is a form of freedom to access political activity and the government's economy and the decisions according to Shende and Bennett (2004). Transparency enables all of the stakeholders to see the government's structure and function, the purpose of the policy and the fiscal projection, and also the last period's (accountability) reports. Katz in Yahya (2006) stated that transparency is an essential democratic process where every citizen could openly and clearly see every single government's activity than let those activities be kept confidential. The spirit of this system is that every citizen has the right to get information through government officials' accountability on their activities. From the explanation, the hypothesis of the research is formulated as below.

Ha<sub>1</sub> Transparency has a positive relationship with local government finance report performance.

#### 2.2.2 <sup>1</sup> Accountability of local government's financial statement

The quality of good governance is not just determined by accountability, transparency, society's participation and the supremacy of law. But, the quality of good governance is also determined by other factors such as responsiveness, consensus orientation, equity efficiency, effectiveness and strategic vision. It is in accordance with the characteristics of good governance which are defined by UNDP and World Bank. According to Mardiasmo (2004), regional financial public accountability is giving information and the disclosure of regional financial activities and performance to the stakeholders so that the public rights, which are the right to know, the right to be kept information and the right to be listened to, can be fulfilled.

The study by Sulistoni in Sopanah et al. (2004) describes the accountability of government. It has the following characteristics:

- 1 able to present governance information openly, fast and precisely to the society
- 2 able to give satisfying service to the public
- 3 able to give a space for the citizens to get involved in the development process and government
- 4 able to explain and be responsible for every public policy proportionally
- 5 there are facilities for public to rate the government's performance.



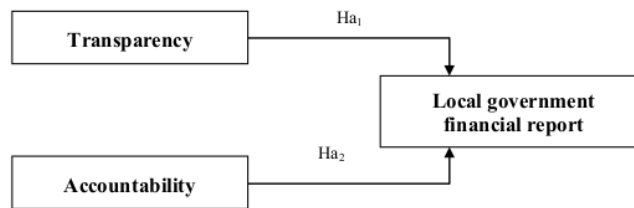
Through public accountability, the society can rate the degree of achievement of programme implementation and the government's activities.

Public accountability can be achieved if the supervision by the council and citizens works effectively. Sopanah et al. (2004) stated that to create accountability to the public, it needs the participation of institute head and the people in preparing and supervision of regional finance (APBD) so that high public accountability will strengthen supervisory function performed by the council. This accountability can be observed from the budget variance which is the difference between expenditure budget and expenditure realisation because the higher the variance is, it shows the lower level of accountability and it also shows that the local government has not done well in managing the expenditure budget. From the explanation, the hypothesis of the research is formulated as below.

Ha<sub>2</sub> Accountability has a positive relationship with local government finance report performance.

The research models that represent both of the hypotheses of this research are shown as below.

**Figure 1** Research model



### 3 Research method

#### 3.1 Data, sources and definition of operational variables

The type of data used is secondary data. This research uses secondary data that can be downloaded from the local government's financial agency in each regency/city across Indonesia.

The data for each variable is explained as below:

- 1 *Transparency*: Transparency is giving open and fair financial information to the citizens based on the consideration that citizens has rights to openly and thoroughly know government's accountability in managing entrusted resources and government's adherence to the law (SAP, 2005). The transparency data will be downloaded from the website of each city and regency across Indonesia. The transparency level is determined from the information which disclosed on the website. The more the disclosure on the website is, the more transparent a city and regency would be.

The disclosure criteria will be categorised in five criteria as explained by Sopanah and Mardiasmo (2003) plus one more for other information which is published by



the local government related to other essential activities that has unbounded criteria, such as free procurement information/tender, investment opportunities information in local area, natural resources information, green government information, and many other that contains valuable information. If it meets the six criteria then that local government will be scored with 6 (six), and so on. The more the information released by the local government to the website is, we can assume that the higher the transparency level of that local government would be.

- 2 *Accountability*: Accountability is the responsibility of resource management and policy enforcement that has been trusted to every reporting entity in achieving the purposes that have been determined periodically (SAP, 2005). This data will be tracked by budget realisation report (*Laporan Realisasi Anggaran – LRA*) period 2009–2011 and the early year budget. The accountability data is acquired by comparing regional expenditure budget and the realisation. The higher the variance of each budget point is, the lower the accountability of the local government's financial statement would be.
- 3 *Performance of the local government's financial statement*: This data would be determined by BPK-RI opinion to the local government's financial statement. The better the performance of local government's financial statement is, the BPK-RI opinion to local government's financial statement will get closer to WTP.

### 3.2 Statistical tools

Statistical tools that are used for hypothesis testing is done by using simple regression analysis for each hypothesis testing. Each test has to be performed because data sources for both independent variables are not same. The purpose of this test is to predict how powerful independent variable influences the dependent variable, so the regression equation for each first and second hypothesis is shown in equation (1) and equation (2) below.

$$Y = \beta_0 + \beta_1 X1 + e_i \quad (1)$$

where

Y BPKs opinion

X1 transparency.

$$Y = \beta_0 + \beta_1 X2 + e_i \quad (2)$$

where

Y BPKs opinion

X2 accountability.

## 4 Results and discussion

### 4.1 Samples and research's final data

Samples used in this research are separated for each first and second hypothesis test. The first hypothesis test states that transparency is positively related with the local government's financial statement performance that is using the samples as shown in Table 2. Whereas the samples for second hypothesis state that the budget's variances is negatively related to the local government's financial statement performance in Table 3.

Table 2 shows that the totals of final samples for transparency are 461 local governments. The broadness transparency for each local government is various, but it can be categorised into six categories as shown in the table. The local government's samples for accountability's measurement taken from 2009, 2010 and 2011 from 2012 budget realisation report shows that most of the local governments in Indonesia got non-WTP opinions during the observation period. The total of the local governments that have been observed are 1,238 local governments, consisting of 1,149 local governments who got non-WTP opinion and 89 local governments who got WTP opinion.

**Table 2** Local government samples for transparency measurement 2013

Totals of identified local government, explanation as follows:		461
a	Local government whose website is inactive per 10 May 2013–30 July 2013	37
b	Local government whose website is inactive for various reason (under construction, hacked by... and has an inaccessible website) per 10 May 2013–30 July 2013	93
c	Local government whose website only loads one category	0
d	Local government whose website simply loads two categories	19
e	Local government whose website simply loads three categories	48
f	Local government whose website simply loads four categories	141
g	Local government whose website simply loads five categories	56
h	Local government whose website loads whole six categories	67

*Source:* Local government website, 2013

**Table 3** Local government's samples for accountability measurement period of 2009, 2010, and 2011

Totals of identified local government, explanation as follows:		1,238
a	Local governments who got non-WTP opinion from BPK	1,149
b	Local governments whose financial statement got WTP opinion from BPK	89

*Source:* Budget Realization Report (LRA), 2012

### 4.2 Research data

Transparency data obtained from the information disclosed by the company in each local government's website. Transparency data are divided into six categories, consisting of:

- 1 information about policies/legislation

- 2 budget documents
- 3 timely financial accountability reports
- 4 citizen's vote/suggestions/interactive media
- 5 information delivery system to public/website existence
- 6 other information, such as regional potential, investment opportunities, regional head's activity, open auction/tender and other valuable information.

#### 4.2.1 Accountability data

Accountability data is obtained by comparing the local government's budgets to the budget realisation. The data were taken from LRA from the periods 2009, 2010 and 2011. From these LRA data, variance of local expenditures with the realisation can be determined. These variance values are then regressed by logistic regression towards BPK-RIs opinion on the related local government's financial statement.

#### 4.2.2 BPKs opinion data

BPK-RIs opinion data used in this research is taken from the actual BPKs data, which was obtained from various sources, such as from BPK office itself, local government website, LRA, and many other sources. Nevertheless, in this research, BPK-RIs opinion data is acquired from *Summary of Audited Results 1st Semester, 2012 – Book Number II* of Financial Statement Audited which is released by BPK-RI.

**Table 4** Descriptive statistics for transparency

<i>Variable</i>	<i>N</i>	<i>Minimum</i>	<i>Maximum</i>	<i>Mean</i>	<i>Std. deviation</i>
BPKs opinion	461	0.00	1.00	0.1438	0.35126
Transparency	461	0.00	6.00	3.1046	2.16310

*Source:* Each local government's website (processed data)

#### 4.3 Descriptive statistics

Explanation related to descriptive statistic gives an illustration about data used in this research. Table 4 shows maximum value, minimum value, mean/average, and standard deviation related to accountability data.

BPK-RIs opinion in 2012 for 461 local governments in Indonesia with the average (mean) at 0.1438 shows that in the period of the year most of the local governments in Indonesia got non-WTP opinion. Minimum value set for BPK-RIs opinion is 0 which represents non-WTP opinion, whereas the maximum value is 1 which represents WTP opinion. The value of standard deviation is 0.35126 which shows the deviation for each observation data is relatively small.

Descriptive statistics for local government's transparency through the website shows average value/mean at 3.1046. This value means the local governments have tendency to do disclosure about their activities, including the financial performance disclosure. This condition is expected to be better in the future. Furthermore, the value of standard deviation is 2.16310 which shows that the deviation for each observed transparency data

is relatively small. Meanwhile, Table 5 shows maximum value, minimum value, mean/average and standard deviation related to local government accountability data.

**Table 5** Descriptive statistics for accountability

<i>Variable</i>	<i>N</i>	<i>Minimum</i>	<i>Maximum</i>	<i>Mean</i>	<i>Std. deviation</i>
Opinion	1,238	0.00	1.00	0.0719	0.25841
Variance	1,238	0.00	55.00	10.1502	6.26523

*Source:* IHPS BPK-RI (processed data)

BPKs opinions in the year of observation 2009, 2010 and 2011 from 1.238 local governments in Indonesia have average value (mean) of 0.0719. This value shows that in three consecutive years, most of the Indonesian local governments got non-WTP opinion. In average, the percentage of Indonesian local governments who got BPKs opinion in 2009–2011 periods is 7.2% (89 of 1.238). Minimum value determined for BPKs opinion is 0 which represents non-WTP opinion whilst the maximum value is 1 which represents WTP opinion. While the standard deviation value is 0.25841, which means the deviation of each observation data is relatively small.

Descriptive statistics for accountability variables (proxied by budget variance) shows average value (mean) of 10.1502. This value indicates the percentages of local government's budget variance reaches 10% from 1.238 local governments observed, averagely. The standard deviation of accountability variables value is 6.26523, which means that the deviation of each transparency data is relatively small.

#### 4.4 Hypothesis testing

This first hypothesis research stated that transparency positively related with local government's financial statement's performance, tested by logistic regression. The results of logistic regression test for the whole built models are significant at level 0.000 with Cox and Snell R-square is 0.107 and Nagelkerke R-square's value is 0.191. These values show that the variables in the models have a corresponding relationship. This could also imply that the research model for the first hypothesis testing is a good model.

**Table 6** Transparency category test result

<i>Independent variables</i>	<i>B</i>	<i>Wald</i>	<i>Sig.</i>
Transparency (0)	3.848	49.943	.000*
Transparency (2)	2.657	33.392	.000*
Transparency (3)	1.930	6.018	.014**
Transparency (4)	1.558	10.664	.001*
Transparency (5)	1.777	24.825	.000*
Transparency (6)	2.662	17.176	.000*

Notes: \*significant on level < 1%; \*\*significant on level < 5%.

Dependent variable: BPKs opinion.

Dependent variable: Opinion BPK.

The next step is identifying whether the test score of government information disclosure through the local government's website have a strong relationship with WTP opinion that has been given by BPK-RI. Statistics test result shows a significant relationship between

the local government's disclosures on website with WTP opinion's score that has given by BPK-RI for the related local government's financial statement. Wald value represents the strong relationship between the independent variables with the dependents, which is 181,039. Coefficient values 0.39688 give a signal if a local government improve their transparency in the website by one point, and then there is a possibility for that local government to get a better BPKs opinion by 0.39688 point. Overall, these significant relationship values between transparency and BPK-RIs opinion at 0.000 gives the rationale that there is a positive relationship between transparency and local government's financial statement's performance. This result becomes the basis to accept the first hypothesis of this research.

As shown in Table 6, it supports the explanation stated that each transparency is positively related and significant on the WTP opinion that has been given by BPK-RI for the related local government's financial statement's activity. Table 6 also shows that there is no local government in the first transparency category. It indicates that through the website, the local government can improve their transparency performance. This finding also means to support the idea given by Mardiasmo and Sopanah (2002) that an activity/performance can be transparent if it contains the following:

- 1 information about policies/legislation
- 2 budget documents
- 3 financial accountability reports
- 4 citizen's suggestion/interactive media
- 5 information delivery system to public/website existence.

The second hypothesis testing stated that accountability is positively related to local government's financial statement's performance which uses logistic regression. This regression logistic test for built models on this second hypothesis shows the significance at level 0.018 with Cox and Snell R-square by 0.04 and Nagelkerke R-square at 0.11. This model testing result indicates that the research models have a strong relationship. This could also imply that the models used in this research for the second hypothesis research is a good model. Reversed value is used to test this second hypothesis, because the data provided is the variance data between the local budgets and the budgets realisation. Furthermore, identification will be done to decide whether the budget variances have a negative relationship towards the BPKs opinion as for the related local government's financial statement.

Statistics test result shows a negative relationship between budgets variances and the WTP opinion given by BPK as for related local government's financial statement. Wald value represent a strong relationship between the independent variables and the dependents for 540,489, B value = -2,558 with significance to 0.029, giving signals that the lower the deviation of the local government budgets with the realisations, the possibilities of the local government financial report's activity to get the WTP opinion would be increased. Furthermore, the coefficient of variance at -0.04832 which means when a local government's budget variance increased by one point, the possibilities for the local government to get BPKs opinion will decrease by 0.39688. This result concludes that budget variance is negatively related to performance of local government's financial statement, so this second hypothesis in this research is acceptable.

**Table 7** Logistic regression testing result

<i>Independent variables</i>	<i>Coefficients</i>	<i>B</i>	<i>Wald</i>	<i>Sig.</i>
Transparency	0.39688	1.789	181,039	0.000*
Accountability	-0.04832	-2.558	540,489	0.0285**

Notes: \*significant on level < 1%; \*\*significant on level < 5%.  
Dependent variables: BPKs opinion.

Accountability is an ethical concept that has a close relationship with public government administration (government executive institution, parliamentary legislative institution and judicial institution) that has other meanings, such as, it is often used as a synonym to the concepts such as accountable concept (Dykstra, 1939). So, an analogy from the explanation and this research results is that the local government who is capable in realising the budgets which is approved by the legislatures in the beginning of budget year is a local government who can carry out accountability concepts which becomes one of the (important) values in accountability. The higher the local government's accountability is, the higher the possibilities to get WTP opinion. The statistic result of this research is shown in Table 7.

## 5 Conclusions, implications, and suggestions research

This section becomes the finale section of this research, which will explain the conclusion of the research, implications, also the limitation and suggestion that can be given by the researcher. In this last chapter, conclusions will be given from the whole research findings. This research found that transparency and accountability have a positive relationship with the local government's financial statement's performance which is reflected by the WTP opinion that's given by BPK-RI. These findings also indicate that a local government which can implement the disclosure of government's activities relatively extensive is a local government which has a good financial reporting performance. This condition is in accordance with the prediction in the signalling theory.

Furthermore, statistic test results showed a negative relationship between budget variance with WTPs opinion value which is given by BPK for related local government's financial statement. Statistic value gave a signal that the lower the difference between local government budgets with the realisation, the possibilities of local government financial report's performance got WTP opinion would be higher. This also concluded that the budget variance is negatively related with the local government financial statement's performance and both of the hypotheses in this research were accepted.

The next implication is, from the accountability issues test's result which is an ethical concept, accountability is actualised when the local government capable in realising the budgets which is approved by the legislatures in the beginning of budget year. An accountable local government is a local government who can fulfil its responsibility in budgeting because it has become one of the important values in accountability.

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