

Quality of Regional Government Financial Reports: The Effect of Internal Control, Quality of Human Resources and Implementation of the Accrual Basis

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Abstract

Quality government financial reports will be reflected in the information presented in the financial reports. Therefore, the control factors applied, the quality of the employees, and the accounting system applied will also determine the quality of the financial reports produced. This research aims to examine three factors, namely internal control, quality of human resources, and the application of the accrual basis to the quality of Regional Government financial reports. Sampling in this research used a non-probability sampling design with a judgment sampling technique using an instrument in the form of 90 questionnaires which were distributed directly. The data analysis method in this research used Structural Equation Model (SEM)-PLS analysis. The research results show that the quality of Human Resources and the application of the accrual basis affect the quality of Regional Government financial reports, but internal control is unable to have a significant impact on the quality of Government financial reports.

Introduction

One form of accountability in the administration of regional government is to realize financial management that is transparent and accountable, both at the central and regional government levels. Therefore, the government financial reports produced must meet timely principles and be prepared according to Government Accounting Standards based on Government Regulation Number 71 of 2010. Government financial reports are submitted to the DPR/DPRD and can then be accessed by the public after being audited by the Financial Audit Agency (BPK). The components of the financial report submitted by PP 71 of 2010 include the Budget Realization Report, Balance Sheet, Operational Report (LO), Equity Change Report, SAL Change Report, Cash Flow Report, and Notes to Financial Reports.

Quality Regional Government Financial Reports (LKPD) are related to the application of the accrual basis. Accrual-based accounting is considered better than cash-based accounting. Accrual-based accounting is believed to produce financial reports that are more reliable, comprehensive, and relevant for economic, social, and political decision-making (Mardiasmo, 2019). Quality financial reports must be prepared by the principles and rules

contained in the applicable accounting standards, therefore the LKPD must refer to the established SAP. Government Accounting Standards (SAP) serve as a reference for whether Regional Government Financial Reports (LKPD) have been prepared based on an adequate system and whether the information contained is by Government Accounting Standards (SAP). Preparing financial reports will be of high quality if they refer to Government Accounting Standards (SAP). This reason is based on research conducted by (Juwita, 2013). Apart from that, the government is required to implement an internal control, reporting, and accounting system by the provisions of applicable laws and regulations (Halim, 2012). The internal control system is an integral process of activities carried out by management and its staff to guarantee the achievement of organizational goals through effective and efficient activities. Apart from that, the reliability of financial reports, security of state assets, and compliance with laws and regulations (Mahmudi, 2016). Increasing the quality of internal control can reduce the desire and opportunity to abuse authority and power. The elements of internal control are elements that are closely intertwined with each other, the control process is integrated into actions and activities carried out continuously by the leadership and all employees, therefore, the foundation of control is the people (HR), in an organization that forms a good control environment in achieving the goals and objectives to be achieved.

Apart from the implementation of Government Accounting Standards (SAP), Accounting Policies, and the Use of Information Technology (IT), another important thing is the quality of Human Resources (HR). The process of preparing financial reports is the most important for an organization to find out how the performance or existence of an organization is in one period, therefore if it is not supported by the quality of the accounting staff itself then the implementation of government accounting standards and the internal control system cannot run effectively and cannot produce financial reports that have quality information that can be used by users of that information (Udiyanti, 2014). Therefore, competent human resources are needed to produce quality financial reports. HR quality is a characteristic of a person that can be seen from the skills, knowledge, and abilities he has in completing the tasks assigned to him (Indriasari, 2016). The human resources required in preparing financial reports should be able to rely on their ability to understand and apply accounting policies that have been determined by PP 71 of 2010 both at the Regional Apparatus Organization (OPD) level as the reporting entity and at the work unit of the Regional Financial and Asset Management Agency (BPKAD) as the Accounting Entity (compiler of the consolidated report), in reality, the Human Resources available in the OPD Services are still not as effective as expected, namely, there is still a lack of professional staff and a lack of staff with an accounting background. The quality of financial reports assessed by the BPK is consolidated financial reports, namely a collection of consolidated financial reports from OPD. Thus, the financial report prepared by the OPD is a source of data in the preparation of the consolidated report, thus the inability to prepare financial reports at the OPD level will affect the quality of the Consolidated Financial Report.

Previous research explaining the quality of local government financial reports was conducted by Tuti Herawati (2019) which states that the internal control system has a positive and significant effect on the quality of financial reports in the Cianjur Regional Government. However, these findings are not in line with Reni Yendrawati's research (2019) carried out at the Yogyakarta Special Region Social Service and UPTD-UPTD within the Yogyakarta Special Region Social Service, which found that internal control hurt the quality of financial reports. Meanwhile, Gimeilia Sarma Research (2023) explained that the implementation of the accrual basis affected the quality of financial reports at the Padang Pariaman Regional Government. This research is not in line with Feni Pirani's research (2023) that the implementation of accrual-based government accounting standards in SKPD Bantul Regency does not affect the quality of financial reports. Explanatory factors for the quality of financial

reports that are linked to the quality of Human Resources were found in Andul Hafiz Tanjung's research (2021) that the quality of human resources has a positive effect on the quality of local government financial reports. The results of this research are different from the findings of Dewi Septiani Sukma (2023) that the reliability of Nagari Government Financial Reporting in Padang Pariaman Regency is not influenced by the quality of human resources. Several previous research results still show differences in the factors that explain the quality of local government financial reports.

This research is structured to include the first part being an introduction, and the second being a literature review and hypothesis development. The third part is the presentation of data and methodology, statistical description, and research design. The fourth section is the results and discussion and finally the research conclusions.

Literature Review and Hypothesis

Agency Theory

Agency theory is a theory that explains the relationship between shareholders (*principal*) and managers (*agent*) which exists because of a contract. The originators of agency theory were MC Jensen and WH Meckling in 1976. This theory assumes that efficient performance and organizational performance can be determined by the efforts made and the influence of environmental conditions. Meanwhile, in general, this theory assumes that the principal can be neutral towards risk, in contrast to agents where agents tend to be resistant to business and risk. Referring to a theory, namely agency theory, public accountability is the obligation of the person holding the mandate (*agent*) to provide all accountability, present, report, and disclose all activities and activities that are their responsibility to the party giving the mandate (*principal*) it has the right and authority to demand accountability (Faristina, 2011).

In connection with various problems in agency, the practice of financial reporting in a public sector organization is a concept that is based on agency theory. In financial reporting, it is the government that holds the position of an agent who is obliged to provide information that is beneficial to users of government financial information acts as a principal in assessing accountability and can make good decisions in terms of economic, social, and political decisions. The implications of *agency* theory are related to research variables related to internal control, the quality of human resources the application of the accrual basis, and the quality of regional financial reports.

In public accountability, the party given the trust (agent) has an obligation in the form of responsibility to report, record, and disclose all activities and activities that are their responsibility to the principal as the party giving the trust where the principal has the right to collect this (Mardiasmo, 2018). Public accountability is divided into two, namely: 1) vertical accountability, namely a form of responsibility for the use of funds to higher parties, and 2) horizontal accountability, namely a form of responsibility for the use of funds to the wider community.

Internal Control _

The MPR (People's Consultative Assembly) decision outlines that it is deemed necessary to empower supervision by state institutions, and political and social institutions. This is related to the People's Consultative Assembly Decree Number, and Nepotism, then the role and function of supervision, court, and examination become very strategic.

According to PP no. 60 of 2008 concerning Government, Internal Control Systems states that internal control is the entire process of activities, reviews, evaluations, monitoring, and other supervisory activities regarding the implementation of organizational tasks and functions to provide adequate confidence that activities have been carried out by

predetermined benchmarks. effectively and efficiently for the interests of leaders in realizing good governance.

Supervision is carried out by internal supervisory officers, to achieve effectiveness and efficiency of activities, reliability of financial reports (budget realization in the government sector), as well as compliance with applicable regulations. Internal control in a region is carried out by the inspectorate in that region which supervises the running of regional government. Internal control is a system step or tool that provides guarantees for the success of the performance targets of an activity (Halim 2012). Internal control is as follows: Supervision activities carried out by leaders or top managers and/or leaders or managers of work units within the organization and their respective units or work units (Nawawi, 2000).

Internal control is an activity carried out by internal officials appointed by regional officials to supervise government activities ranging from implemented programs to regional financial management so that they comply with applicable procedures. The purpose of internal control is divided into two, namely maintaining company assets and checking the accuracy and reliability of accounting data (Mulyadi, 2015). The main objective of internal control is to ensure loyalty to management policies and instructions for achieving organizational goals, protecting assets, safeguarding necessary information, reliable information, information integrity, ensuring completeness and accuracy of records, and ensuring compliance with the demands of the law. (Halim, 2012)

From the points above it can be concluded that internal control aims to encourage the government to realize regional financial accountability which is getting better and better, and is directed at creating transparency and accountability of regional financial administrators which is characterized by the implementation of *Good Governance*. The implementation of supervision carried out by various institutions is inefficient and ineffective and even creates and increases irregularities and the occurrence of worker *overlapping*. Another objective of internal control is to obtain objective information from the activities being supervised. Audit results must be widely published to the public so that what is presented, reported, and accounted for is by the wishes of the community in its implementation activities.

The Ministry of Home Affairs operates efficiently and effectively by plans and provisions of statutory regulations, such as Article 1 paragraph (1) of Minister of Home Affairs Regulation Number 2 of 2008. This article is about guidelines for regular inspections within the Ministry of Home Affairs, which states that regular inspections, hereinafter referred to as inspections, are activities to know and assess carefully and thoroughly the targets of the objects being inspected and are carried out on a scheduled basis.

Based on the regulations and expected objectives, an instrument was developed to measure internal control with six (6) dimensions, namely internal control program, implementation, follow-up, coordination, increasing the capacity of the internal control apparatus (API), and the condition of Human Resources (HR). According to Wiratna, (2017), Internal control consists of 5 indicators, namely; control environment, risk assessment, control procedures, information and communication, and *monitoring*.

Quality of Human Resources

The quality of human resources is the ability of human resources to carry out the duties and responsibilities given to them with sufficient education, training, and experience. Human resources are the main supporting pillar as well as the driving force of an organization in its efforts to realize the vision, mission, and goals of the organization. Human resources are a very important organizational element, therefore it must be ensured that human resource management is carried out as well as possible so that they can contribute optimally in efforts to achieve organizational goals.

In good regional financial management, SKPD must have quality human resources, supported by an accounting educational background, frequent education and training, and experience in the financial sector. So to implement an accounting system, quality human resources (HR) will be able to understand accounting logic well. The failure of local government human resources to understand and apply accounting logic will have an impact on errors in financial reports made and non-conformity of reports with standards set by the government. However, nowadays many human resources do not have an accounting education background, but because they often attend training and so on so that they can understand and understand accounting, this can also be said to be human resources who have quality.

Competence is a characteristic of a person that can be seen from the skills, knowledge, and abilities he has in completing the tasks assigned to him (Indriasari, 2016). Competence is the basis for a person to achieve high performance in completing their work. Human resources who do not have competence will not be able to complete their work efficiently, effectively, and economically. In this case, the work produced will not be on time and there will be a waste of time and energy. With human resource competence, time for preparing financial reports will be saved. This is because human resources already have knowledge and understanding of the things that must be done so that the financial reports prepared can be completed and presented on time. The sooner financial reports are presented, the better it will be in terms of decision-making (Mardiasmo, 2012).

The theory of human resource (HR) quality in this research was put forward by Rani (2015) According to him, HR quality can be measured using theory, namely physical quality which is determined by aspects of skills, energy strength, or health, and non-physical quality in the form of education, experience or maturity, attitudes and values.

Accrual Basis

The accrual basis of accounting, as has been concluded by (KSAP, 2006), is an accounting basis on which economic transactions and other events are recognized, recorded, and presented in the financial statements at the time the transaction occurs, without regard to the time cash or cash equivalents are received or paid. Furthermore, in the same paper, KSAP stated that in accounting-based accrual, recording time *corresponds* to when the resource flow occurs, so it can provide the most comprehensive information possible throughout resource flows. It can be concluded that the accrual basis can fulfill reporting objectives that cannot be met by the cash basis, those reporting objectives are managerial and supervisory goals.

From the explanation of the meaning of accrual basis accounting above, it can be concluded that accrual basis accounting is an accounting basis on which rights and obligations are based. A transaction or other economic event is recognized when it occurs events, regardless of cash or cash equivalents received or paid. Additionally, base Accruals can meet reporting objectives that cannot be met on a cash basis including managerial and supervisory objectives.

The accrual-based accounting system is an accounting basis in which economic transactions and other events are recognized, recorded, and presented in the financial statements at the time the transaction occurs, without regard to the time cash or cash equivalents are received or paid. The indicators for implementing the accrual basis (KSAP, 2006) consist of 1) Integrity/commitment, 2) Human Resource Readiness, 3) Facilities and Infrastructure Readiness, and 4) Information System Readiness.

Quality of Financial Reports

Financial reports are the final product of the accounting system that applies to an organization, both private organizations and government organizations. Financial reports in government organizations are assertions from government management that inform other parties (*stakeholders*) about the government's financial condition. In Indonesia, the basic financial reports that must be made by the government as stated in Article 30, Law No. 17/2003 concerning state finances include APBN/D realization reports, balance sheets, cash flow reports, and notes to financial reports.

The purpose of financial reports according to PP No.71/2010 is to be used for accountability, namely to account for the management of resources and implementation of policies entrusted to the reporting entity in achieving goals that have been set periodically; and management, namely helping users to evaluate the implementation of the activities of a reporting entity in the reporting period to facilitate planning, management and control functions over all assets, liabilities, and equity of government funds for the benefit of the community.

The purpose of financial reports is important for both private organizations and governments, so the government needs to pay attention to the quality of these financial reports. Quality is something that meets or exceeds predetermined expectations or criteria. The criteria for assessing the quality of financial reports according to PP No.71/2010 concerning Indonesian Government Accounting Standards are understandable, relevant, reliable, and comparable. The criteria mentioned above refer to the information presented in the financial statements. The quality of financial reports will improve the quality of the information presented in financial reports. Users of financial reports are confident in making decisions because they are based on information that has been well prepared, approved, and audited in a transparent, accountable, and quality manner. This opinion shows that the quality of financial reports is the extent to which financial reports present correct and honest information. This means that the quality of financial reports shows the concept of the quality of information from the report.

Based on PP No.71/2010 concerning Government Accounting Standards regarding the quality of regional government financial reports, as previously explained, the qualitative characteristics of financial reports are normative measures that need to be realized in accounting information so that it can fulfill its objectives. The following four characteristics are normative prerequisites needed so that government financial reports can meet the desired quality, namely; relevant, reliable, comparable, and understandable.

Hypothesis

Internal control is not only for carrying out verification actions but is also intended to assist the supervised party in carrying out their duties better. In the Indonesian government's organizational structure, the internal control function is carried out by the Financial and Development Supervisory Agency (BPKP) and the Inspectorate General of Development (Irjenbang). Previous research explaining the internal control system was carried out by Tuti Herawati (2019), Gimeilia Sarma (2023), Feni Pirani (2023), and Dewi Septiani Sukma (2023) who stated that the internal control system has a positive and significant effect on the quality of Regional Government financial reports. *Abdul Hafiz Tanjung (2021)*, states that the internal control system hurts the quality of financial report information.

The new regional government accounting system already regulates accrual-based accounting. If the financial report is presented, it meets the characteristics of a reliable financial report, meaning that the financial report contains information that is presented honestly and fairly. The effectiveness of an internal control system is needed to assist organizational activities in making objective and accountable decisions. Apart from that, the

use of technology also plays an important role in the timely presentation of financial reports and the data processing process. The better the level of technology used, the higher the quality of the financial reports produced (Tampubolon and Basid, 2019). Human resource competency is an individual's ability to do a job. With good human resource competence, it can save time in preparing financial reporting (Apriansyah, et al, 2020). Quality resources are needed to produce quality financial reports (Suparno, 2017). According to Sutaryo (Sutaryo, 2011), human resources are a factor that influences the readiness and effectiveness of implementing regional financial accounting systems. According to (Guy., 2002). Competency is the knowledge and skills required to complete a task. Adequate human resource competency in terms of quantity and quality will increase the value of information in local government financial reporting. Human resource capacity has a positive effect on the quality of financial report information (Reni Yendrawati, 2019). *Results*

The change in the accounting basis from the cash basis to the accrual basis is expected to provide benefits related to information on *cost determination* in the context of *cost-saving programs* as well as information on assets to provide accurate information regarding increasing revenue (*revenue generating*). The implementation of accrual-based accounting is expected to increase accountability, and sustainability, provide a better basis for measuring the impact of government policies, increase organizational efficiency and effectiveness, and encourage increased integrity. An accrual-based accounting framework is very important for determining the total cost (*full cost*) of government activities systematically, which ultimately plays an important role in achieving a more efficient and effective public sector performance management framework (Irawan, 2013). Several previous studies stated that the application of accrual basis accounting provides positive value for improving the quality of Regional Government financial reports Gimeilia Sarma (2023).

The research hypothesis formulated in this study:

H₁: Internal control influences the quality of financial reports

H₂: The quality of human resources influences the quality of financial reports.

H₃: Implementation of the Accrual Basis influences the quality of financial reports.

Research Methods

This type of research is quantitative research with a survey method. The survey was conducted on all Papua Province government employees, using judgment sampling techniques and a sample of 90 respondents was obtained that met the requirements (Sekaran & Boogie, 2021). Meanwhile, the PLS structural equation modeling (SEM) analysis method was carried out to process and analyze research sample data which includes; measurement model testing (validity and reliability), model suitability testing, and hypothesis testing.

Data analysis testing begins with testing the validity of the data using the *outer model test* of each construct or variable. The *outer loading* value is provided that the value is > 0.7 . Data validity testing also uses the *convergent validity (AVE) value* with the measurement value having to be greater than 0.5 (Solimun et al., 2017) while data reliability testing uses *composite reliability* and *Cronbach's alpha* which is based on the latent variable coefficients. The measurement instrument for reliability values is based on internal consistency and *Cronbach's values alpha*. If the value is > 0.70 , so construct has high-quality *reliability* (Solimun et al., 2017). Meanwhile, testing the model for the accuracy of prediction of the independent variable on the dependent variable (*The goodness of fit*) uses the *R-squared* value of the variable. *R-Square* Value > 0 shows the model has a predictive relationship and if the *R-Square value* = 0 shows that the model lacks predictive relationship value. Hypothesis testing in this research uses the *t-test* on the outside model

and *inner models*. Hypothesis statistics for the inner model from the influence of latent variables exogenous against variables Endogenous is $H_0: \beta=0$ and $H_1: \beta \neq 0$.

Results and Discussion

Respondent Profile

The respondents used as samples for this research were 90 employees in Papua Province. A total of 105 questionnaires were distributed with a questionnaire return rate of 85.71 % as shown in Table 1.

Table 1. Questionnaire Return Rate

Description	Amount	Percentage (%)
Distributed questionnaires	105	100
Unreturned questionnaires	15	15.29
Number of questionnaires returned and eligible	90	85.71

Source: SEM-PLS processing results

Table 1. describes the rate of return of questionnaires from research respondents which were distributed directly to the Regional Apparatus Organization Financial Administration Officer (PPK-OPD), Accounting and Regional Assets Section of BPKAD Papua Province. The number of questionnaires returned was 90 questionnaires or 85.71% of the 105 distributed and met the requirements to be used as a sample after validating the questionnaire.

Evaluation of validity testing through quality testing criteria produces an *outer model value* >7 and this means that the validity of the data meets the valid criteria. The results of the *outer model* are explained in Figure 1 while the results of the reliability test are shown in Table 2.

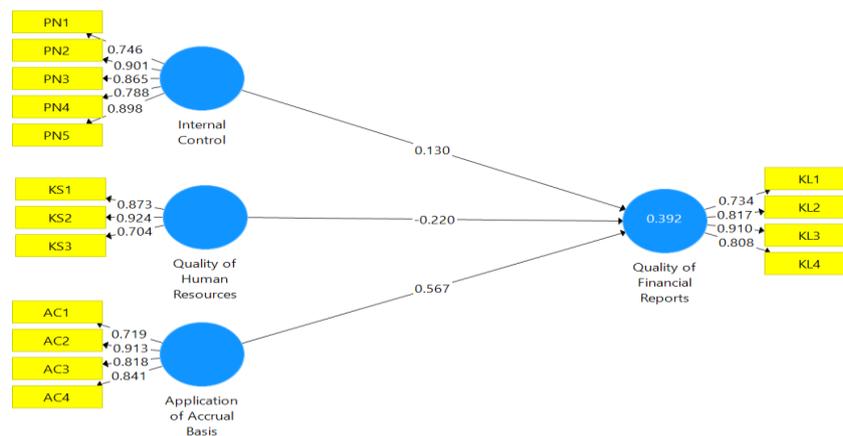


Figure 1. Outer Model Results

Table 2. Reliability Test Results

Variable	Measurement Items	Indicator	Cronbach's Alpha	Composite Reliability
Inter Control	PN1	Control environment	0.909	0.924
	PN2	Monitoring		
	PN3	Risk assessment		
	PN4	Control activities		
	PN5	Information and communication		
Quality of Human	KS1	Knowledge	0.787	0.876
	KS2	Skills		

Variable	Measurement Items	Indicator	Cronbach's Alpha	Composite Reliability
Resources	KS3	Attitude	0.843	0.895
	AC1	Integrity/Commitment		
	AC2	HR Readiness		
	AC3	Readiness of facilities and infrastructure		
Application of Accrual Basis	AC4	Information system readiness	0.836	0.926
	KL1	Relevant		
Quality of Financial Reports	KL2	Reliable	0.836	0.926
	KL3	Comparable		
	KL4	Understandable		

Source: Smart-PLS processing results

Table 2 shows the results of the reliability test using *Cronbach's values Alpha* and *Composite Reliability*. The test results meet the test criteria where the value of each *Cronbach's Alpha* variable is > 0.60, and the value of *Composite Reliability* also has a value above > 0.70. This result means that each variable, namely internal control, quality of human resources, application of the accrual basis, and quality of financial reports has a reliable construct.

Table 3, discriminant validity test results using the *Fornell-Lacker* value shows that the square root value of each variable produces a value that is greater than the correlation value. The square root value of internal control (0.491), HR quality (0.839), application of the accrual basis (0.826), and constant financial report quality (0.819). Because the correlation value between variables compared to the constructed value is lower, it is concluded that the variables studied (internal control, quality of human resources, application of the accrual basis, and quality of financial reports) meet discriminant validity.

Table 3. Discriminant Validity Test Results (*Fornell Lacker*)

	Quality of Financial Reports	Quality HR	Application of Accrual Basis	Control Internal
Quality of Financial Reports	0.819			
Application of Accrual Basis	0.596	-0.263	0.826	
Internal Control	-0.105	0.491	-0.222	0.842
Quality of HR	-0.306	0.839		

Source: Smart-PLS processing results

Inner model testing (*Structural Model*) using *R-square* for the dependent construct. The inner model test results include the coefficient of determination (*R-square*), as shown in table 4 below:

Table 4. Coefficient of Determination Results

Variable	R-Square	Adjusted R-Square
Quality of financial reports	0.392	0.370

Source: SEM-PLS processing results

The results of the coefficient of determination test of the influence of internal control and control and supervision on the quality of financial reports obtained an *R-Square value*

of 0.392 and an *Adjusted R-Square* 0.370, meaning that the quality of financial reports can still be explained by internal control and control and supervision of assets by 37%. These results illustrate that the quality of the research model which explains the relationship between fixed financial report quality variables and internal control and control and supervision variables is relatively not strong enough.

Hypothesis testing using a table value of 1.96 with an alpha value of 5%. The criteria for accepting the hypothesis is if the t-statistic value is greater than 1.96 or the probability value is smaller than alpha 5% and vice versa. The results of the hypothesis test are shown in the *inner model* coefficient values in Figure 2 and Table 5.

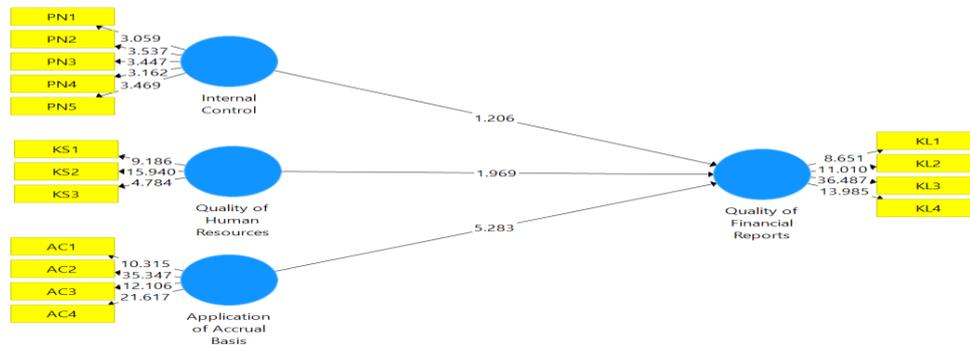


Figure 2. Inner Model Coefficient Values

Table 5. Hypothesis Test Results

Variable	Original Sample	t-statistics	p-Value
Internal control quality of financial reports	0.130	1,206	0.229
Quality of HR → Quality of financial reports	- 0,220	1,969	0.050
Application of accrual basis → Quality of financial reports	0.567	5,283	0,000

Source: SEM-PLS processing results

Table 5, Hypothesis test results show that the quality of human resources and the application of the accrual basis influence the quality of regional government financial reports with their respective probability values (0.050 and 0.000 < 0.025). The same results are also shown in Figure 2 where the t-statistic values are respectively 1.969 and 5.283 which are greater than the t-table value of 1.96. Therefore, testing the hypothesis of the influence of human resource quality and the application of the accrual basis on the quality of local government financial reports is proven to be significant, while internal control on the quality of government financial reports is not significant. These results illustrate that the quality of human resources owned by the Regional Government of Papua Province helps improve the quality of the financial reports presented. The same thing applies to the accrual basis system as a replacement for the historical cost system in recording the accounting system applied which has a significant influence on the Regional Government's financial reports. Thus, these two factors have had an impact on the quality of financial reports that are relevant, reliable, and understandable, compared to the Regional Government of Papua Province.

Conclusion

This study examines and analyzes the influence of internal control, human resource quality, and the application of the accrual basis on the quality of financial reports. This study used a sample of 90 Papua Province employees as respondents. The results state that the quality of financial reports is influenced by the quality of human resources and the application of the accrual basis. Meanwhile, internal control cannot affect the quality of financial reports. This is because internal control is not implemented properly.

This study emphasizes the factors that influence the quality of local government financial reports, especially the variables of human resource quality and the application of the accrual basis. However, this study has limitations, namely that the results are unable to accommodate the population in the regional government organizations of Papua Province. Therefore, future researchers can research again by taking different objects and with saturated samples so that they better describe the responses of the respondents.

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