

# **Influence of Implementation of Government Accounting Standard and the Effectiveness of Government's Internal Control System on the Quality of Local Financial Report and Its Impact Toward the Accountability of Regional Financial Management (A Research on Government Agencies of Aceh Province, Indonesia)**

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## **Abstract**

This research is intended to examine the influence of implementing the of government accounting standard and the effectiveness of government's internal control systems on the quality of local government financial report and its impact on the accountability of regional financial management in Aceh Government's work units. The population in this research is finance administration officers on 48 work units (SKPA) in Aceh Government. This research uses census method. The data source of this research comes from the primary data which obtained from the respondents through distributed questionnaires. Analysis method used is path analysis. The result of this research shows the implementation of government accounting standards has a significant effect on the quality of local government's financial reports, the effectiveness of government internal control system significantly affect the quality of local government financial reports, the Implementation of government accounting standards has an effect on the accountability of regional financial management either directly or indirectly, the effectiveness of government internal control system has a direct or indirect effect on the accountability of regional financial management, and the quality of local government's financial reports significantly affect the accountability of regional financial management.

**Keywords:** Government Accounting Standard, Internal Control System, Quality of Financial Report, Accountability, and Financial management.

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## **I. INTRODUCTION**

Accountability, basically, can be interpreted as a form of an obligation to account of the implementation of a certain organization's mission in achieving the goals and objectives whether it was succeeded or failed which predetermined through some kind of liability media periodically. (Stanbury et al., 2003: 360). It is believed that it is capable to change the government conditions that cannot provide good public services and corruption towards a democratic system.

As one of the areas that already has the right to autonomy, the Government of Aceh is required to account for its performance to the public, where every activity and final results of state administration must be accountable to the public. Aceh Regional Secretary stated, "Although the accountability system has been adopted, in accordance with Government Regulation No. 21 of 2004, but it looks currently not complete. So it can be understood that the current Government of Aceh continue to strive to be able to make itself as an area that is transparent and accountable "(Bachtiar, 2009).

The statement indicates that accountability allows the public to assess the government accountable for all activities performed. An appropriate measure to achieve transparency and accountability in financial management of government is to submit accountability reports such as financial reports. The absence of financial reports shows lack of accountability. The statement also indicates that the financial statements of the government should be able to help the user in making economic, social, and political decisions by comparing the financial performance of actual to budgeted, assess the financial condition and results of operations, to help determine the degree of compliance with laws and regulations related to the financial and other provisions. In addition, it is also as a means of evaluating the level of efficiency and effectiveness. Preparing the financial statements with a high degree of transparency and accountability is one of the openness of government activities to public services.

The financial reports should be presented in accordance with government accounting standards and based on an adequate internal control system. Moreover, it is also in line with government accounting standards

stipulated in Government Regulation act (PP) No. 24 of 2005 which has been revised to the Government Regulation (PP) No. 71 of 2010 concerning the Government Accounting Standards (*SAP - Standar Akuntansi Pemerintahan*). The SAP is the accounting principles applied in preparing and presenting the financial statements of the government.

The supervisory control is performed by the chief of the regional government through an internal control system. It serves as an integral process in actions and activities carried out continuously by the management and all employees to provide reasonable assurance on the achievement of organizational objectives through effective and efficient activities. It also would lead to the reliability of financial reporting, safeguard of state assets, and obedience of laws (PP No. 71 of 2010).

Indonesian Law No. 17 of 2003 stated that the government accountability reports also known as the financial reports of the government must be audited by the Indonesian Supreme Audit Institution (BPK RI) before submission to the legislative in regard with its authority. The audits result on local government financial report (LKPD) is presented in three different parts: the opinion, the system of internal control, and compliance with laws and regulations.

The opinion given to LKPD is a reflection of the quality of financial accountability for regional budget implementation. The examination of LKPD is prepared to provide an opinion(s) on the fairness of the financial information presented in LKPD based on; compliance with government accounting standards (SAP); the adequacy of disclosure; compliance with laws and regulations; the effectiveness and the reliability of the internal control system (IHPS I 2015).

As an example, from the results of State Audit Agency (BPK) on Aceh Government Financial Reports for Fiscal Year of 2014, the BPK provides a "Qualified Opinion" (*Wajar Dengan Pengecualian*). The same opinion was given by BPK on local government financial report (LKPD) of 2013. During the year of 2014, the Government of Aceh has reformed some problems that affect the fairness of the financial reports of 2013. However, the follow-up has not been fully effective to solve existing problems that related to; inventory, investments, fixed assets, reserved funds, short-term debt, and unforeseen expenditures so that these problems still occurred in LKPA Examination of 2014 (Press Release of BPK, 2015).

In regard to these six constraints, the BPK has conducted an examination on the suitability standard and adequacy of disclosures in the financial reports, the effectiveness of internal control systems and the degree of compliance with laws and regulations. The internal control weaknesses and the incompatibility with the government accounting standard (SAP) affect the fairness of the information in the financial reports of which in turn will have a complication on accountability of the financial statements that are made.

A research focusing on the accountability had ever done by Zeyn (2011) on regional work units (SKPD) of Sukamara, Central Kalimantan Province, Indonesia. The conclusion of the research showed the application of accounting standards significantly influence the government's financial reports, the implementation of good governance whereas no significant effect on financial accountability. Good governance and government accounting standards were affecting the financial accountability of 60.1%. Another research conducted by the Pamungkas (2012) at the local government located in Yogyakarta. The results concluded the practice of public sector accounting and monitoring practice affects the quality of government financial reports either partially or simultaneously. The practice of public sector accounting, supervision, and the quality of financial reports affect the accountability performance of government agencies.

Based on various phenomena that have been previously described, the author is interested to further analyze the practice of government accounting standards and the effectiveness of the government internal control system and its influences on the quality of financial report and thus intend to conduct a research entitled "*The Effect of Implementing The Government Accounting Standards and The Effectiveness of Government's Internal Control Systems on The Quality of Local Financial Reports And Its Consequences on The Accountability of Regional Financial Management*".

## II. LITERATURE REVIEW, FRAMEWORK AND HYPOTHESIS

### 2.1. Literature Review

#### 2.1.1 The Accountability of Regional Financial Management

One of public accountabilities from the control measures viewpoint is financial accountability which requires public sectors to make financial reports that describe financial activities in order to be hold accountable to third parties (Halim, 2002: 145). LAN and BPKP (2000: 28) stated that financial accountability is an accountability which concern integrity, disclosure, and law abiding. Its objectives are including the financial reports and regulations that govern receiving, storing, and budget expenditure of government agencies.

#### 2.1.2 The Quality of Local Government's Financial Management

The financial report of local government is the last stage of the accounting process for local government's financial management. The comprehensible of local government financial report can serve as a feature to provide a public transparency and accountability. A good quality of financial report is the report that meets the

characteristic of financial statement conditions, which is relevant, reliable, comparable and understandable (PP No. 71 of 2010).

### **2.1.3 The Implementation of Government Accounting Standards**

The accounting standards used by financial accountants are guidance to prepare and to present financial reports of the government. In Indonesian government organizations, accounting standards are based on Government Regulation (PP) No. 71 of 2010 concerning the Government Accounting Standards, it defines the Government Accounting Standards (SAP) as the accounting principles which applied in preparation and presentation of the financial statements of the government.

### **2.1.4 The Effectiveness of Government's Internal Control System**

The internal control, legally, is based on Government Regulations (PP) No. 60 of 2008 concerning the Internal Control System of the Government. It specifically defines the internal control systems as an integral process in actions and activities carried out continuously by the management and employees to provide reasonable assurance regarding the achievement of organization's objectives through effective and efficient activities, a reliable financial report, safeguard of state's assets, and compliance with laws. The Government Internal Control System, hereinafter will be referred as SPIP, is an organized internal control system which implemented in all sectors of the central government and local governments alike.

### **2.1.5 Framework The Correlation between the Implementation of Government Accounting Standards and the Quality of Local Government's Financial Management**

The Government Accounting Standards are one of most important aspect that is needed to improve the quality of government financial management and reports. In accord to the Government Regulations (PP) No 71 of 2010 there is a relation between the government accounting standards and the quality of financial statements, which is; "the Government Accounting Standards, hereinafter called SAP (*Standar Akuntansi Pemerintahan*), is the accounting principles which applied in preparation and presentation of the financial statements of the government. To conclude, the SAP is a requirement which has the force of law in an effort to improve the quality of financial reports in Indonesia".

Additionally, Nordiawan (2009: 25) also states that there is, in fact, an effect of government accounting standards on the quality of local government's financial reports, namely; "SAP is conducted in the all sectors of governance, both at the central government and its departments, as well as in the local government agencies and its work units. The practice of SAP is believed to have an impact on improving the quality of financial reporting in both central and local government".

### **2.1.6. The Correlation between the Effectiveness of Internal Control Systems and the Quality of Local Government's Financial Report**

Mahmudi (2011: 27) describes that in order to produce the local government's financial reports, some particular processes and stages must be passed in accord to the accounting procedures of local government. It is specifically explained about internal control systems. The quality of financial reports, whether it is good or not, depends on the internal control system that is owned by the local government itself.

Consequently, the quality of financial managements has an impact on opinion given by BPK (Badan Pemeriksa Keuangan). The opinion is given based on its assessment on evaluation and the effectiveness of the internal control system. The internal control system will be graded suffice if the elements in it presents a control of interconnected and assuring users that the financial reports are free of material misstatement (IHPS II of 2014). Otherwise, based on the results of the audit conducted by BPK, they provide opinions "disclaimer" which are probably caused by the weakness of the local government's internal control system. (Indonesia Supreme Audit Agency, BPK, 2011).

### **2.1.7 The Correlation between the Government Accounting Standards and the Accountability of Regional Financial Management**

The Government Regulations (PP) No. 71 of 2010 concerning the Government Accounting Standards, mentioned that one of the measures taken in order to achieve transparency and accountability of financial report is to ensure that it consist the principles of timely and compiled by following the government accounting standards (SAP). Additionally, this regulation also states that any reports entity has an obligation to report its activities and results systematically and must be organized in a certain reporting period for accountability purposes.

It is synchronized with a research conducted by Mardiasmo (2006) which states that the practice of public sector accounting is an effective method to create accountability and transparency. So that public accountability and transparency will be realised as part of activities to achieve *good governance*

### **2.1.8. The Correlation between the Effectiveness of Internal Control Systems and the Accountability of Regional Financial Management**

The primary cause of low grade accountability and transparency of public financial management in Indonesia is the failure of the Ministry of State institutions, state owned/ local owned enterprises, local government and other state sectors in implementing SPIP (Yasin, 2013). In need to achieve an effective, efficient, transparent and

accountable financial report, the Governors and Regents / Mayors need to exercise control over the implementation of their activities. SPIP has the function to provide reasonable assurance for the achievement of effectiveness and efficiency financial report, the security of state assets, and compliance with laws (Government Regulation No. 60 of 2008).

The explanation above is also similar with a research presented by Mardiasmo (2001: 442) which states that the supervision and inspection of the performance are important aspect in the practice of regional autonomy. Supervision will also encourage creating accountability and also will encourage efficiency and effectiveness.

### 2.1.9. The Correlation between the Quality of Local Government's Financial Report and the Accountability of Local Financial Management

One of the methods to facilitate the creation of transparency and accountability in the form of government transparency on its activities of managing public resources is through the presentation of comprehensive financial reports of local government (Mardiasmo, 2009: 36). The purpose of government financial report, specifically, is to provide useful information for decision-making and to demonstrate accountability report entity for the resources entrusted to it (PP No. 71 of 2010).

Nonetheless, the financial reports are important component to create accountability in public sectors and also a way to measure financial performance of local governments (Yuhertiana, 2007: 404). In addition, it is also an expression of local financial accountability and the responsibility for public and a way to indicate the success of local government (Sinaga, 2005). In other words, the accountability entails an obligation to present and report on financial report in the local area of financial management. Schematically, a framework of this research is shown in the following picture:

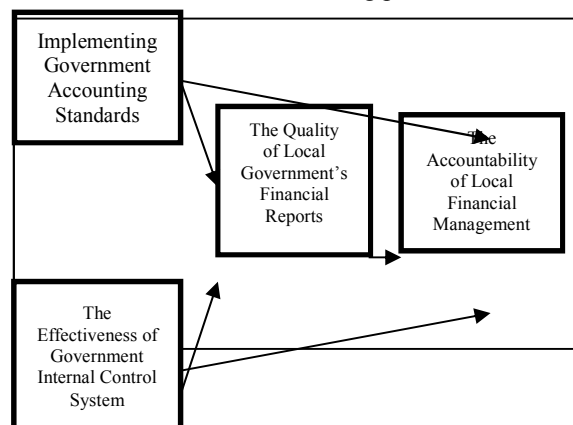


Figure 1.1 Research Framework

## 2.2. Hypothesis Development

Based on the framework that mention above, the hypothesis of this research is the implementation of government accounting standards has been affecting the quality of local government's financial reports; the effectiveness of government's internal control system has influenced on the quality of local government financial reports; the application of accounting standards affects the accountability of government financial management; the effectiveness of government's internal control systems influence the accountability of financial management; and the quality of financial report affect the accountability of local government's financial management.

## III, RESEARCH METHODOLOGY

### 3.1. Population and Sample Research

This research uses sampling jenuh method (census) which means every members of the population used as a sample (Sugiyono, 2004: 78). Its population is the 48 entire work units of Aceh government (SKPA). Whereas, Finance Administration Officers on each work units are specifically the survey respondents. It is due to they are directly involved in financial management.

### 3.2. Data Collection Technique

In regard to data collection, this research distributes questionnaires to the respondents. They were asked to give an assessment to some statements by choosing one of five answers provided.

### 3.3. The Hypothesis Drafting and Testing

In order to perform data analysis, it is necessary to test the quality of the data, such as; its validity, reliability, correlation, and lastly mediation test, after the questionnaires collected. Testing was conducted to determine

whether the measure instruments used in accord with the measured or not and its consistency as well.

Data analysis on hypothesis testing is performed using path analysis with two substructure models. The first substructure is the implementation of government's accounting standards and the effectiveness of its internal control system to the quality of local government's financial reports. The influence of these variables is determined by the coefficient paths using the equation below:

$$Y = \rho_{yx_1} X_1 + \rho_{yx_2} X_2 + \varepsilon_1$$

The second substructure is the implementation of government accounting standards, the effectiveness of its internal control system, and the quality of the local government's financial reports in effect with the accountability of local financial management. The influence of these variables is determined by the path coefficients using the following equation:

$$Z = \rho_{zx_1} X_1 + \rho_{zx_2} X_2 + \rho_{zy} Y + \varepsilon_2$$

Explanations:

- $X_1$  : The implementation of government accounting standards
- $X_2$  : The effectiveness of government's internal control system
- $Y$  : The quality of local government's financial reports
- $Z$  : The accountability of financial management
- $\rho$  : Path coefficients
- $\varepsilon_1$  : Other variables that affecting Y
- $\varepsilon_2$  : Other variables that affecting Z

#### IV. RESULTS AND DISCUSSIONS

##### 4.1. RESULTS

All of the 48 questionnaires which given to each respondents in work units of Aceh government (SKPA), the total questionnaires received back by the author is as much as 48 copies, and all of them are willing to answer and fill out questionnaires.

##### 4.1.1 The Substructure Hypothesis Test Result 1

The result of substructure hypothesis test number 1 is as shown on the following table.

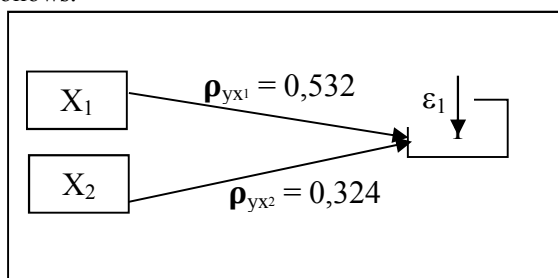
**Table 1.1**  
**Coefficient Substructure 1**

Model	Unstandardized Coefficients		Std. Coef.	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	18,571	8,440		2,200	,033
SAP Implementation	,470	,141	,532	3,331	,002
The effectiveness of SPIP	,014	,081	,324	,176	,021

a. Dependent Variable: The quality of LKPD

Source: Data Processed (2016)

According to the Table 1.1, the equation of  $Y = 0,532X_1 + 0,324X_2$  the structural model is as shown as follows.



**Figure 1.2 Substructure Path Diagram 1**

According to the data, the result of substructure hypothesis test number 1 can be simply interpreted as follows:

- a. The effect of implementing government accounting standards on the quality of local government's financial reports, based on Table 1.1, the values of probability obtained (sig.) = 0,002 < 0,05. So then  $H_a$  is accepted. The magnitude effect of variable  $X_1$  against variable Y is  $(0,532)^2 \times 100\% = 28,30\%$ .
- b. The effectiveness of government's internal control system affect the quality of local government's financial reports, according on Table 1.1, the probability values obtained is (sig.) = 0,021 < 0,05. Thus  $H_a$  is accepted. The magnitude effect of variable  $X_2$  against variable Y is  $(0,324)^2 \times 100\% = 10,50\%$ .

#### 4.1.2. The Substructure Hypothesis Test Result 2

The result of substructure hypothesis test number 2 is as shown on the table below.

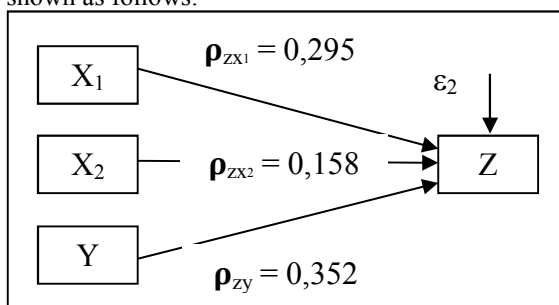
**Table 1.2**  
**Coefficient Substructure 2**

Model	Unstandardized Coefficients		Std. Coef.	T	Sig.
	B	Std. Error	Beta		
1 (Constant)	14,497	5,584		2,596	,013
SAP Implementation	,058	,099	,295	,587	,046
The effectiveness of SPIP	,021	,051	,158	,404	,036
The quality of LKPD	,213	,094	,352	2,271	,028

a. Dependent Variable: The accountability of local government's financial management

Source: Data Processed (2016)

According to the Table 1.2, the equation of  $Z = 0,295X_1 + 0,158X_2 + 0,352Y$  the structural model is as shown as follows.



**Figure 1.3 Substructure Path Diagram 2**

According to the data, the result of substructure hypothesis test number 2 can be explained as follows:

- The effect of implementing government accounting standards on the accountability of local government's financial management, based on Table 1.2, the probability values obtained (sig.) = 0,046 < 0,05. Thus  $H_a$  is accepted. The magnitude effect of variable  $X_1$  against variable  $Z$  is  $(0,295)^2 \times 100\% = 8,70\%$ .
- The effectiveness of the internal control system of government has an effect on the accountability of financial report, based on Table 1.2 the values obtained probability (sig.) = 0,036 < 0,05. Thus  $H_a$  accepted. The magnitude of the effect of variable  $X_2$  against variable  $Z$  is  $(0,158)^2 \times 100\% = 2,50\%$ .
- The quality of financial reports of local government is affecting the accountability of financial report, in accord to the Table 1.2 the values obtained probability is (sig.) = 0,028 < 0,05. Thus  $H_a$  accepted. The magnitude of the effect of variable  $Y$  against variable  $Z$  is  $(0,352)^2 \times 100\% = 12,39\%$ .

Clearly, the Table 1.3 and the Table 1.4 include the entire results of path coefficients as well as indirectly influence and total influence..

**Table 1.3**  
**Direct and indirect influences of  $X_1$  and  $X_2$  on  $Y$**

No	Variables	Path coefficients	Influences			Exp
			Direct	Indirect	Total	
1	$X_1$ on $Y$	0,532	0,283	-	0,283	Strong
2	$X_2$ on $Y$	0,324	0,105	-	0,105	Intermediate
3	$X_1$ on $Y$ through $X_2$	0,621*)	-	2 (0,532 x 0,324 x 0,621)	0,214	Intermediate
	Total Influences				0,602	
	Other Variables				0,398	

Source: Data Processed (2016)

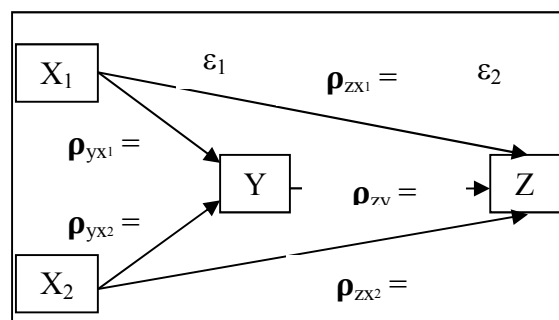
Furthermore, Table 1.3 shows that the  $X_1$  directly has strong influence on  $Y$  at  $(0,532)^2$  or 28,3% and has medium influence when through  $X_2$  that is at 21,4%. Similarly, for the  $X_2$  against  $Y$  has intermediate effect at  $(0,324)^2$  or 10,5%.

**Table 1.4**  
**Direct and indirect influences of  $X_1$  and  $X_2$  on Y and its effect on Z**

No	Variables	Path coefficients	Influences			Exp
			Direct	Indirect	Total	
1	$X_1$ on Z	0,295	0,087	-	0,087	Intermediate
2	$X_2$ on Z	0,158	0,025	-	0,025	Weak
3	Y on Z	0,352	0,124	-	0,124	Intermediate
4	$X_1$ on Z through $X_2$	0,621	-	$2(0,295 \times 0,158 \times 0,621)$	0,057	Weak
5	$X_1$ on Z through Y	0,741	-	$2(0,295 \times 0,352 \times 0,741)$	0,154	Intermediate
6	$X_1$ on Z through Y	0,674	-	$2(0,158 \times 0,352 \times 0,674)$	0,075	Weak
Total Influences					0,522	
Other Variables					0,478	

Source: Data Processed (2016)

Subsequently, from the Table 1.4, it is clearly shown that there is indeed a direct and intermediate influence of  $X_1$  on Z at  $(0,295)^2$  or 8,7% and indirectly has intermediate influence on Y at 15,4% and also has a week influence when through  $X_2$  at 5,7%. Variable  $X_2$  against Z has a weak direct influence at 2,5% and has weak influence when through Y at 7,5% as well. Both of these conditions are called partially mediated, meaning it is a condition in which the independent variables affect the dependent variables, either directly or through mediating variables. Overall, the hypothesis testing result of this research is as shown as follows.



**Figure 1.4 Path Diagram Hypothesis Testing Result**

## 4.2. DISCUSSIONS

### 4.2.1. The Effect of Implementing Government Accounting Standards on The Quality of Local Government's Financial Report

The research describes that there is a significant influence implementing government accounting standards on the quality of local government's financial reports. Meaning that high and low quality of local government's financial reports are affected by the implementation of government accounting standards and the influence rate of implementing the government accounting standards on the quality of government financial reports is at 28.3%. The path coefficient is at 0,532 and it is trending positive which means that if the implementation of government accounting standards up by one point then the quality of local government's financial reports will rise by 0,532 points. It is concluded that the effect of it is a strong influence.

### 4.2.2. The Effectiveness of Government's Internal Control System Influence on The Quality of Local Government Financial Reports

The research shows that there is a significant influence the effectiveness of government's internal control system do to the quality of local government's financial reports. It leads to high and low quality of local government's financial reports is definitely influenced by the effectiveness of government's internal control system and its the level of influence to the quality of local government's financial reports counted to about 10.50%. Path coefficients at 0.324 and it is positively directional, meaning if the effectiveness of government's internal control system raise by one point, thus the quality of financial reports of local government will rise 0.324 points . It is concluded that the effect of it is an intermediate influence.

### 4.2.3. The Effect of Implementing Government Accounting Standards on the Accountability of Local Government Financial Management

The test results of path coefficient substructure number 2 shows that there is an influence either directly affecting by 8.70% with moderate intensity or indirectly affecting through the effectiveness of the government's internal control system approximately at 5.70% with a moderate intensity and through the quality of local government's financial report amounted at 15.4 % with weak intensity. That is, the level accountability of local's financial management is affected by the implementation of government accounting standards. Therefore, in order to

optimize the management accountability of local financial, institutions need to implant the government accounting standards.

#### **4.2.4. The Effectiveness of Government's Internal Control System Influence on the Accountability of Local Government Financial Management**

The test results of path coefficient substructure number 2 explains that there is a weak intensity of influence, either directly or indirectly, the effectiveness of government internal control system on the accountability of local government financial management at 2.50% and its intensity is at 7.50%. It means that the level of accountability of local government financial management is influenced by the effectiveness of government's internal control system.

#### **4.2.5. The Quality of Local Government Financial Reports influence on the Accountability of Local Government's Financial Management**

The research concludes that the quality of local government's financial reports intermediately has an effect on the accountability of local government financial management at 12.39%. Meaning, the level of accountability of government financial management is influenced by the quality of local government financial reports. Its path coefficients at 0.352 and positively directional, which mean that if the quality of the financial reports of local governments rise to one point, then of the accountability of local financial management will also rise at 0.352 points.

## **V. CONCLUSIONS AND RECOMENDATIONS**

### **5.1 CONCLUSIONS**

1. The implementation of government accounting standards strongly influences the quality of local government's financial reports. It indicates that the practice of government accounting standards is capable to affect the quality of local government's financial reports.
2. The effectiveness of government's internal control system has influenced on the quality of local government's financial reports. This shows that the effectiveness of government internal control system is able to affect the quality of local government financial reports.
3. The implementation of government accounting standard intermediately affects the accountability of local financial management directly and indirectly through the effectiveness of government internal control system; however, the effect is kind of weak and indirectly through the quality of local government financial reports. This indicates that the practice of government accounting standards able to influence the accountability of local government's financial management either directly or indirectly through the *partially mediated*.
4. The effectiveness of government internal control system influence is weak on the accountability of local financial management either directly or indirectly through the quality of local government financial reports. This shows that the effectiveness of the internal control system of government least able to affect the accountability of financial management either directly or indirectly through the *partially mediated*.
5. The quality of government financial reports influences the accountability of local government financial management. This indicates that the quality of financial reports of local government is able to influence the accountability of local government financial management.

### **5.2. RECOMMENDATIONS**

1. Provide more considerable amount of time to the respondents in filling out questionnaires, with expectations that respondents would answer questionnaires honestly and properly, and adding some more instruments used in data collection such as observation and interviews to obtain more accurate data.
2. Accountability of regional financial management only from the aspects quality of local government's financial reports, implementing government accounting standards, and effectiveness of government's internal control system. For further research is recommended to add some other independent variables in order to increase the value  $R^2$ , such as the quality of human resources, the principles of financial management, use of information technology, transparency and accessibility of financial statements, the disclosure of financial statements, or completion of the audit findings so that it can be seen that the accountability of regional financial management is also influenced by other variables that are not covered in this research.

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