

# Determinants Of The Quality Of Local Government Financial Statements In Indonesia: Coercive Pressure Dominates

*by* Johan Arifin

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maintain good governance, every Indonesian local government is required to realize transparent and accountable financial management (Maulana & Handayani, 2015).

Public accountability is achieved by complying with government accounting systems and standards to achieve good governance. The Local government financial statements are submitted to stakeholders in one period to realize transparent and accountable financial reports in local government financial management under Law of the Republic of Indonesia No. 17 of 2003 concerning State Finances and Law of the Republic of Indonesia No. 9 2015 on Local Government.

The financial statements released by the local government are referred to by stakeholders in the decision-making process. Thus, the information contained in financial statements must be under the user's needs, must provide benefit by supporting decision making, and can be easily understood by users (Safkaur, Afiah, Poulus, & Dahlan, 2019). Accounting information in financial statements must comply with the Government Accounting Standards as stipulated in Government Regulation No. 71 of 2010, which is relevant, reliable, comparable, and understandable.

However, Mokoginta, Lambey, and Pontoh (2017) noted that the quality of Indonesian local government financial statements is generally far below the standard requirements. In other words, the local government's financial statements are yet to meet the government's expectations, despite some quality improvements from year to year. In addition, Arifin (2020) revealed that the level of mandatory disclosure of local government financial statements in Indonesia is 62%, indicating that not all local governments have disclosed their financial statements to applicable regulations.

This study used the quality of the local government financial statements as the dependent variable based on the Indonesian Supreme Audit Board (SAB) audit of local government financial statements in several districts/municipalities in Indonesia. This study aimed to address some factors to affect the quality of local government's financial statements. The predictor variables of this study were the number of local parliamentarians and the number of civil servants to test the theory of coercive isomorphism. A comparative study variable was used to examine the applicability of mimetic isomorphism theory, while regional head education variables and the level of urbanization were used to examine the applicability of normative isomorphism theory. The Mimetic isomorphism theory is related to the pressure to imitate other organizational practices with the aim of improving performance. The mimetic pressure is often referred to as the conduct of comparative studies of local governments that have better quality of financial statements and then mimic their practices with the aim of improving the quality of financial statements.

The quality of financial accountability of a country or local government is revealed by an assessment carried out by a competent and independent institution (Ahmad & Saad, 2020). The Law of the Republic of Indonesia No. 17 of 2003 concerning State Finances has stipulated that local governments must be held accountable for the implementation of regional revenue and expenditure budget by submitting their financial statements to the local parliamentarians as a legislative body. As a legislative institution, a local parliamentarian is in charge of supervising the implementation of local government (Arifin, Tower, & Porter, 2015). Many local parliamentarians are expected to improve the quality of supervision of local governments and contribute positively to the quality of financial statements. In addition to local parliamentarians' supervision, public accountability and trust in the information of the local government financial statements are enhanced by the audits of the Supreme Audit Board (SAB). The Supreme Audit Board is the only external financial examiner in Indonesia that has great authority to provide opinions on the financial statements of government institutions (Raba, 2017). The audit is carried out annually to assess and state the fairness of the financial information presented in the financial statements.

To obtain an unqualified opinion from the SAB, a local government may learn from other local governments that receive the unqualified opinion from the SAB through a comparative study. Such a method is believed to provide additional knowledge in dealing with changes or adjustments to the work system in future (Wungow,

Lambey, & Pontoh, 2016). Comparative studies allow the government to improve the system, enhance quality, determine new policies, and add insight related to the quality of financial reports (Rudyanto, 2019).

In addition, every financial manager must gain an insight into the quality financial statements to ensure that the submitted financial statements are free from material misstatement. Education is one indicator of quality human resources. A high level of education can assist the apparatus in completing their tasks, including the preparation of high-quality and on-time local government budget and financial statements (Erlina, Tarigan, & Muda, 2017).

Furthermore, Suhardjanto and Yulianingtyas (2011) revealed that the number of civil servants as the state apparatus can serve as the potential determinant of the quality of financial statements in government organizations. The number of civil servants represents the number of prioritized affairs for local governments to develop the area. The larger the number of affairs of a certain region, the greater is the number of civil servants who shall prepare the financial reports of each affair. The achievement of good financial reports cannot be separated from the rules and regulations of the organization. An organization with a large number of employees will generally apply many rules and regulations, but this large number of employees also can better provide more public services.

Another factor to affect the quality of local government financial statements is the level of urbanization. The government needs to support the increasing population in urban areas by implementing development programs to empower the population for the good sake of the community. Development programs in some developed areas are the right answer to trigger economic growth. The better development programs resulted in a higher level of financial statement compliance of the metropolitan areas to the government standards. As a result, urban areas serve as a magnetic attraction for people who have higher education, which eventually leads to higher and progressive demands for public, social, and economic reform agendas in the densely populated urban areas (Ratmono, 2013). Thus, urbanization is a natural process of change to improve the quality of financial statements.

Broadly speaking, this study examined several key variables assumed to affect the quality of Indonesian local government financial statements. Three main important aspects were addressed in this study. First, this study used an institutional isomorphism theory to examine the quality of local government financial statements, since this theory had a perspective broader than other theories, especially to examine the quality of local government financial statements (Martínez-Ferrero & García-Sánchez, 2017). Second, this research was conducted in Indonesia, since this country is known for its unique government structure consisting of some tiers, ranging from the central government, provincial government, and local government that manages districts and municipalities. This study focused on the financial statements of the district and municipal levels, which in this study are referred to as local governments. Third, this study used the number of civil servants working in local governments as one of the predictor variables. The use of a predictive variable aimed to measure the effect of a reduction in the number of employees in each local government in Indonesia due to the introduction of information technology in local governments.

## 2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

### 2.1. Previous Studies and Discussion of Institutional Theory

According to DiMaggio and Powell (1983), organizations are formed by the surrounding institutional environment. Influential ideas from the surrounding area are institutionalized and considered valid and accepted as the way of thinking of the organization. To legitimate this way of thinking, the organizations apply the pressure by way of producing qualitative regulations and statements. There have been many studies on the quality of financial statements in public sector organizations by adopting various basic theories, for example, Legitimacy theory (Ali, Lodhia, & Narayan, 2021; Deegan, 2019; Hassan & Guo, 2017) Stakeholder theory (Beske, Hausteine, & Lorson, 2020; Rudyanto, & Siregar, 2018; Zhang, Chong, & Jia, 2019) Agency theory (Goebel, 2019; Nirwana & Haliah, 2018; Shahzad, Rehman, Hanif, Asim, & Baig, 2019) Stewardship theory (Camilleri, 2018; Dumay & Cai,

2015) Institutional theory (Carungu, Di Pietra, & Molinari, 2021; Simoni, Bini, & Bellucci, 2020; Vitolla, Raimo, Rubino, & Garzoni, 2020).

Of these several theories, Agency theory and Institutional theory are the most frequently used theories to predict potential factors that affect financial statements. Institutional theory is known for its assertion of organizations as mere symbols and rituals. In terms of organizational studies, many researchers have often used the institutional theory as the basic research framework. Institutional theory means that the existence of an organization is influenced by normative pressures arising from external or internal sources (Hyatt & Berente, 2017). Institutional theory is usually referred to as explaining action and decision-making in a public organization (Alvesson & Spicer, 2019). The institutional theory also states that institutions outside the organization may influence organizational behavior or decisions taken by the organization. The institutional theory explains that organizations that prioritize legitimacy will tend to try to conform to external expectations or social expectations where the organization is located. As a result of the adjustment to external or social expectations, organizations tend to separate their internal activities and focus on systems that are symbolic of external parties.

This fact is also held by Boxenbaum and Jonsson (2017) who believed that the considerable impact of external pressure has forced organizations to survive by seeking to adapt to the condition, an attempt known as isomorphism. Isomorphism refers to a process of pushing one unit in a population to resemble another unit in the face of the same environmental conditions. Public organizations that tend to gain legitimacy may have similarities or isomorphism with various other public organizations. Thus this isomorphism theory is suitable to be used as a basis theory in predicting various factors that potentially influence the practice of preparing quality financial statements in the Indonesian local governments. This is because this theory has a broader perspective including coercive, mimetic, and normative pressures perspective. Each of these pressures will be explained in the development of hypotheses section in this study.

Institutional theory also predicts that if organizations can imitate other organizations because of institutional pressure, the pressure will cause the need to adapt to the environment by applying three forms of changes or efforts of the organization. The first form is a coercive isomorphism, namely the process of adjustment towards equality by way of "coercion" of the powerful stakeholders. This form of adaptation will draw the responding organization to be highly dependent. For example, pressure comes because government regulations have sanctions for those who violate them. The second type is a mimetic isomorphism, or the process of imitating other organizations that are successful in one field, not because of encouragement, but because of ambiguous goals or symbiotic environmental uncertainty (Hwang & Choi, 2017). Therefore, organizations in this type of adaptation will tend to make themselves the same model as other organizations and encourage other organizations to imitate them. According to Alsharari (2020) the process of imitating other organizations normally occurs in an uncertain environment. In connection with this research, for example, a local government will try to imitate the practice of preparing financial statements of other local governments that get the best opinion from the government auditor (SAB). The third type of normative isomorphism refers to the role of a group that is often associated with professionalism and struggles for adoption practices that should be carried out. In the context of improving the quality of financial statements such as the level of education of regional heads and members of local parliamentarians in each Indonesian local government.

## 2.2. Financial Statements Quality

To ensure the benefits for their users, the financial statements are required to provide high-quality information which is very useful for decision making (Stolowy & Paugam, 2018). The quality of the Indonesian financial statements of government institutions can be measured using the opinion of the Indonesian auditor institution, namely the Supreme Audit Board (SAB). The opinion by the Indonesian Supreme Audit Board on the financial statements is provided by conforming to the Law of the Republic of Indonesia No. 15 of 2004 concerning the Audit of State Finance Management and Accountability. Article 16 paragraph 1 of the law explains that opinion is an



auditor's professional statement regarding the fairness of financial information that has been presented in financial statements based on criteria: compliance with government accounting standards, adequate disclosure, compliance with laws and regulations, and the effectiveness of the internal control system. The opinion given by the Supreme Audit Board (SAB) must also consider the level of conformity, adequate disclosure of financial statements related to the predetermined materiality level, and follow-up on the results of the examination in the previous year (Habiby, 2020).

The quality of financial statements as measured using SAB's opinion, according to institutional theory can be seen as a socially acceptable practice to gain legitimacy from their institutional context (Adiputra, Utama, & Rossietta, 2018). The SAB's opinion obtained by the local government is intended to gain legitimacy from the community, the central government, or other organizations that the local government has the ability and good commitment to producing quality financial statements.

In this study, audit opinions are divided into 2 types, namely unqualified opinions which reflect very good audit results, and qualified opinions which reflect audit results that are not so good. An unqualified opinion is given when the financial statements have presented all material respects fairly and are under generally accepted accounting principles. In contrast, qualified opinion is given when the financial statements have presented all financial statements fairly in all material respects, under generally accepted accounting principles, but with several exclusions (Ardi, Saputra, & Mulyani, 2019). The quality of financial statements influences accountability because good quality financial statements will lead to accountability of the submitted financial statements (Setyowati, Isthika, & Pratiwi, 2016). The Indonesian Local Government whose financial statements have received "unqualified opinion" (which reflect very good audit results) from the Supreme Audit Board (SAB) is considered to have implemented public accountability well. Therefore, the Indonesian central government once also rewarded the local governments three times in a row for getting "unqualified opinion" from the SAB.

### 2.3. Hypotheses Related to Coercive Isomorphism

#### 2.3.1. The Number of Local Parliamentarians

This study examines the predictor variables for the number of local parliamentarians in the framework of coercive isomorphism. The number of local parliamentarians as a research variable has been used in several previous kinds of research on public sector organizations as a strong determinant, for example, to test the level of financial statement disclosure (Arifin et al., 2015); (Nurlianto & Aswar, 2020).

In the perspective of institutional theory, coercive pressure refers to pressure from external parties to improve the quality of local government financial reports. A research by Murtini, Suhardjanto, Djuminah, and Probodono (2021) reveals that there is a potentially great pressure from parliamentarians to make disclosures of local government financial statements. In line with the aspect of coercive isomorphism in institutional theory, local parliamentarians are considered to have the power to pressurize local government administrators to be in line with the community's aspirations. Therefore, this study used the number of local parliamentarians as a predictor to measure the quality of financial reports.

As the people's representative, a local parliamentarian has a supervisory function to control the running of the government to make sure that it is in line with the community aspirations and other functions. The local parliamentarians supervise the implementation and reporting of local government financial information to improve its transparency and build accountability of the local government's financial reports. Therefore, it is assumed that the higher number of local parliamentarians can help prepare and present better and more accountable financial reports since there will be better supervision, feedback, and encouragement to local governments to make the best use of their existing budget properly (Bolívar, Galera, Subirés, & Muñoz, 2018).

In the perspective of institutional theory, the supervisory function of the local parliamentarians serves as a coercive pressure from external parties to local governments to change their accountability system and achieve a

higher quality in local government financial reports. Logically, the greater the number of local parliamentarians, the stronger is the coercive pressure on the behavior of local governments in producing quality financial statements.

Article 21 of the Law of the Republic of Indonesia No. 15 of 2004 concerning Local Financial Management stipulated that the local parliamentarians could ask the local government to carry out a follow-up on the results of the audit to improve the quality of its financial reports. Thus, an increasing number of local parliamentarians can potentially improve the quality of financial reports (Effendi, 2021). Based on this description, the following research hypothesis is proposed:

*H: The number of local parliamentarians is positively correlated with the quality of local government financial statements.*

### 2.3.2. The Number of Civil Servants

Another predictor variable used in this study as a part of the coercive isomorphism framework was the number of civil servants. Coercive pressure refers to the need for an organization to apply certain norms due to the pressure from other organizations or society. In this case, the number of civil servants is one of the potential variables that may have a coercive pressure since there will be some pressures from the government executives as one of the users of financial statements. The number of civil servants is understood in the number of affairs to be prioritized by local governments in regional development. In this context, the greater is the number of government affairs, the more complex is the government structure and the more complex becomes a government structure, the greater should be the number of civil servants. As a result, the more the number of civil servants, the greater information is disclosed as a way to reduce asymmetrical information and as a way to show better performance (Martínez-Ferrero & García-Sánchez, 2017). Thus, a larger number of civil servants is expected to result in higher fulfillment of local government financial statement disclosures with better quality of financial statements (Khasanah & Rahardjo, 2014).

The Indonesian Government Regulation No.71 of 2010 concerning Government Accounting Standards has stipulated the obligation for the local governments to submit an accountability report in the form of financial statements. In this case, the local government is one of the reporting entities and a government unit consisting of one or more accounting entities. From this definition, the accounting entity refers to a civil servant or local work unit. In the Indonesian government structure, civil servants are accounting entities that are required to record transactions that occur within government institutions. Thus, a more number of civil servants results in a more complex government unit, which is expected to achieve a better quality of the financial statements (Hermansyah & Marlina, 2019).

Logically, a more functional differentiation within the local government can increase the available ideas, information, and innovations regarding the quality of good financial reports. Furthermore, Pradono and Basukianto (2015) revealed that the greater number of civil servants in a government organization will improve the performance of the government organization. Based on the given description, the following research hypothesis is proposed:

*H: The number of civil servants is positively correlated with the quality of local government financial statements.*

## 2.4. Hypothesis Related to Mimetic Isomorphism

### 2.4.1. Comparative Study

The predictor variable in the mimetic isomorphism framework is the implementation of a comparative study by one local government to another local government. The implementation of comparative study is closely related to the pressure of mimetic isomorphism. In this case, when a local government is facing uncertainty or an unsolved problem, the comparative study provides one way to solve the existing problems. The comparative study enables one local government to imitate the practices of other local governments as the object of a comparative study. This

comparative study is generally applied to organizations that are seen to have better achievement and gain better legitimacy than the organizations that imitate them.

Comparative studies are the process of extracting certain knowledge from other locations and institutions to be applied and developed in their institution. Comparative studies are a part of competency development and employee career development through increased knowledge and skills (Bach & Veit, 2018). A comparative study is an educational process carried out by an organization or company, which enables a short-term learning process to improve insight, attitudes, and skills, as well as knowledge to be applied for future betterment. These activities are known to be useful for the need for future developments to meet the expected outcome.

A comparative study in terms of local government organizations is intended to dig up information, add insight about other local governments, compare the performance of other local governments that have good quality financial statements, and transfer knowledge on the way to achieve the unqualified opinion from the Indonesian Supreme Audit Board (SAB) on their financial statements. This fact was revealed by Zhang and Zhao (2019) in their research, which stated that comparative studies can improve employee performance. Thus, the improvement in employee performance can produce higher-quality financial statements. Based on the above-mentioned description, the following hypothesis is proposed in this study:

H: Comparative studies are positively correlated with the quality of local government financial statements.

## 2.5. Hypotheses Related to Normative Isomorphism

### 2.5.1. Regional Head's Educational Background

The next predictor variable is the regional head's educational background. This variable was included in the framework of normative isomorphism, which is associated with the homogenization process of the organization through the educational process and the association of professional organizations. Within the framework of normative isomorphism, it is explained that a person or an organization adopts various forms because of the professional demands of the organization.

Education is a process of changing the attitudes and behavior of a person or group as an effort to increase the maturity level of a person through teaching and training (Kroesen, Handy, & Chorus, 2017). Education can enhance someone's knowledge abilities and improve his/her quality because educated people are expected to think and act more rationally and understand the duties and responsibilities assigned to them more appropriately. Employees with good self-acknowledgment should be able to improve their performance and produce work reports of better quality (Jonker & Botma, 2012). Panagiotakopoulos (2020) further stated that in terms of job completion, educational background and level serve as considerable important factors that affect job completion.

Someone with a formal educational background has more complex information because the level of education can reflect the individual's self-acknowledgment and skills (Pratiwi & Aryani, 2017). Education in a particular field (specialization) will increase knowledge and confidence in areas related to one's work (Carr, Loucks, & Blöschl, 2018). Increasing knowledge and skills are part of an educational path that can enhance one's competence and career development (Jafari-Sadeghi, Kimiagari, & Biancone, 2020). In other words, educational background plays an essential role in enhancing the quality of a person.

The regional head plays a central and strategic role in the government system at the regional level. As a leader, the regional head shall direct the thoughts and opinions of members of the organization, guide, set organizational goals, motivate members of the organization to conform to organizational goals, influence, and supervise members of the group he leads. The Law of the Republic of Indonesia No. 32 of 2004 concerning Local Government stipulates those regional heads are regional leaders who are required and authorized to lead the administration of local governments. In addition, regional heads are accountable for regional financial management, and they are required to be able to produce financial reports of the organizations they lead under applicable government accounting regulations and standards. Logically, regional heads with a higher educational background will find it



easier to understand and apply all kinds of existing regulations, including government accounting standards in the presentation of financial statements.

The level of education indicates a person's level of professionalism in carrying out their duties. Therefore, an adequate level of education allows a person to carry out his/her duties more easily in good financial management (Abualoush, Bataineh, & Alrowwad, 2018). A high level of education potentially can improve employee performance. Hence, when an employee performance increases, it may lead to the production of good quality financial reports (Maqbool & Zameer, 2018). Based on this description, the following hypothesis is proposed:

*H<sub>5</sub>: The education level of the regional head is positively correlated with the quality of local government financial statements.*

### 2.5.2. The Level of Urbanization

The last predictor variable in this study was the level of urbanization. Urbanization is popularly defined as the movement of people from rural to urban areas. Several studies and data show that the more advanced the level of a country's economy, the higher is the level of urbanization (Zheng & Walsh, 2019). Thus, urbanization is a natural phenomenon in line with the development and economic growth and the level of welfare of the population in a country.

According to Masoumi, Hosseini, and Gouda (2018) urbanization is not merely a population-related phenomenon, but in a broader scope, urbanization is seen as a political, social, cultural, and economic phenomenon. There is a tendency that some big cities will grow and develop, then form mega-scale level cities known as metropolitan cities. Urbanization and economic factors will certainly lead to some significant changes in all aspects, such as population, politics, culture, social, technology, environmental resources, and historical results (Zhang & Zhao, 2019). Urban development and urbanization are strongly influenced by economic development in the area. Thus, the more advanced is the economic level of an area, the higher is the level of urbanization. Hence, this condition will have an impact on increasing public accountability in the area and will result in a better quality of financial statements from the region.

In this context, the variable of the level of urbanization was classified under the normative isomorphism framework, since the higher level of urbanization certainly requires more need for special skills, education, and adequate experience. There exists a high level of competitiveness in urban areas that requires a higher level of professionalism. An individual who does not have special expertise or experience will certainly be displaced from the existing professional competition.

In addition, urban areas have a higher population density, thus enabling them to have more legislators and a more educated population than non-urban areas. Therefore, urban areas generally have higher and more progressive demands for political, social, and economic reform agenda (Yoshida, 2020). Based on the institutional theory, it can be argued that the demand for normative isomorphism, such as the quality of financial statements, will be better for local governments with higher urbanization rates. Given the above-mentioned description, the following hypothesis is proposed in this study:

*H<sub>6</sub>: The level of urbanization is positively correlated with the quality of local government financial statements.*

## 2.6. Control Variable

### 2.6.1. Intergovernmental Revenue

Intergovernmental revenue or the level of dependence on the central government is the amount of local government revenue obtained from central government and is transferred to local governments to finance regional operations. It also refers to funds given by the central government in the form of balancing funds (Girsang & Yuyetta, 2015). According to Marhawai (2015) the fiscal imbalances result from the central government's policy in the field of fiscal decentralization for the sake of fiscal imbalances between the central and regional governments. The central government will demand that local governments make sufficient disclosures with supporting

information as a basis for monitoring <sup>5</sup> the performance of local governments on the use of transfer funds. The level of dependence of local governments on the central government can make local governments comply with applicable regulations (Cohen & Hlepas, 2017). In this regard, local governments are encouraged to increase the transparency of the funds they receive to increase the trust of the central government and to demonstrate compliance with relevant regulations. In this study, intergovernmental revenue is used as a control variable, which is measured using total balancing funds divided by total income. Based on the discussion of all predictor variables and control variables in advance, the research framework can be presented as follows:

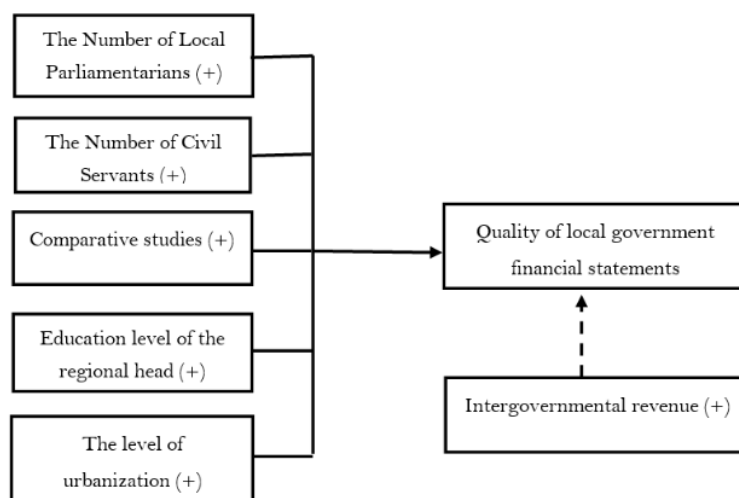


Figure 1. Research framework.

### 3. RESEARCH METHODOLOGY

#### 3.1. Population and Sample

The research population of this study was the district/municipality government in Indonesia totaling 540 districts/municipalities in the 2018 fiscal year, which were audited by the Indonesian Supreme Audit Board (SAB) and met the required information <sup>13</sup> related to the research variables.

Samples were selected using purposive sampling method based on the following criteria: The Indonesian local governments that have official websites containing information about government financial statements and audit <sup>13</sup> results in the form of opinions from auditors, information on regional head profiles, data on the number of civil servants, urbanization levels, as well as information on the number of local parliamentarians. Based on these criteria, 220 research samples were selected.

#### 3.2. Dependent Variable

According to the problem under study, the dependent variable of quality of local government financial statements in Indonesia was measured by point 1 if the local government obtained an unqualified opinion (good) and point 0 if the district/municipality government received a qualified opinion (not good).

#### 3.3. Independent Variables

##### 3.3.1. Number of Local Parliamentarians

The number of local parliamentarians in this study was used as a proxy in measuring legislative size. The number of local parliamentarians was a proxy of the natural logarithm ( $\ln$ ) of the number of local parliamentarians.

The measurement was done because there had been a significant difference in the number of local parliamentarians from one local government to another, which can lead to extremely different values.

$$\text{Local Parliamentarians} = \text{Ln (Number of local parliamentarians)}$$

### 3.3.2. Number of Civil Servants

The website of the Central Bureau of Statistics provides <sup>1</sup> data on the number of civil servants in each local government in Indonesia. According to Government Regulation of the Republic of Indonesia No. 71 of 2010 concerning Government Accounting Standards, it is stated that civil servants are an accounting entity that has the task of managing the budget, assets, and the obligation to carry out accounting and present financial statements based on applicable rules and standards.

$$\text{Civil Servants} = \text{LN (Number of Civil Servants)}$$

### 3.3.3. Comparative Studies

The variable of comparative studies in this context was emphasized to improve the civil servants' ability to do more specific jobs, especially those related to accounting and finance. The comparative studies variable was measured based on the following measurements: 1 point awarded if the local government conducts a comparative study and 0 point if the local government does not conduct a comparative study.

### 3.3.4. Educational Background of Regional Heads

Education is essential for human life because it allows a person to enhance his potential to realize expected personality, intelligence, and skills. The higher is the level of education, the more complex are the knowledge, skills, and experience they have. In this study, the element of the regional head's education level was seen from the highest level of formal education completed by the regional heads.

### 3.3.5. Urbanization Level

Urbanization is generally defined as the movement of people from rural areas to cities. The level of urbanization is used as a proxy of the natural logarithm (Ln) of the population density per km<sup>2</sup>. This measurement was done because there had been a large gap in population density from one local government to another, which can lead to an extremely different level of urbanization.

$$\text{Urbanization} = \text{Ln (Population Density per Km}^2\text{)}$$

## 3.4. Control Variable

### 3.4.1. Intergovernmental Revenue <sup>7</sup>

Intergovernmental revenue is a type of local government revenue generated from transfers from the central government to local governments to finance local government operations. In this research, the authors used the following formula to compare total revenue as a way to measure intergovernmental revenue (Xiao, 2020):

$$IGROV = \frac{\text{Total Fiscal Imbalances}}{\text{Total Revenue}}$$

#### 4. DATA ANALYSIS

The purpose of this study was to determine the effect of the number of local parliamentarians, the number of civil servants, comparative studies, educational background of regional heads, the level of urbanization, and intergovernmental revenue on the quality of local government financial statements. It analyzed the data derived from 220 local government financial statements in districts/municipalities in Indonesia in 2018 that had met the predetermined criteria. These data were included in local government financial statements.

##### 4.1. Descriptive Statistical Analysis

The independent variables in this study were the educational background of regional heads, the number of civil servants, comparative study activities, the level of urbanization, and the number of local parliamentarians, while the intergovernmental revenue was a control variable. Furthermore, the quality of local government financial statements was determined as the dependent variable. These variables were tested statistically descriptively as shown in Table 1:

Table 1. Descriptive statistical analysis.

Variables	n	Minimum	Maximum	Mean	Standard Deviation
Number of local parliamentarians (X1)	220	18	50	36.07	10.463
Number of civil servants (X2)	220	524	20580	6118	3760.251
Comparative studies (X3)	220	0	1	0.71	0.456
Educational background of regional heads (X4)	220	1	4	2.78	1.001
Urbanization level (X5)	220	2.99	13340.00	2108.75	2887.61
Intergovernmental revenue (X6)	220	0.063	1.229	0.50485	0.166105
Local government financial statements quality (SAB opinion) (Y)	220	0	1	0.84	0.368

##### 4.2. Testing the Feasibility of the Regression Model

Hosmer and Lemeshow's Goodness of fit test is shown in Table 2:

Table 2. Regression model feasibility test results.

Step	Chi-square	df	Sig.
1	3.651	8	0.885

Table 2 indicates that the feasibility criteria of the model tested by Hosmer and Lemeshow's goodness of fit test was met by the chi-square of 3.651 with a significant probability of 0.885. A significance value greater than 0.05 caused the  $H_0$  hypothesis to fail and get rejected. This means that there was no difference between the estimation data of the logistic regression model and the observation data, so the model was feasible and appropriate to use. Therefore, it can be concluded that the model used in the research, in general, was appropriate and feasible.

Table 3. Results of regression model analysis.

Variables	B	S.E.	Wald	df	Sig.	Exp (B)
ZX1	0.615	0.480	1.802	1	0.041	1.904
ZX2	0.627	0.441	2.124	1	0.030	0.526
ZX3	0.035	0.281	0.015	1	0.913	1.034
ZX4	-0.061	0.303	0.040	1	0.812	0.941
ZX5	0.042	0.311	0.017	1	0.822	1.043
ZX6	-0.461	0.298	2.401	1	0.122	0.630
Constant	1.787	0.304	34.614	1	0.000	5.974

Note: ZX1: Number of local parliamentarians; ZX2: Number of civil servants; ZX3: Comparative studies; ZX4: Educational background; ZX5: Level of urbanization; ZX6: Intergovernmental revenue.



#### 4.3. Logistic Regression Analysis

Logistic regression model analysis was conducted to determine how the probable occurrence of the dependent variable can be predicted with the independent variable, which gave a reason to conduct this analysis. Table 3 shows the results of the regression model coefficient analysis.

The data analysis in this study obtained the following regression model:

$$Y = 1.787 - 0.061 ZX1 + 0.627 ZX2 + 0.035 ZX3 + 0.042 ZX4 + 0.615 ZX5 - 0.461 ZX6$$

#### 4.4. Hypotheses Testing

Table 4 Describes the results of hypotheses testing in this study.

Table 4. Summary of hypotheses testing results.

Hypothesis	Descriptive	B	Sig (p-value)	Results
H <sub>1</sub>	Number of local parliamentarians	0.615	0.041	Supported
H <sub>2</sub>	Number of civil servants	0.627	0.030	Supported
H <sub>3</sub>	Comparative studies	0.035	0.913	Not Supported
H <sub>4</sub>	Educational background of regional heads	-0.061	0.812	Not Supported
H <sub>5</sub>	Level of urbanization	0.042	0.822	Not Supported

#### 4.5. Discussion

##### 4.5.1. The Effect of the Number of Local Parliamentarians on the Quality of Local Government Financial Statements

The hypothesis testing proves that the number of local parliamentarians was positively correlated with the quality of local government financial reports based on the p-value of 0.041, which was smaller than the alpha value of 0.05 and with the direction of the regression coefficient which was the same as the hypothesis. The results of this test are in line with the researcher's expectations that a greater number of local parliamentarians will result in better-quality financial statements. The local parliamentarian members are the people's representatives who have a supervisory function and can control the running of a government to ensure that it meets the aspirations of the people. In addition, they also have the task of supervising the implementation and reporting of local government financial information to create an accountable and transparent government. This shows that local parliamentarians have the power to pressurize governments to improve the quality of their financial statements. The institutional theory applies a coercive isomorphism pressure, as indicated by an external pressure given by local parliamentarians to local governments to improve the quality of their financial statements. Thus, it can be concluded that in this study the coercive pressure caused by the number of local parliamentarians can support the improvement in the quality of local government financial statements.

This is different from Madelia (2018) which revealed that a large number of local parliamentarians did not necessarily affect the better function and role in the supervisory process exercised by the local parliamentarians. Many issues regarding corruption committed by local parliamentarians have led to a decrease in government performance which had a negative impact and resulted in a decrease in the performance of the quality of local government financial statements. Thus, it can be concluded that the quality of local parliamentarians is more important than the number of local parliamentarians to create a good supervisory function in government, resulting in the evidence that many local parliamentarians cannot improve the quality of local government financial statements.

##### 4.5.2. The Effect of the Number of Civil Servants on the Quality of Local Government Financial Statements

The statistical tests prove that the number of civil servants was positively correlated with the quality of local government financial statements based on the p-value of 0.030, which was smaller than the alpha value of 0.05. In addition, the regression coefficient value was 0.627 with a positive direction. The results of this test are in line with

the expectation that a higher number of civil servants will result in better quality financial statements than local governments with fewer civil servants. According to Chen, Lam, and Zhu (2021) the preparation and arrangement of quality financial statements require a lot of human resources who are expert in government accounting. Human resource is a key factor in creating quality financial statements because only those having the expertise in Government Accounting Standards shall compile government financial statements. Financial statements must be submitted by the regional government consisting of one or more accounting entities. In this process, the regional head as the highest level of authority shall administer the regional government and regional financial management, and delegate his authority to be carried out by each civil servant in each district/municipality area. In the government structure in Indonesia, civil servants are accounting entities that are required to record transactions that occur within the local government environment. This shows that civil servants have the coercive power of pressuring local governments to carry out activities under determined plans and applicable regulations. This pressure includes the pressure exerted by civil servants on local governments to produce better quality financial statements as an indication of public accountability.

#### 4.5.3. The Effect of Comparative Studies on the Quality of Local Government Financial Statements

The hypothesis testing proves that conducting comparative studies was not positively correlated with the quality of local government financial statements based on the p-value of 0.913, which was greater than the alpha value of 0.05. The results of this test are not in line with the researchers' expectations that a comparative study shall improve employee performance, including in their performance to prepare good quality financial statements. The ineffectiveness of this variable is probably because the materials provided in the comparative study to improve the quality of the preparation of financial statements has not been effective. After all, the comparative study participants have different scientific experiences and competencies. Another possibility is due to different situations and conditions found during the process of adopting comparative study materials as implemented in the local government conducting comparative studies.

There are some obstacles in the implementation of a comparative study by a local government with poor quality financial statements to local governments that are considered to have better quality management and financial reporting. These obstacles may be due to several factors including the quality of human resources, infrastructure facilities, regulatory systems, and local government policies (Ratnadila, 2018). Related to this, the local government needs to try to overcome these problems before deciding to conduct a comparative study in other regions.

In this regard, it is conclusive that there has not been a good process of mimetic pressure of isomorphism on the implementation of comparative studies between the local governments with poor financial reports to other local governments with better quality financial reports. There are no certain achievable positive outcomes of the local governments that have participated in comparative studies in the improvement in the quality of their financial statements because the comparative study activities do not cause a local government to take mimetic actions (imitate) the knowledge gained to make an optimal contribution to the region.

This study is in line with Trawarda, Prasetya, and Mayowan (2015) who demonstrated that comparative studies do not contribute positively to the quality of local government financial reports, because comparative studies have not been able to influence the work ability of employees which has an impact on improving government performance. Therefore, it can be concluded that comparative studies conducted by local governments in Indonesia have not been able to improve the quality of local government financial statements.

#### 4.5.4. The Effect of Educational Background of Regional Heads on the Quality of Local Government Financial Statements

The hypothesis testing proves that the educational background of regional heads was not positively correlated with the quality of local government financial reports based on the p-value of 0.812, which was greater than the

alpha value of 0.05 and the different direction of the coefficient. This result indicates that a higher educational level of the regional heads does not correspond to their ability in preparing good quality local government financial statements. It was assumed that the higher is the educational level of the regional heads, the better is their ability in managing the region, including in preparing regional financial statements. However, this study revealed that the educational background of regional heads did not cause any considerable effect on the quality of financial statements. This is likely because regional heads who have higher education do not have a degree and proficiency in accounting, business, or economic education background, which makes them have a low level of understanding the preparation and presentation of correct financial statements. On this basis, regional heads who have higher educational backgrounds do not necessarily have a better understanding of the government administration, especially related to financial statements.

Based on institutional theory, the educational background of regional heads is classified as normative isomorphism pressure because regional heads' education plays a professional role in the attempt of adoption of standard practices as required. Logically, the regional heads play an essential role in influencing the preparation and presentation of local government financial statements, because a higher level of education will help them to know and understand the preparation of quality regional financial statements.

The results of this study are not in line with the researchers' expectations that regional heads who have higher education levels will be better at producing quality financial statements. A different result, however, was revealed by Jaenudin and Chairunisa (2015) who stated that the higher level of education of leaders is positively correlated with the quality of local government financial reports because they improve the performance of the employees working in the financial section. In this way, the improvement in the performance of employees in the financial section can produce good quality financial statements.

A research by Wungow et al. (2016) demonstrated that not all employees who have a high level of education can understand and have the ability to solve problems in regional financial statements because many employees in each Regional Work Unit are placed not under their field of expertise, not to mention the lack of employees with the backgrounds of accounting as required for the position in the financial sectors. Employees with accounting backgrounds generally have a good understanding of accounting and financial reporting. A person is said to have a good understanding of accounting if he/she understands the process to carry out a good accounting to prepare for a proper financial statement that meets the principles and standards of financial statements as stipulated in the regulations (laws). The results of this study are in line with research by Hanifah, Sarpingah, and Putra (2020) which states that the latest education of regional heads does not affect the quality of local government financial statements.

#### 4.5.5. The Effect of Urbanization Level on the Quality of Local Government Financial Statements

The hypothesis testing proves that the urbanization level was not positively correlated with the quality of local government financial reports based on the p-value of 0.822, which was greater than the alpha value of 0.05. The results of this test are not in line with the researchers' expectations that urban areas will produce good quality financial reports. It was assumed that the local governments with a higher level of urbanization would produce a better quality of financial reports given the higher level of political, social, and economic reform agendas and development programs as compared to non-urban areas (Bambang, Pusparini, & Nurabiah, 2020).

Based on the research, one possible factor to cause the lack of positive correlation between the level of urbanization and the quality of financial reports is the uneven distribution of the population with higher concentration in certain areas, which thus impedes the development of the whole community. The results of this study are in line with Huda (2015) which revealed that the level of urbanization did not contribute positively to the quality of local government financial statements. This finding does not support the institutional theory, since the

level of urbanization does not cause an organization to be pressured by normative isomorphism to increase professionalism, especially related to improving the quality of local government financial statements.

#### 4.5.6. *The Effect of Intergovernmental Revenue on the Quality of Local Government Financial Statements*

The results of statistical testing also prove that intergovernmental revenue (as a control variable) was not positively correlated with the quality of local government financial statements. This result is attributed to the fact that the central and local governments are no longer closely related during the decentralization, which may lead to a lack of special monitoring from the central government, especially regarding the quality of local government financial statements. There has been declining monitoring activity on local government financial performance because the result is not referred to in determining the regional fiscal imbalances. As a result, it does not encourage local governments to improve the quality of their financial statements. Thus, it can be concluded that the amount of intergovernmental revenue has not been able to improve the quality of local government financial statements.

## 5. CONCLUSION AND RECOMMENDATIONS

The research presented in this paper focuses on an empirical analysis of the veracity of isomorphic institutional theory to find factors that affect the quality of local government financial statements. In summary, from the three isomorphic components including coercive, mimetic, and normative, only coercive components have a significant effect on the quality of financial statements of Indonesian local governments. These components include the number of civil servants and the number of local parliamentarians. These coercive variables provide evidence that pressure from outside of the organization which includes the number of civil servants, and the number of local parliamentarian members are the dominant factor affecting the quality of local government financial statements in Indonesia.

It has been proven in this study that the number of civil servants is positively correlated with the quality of local government financial statements. It means the quantity and competence of civil servants are indispensable in meeting various needs to ensure that the quality of financial statements is under applicable rules or regulations. This implies that the coercive pressure caused by a large number of civil servants can encourage the improvement of the quality of local government financial statements in Indonesia. In addition, this study also proves that the pressure arising from the number of local parliamentarians affects the quality of local government financial statements. This result shows that coercive pressure resulting from a large number of local parliamentarians has the power to pressure local governments to improve the quality of their financial statements.

These findings can be used as input for the Indonesian government in formulating public policy taking into account the potential factors that are expected to increase the strength of coercive pressure, such as creating more effective regulations that encourage the practice of preparing quality financial statements or applying law enforcement more consistently. The lack of regulation and effective law enforcement is likely to contribute to the different impact of the coercive variables used in research (civil servants and local parliamentarians), related to efforts to improve the quality of the Indonesian Regional Government Financial Report.

Moreover, empirical findings from this study are potentially important for regulatory bodies, professional accounting agencies, local governments, central governments, and users of local government financial statements. These findings can be applied to develop and improve public sector governance. In particular, these findings can be input for public policy making in calibrating the implementation of regulations on Government Accounting Standards in Indonesia (Government Regulation No. 71 of 2010, 2010) better in supporting the quality improvement of the Regional Government Financial Report in Indonesia.

Finally, from various previous discussions, the results of this study contribute to the public sector accounting literature in some important things. First, this research relates to the quality of financial statements in Indonesia which is one of the first studies known to examine the quality of financial statements in the context of the local



government by using the principle of isomorphic institutional theory. In the Indonesian environment, it is often stated that the Indonesian local government has shown financial statements that tend to decline in quality. However, there are very few empirical studies that provide evidence to support or deny this view. Therefore, the findings of this thesis are expected to be the basis for subsequent studies that examine institutional key factors related to improving the quality of financial statements. While from theoretical perspective, this study provides evidence to support the use of isomorphic institutional theory as a useful framework for explaining the determinants of the quality of local government financial statements or other public sector entities, especially those related to the influence of coercive pressure. Finally, to increase the strength of the research results, we suggest that the coming research is designed by a research scenario using time series data, where data is taken from several fiscal years.

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