

EFFECTIVENESS OF INTERNAL CONTROL, GOOD GOVERNANCE, AND ACCOUNTING INFORMATION QUALITY ON BUDGETARY DISCIPLINE

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ABSTRACT

Government budgeting tends to be undisciplined (Rosen and Gayer, 2014:465). Undisciplined government budgeting is effected not only by state's economic stability but also by other factors. In this study, effectiveness of internal control, good governance, and quality of accounting information are identified as factors which may affect budgetary discipline. Optimal internal control, good governance of the organization and accuracy of accounting information will improve the level of discipline in budgeting. This paper is based on existing literature studies and case analyses, and it is therefore considered necessary to carry out field research in order to determine the magnitude of influence of the above variables on the level of budget discipline.

Keywords: Effectiveness of Internal Control, Good Governance, Accounting Information Quality and Budget Discipline

1. Introduction

Government budgeting tends to be undisciplined (Rosen and Gayer, 2014:465). Undisciplined government budgeting is effected not only by state's economic stability but also by other factors such as the effectiveness of internal controls (McCarten, 2003; Worldbank, 2012), good governance issues (Alesina 1996, Deng, 2011, Egbide, 2012, Bappenas, 2012; Giosi, 2014) and the accuracy of accounting information (Safakli, 2011; Harryanto at al, 2014; Cohen, 2014). The purpose of this study is to explain how much influence the above factors have on budgetary discipline based on literature studies and case analyses in Indonesia.

The Government of Indonesia has a legislated internal control system, organizational governance, and accounting information system that encourage the realization of budgetary discipline. On the other hand, in recent years some cases have shown that budgeting in Indonesia may suffer from undisciplined inducement practices caused by weak policy implementation these factors. For instance, cases of budgetary such as Hambalang in 2012 (Rappler, 2016), SKK Migas in 2013 (Kompas, 2013), E-ID Card in 2014 (Detiknews, 2017).

The level of indiscipline of the government on budgeting is also reflected in the results of the examination conducted by the Supreme Audit Agency of the Republic of Indonesia (BPK-RI) to the State Budget (APBN) of 2014.

**Table 1. Findings on Financial Statement Inspection of Central Government
– Budget State (APBN) 2014**

No.	Remark	Number of cases	State's potential loss (Million)	
			In IDR	In USD*
1.	Weakness of Internal Control System	1,180 cases	-	-
2.	Non-compliance with statutory requirement resulting in:			
	2.1. Losses *	522 cases	544,110.32	41.22
	2.2. Potential Losses *	83 cases	1,335,777.21	101.20
	2.3. Disadvantages of Acceptance *	187 cases	6,765,236.33	512.52
	2.4. Administrative flaws	548 cases	-	-
	2.5. Inadequacy **	3 cases	14,249.16	1.08
	2.6. Inefficiency	1 cases	-	-
	2.7. Ineffectiveness	11 cases	139,383.37	10.56
	Total	2,535 cases	8,798,756.39	666.58

Source: IHPS Semester I, year 2015- BPK RI (data compiled). www.bpk.go.id

*Exchange rate USD 1 = Rp 13,200

Examination results show, it was found that 2,535 budgeting cases potentially harm the state finances of Rp. 8.7 trillion. This potential loss is driven by the weaknesses of internal control, good governance (*) and is partly alleged due to the quality of accounting information (**) in terms of budgetary austerity. The other phenomenon that reflects the level of indiscipline of government budget disbursement of the first semester of year 2009 - 2015.

Table 2. List of Budget Disbursement of First Semester State Budget of 2009 – 2015 in 10 Ministries / Institutions with the Biggest Budget Ceiling (by percentage)

No.	Ministries/ Institutions	Year						
		2009	2010	2011	2012	2013	2014	2015
1	Ministry of Public Works and Housing	26.1	24.8	21.6	22.1	24.5	29.4	16.8
2	Ministry of Defense	55.2	41.2	39.3	40.7	33.7	31.2	31.3
3	Ministry of Transportation	22.9	24.2	23.1	20.5	17.6	15.6	10.7
4	Ministry of Religious Affairs	32.4	27.8	28.0	31.1	27.0	27.9	25.2
5	Indonesian National Police	49.2	43.9	39.7	40.0	35.0	38.7	41.1
6	Ministry of Education and Culture	32.3	29.7	14.0	30.6	17.9	26.7	28.5
7	Ministry of Health	22.1	24.4	19.7	30.3	31.0	36.3	38.9
8	Ministry of Research, Technology and Higher Education	29.6	24.3	25.8	45.9	29.0	25.2	25.0
9	Ministry of Agriculture	25.1	18.8	22.6	42.1	36.4	38.2	24.6
10	Ministry of Finance	35.1	33.1	32.3	37.4	35.3	38.7	40.4

Source: Financial report of Central Government, Semester I, year of 2015. www.bpk.go.id (data compiled)

Of the 10 ministries which gain the largest budget ceiling in almost every year, it was found that the disbursement of the first semester budget is below the target set. As a benchmark, the first semester budget disbursement is categorized as poor when the budget disbursement is less than 20%, medium when budget is between 20% - 26.1% disbursed, and excellent if the disbursement of budget is above 26.2% (Central Government Financial Report Semester I - 2015, BPK-RI).

This literature study is a further research by which explains the more detailed formulas of internal control indicators, good governance and the quality of accounting information which affect budget discipline. This research is organized into five stages. The first stage is the introduction; the second one is the theoretical basis on which the research is established; the third is research proposition; the fourth is research model and the fifth, as the last stage comprises the conclusion.

2. Theoretical Study

2.1. Budget Discipline

According to Cambridge dictionary (2015), the term 'discipline' means order, obedience to the rules. Meanwhile, Robbins (2014), states that discipline is obedience and respect to applicable rules within the organization. On the other hand, Nicolae (2013), defined that the term 'discipline' is a behavior that is bound to the rules. Wren (2009), interpreted that 'discipline' is the obedience to the agreement which has been established. Furthermore, King report (2002), stated that discipline is a commitment to adhere to behavior that is generally recognized as truth (correctness) and fairness (properness). In accordance to the above definitions, Horák & Šimáčková (2014), defined that budget discipline is as a compliance with laws, contracts, and other legitimate decisions in implementing an authorized use of budget.

Moreover, Lubis (2011) proposed discipline from the perspective of an organization, which can be interpreted as the obedience of every member of the organization to all rules that apply within the organization. Iron (2004), stated that budgetary discipline is an obedience in fulfilling a set amount of income and expenses, while Gronendijk (1999) defined budget discipline as a commitment to adhere to targets of numbers and procedures. Meanwhile, Umar (2011), defined the budget discipline as order and obedience to the rules or guidelines underlying budgeting. Therefore, the budget discipline can be concluded as a compliance (obedience) to the rules and procedures underlying the whole process of budgeting.

According to Horák & Šimáčková (2014), scopes of budget discipline consist of:

1. Requests for approved financial resources to be spent on norms, set prices, tariffs and agreed items of activities (tables of numbers);
2. Expenditure of financial resources without the approval of superiors is not allowed;
3. Employees are not allowed to use financial resources entrusted to them for personal gain;
4. When finding activities that cause losses or damage to state assets, employees are obliged to report to the respective authorities;

5. Payment requests are made correctly and within the time limit specified;
6. Accounting documents are kept in complete, convincing, accurate and clear manner;
7. Forbidden to falsify documents.

Based on the views of expert above the budgetary discipline interpreted as government compliance with the rules underlying the budgeting. Budget discipline is proxied by disbursement of government budget in the first and second semester (Gronendijk, 1999). The budget disbursement reflects the level of government discipline in implementing budgeting that has been agreed with the council.

2.2. Effectivity of Internal Control

Internal control of an organization comprises all methods, policies and procedures of the organization which ensure the security of corporate assets, accuracy and feasibility of data and management operations standards to achieve set of targets of the organization (Azhar Susanto, 2013). Meanwhile, internal control contains policies and procedures designed to provide adequate assurance to management of the goals and objectives to be achieved (Arens et al., 2014).

In agreement with that, Collier (2007) expressed that "*internal control is the whole system of internal control, financial and otherwise, established in order to provide reasonable and effective efficient operation, internal financial control and compliance with laws and regulations.*" Moreover, Boynton et al (2001); Elder et al (2009); Jhonstoner et al (2012); Konrath (2002) and Ricchiute (2006) agreed that internal control is almost the same as COSO (2013), a process influenced by boards of directors, management, and employees, is designed to provide adequate assurance in achieving the organization's effectively and efficiently operational objectives, reliable financial reporting and compliance with applicable laws and regulations.

The main purpose of internal control is to establish a reliable financial reporting, efficiency and effectiveness of operations, compliance with laws and regulations (Arens et al., 2014). Meanwhile, Soltani (2007: 302) stated that the purpose of internal control is to safeguard the resources of error and fraud, reliable information and operating system as planned. Thus, it can be concluded that the effectiveness of internal control is a process aiming to provide reasonable assurance of operational effectiveness and efficiency, reliable financial reporting, and compliance with applicable laws and regulations.

Internal control is proxied by control environment, risk assessment, control activities, information and communications, and internal control monitoring (COSO, 2013). It is assumed that the dimensions of internal control can affect the level of budget discipline.

2.3. Good Governance

Good governance is a system of how an organization is directed by control of its leader (Cadbury Report, 1992; Ghilyer, 2014). The system governs the relationship between the organization and the interested parties with the organization (OECD-G20, 2015).

Good governance within governmental organization is a process of decision-making by leaders of the agencies (Bastian, 2014). Meanwhile, CIPFA (2014) defined that public governance:

"comprises the comprehensive arrangements put in place to ensure that the intended outcomes for stakeholders are defined and achieved (includes political, economic, social, environmental, administrative, legal, and other arrangements)".

The purpose of good governance is to achieve organizational plans by controlling the running of the organization's operations, managing relationships between stakeholders, determining direction and performance achievements (Wheelen and Hunger, 2012). The goals of good governance generally provide benefits to all parties involved either directly or indirectly within the organization (Carpenter and Sanders, 2007:370). The aim of the governance in public organizations is to enhance organizational competitiveness, accountability and performance of organizational management, efficiency, effectiveness, and productivity of organizational resources (Bastian, 2014)

In Act Number 28 Year 1999, the purpose of good governance in government is the implementation of clean state apparatus, free from the practice of corruption, collusion and nepotism, as well as other disgraceful acts and adhering to the prevailing rules. Whereas in the Regulation of the State Minister for State Apparatus Empowerment Number 15 of 2008, the objective of governance of governmental organizations is to build profiles and behavior of clean, high integrity, high productivity and responsible, transparent and accountable public officials and to enhance efficiency, effectiveness and excellent service to the community.

From the above statement, it can be concluded that the governance of public sector organizations is a system, process, and set of rules that govern the relationship between the organization with partners and stakeholders to accord the expected conditions. These encompass political, economic, social, environmental, administrative, legal and other stability so that the intended objectives by interested parties can be achieved by embracing the principles of the state administration free of corruption, collusion and nepotism, and other disgraceful acts.

Good governance is proxied by dimension of behaving with integrity, ensuring openness and comprehensive stakeholder engagement, defining outcomes in terms of sustainable economic, social, and environmental benefits, determining the interventions required to optimize the achievement of the expected outcomes, developing entity capacity, including leadership and individual capabilities, managing risks and performance through internal control and robust public financial management, implementing sound practices in transparency, reporting and auditing to provide effective accountability (CIPFA, 2014). It is assumed that the dimensions of good governance can improve the budget discipline.

2.4. Quality of Accounting Information

The purpose of the public sector accounting will be achieved when the information provided to the users is useful. Yadiati (2007) affirmed that information is considered useful when it is qualified. On the other hand, Dull et al (2012), stated that quality information is useful information for users in decision making. In line with their statement, Porter and Norton (2011) stated the relevant information is one that can be used for decision making.

There are a number of requirements particular information can be used for the basis of the decision making, which are to have characteristics: relevant, timeliness, accuracy, completeness, understandable, verifiable, accessible, and summarization (Azhar Susanto, 2013; Hall, 2013; Romney and Steinbart, 2012). Brief information is defined as the core of information conveyed to users for decision making.

Accounting information can be said to be qualified if it fulfills the requirement when presented, it is relevant and honest (faithful representation). Furthermore, information is viewed to be relevant when it has element of predictive value, confirmatory value, and materiality. Information is said to be presented honestly when it has complete, neutral and free from error. Meanwhile, additional requirements for information to be said as qualified are comparability, verifiability, timeliness and understandability (Kieso, 2014).

The quality of accounting information is proxied by the opinion of the financial statements issued by the Supreme Audit Agency of the Republic of Indonesia (BPK-RI) and the accuracy of the submission of financial statements to the Ministry of Finance. It is assumed that opinion of financial statements and timeliness of submission of financial statements can improve the discipline of the budget.

3. Research Propositions

3.1. Effect of Internal Control on Budget Discipline

Managers tend to intentionally engage in budget indiscipline such as budget slack and other things (Schiff and Lewin, 1974). The budget uncertainty can be overcome either by internal control in the form of monitoring (Suartana, 2010; Schiff and Lewin, 1974).

Willoughby (2014) stated that no one is to be budget disciplined if it turns out that the costs tend to rise exceeding the estimates made in the budget. Furthermore, Willoughby (2014), stated that to overcome this issue, it requires strong internal control which will create checks and balances in budgeting. By doing so, it will eventually increase the budget balance.

The research of Kraan (2006) proved that increasing the discipline of budget requires strong internal control. Control in the form of supervision is necessary to maintain discipline on the budget. Without any control of the budget will lead to additional-budgetary expenditure (Inyang, 2014) and it will cause a setback from the budget itself (Sekwat, 1997). Similarly, the study conducted by Ramakrishnan (1998b) proved that the main problem of the budget is ineffective control.

Budgeting requires control in the form of monitoring which begins from planning, implementation and reporting in order to be more effective (Mardiasmo, 2009). Control is required in the planning stage to plan activities to be implemented in line with the vision and mission of the organization. Control of budget planning also reviews the previous year's budget failures to avoid recurrence in subsequent budgets. Control in the implementation stage is required in order that the activities are carried out on time, economical, efficient and effective in accordance with established procedures. Meanwhile, the control in the reporting stage (accountability) is required in order that activities that have been implemented can be reported on time, transparent and in accordance with applicable rules.

Control is required in budgeting to keep the quality budget, i.e. to produce high performance and to be able to meet the expectations of the community (Bastian, 2010). Research conducted by Ozer & Yilmaz (2011), Zulkarnaini (2013) revealed that there is a positive relationship between internal controls of budget discipline with decreasing opportunities for budget slack to occur.

Based on the literature review of previous research on the influence of internal control on budget discipline, only few researchers have focused on evaluating the magnitude of the influence of internal control over budgetary discipline in governmental institutions using the control dimension of COSO (2013). Therefore, the following research propositions can be made as follows:

H_{01} = There is no positive influence of internal control on budget discipline

H_{A1} = There is a positive influence of internal control on budget discipline

3.2. Effect of Good governance on Budget Discipline

Inadequate good governance will cause the low level of discipline on the budget (Egbide, 2013). Similarly, Uppal (2011) stated that good governance will have an effect on the conducive budget discipline. The main function of good governance is to direct the organization's objectives (Solomon, 2007). In order that the budget can be implemented in accordance with the established plan, the budget discipline requires direction. Research conducted by Egbide & Godwyns (2012) found that there is a close relationship between good governance with budget discipline.

In line with the above statement, Tommasi (2007) argued that to improve budgetary discipline, it is necessary to increase accountability to those who implement the budget. A similar opinion is also supported in Deng's (2011) study, in which he stated that the cause of the gap between the established budget and its realization is the lack of accountability in governance. This is in line with research conducted by Ramakrishnan (1998b), in which he found that there are two main factors causing weak public budget one of which is accountability.

Effective governance is characterized a number of indicators, one of which is applying budget discipline and efficient spending (Andrews, 2008). Budget discipline encourages the government to implement the budget in accordance with the commitment, time and procedures established. Commitment, adherence to time and procedure can only be carried out if there is integrity, transparency, intervention and accountable in running the government. Therefore it can be underlined that to run the budget discipline requires the existence of good governance.

A study conducted by Stein et al (2009) found that low transparency and accountability of public budget managers could weaken budgetary conditions by 20 - 30%. Meanwhile, Rigaud (2013) stated that to encourage the efficiency of the implementation of government budget requires good governance organization. Similarly, it was expressed by Bräutigam (2004) that good governance will have a positive impact on the regulation of expenditure and sustainable sources of income.

Based on the literature review of previous research on the influence of good governance to budget discipline, the research proposition are arranged as follows:

H₀₂ = There is no positive effect of good governance on budget discipline

H_{A2} = There is a positive influence of good governance on budget discipline

3.3. Effect of Accounting Information Quality on Budget Discipline

Budgetary discipline can be implemented if it is supported by the quality of accounting information (Sevilla, 2005). This is because firstly, budget discipline requires that every activity should be reasonably justified. Media that provides accountability information of activities is an accounting information system. Secondly, public management requires information on the level of achievement (performance) budgeting only from accounting information (Nur Afiah, 2010; Parker et al., 1989). Thirdly, the obedience (discipline) to the realization of the budget is only known from the financial statement information (Nur Afiah, 2010). The higher achievement of budget performance indicates the higher level of budget discipline.

Third, budget discipline requires the use of budget economically, efficiently and effectively. Information which can support that the budget is used economically, efficiently and effectively is accounting information. This is in line with the opinion of Khan & Hildreth (2000), which stated that accounting information can provide information on the upper limit of budget expenditure that has been done and can be used as a guide to allocate the next budget.

Accounting data is required in budgeting process (Fernsler, 1999; Parker et al., 1989; Rodriguez, 1995). This is in line with Guess's opinion (2011), which stated that the accounting system provides data used as information in preparing the budget and analysis of policy outcomes. Similar opinion was also expressed by Jones (2010), stating that for the analysis of the achievement of discipline (commitment) on budget, it is required information about the realization of receipts and expenditures. This information is only generated by the accounting system.

The budget is in some ways based on historical data partly generated by the accounting system (Nafarin, 2007). Accounting information systems provide not only information about historical data, but also updated information on receipts and expenditures. The government will adopt a policy if it turns out that revenue and expenditure are still far below the target. This is done to fulfill the commitment to the agreed revenue and expenditure with the stipulated deadline and the applicable rules.

Based on the literature review of previous research on the influence of accounting information quality to budget discipline, the research proposition are made as follows:

H₀₃ = There is no positive effect of the quality of accounting information on budget discipline

H_{A3} = There is a positive effect of the quality of accounting information on budget discipline

4. Research Model

Based on the phenomena, previous research and research propositions above, a research model can be made as follows:

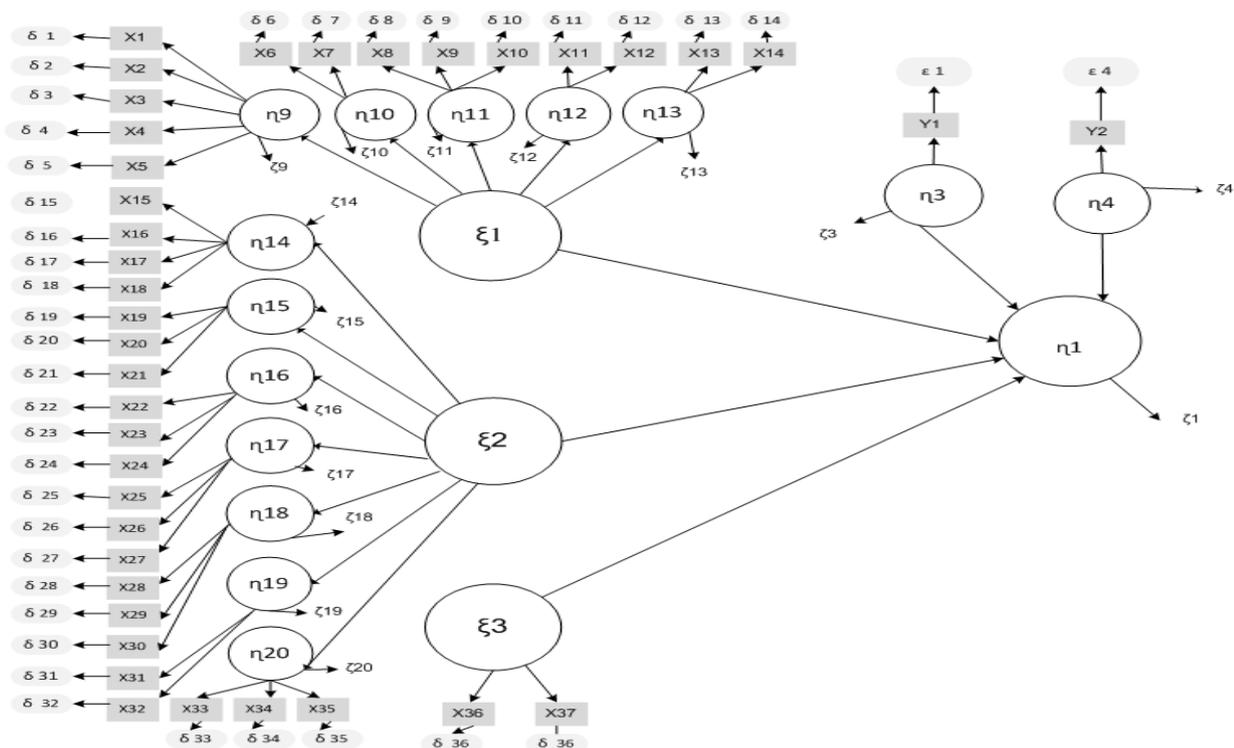


Figure 1. Research Model

The relationship formula between independent variables and dependent variables can be written as follows:

$$\eta_1 = (Y_{11} * \xi_1) + (Y_{12} * \xi_2) + (Y_{13} * \xi_3) + \zeta$$

Where :

- η_1 = Latent variable in budgetary discipline
- Y = Path coefficient between latent variables
- ξ_1 = Latent variable effectiveness of internal control
- ξ_2 = Latent variable good organizational governance
- ξ_3 = Latent variable accounting information quality
- ζ = Error

The research model uses path analysis which is expected to answer the research gap. The magnitude of the influence of the factors on the budgetary discipline will provide input to the apparatus in the government policy making to increase organizational performance.

5. Conclusion

Government budgeting tends to be undisciplined (Rosen and Gayer, 2014:465). Undisciplined government budgeting is effected not only by state's economic stability but also by other factors such as the effectiveness of internal controls (McCarten, 2003; Worldbank, 2012), good governance issues (Alesina 1996, Deng, 2011, Egbide, 2012, Bappenas, 2012; Giosi, 2014) and the accuracy of accounting information (Safakli, 2011; Harryanto et al, 2014; Cohen, 2014). The purpose of this study is to explain how much influence the above factors have on budgetary discipline based on literature studies and case analyses in Indonesia.

Indiscipline in budgeting can be overcome by the first, increasing the effectiveness of internal controls (Kraan 2006; Ramakrishnan, 1998b; Schiff and Lewin, 1974; Suartana, 2010). The second, it can be overcome by improving good governance (Deng, 2011; Egbide, 2013; Rigaud, 2013; Solomon, 2007; Stein et al, 2009; Tommasi, 2007; and Uppal, 2011). Finally, budgeting indiscipline can be tackled by improving the quality of accounting information (Fernsler, 1999; Guess, 2011; Khan & Hildreth, 2000; Parker et al., 1989; Rodriguez, 1995; and Sevilla, 2005).

This paper is written based on existing literature studies and budgeting phenomena in Indonesia and needs further study. Therefore, it is necessary to conduct a field research to determine the magnitude of influence of the above variable on the level of budget discipline and to answer the above hypothesis.

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