



## **Factors Affecting The Quality of The Government of Medan's Financial Reports With The Government Internal Control System As A Mediation Variable**

**Bima Adiguna Nasution<sup>1</sup>, Iskandar Muda<sup>2</sup>, Parapat Gultom<sup>3</sup>**

<sup>1,2,3</sup>Universitas Sumatera Utara, Medan, Indonesia

<sup>3</sup>Email Corresponding : bimaadigunan@gmail.com

**Abstract.** This study aims to analyze whether the existing factors influence the quality of the Medan city government's financial reports. In addition, this study also aims to determine whether the government's internal control system can mediate the relationship between these factors and the quality of financial reports. The research design used in this study was explanatory research. Still, the data studied were data from samples taken from the population to find relative events, distribution, and relationships between sociological and psychological variables using primary data types, namely in the form of perceptions of respondents (subjects) of research obtained through direct distribution of questionnaires to financial administration officials. Data was collected using a questionnaire distributed to 75 respondents who were economic administration officials in the city of Medan. Hypothesis testing and mediation testing with the help of the SmartPLS program. The results of this study indicate that the existing factors have a positive and significant effect on the government's internal control system. The government's internal control system positively and significantly impacts the quality of local government financial reports. The existing factors positively and significantly affect the quality of local government financial reports. Furthermore, the factors that exist indirectly significantly affect the quality of local government financial reports through the government's internal control system.

**Keywords:** Quality of local government financial reports, competence of human resources, utilization of information technology, government internal control system.

### **INTRODUCTION**

Along with the development of accounting in the public sector in Indonesia, accountability for government performance to the people is becoming common. Soimah (2014) explained that the increasing demands oblige government agencies/institutions to disclose reports of their activities and performance to the broader community. Public sector organizations are often associated with the government responsible for administering public services to provide good welfare in various aspects of life. Haryanto (2012) said that the government is a public entity that must be able to account for its performance in the format of an accountability report in the monetary sector. The central and regional governments must carry out their financial activities disciplined, comply with laws and regulations, and be effective, accurate, efficient and open (Muda et al., 2018).

The government in Indonesia delegates rights and authorities to village governments (Kades) in matters of controlling and organizing their activities. This is contained in Law No. 6 of 2014. The regional government delegates power to the village government to manage village funds and carry out affairs relating to village communities by using government management, empowerment and development as stipulated in Law No. 60 of 2014. As the law explains, village funds are funds from the State Revenue and Expenditure Budget specifically for villages sent through the district/city Regional Revenue and Expenditure Budget, which are used for managing and administering village administration.

BPK carries out assessments that refer to central and regional government financial reports after examining and observing financial statements that produce an output as an opinion. BPK audit results are poured into four opinions, namely Unqualified Opinion (UO), including Modified Unqualified Opinion. Qualified Opinion (QO), Adverse Opinion (AO), and the last one is Disclaimer of Opinion (DO).

Sudiarianti (2015) said that the financial reports from local governments that received the Unqualified Opinion (UO) predicate still needed to be higher. Audit data obtained from BPK taken from IHPS I 2015, UO including Modified Unqualified Opinion is 40.89%, QO is 45.64%, AO is 0.79%, DO there was as much as 3.77% (IHPS I BPK, 2015).

From the data above, it can be seen that there are still problems when preparing financial reports. Several aspects are suspected of making the reliability of preparing a financial report for local governments less reliable, namely the low capability of human resources (human resources capability), the use of information technology (information technology usage) which cannot be optimized as the triggering aspect of not achieving the UO predicate as government aspirations. The description regarding the fairness of the information from the financial statements is disclosed based on a legal opinion in line with what is stated in Law No. 15 of 2004. According to SAP, the benchmarks for this opinion are disclosure, compliance with laws and regulations, and the effectiveness of the government's internal control system (SPIP).

Asterini (2015) argues that the information contained in government financial reports must also pay attention to the standard requirements for qualitative characteristics as required by law, this can be said that the central and regional governments can raise the quality level of published financial reports, which means that local governments participate realise the desired openness and accountability. The data published in the financial statements must be compatible with the standards required in the laws and regulations (Muda et al., 2017). This is because the quality of financial reports is a benchmark for accountability report requirements that are felt to meet the interests of users and report readers.

The Medan City Government (Pemko) is one of the cities examined by the BPK in 2020, which received the Unqualified Opinion (UO). The predicate given by the BPK has increased compared to previous years, from the predicate of Qualified Opinion (QO) in 4 consecutive years to the predicate of Unqualified Opinion (UO) in 2020, which can be seen in Table 1. This increase in opinion occurred because the organization had made improvements to defects in financial statements in the past years.

**Table 1. LKPD Opinion List of Medan for 2016-2020**

No.	Year	BPK Audit Opinion
1.	2016	QO
2.	2017	QO
3.	2018	QO
4.	2019	QO
5.	2020	UO

Source: IHPS I BPK RI, 2020

The data above indicates that Pemko Medan's financial reports must indicate better quality. This situation can be seen from the perspective of human resources that still need to be qualified and have yet to prove their quality in managing regional finances. Comprehensive knowledge of the application of accrual-based government accounting standards is still very much needed by regional financial management employees, due to the divergence between the previously used accounting standards, which were cash-to-accrual-based, on the other hand, law demands require accrual-based SAP. had to run in 2015.

The results of a study conducted by the BPK from 2004 - 2008 on the subject of financial executor resources are the lack of human resources with an education background in accounting, the distribution of resources is not in place, the quality of the basic understanding of employees regarding the management of state finances is still inadequate, and lack of respect for them (Triani, 2013).

Appropriately, human resources are needed on an accounting school basis to fill financial management positions or positions. Systematic development of continuing education is also needed, such as training, seminars and sharing sessions (Forum Dosen Akuntansi Publik, 2006).

Other components or aspects that influence LKPD besides HR competencies include information technology. Information technology can also be seen as an instrument someone uses in doing his job (Nurillah, 2014). The use of technology is an element in realizing an accountability report which in its presentation has advantages in speed and timeliness. Also, the data contained in it can be relied upon. The use of information technology to manage regional finances is regulated in Permendagri No. 13 Article 225 of 2006, where Permendagri allows computer software to manage regional finances, resulting in a regional financial management information system.

The next component that is assumed to affect the financial reports of local governments is the application of government accounting standards (SAP). The State of Indonesia is moving SAP implementation from cash-based to accrual-based as stipulated in Government Regulation 71 of 2010. Its implementation is moving slowly due to the changing regulations that follow it. It is still being implemented slowly, with the low level of human resources who control the accrual basis, the immature notification and training regarding Government Regulation No. 71 of 2010, also the minimal use of information technology in financial reporting.

Another criterion the BPK assesses is giving its opinion in compliance with laws and regulations. Based on IHPS I 2020, the results obtained were still high, most of which were findings of local government disobedience to laws and regulations. Changing the regulations used from cash-based to accrual-based to fully accrual-based requires time and a process for adjustments in implementing old regulations and legislation towards new regulations. To ensure that the officials preparing the financial reports obey and comply with the laws and regulations that are currently in use, the role of internal control is essential.

The element that influences the quality/quality of the financial reports of the regional/municipal government and so on is organizational commitment. Commitment is one of the factors needed in carrying out the duties of an official. If there is no strong commitment, an official will often make mistakes that he is aware of. The internal control system will be less valuable if all members who carry out their duties are committed to fulfilling them with complete integrity (Janrosl and Muda, 2021). However, the need for a control system within an agency helps minimize the possibility of errors and fraud in preparing financial reports (Laurensius and Muda, 2021).

Yuliani et al. (2010) explained that understanding accounting is one of the elements affecting the quality of financial reports. To obtain good financial reports, the competence of individuals who compile and make financial reports must be the primary concern. That is, employees who are involved in these activities must understand the procedures, processes and preparation of accounting reports carried out based on the rules used. If the employees understand and understand accounting procedures, the quality of financial reports will improve.

The results obtained from BPK's inspections indicate that BPK is still experiencing problems related to weak internal controls as well as non-compliance and non-compliance with laws and regulations. Inspection results obtained by BPK in 2015 showed a weak control system. Furthermore, BPK also discovered problems with laws and regulations that caused losses to local government entities, lack of acceptance and weak administration with a value of Rp. 2.52 trillion.

The findings from the BPK regarding the big problem of weak SPI indicate that the level of effectiveness of the local government SPI has not been maximized. BPK encountered several problems, namely, not yet being implemented and inaccurate recording, not complying with the provisions in the report preparation process, inadequate SIA (accounting information system), inadequate human resources, and the slow process of issuing reports. The problem of weak regional SPIP indicates that the published financial reports still do not meet the qualifications and special qualitative requirements stipulated in PP No. 71 of 2010.

Referring to the explanation above, researchers are encouraged to observe further the influence of human resource competence (HR), utilization of information technology, application of government accounting standards, compliance with laws and regulations, organizational commitment

and understanding of accounting on the quality of local government financial reports through the government's internal control system at the Medan City Government uses the reason that there is a phenomenon that the quality of local government financial reports at the Medan City Government is not optimal. This is evidenced by obtaining the predicate of a reasonable opinion, that was Modified Unqualified Opinion of the BPK on LKPD Pemko Medan.

## **LITERATURE REVIEW**

### **Stewardship Theory**

The assumptions on the principles of this theory are based on the nature and attitudes of humans who can be trusted, have sincerity and morality, are responsible for their actions and do things honestly and fairly to all groups, including society as a principal, which puts forward where happiness is. Furthermore, achieving performance results is closely related to an entity/organization. Stewardship theory describes a situation where management does not aim to obtain individual results but aims at the main objectives of management for the benefit of the entity/organization and assumes that there is a close relationship between satisfaction and success from the organization (Sudaryo et al., 2017).

The stewardship theory for this research implies that this theory can explain the role of the Medan City Government as an agency or means of liaison that can be entrusted with managing and providing quality services to the public and can provide financial accountability that has been entrusted by the public, which in the end the goals of a good economy are implemented and also the welfare of society can be achieved optimally.

### **Quality of Government Financial Reports**

Financial reports can be seen as data. They can also be seen as information. Bastian (2005) explains that LKPD is a component of financial reporting procedures in a local government that neatly describes the financial position of transactions carried out by a local government entity. LKPD is the overall product, commonly called consolidation of the Regional Work Units (SKPD) financial reports or Regional Apparatus Organizations (OPD). Financial reports can provide usefulness to users of local government financial information (stakeholders). Therefore, financial reports must have good information value and quality and be helpful in decision-making.

The quality of local government financial reports is a manifestation of the totality of accountability from a resource manager. The mission of compiling financial reports is to provide information regarding the company's financial position, budget absorbed or not, cash flow, and financial performance of an organization/valuable entity for users when making decisions. In his writings, Gamayuni (2018) explains that the purpose of financial reports is to fulfil the interests of the many users of the report. In order to achieve this target, the standards are set to govern all considerations for the benefit of the presentation of financial statements and the rules for the form and content of the financial statements.

### **Competency of Human Resources (HR)**

Sukmaningrum (2012) stated in his research that human resources are the main pillar and initiator of the organization to realize the vision, mission, and goals of the organization. No matter how well a system is built, it becomes useless if it is not supported by sufficient quality human resources, especially the personal qualities of human resources which include intelligence in the fields of education, experience and training and can be measured from the knowledge possessed, skills and behaviour of these HR.

### **Utilization of Information Technology**

Nurillah (2014) says that IT can mean a technology that is used in terms of processing, compiling, processing, storing, and manipulating data in various ways in order to obtain quality information, namely information that is relevant, accurate, and timely that is used for personal, business, and government interests and is an essential ingredient in making decisions. Utilization of

information technology can provide a way for various groups to be able to access, organize and use information quickly and accurately in order to support the realization of a government that is clean, has integrity and can meet transition pressures adequately.

### **Application of Government Accounting Standards (SAP)**

The issued financial reports must be made under applicable standards so that the financial statements can be compared with financial reports in the past or compared with the financial reports of other entities/institutions. In order to achieve the objective of the entity/organization in preparing reliable financial reporting, it must be based on applying the applicable accounting standards. Namely, PP No. 24 of 2005 was amended by PP No. 71 of 2010. By compiling and providing financial reports according to applicable accounting standards, internal control in government will be better.

### **Compliance with Legislation**

Regulation of the Minister of Home Affairs No. 13 of 2006 stipulates that finance in the regions must be operated orderly, comply with laws and regulations, effective, efficient, economical, transparent and responsible by considering the principles of justice, fairness and benefit to society. This becomes the basis for carrying out the control system's function within central and regional government organisations. Internal control in OPD must obey the rules and regulations that apply. By obeying and implementing the applicable laws and regulations, it will improve the internal control system in government.

### **Organizational Commitment**

Organizational commitment is a condition of taking sides and the willingness of organizational personnel to be in the organization and a high drive to work and be responsible for the work assigned to achieve organizational goals. Sopiah (2008) also explains that organizational commitment is a psychological bond between employees and their organization which is seen by the presence of confidence and a high response to the goals and values of the entity/organization, a desire to seek to achieve the interests of the entity/organization, and a high willingness to protect its membership as a member of the organization. personnel or members of the organization. One of the organisation's interests is the optimal functioning of the internal control system. SPI runs well and ideally if the employee is highly committed to the organisation.

### **Accounting Understanding**

In order to realise a quality financial report that refers to the basis and standards for preparation, an understanding of the internal control system is required. Someone familiar with accounting rules and guidelines should understand that in order to get good financial reports, good internal controls are also needed so that later when the financial statements are audited, there will be minimal errors from the internal control side. The better an employee understands accounting, the better the organization's SPI will be.

### **Government Internal Control System (SPIP)**

Adequate implementation of internal controls provides sufficient confidence in the quality and reliability of financial reports. Internal control at the central and regional governments was built regarding PP no. 60 of 2008. SPIP provides sufficient confidence in achieving effectiveness and efficiency in the accounting process, mainly to produce reliability of a financial report. So that the implementation of the internal control system can increase the reliability and neutrality of information, minimize inconsistencies and ease the audit report process.

There are still many problems with the fragility of the internal control system, which results in fraud or errors in a local government financial report by the BPK, notifying that the local government financial report has not completed the specified financial report requirements. The

acquisition of an audit carried out by the BPK received a "reasonable opinion" opinion, partly due to the fragility of the SPI owned by the regional government (BPK, 2021).

## **METHODS**

This research type is explanatory research, which is intended to analyze the relationship between one variable and another or how a variable affects other variables (Umar, 2003). The interval scale is the type of scale to measure the variables used in the following research. At the same time, the scale method used in measuring answers from interviewees to the questionnaire is the Likert Scale. In the following observation/research, the measurement scale used is a Likert Scale of 1 to 5, namely a score of 5 (SS = Strongly Agree), a score of 4 (S = Agree), a score 3 (N = Neutral), score 2 (NA = Not Agree), and score 1 (SD = Strongly Disagree).

The population to be examined in this study is 35 Regional Apparatus Organizations (OPD) / Regional Work Units (SKPD) in Medan. The sampling technique in the following research is total sampling. Total sampling is a technique in which the number of samples equals the total population (Sugiyono, 2010). The sampling technique used to determine the sample for this study was a saturated sample (census), where the sample was taken as a whole. Each OPD/SKPD will be given 2 (two) or 3 (three) questionnaires to the PPK (Financial Administration Officer), which is the administrator in charge of financial administration at the OPD or also known as the spending treasurer. The data analysis method used in this research is descriptive statistics, data quality testing and hypothesis testing. The data obtained will be processed using SmartPLS software version 3.3.5.

## **RESULT & DISCUSSION**

### **RESULT**

#### **A. Descriptive Statistical Analysis**

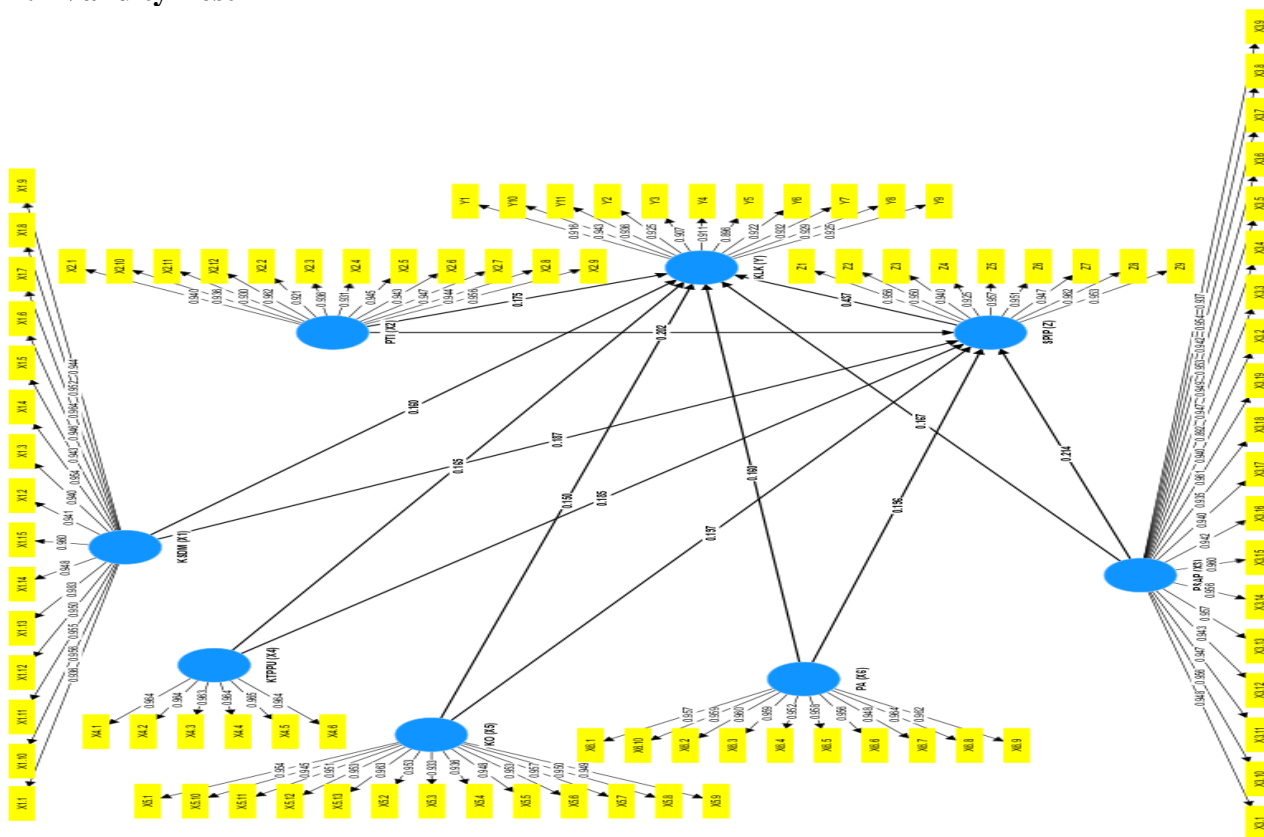
Information obtained through descriptive statistics includes data concentration (mean, median) and data distribution (Muchson, 2020). Descriptive statistical analysis in the following research provides a snapshot of the statements of the variables used in the study.

**Table 2.**  
**Descriptive Statistics Test Result**

<b>Research Variable</b>	<b>Average</b>	<b>Category</b>
Human Resource Competency	3,87	High
Utilization of Information Technology	3,88	High
Application of Government Accounting Standards	3,89	High
Compliance with Legislation	3,9	High
Organizational Commitment	3,89	High
Accounting Understanding	3,91	High
Government Internal Control System	4,03	High
Quality of Financial Statements	4,12	High

Source: Primary data processed (2023)

**B. Data Quality Testing**  
**Outer Model Evaluation**  
**1. Validity Test**



Source: Primary data processed (2023)

**Figure 2.**  
**Outer Model PLS Algorithm Results (2023)**

Based on the picture above, the discriminant validity test shows that all indicators on each research variable have a cross-loading value greater than 0.07 on the variable it forms compared to the cross-loading value on other variables. Based on the results of discriminant validity testing in the research model above, it can be stated that the indicators used in this study already have good discriminant validity in constructing each variable.

**2. Reliability Test**

**Table 3.**  
**Composite Reliability Result**

	<i>Composite Reliability</i>
Human Resource Competency	0,993
Utilization of Information Technology	0,989
Application of Government Accounting Standards	0,994
Compliance with Legislation	0,987
Organizational Commitment	0,992
Accounting Understanding	0,991
Government Internal Control System	0,988
Quality of Financial Statements	0,984

Source: Primary data processed (2023)

From the table above, it is known that all variable Composite Reliability values are greater than 0.7, which means that they meet the reliability requirements based on Composite Reliability. Thus these results can indicate that each research variable has a high level of reliability.

## Hypothesis Test

### 1. Direct Effects

**Table 4.**  
**Direct Effect Test Results**

	<i>Path Coefficient</i>	<i>Sample Mean</i>	<i>Std. Dev</i>	<i>P-Values</i>
(X1) → (Z)	0,187	0,187	0,056	0,000
(X2) → (Z)	0,202	0,201	0,055	0,000
(X3) → (Z)	0,214	0,216	0,060	0,000
(X4) → (Z)	0,185	0,180	0,053	0,000
(X5) → (Z)	0,197	0,191	0,050	0,000
(X6) → (Z)	0,196	0,191	0,054	0,000
(Z) → (Y)	0,437	0,436	0,143	0,001
(X1) → (Y)	0,160	0,158	0,057	0,003
(X2) → (Y)	0,175	0,174	0,054	0,001
(X3) → (Y)	0,167	0,165	0,059	0,003
(X4) → (Y)	0,165	0,165	0,056	0,002
(X5) → (Y)	0,150	0,147	0,056	0,004
(X6) → (Y)	0,160	0,157	0,058	0,003

Source: Primary data processed (2023)

Based on the picture above, it can be concluded that: Human Resource Competence, Utilization of Information Technology, Application of Government Accounting Standards, Compliance with Laws and Regulations, Organizational Commitment, Understanding of Accounting, and Government Internal Control Systems positively and significantly affect the Government Internal Control System.

Human Resource Competence, Utilization of Information Technology, Application of Government Accounting Standards, Compliance with Legislation, Organizational Commitment, and Understanding of Accounting positively and significantly affect the Quality of Financial Statements.

### 2. Indirect Effects (Indirect Effects)

**Table 5.**  
**Mediation Test Results (Indirect Effect)**

	<i>Path Coefficient</i>	<i>P-Values</i>
(X1) → (Z) → (Y)	0,082	0,010
(X2) → (Z) → (Y)	0,088	0,019
(X3) → (Z) → (Y)	0,093	0,022
(X4) → (Z) → (Y)	0,081	0,017
(X5) → (Z) → (Y)	0,086	0,013
(X6) → (Z) → (Y)	0,086	0,014

Source: Primary data processed (2023)

Based on the table above, it can be concluded that Human Resource Competence indirectly significantly influences the Quality of Financial Reports, Utilization of Information Technology, Application of Government Accounting Standards, Compliance with Legislation, Organizational Commitment, and Understanding of Accounting through the Government's Internal Control System.



### 3. Overall Effects (Total Effects)

**Table 6.**  
**Results Overall Effects (Total Effects)**

	<i>Path Coefficient</i>	<i>P-Values</i>
(X1) → (Z)	0,187	0,015
(X1) → (Y)	0,242	0,000
(X2) → (Z)	0,202	0,001
(X2) → (Y)	0,263	0,000
(X3) → (Z)	0,214	0,006
(X3) → (Y)	0,261	0,000
(X4) → (Z)	0,185	0,002
(X4) → (Y)	0,246	0,000
(X5) → (Z)	0,197	0,002
(X5) → (Y)	0,236	0,000
(X6) → (Z)	0,196	0,001
(X6) → (Y)	0,246	0,000
(Z) → (Y)	0,437	0,000

Source: Primary data processed (2023)

### 4. Determination Coefficient Test (R Square)

**Table 7.**  
**Determination Coefficient Results**

	<i>R Square</i>
Government Internal Control System (Z)	0,432
Quality of Financial Statements (Y)	0,797

Source: Primary data processed (2023)

The table above shows that the coefficient of determination ( $R^2$ ) of the Government's Internal Control System (Z) is 0.432. This indicates that the independent variables, namely Human Resource Competence, Utilization of Information Technology, Application of Government Accounting Standards, Compliance with Legislation, Organizational Commitment, and Understanding of Accounting, can affect the Government's Internal Control System by 43.2%. In contrast, 56.8% is influenced by other factors. So it can be concluded that the effect produced by the independent variables is moderate.

The coefficient of determination ( $R^2$ ) for the quality of financial statements (Y) is 0.797. This indicates that the independent variables, namely Human Resource Competence, Utilization of Information Technology, Application of Government Accounting Standards, Compliance with Laws and Regulations, Organizational Commitment, and Understanding of Accounting and Government Internal Control Systems, can affect the quality of financial statements by 79.7%. In contrast, 20.3% is influenced by other factors. So it can be concluded that the influence produced by the independent variables is strong.

## CONCLUSION

The results of the research conducted can provide several conclusions based on the discussion of the research that has been done. Following are some conclusions that can be drawn and summarized from this research:

- 1) Competence of human resources has a positive and significant effect on the government's internal control system.
- 2) Information technology positively and significantly affects the government's internal control system.

- 3) Applying government accounting standards positively and significantly affects the government's internal control system.
- 4) Compliance with laws and regulations positively and significantly affects the government's internal control system.
- 5) Organizational commitment positively and significantly affects the government's internal control system.
- 6) Understanding accounting positively and significantly affects the government's internal control system.
- 7) The government's internal control system has a positive and significant effect on the quality of local government financial reports.
- 8) Competence of human resources has a positive and significant effect on the quality of local government financial reports.
- 9) Utilization of information technology has a positive and significant effect on the quality of local government financial reports.
- 10) Application of government accounting standards has a positive and significant effect on the quality of local government financial reports.
- 11) Compliance with laws and regulations positively and significantly affects the quality of local government financial reports.
- 12) Organizational commitment positively and significantly affects the quality of local government financial reports.
- 13) Understanding accounting has a positive and significant effect on the quality of local government financial reports.
- 14) Competence of human resources indirectly significantly affects the quality of local government financial reports through the government's internal control system.
- 15) Utilization of information technology indirectly significantly affects the quality of local government financial reports through the government's internal control system.
- 16) Application of government accounting standards indirectly significantly affects the quality of local government financial reports through the government's internal control system.
- 17) Compliance with laws and regulations indirectly significantly affects the quality of local government financial reports through the government's internal control system.
- 18) Organizational commitment significantly indirectly affects the quality of local government financial reports through the government's internal control system.
- 19) Understanding accounting indirectly significantly influences the quality of local government financial reports through the government's internal control system.

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