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## ENHANCING VALUE FOR MONEY PERFORMANCE IN LOCAL GOVERNMENT ORGANIZATIONS: THE ROLE OF PUBLIC FINANCIAL ACCOUNTABILITY AND INTERNAL CONTROL

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### ABSTRACT

This study examines the role of public financial accountability and internal control implementation on the performance of value for money of Local Government Organizations (LGOs). This study also investigates the role of internal control on public financial accountability and the intervening role of public financial accountability. This study was conducted at the Yogyakarta City Government from October 1 to November 15, 2021, using a survey method. Questionnaire responses obtained were 121, coming from 30 LGOs. The partial least square (PLS) technique was then employed to test the hypotheses. The results revealed that the public financial accountability and internal control implementation were directly associated with the value for money performance of LGOs. Additionally, the internal control implementation was positively associated with public financial accountability, while the public financial accountability played a role as a partial intervening variable (p-value = 0.012). It was also found that the variable with the greatest significant effect on value for money performance was an internal control (p-value = 0.00). The results of this study provide critical practical implications to be considered by local governments to improve their value for money performance through strengthening accounting policy aspects.

**KEYWORDS:** Internal Control; Local Government Organizations; Public Financial Accountability; Value for Money Performance.

## INTRODUCTION

The decentralization of government in Indonesia impacts financial management and accountability in local government (Harun & Shariyani, 2019). To improve public financial accountability practices, which are eventually expected to improve local government performance, a Self-Assessment of the Implementation of Bureaucratic Reform was initiated (Harun & Shariyani, 2019). As a local government, the Yogyakarta City Government cannot be separated from the demands of this regulation. However, the results obtained by the Yogyakarta City Government in 2020 still appeared to be unsatisfactory, as indicated by the value for money performance below the average (Ansori, 2020). The value for money performance assessment of local government is carried out by referring to three main indicators: economy, effectiveness, and efficiency (Ulum & Sofyani, 2016).

Until today, research on the determinants of value for money performance in Local Government Organizations (LGOs) has been carried out several times (e.g., Aprilia, Nur DP, & Rofika, 2016; Al Khajeh, 2018; Dahlan & Madjodjo, 2020). In detail, some of these prior studies found that important determinants of LGO's value for money performance encompass internal control implementation (Aprilia et al., 2016; Atarwaman, 2019; Yudhasena & Putri, 2019), leadership style (Akpaprep, Jengre, & Mogre, 2019; Al Khajeh, 2018; Kusumayanti, Ratnasari, & Hakim, 2020), organizational culture (Laras, Santana, Jatmiko, & Utami, 2021; Manggis, Yuesti, & Saptia, 2018), and organizational commitment (Adi, Suardikha, & Putri, 2017; Dahlan & Madjodjo, 2020). However, most of the above studies come from the view of management science, while those from the perspective of public sector accounting are still rare. Additionally, these prior studies have uncovered conflicting results. In accounting-related research, for instance, it was found that while Aprilia et al. (2016), Atarwaman (2019), and Yudhasena and Putri (2019) claimed that internal control implementation had a significant role in enhancing LGO performance, Erawati and Winangsit (2019) noted that it had no relationship with LGO performance. The same result was also disclosed by Dewi, Nasfi, and Yuliza (2021) that internal control did not contribute to increasing financial accountability in the village government. This inconsistency in previous study results has opened a research gap on this topic.

Furthermore, the inconsistency of prior studies related to internal control implementation's role on value for money performance in LGO may be due to the lack of consideration of public financial accountability, an accounting issue, as a critical determinant in promoting the value for money performance of LGO. Altrichter and Kemethofer (2015) noted that accountability pressure improves organizational performance. Specifically, they found that accountability pressure encourages the organization to be more sensitive to stakeholders' demands and audit results and increases the management's involvement in activities improvement. On the other hand, according to an agency theory perspective, LGO employees seen as agents (government administrators) may be motivated to fulfill their desires when performing government duties. As a result, their actions in utilizing government budget or financial resources are only limited to fulfilling work obligations rather than improving the principal's welfare, i.e., the community (Halim & Abdullah, 2006; Sofyani, Akbar, & Ferrer, 2018; Ahyaruddin & Akbar, 2018). Such behavior may tend to ignore the value for money performance of the organization. To mitigate the possible negative impact of agency problems in the realm of LGO financial issues, it is crucial to emphasize the strengthening of accounting policy through public financial accountability (Sofyani, Pratolo, & Saleh, 2022). By doing so, the value for money performance of LGO can be enhanced (Sayuti, Majid, & Juardi, 2018). Given the preceding discussions, it is deduced that the

internal control implementation in local governments must first lead to strengthening public financial accountability before finally creating value for money performance.

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Based on the discussions mentioned earlier, the current study tries to assess the role of public financial accountability and internal control on the value-for-money performance of LGOs. Additionally, to address the empirical gap in the inconsistency of previous studies' results, this study also tests public financial accountability as an intervening variable. By doing so, this research contributes to the literature on how key factors should be designed to pursue value for money performance in LGOs. In addition, this study explicitly presents a new discussion regarding the role of public financial accountability as an intervening variable. In this respect, public financial accountability is becoming an essential concern in planning, implementation, and accountability pattern of local government financial issues (Sayuti et al., 2018), especially to increase performance and public trust. For this reason, this study is crucial to conduct so that the problem of improving performance in the public sector in Indonesia can be analyzed. Finally, solutions for practical implications can be obtained.

### Hypotheses Development

Public financial accountability is the obligation of the management (agent) to provide accountability by presenting, reporting, and disclosing all activities, both financial (government budget) and those with indirect financial implications, which are their responsibility to the trustee (principal/community) with the rights to demand accountability (Mardiasmo, 2016). Sayuti et al. (2018) defined public financial accountability as providing information and disclosure on local government financial activities and performance to all interested parties (stakeholders) so that public rights, including the right to know, the right to be informed, and the right to listen, can be fulfilled.

On the other hand, the public sector is often seen as a hotbed of inefficiency, waste, a source of leakage of funds, and institutions that are always at a loss (Sayuti et al., 2018). Agency theory also views management as selfish by utilizing financial resources (Arifah, 2012; Halim & Abdullah, 2006). To minimize these risks in local governments, public financial accountability is especially pivotal, specifically in promoting a control mechanism within the organization to ensure that the government budget is utilized properly (Sayuti et al., 2018; Sofyani et al., 2022). In this case, the public financial accountability pressure can be a tool to encourage agents to follow what is mandated by related regulations (Sofyani et al., 2022), including a performance from a value for money perspective (Noviyana & Pratolo, 2018; Novatiani, Kusumah, & Vabiani, 2019). Departing from the explanations above, the hypothesis was built as follows:

*H1: Public financial accountability is positively associated with the value for money performance of LGOs.*

An internal control implementation is an organization's internal policy that aims to strengthen good governance practices within the organization (Sofyani & Ardiyanto, 2022), especially accountability, and to achieve more optimal performance (Abdullahi, Abdullahi, & Muturi, 2016; Sofyani, Abu Hasan, & Saleh, 2022). Putri (2013) argued that the government's internal control could be used to improve performance since it can help oversee the use of public funds managed by government employees. By doing so, the target value for money will be achieved. Besides, internal control can minimize the potential for agency problems that arise from the opportunistic attitude of management by mitigating financial information asymmetry. As such, organizational performance, accountability, and transparency can be improved (Sofyani & Ardiyanto, 2022). Based on the explanations above, the hypothesis was put forward as follows:

**H2:** *Internal control implementation is positively associated with the value for money performance of LGOs.*

Conceptually, the COSO internal control-integrated framework of 2013, which the Indonesian government officially adopted, formulated three main objectives of internal control implementation in the organization: to ensure the reliability of reporting and accountability practices, the effectiveness and efficiency of operations, and compliance with various applicable regulations (Sofyani, Abu Hasan, & Saleh, 2022). From this insight, it is clear that the internal control implemented at LGO should promote public financial accountability. In addition, strengthening the internal control issue is inseparable from the case of mitigating agency problems and information asymmetry within the organization, which can lead to financial resource fraud, as highlighted by agency theory. Therefore, internal control is considered a mechanism that can alleviate the potential for fraud, error, leakage, and financial inefficiency to further improve organizational performance (Duh, Chen, Lin, & Kuo, 2014; Nawawi & Salin, 2018). Several previous studies have provided empirical evidence regarding this claim. For example, Adeyemi and Olarewaju (2018) found that internal control in the public sector could promote effective and efficient financial accountability. In a similar vein, Utami and Ganika (2021) uncovered that a rising government internal control system would raise regional financial accountability. Based on the previous arguments, the hypothesis was formulated as follows:

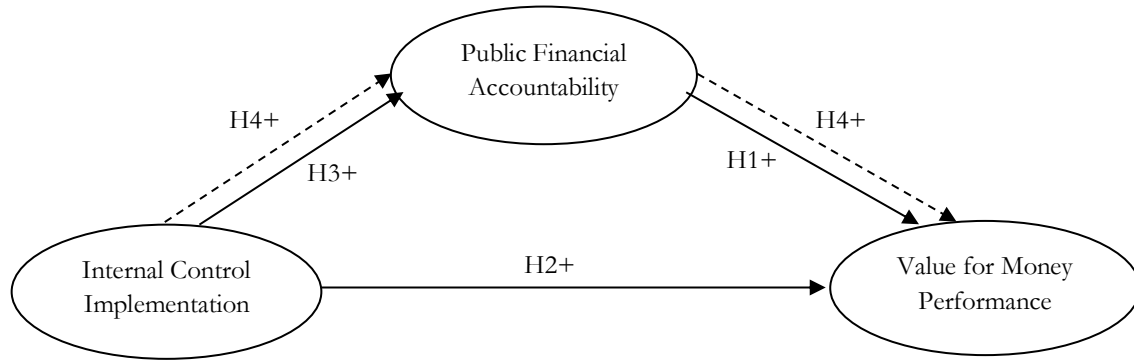
**H3:** *Internal control implementation is positively associated with public financial accountability.*

From the agency theory perspective, the low quality of local government governance, especially accountability, can cause employees to take actions that benefit themselves by utilizing the organization's internal resources, namely the financial ones (Arifah, 2012; Halim & Abdullah, 2006). Therefore, although several crucial factors have been introduced in the organization to pursue performance, such as internal control implementation, such policy may not promote performance without good accountability practices. It may be the reason previous studies found inconsistent results on internal control-value for money performance relationships in public sector organizations. Moreover, the financial governance issue in Indonesia is crucial to implement, given the prominent level of corruption in this kind of institution. On the other hand, effective accountability in the management of financial resources is a requirement for pursuing value for money performance in public sector organizations, considering that the main indicator of value for money is closely related to financial management and governance (Bastian, 2016; Pratolo, 2022; Ulum & Sofyani, 2016). Hence, it is suspected that the effectiveness of public financial accountability practices is the main prerequisite (intervening) in achieving value for money performance in LGOs (Noviyana & Pratolo, 2018). Based on the above explanations, the intervening hypothesis was constructed as follows:

**H4:** *Internal control implementation is positively associated with the value for money performance of LGOs through public financial accountability.*

Based on the theoretical framework and hypotheses developed above, the research model was formulated as presented in Figure 1.

**Figure 1.**  
Research  
Model:  
Modified from  
Noviyana and  
Pratolo (2018)  
and Sofyani and  
Ardiyanto  
(2022)



**METHOD**

This research was conducted at the Yogyakarta City Government from October 1 to November 15, 2021, using 30 LGOs as research samples. The sampling technique in determining the sampling unit (respondents) employed purposive sampling, with the criteria: the respondents were accounting or finance staff or people involved in accounting practices, financial/budget management, and the pursuit of value for money performance at LGOs. It was intended that respondents had sufficient capability to answer various questions in the questionnaire, especially those relating to public financial accountability and value for money performance. Furthermore, agencies and offices were selected because they are LGOs that prepare, use, and report finance and performance achievements (Abdullah, 2004).

The data collection technique used was a survey method by distributing questionnaires directly to the LGOs so that the questionnaire returns could be high. The instruments utilized were adapted from several previous studies, i.e., Susanti (2014) for value for money performance of LGO, Amelia, Desmiyawati, and Azlina (2014) for internal control implementation in LGO, and Putra (2013) for public financial accountability. The questionnaire measured a Likert scale of 1 to 5, where 1 indicates "strongly disagree" to 5 signifies "strongly agree". It was used as a standard scale for survey research in Indonesia's public sector accounting field. Some indicators in the questionnaire were also made with negative nuances. It was to detect whether the questionnaire was completed correctly or randomly.

Partial Least Square (PLS) was then used to test the hypotheses. It was suitable for use in this study as it allows for a relatively small sample size (Akbar, Pilcher, & Perrin, 2012; Pratolo, Sofyani, & Anwar, 2020). In addition, PLS fits this study, focusing on assessing the relationship between variables rather than the goodness of fit of the research model. However, it should be noted that the PLS approach is limited to exploring the relationship between variables and does not represent the strength of the model under study. Hence, the theoretical implications obtained from PLS test results are still the concern of many statistical academics (Haryono, 2016; Abdillah & Hartono, 2015).

Moreover, the minimum observation number when using PLS as an analysis technique is the '10 times rule' (Hair, Black, Babin, Anderson, & Tatham, 2010). Thus, the observation numbers should be greater than a variable with the highest number of indicators within a model. As value for money is a variable with a maximum number of indicators (9), thus, the minimum observation numbers, as suggested by Hair et al. (2010), should be 90 (9x10). This minimum sample size requirement had been met, with 121 responses successfully collected for this study.

## RESULTS AND DISCUSSIONS

The questionnaires were distributed for two months, and a total of 150 questionnaires were successfully distributed to 30 LGOs within the Yogyakarta City Government. The number of successfully re-collected questionnaires was 125 pieces, or 83.33%. However, it was found that four pieces could not be analyzed because they were filled out incompletely. Thus, 121 questionnaires could be analyzed.

Table 1 shows the statistical data on respondent characteristics, displaying details regarding the identity of respondents based on gender, age, education level, position, and length of tenure.

Characteristic	Description	Number	Percentage (%)
Position	Total Respondents	121	100
	Head of Division/Section	72	59
	Accounting/Financial Staff	36	30
	Secretary of LGO	13	11
Education level	Total Respondents	121	100
	Diploma-3	7	6
	Undergraduate	72	59
	Master	42	35
Length of tenure	Total Respondents	121	100
	<1 year	27	22
	1 to 5 years	53	44
	6 to 10 years	18	18
	>10 years	20	16

**Table 1.**  
Characteristics  
of Respondents

As this study used the PLS technique for data analysis, before hypothesis testing was performed, the validity and reliability of the instrument were first tested through measurement model assessment. In the first test, it was found that several indicators of the constructs had loading values less than 0.5, so according to Hair, Hult, Ringle, and Sarstedt (2021), it was recommended to delete them. It is because weak loading values will also affect the low Cronbach's Alpha and Average Variance Extracted values (Hair et al., 2021). In the second test, all the rules of thumb covering convergent validity, discriminant validity, and reliability had been met. Table 2 presents the loading values of all remaining indicators and the AVE, which all agreed to the rule of thumb at 0.5 (Hair et al., 2021).

Code	Indicator	Loading
<b>Public Financial Accountability (PFA) – AVE: 0.505</b>		
PFA3	Public interest is the primary concern in budget management on performance achievement.	0.768
PFA4	The performance outcome indicators to be achieved have been used to evaluate the budget.	0.724
PFA5	The leadership continuously monitors the process of accountability for performance.	0.731
PFA9	Budget management is accountable to the broader community.	0.610
<b>Internal Control (IC) – AVE: 0.566</b>		
IC1	The rules of conduct are applied to all levels of management and subordinates.	0.713
IC2	The leader where I work analyzes the tasks that have been carried out and provides consideration and supervision.	0.793
IC4	The leader where I work is involved in the preparation of strategic plans and annual work plans.	0.793
IC5	Where I work, financial information is provided on time so that it is possible to take appropriate corrective action.	0.787
IC6	Duties assigned to employees can be communicated and understood by internal controls.	0.578
IC7	The leader where I work follows up on the recommendations found by the internal audit team.	0.774
IC8	The leadership where I work determines the appropriate action from the follow-up results to the audit findings' recommendations.	0.802
<b>Value for Money Performance (VFMP) – AVE: 0.562</b>		
VFMP3	The LGO leaders where I work make decisions on financial problems quickly to respond to issues within the organization.	0.699
VFMP4	The LGO leaders where I work respond quickly to the dynamics within the financial organization.	0.811
VFMP6	The LGO where I work emphasizes the vision and mission of the organization to all employees so that organizational goals are achieved.	0.795
VFMP7	The LGO where I work appreciates employees with an excellent work ethic.	0.752
VFMP8	The LGO where I work is open to public complaints, which can improve the organization's quality.	0.793
VFMP9	The management at the LGO where I work puts forward new ways of solving problems that arise concerning financial issues.	0.633

**Table 2.**  
Validity Test Results

\*Indicators with negative nuances are scaled in reverse; AVE = Average Variance Extracted

Next are the discriminant validity testing results (Table 3). The test results concerning the Fornell and Larcker method signify that discriminant validity had been established. It can be seen from the AVE root value on the diagonal order (bold) higher than the correlation construct with other constructs (Fornell & Larcker, 1981).

**Table 3.**  
Discriminant  
Validity Test  
(Fornell and  
Larcker)

Construct	Internal Control	Public Financial Accountability	Financial Value for Money Performance
Internal Control	<b>0.752</b>		
Public Financial Accountability	0.566	<b>0.711</b>	
Value for Money Performance	0.614	0.517	<b>0.750</b>

Moreover, the reliability test results to ensure the consistency of the indicators in measuring the construct also agreed on the rule of thumbs (Table 4). It can be seen from Cronbach's Alpha and Composite reliability values greater than 0.6 and 0.7, respectively (Chin, Marcolin, & Newsted, 2003; Hair et al., 2021). Therefore, since the measurement model assessment results met all the specified requirements, the hypothesis testing with a structural assessment could proceed (Table 5 and Figure 2).

**Table 4.**  
Reliability Test  
Results

Construct	Cronbach's Alpha	Composite Reliability
Internal Control	0.870	0.900
Public Financial Accountability	0.676	0.802
Value for Money Performance	0.846	0.884

Direct Relationship	Code	Coefficient	SE	T statistic	P-value
Public Financial Accountability → Value for Money Performance	H1+	0.248	0.095	2.624	0.003
Internal Control → Public Financial Accountability	H2+	0.566	0.070	8.112	0.000
Internal Control → Value for Money Performance	H3+	0.475	0.102	4.645	0.000

Indirect Relationship

**Table 5.**  
Structural  
Model  
Assessment  
Results

Internal Control → Public Financial Accountability → Value for Money Performance	H4+	0.140	0.062	2.264	0.012
Adjusted R <sup>2</sup> : 0.409					



From Table 5, the adjusted R<sup>2</sup> value showed a moderate level of 0.409 (Chin, 1998). This result implies that 40.9% of the value for the money variable was explained by the determinants in the model, while other factors outside the model explained the rest. Thus, the current research model is vital to take into account the practical implications made. Furthermore, all hypotheses were supported, where H1, H2, and H3 were supported at a p-value of 0.01 and H4, predicting the intervening hypothesis, was supported at a p-value of 0.05. However, the intervening hypothesis was only partially supported as the direct relationship between internal control and value for money performance was statistically significant.

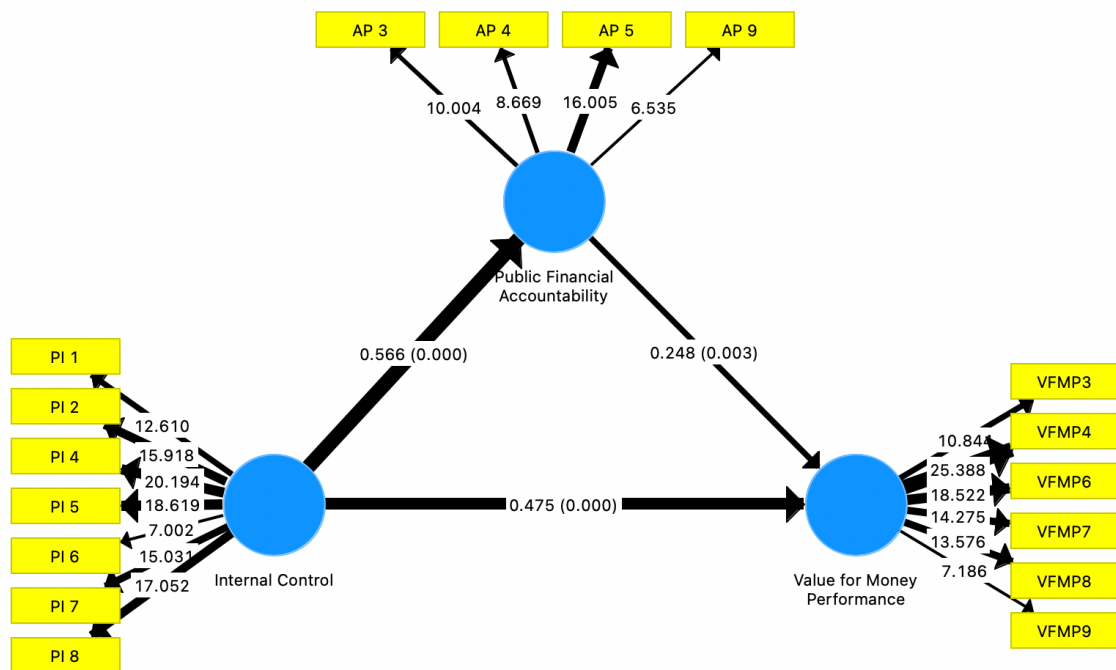


Figure 2. Structural Model Assessment Results

Moreover, from Figure 2, it can be seen that the variable with the strongest significance value in promoting value for money performance at LGOs was internal control implementation (p-value of 0.00), indicated by the relationship line that appears thicker than that of public financial accountability. Furthermore, the significance of the internal control effect also appeared to be exceptionally large on public financial accountability, even the strongest among other relationships. It confirms COSO (2013) and government regulations related to internal control that the main purpose of internal control initiated in this local government is to improve good governance practices in government agencies, especially regarding public financial accountability (Sofyani & Ardiyanto, 2022). These findings also strengthen the indication of agency theory that occurs in the public sector, where internal control is presented to mitigate agency problems and information asymmetry. In doing so, public financial accountability is the concern (Maria & Halim, 2021). Further, although public financial accountability in this study had a smaller effect than internal control (p-value=0.003), it still had a positive role on LGOs' value for money performance. This finding also reinforces the perspective of agency theory, where accountability as a control approach can achieve its goal of improving organizational performance, as found by Noviyana and Pratolo (2018) and Novatiani et al. (2019).

### **Public Financial Accountability, Internal Control, and Value for Money Performance**

Public financial accountability was found to have a positive relationship with the value for money performance of LGOs (H1). This finding is in line with Setiawan and Safri (2016) and Aprilia et al. (2016). Abdullah and Arisanti (2010) argued that accountability is closely related to organizational performance because it can prevent the emergence of moral hazard in using organizational resources that should be allocated to pursue performance. In addition, the pressure of public financial accountability, as part of good governance, is deemed to be able to prevent various forms of irregularities that may occur within the organization, either related to fraud or inefficiency and ineffectiveness issues (Bastian, 2016; Sofyani et al., 2022). Thus, the findings of this study simply conclude that the pursuit of performance can run well if the practice of public financial accountability in LGO also runs well. This finding confirms the agency theory in the context of public sector accounting.

Furthermore, the H2 testing result deduced that internal control had a positive direct relationship to the performance of value for money of LGOs. This result corroborates the findings of Putri (2013) and Al-Thuneibat, Al-Rehaily, and Basodan (2015), which concluded that internal control plays a vital role in improving organizational performance. Internal control is also positively related to public financial accountability (H3). As such, this finding affirms the study by Adeyemi and Olarewaju (2018) and Utami and Ganika (2021). In addition, Duh et al. (2014) and Nawawi and Salin (2018) highlighted that internal control corroboration is related to efforts to mitigate agency problems and information asymmetry within the organization as they can lead to financial resources fraud and eventually interfere with organizational performance improvement. Drawing from this insight, to improve LGOs performance and public financial accountability, the local governments need to maintain and improve the quality of internal control implementation. Additionally, effective internal control will assist in overseeing the use of the budget, which the government utilized incidentally as a public fund, and then controlling it to achieve value for money performance targets (effectiveness, efficiency, economy). It is also in proportion to Aprilia et al. (2016) that good internal control will help government organizations to control existing financial resources from potential agency problems that may lead to fraud that interferes with value-for-money performance.

### **The Intervening Role of Public Financial Accountability**

From intervening test results (H4), internal control implementation had a positive indirect relationship with the value for money performance of LGOs through public financial accountability. Meanwhile, internal control implementation was directly associated with the value for money performance of LGOs. From these findings, it can be indicated that the role of public financial accountability was partially intervening. These findings address inconsistencies in the results of previous studies highlighted earlier. These results also affirm studies by Bastian (2016), Noviyana and Pratolo (2018), and Sofyani et al. (2022) that good governance mechanisms are needed to be a prerequisite for improving organizational performance. Besides, it signifies that specific organizational control policies may not contribute to the achievement of LGO performance if the practice of public financial accountability, as a control mechanism within government institutions, has not been carried out properly. Thus, this finding underpins the importance of internal control in strengthening the accounting policy aspect over financial management and governance in LGO to control and reduce potential agency problems. By so doing, it can further encourage value for money performance (Chen, Yang, Zhang, & Zhou, 2020; Halim & Abdullah, 2006). Hence, theoretically, this study confirms that the agency theory perspective is still relevant in the

context of public sector accounting, although some researchers mentioned that stewardship theory is the basis for public sector accounting practices in Indonesia, especially in local governments (see: Pratolo, 2022; Ritonga, 2020). Practically speaking, the results of this study also strengthen the support for the importance of increasing public financial accountability in LGOs to improve value for money performance in that organization.

## CONCLUSION

This study empirically examined the relationship between public financial accountability, internal control implementation, and value for money performance by positioning public financial accountability as an intervening variable in LGOs in Yogyakarta City. The results of PLS analysis involving 121 survey data implied that public financial accountability and internal control implementation had a direct positive relationship with the value for money performance of LGOs. In addition, internal control was positively associated with public financial accountability, and public financial accountability played a partial intervening variable in the internal control-value for money performance relationship. From these results, an essential note underlined is that both critical factors, i.e., public financial accountability and internal control implementation, must continue to be improved due to their crucial roles in promoting value for money performance in LGO. Specifically, it aims to minimize agency problems in financial governance in local government, which might interfere with value for money performance.

This study has limitations that are important to note for readers. First, this research was only conducted within the scope of the LGOs in Yogyakarta City. This condition impacted the lack of generalizability of the study results. Therefore, further research on associated topics needs to be carried out in other areas to continue to develop discussions related to value for money performance and public financial accountability in LGO. Another limitation of this study is that it did not perform cross-validation since the required secondary data were not publicly available. To follow up on this limitation, further studies can perhaps be carried out with a qualitative approach to provide more in-depth and detailed exploration results regarding the practice and role of each variable in improving the performance of LGO.

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