

# The Local Government Performance in Indonesia

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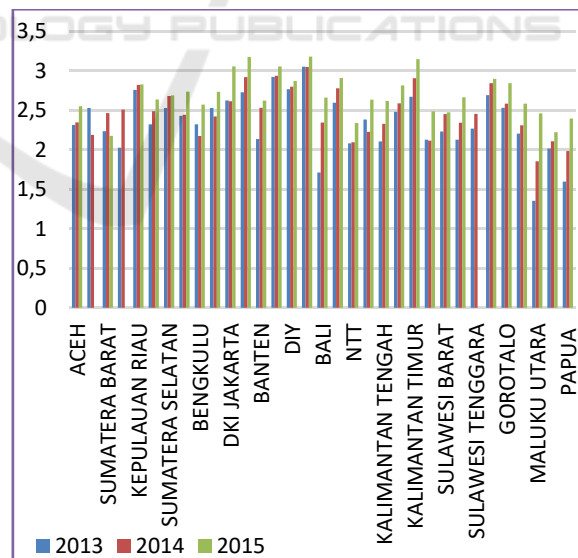
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**Abstract:** The provision of public services and the target of national development objective is one of the roles of local government. Evaluation and measurement of systematic performance is needed to measure the success or performance of a government. Local governments in Indonesia use performance evaluations of local governments that produce local government performance (LGP) scores. However, there are still provinces in Indonesia with moderate government performance status. This study aims to determine the influence of regional wealth (RW), intergovernmental revenue (IR), regional size (RS), and regional expenditure (RE) on the LGP in the Province of Indonesia during 2013-2015. Sample used in this study is purposive sampling counted 29 provincial governments. The analytical method used is panel data regression using Fixed Effect Model (FEM). This study proved that RW partially has a positive and significant effect on the LGP. Meanwhile, IR, RS, and RE have no significant effect on the LGP. There is a significant influence between RW, IR, RS, and RE on the LGP.

## 1 INTRODUCTION

Article 69 paragraph 1 of Law number 32 of 2014 (Indonesia, Regional Government, 2014) confirms that regional heads must submit reports on the implementation of local government as a form of accountability in carrying out their government. The reports will be used as basis for the government in evaluating the performance of local government operations.

Local Government Implementation Performance Evaluation (LGPE) is carried out by national and regional assessment teams that will conduct research with the government and countries in Indonesia. There are provinces in Indonesia that have experienced an increase or decrease in their local government performance (Figure 1).



Source: Data processed (Home Affairs Ministerial Decree Number 120-4761 of 2014, Number 800-35 of 2016 and Number 120-10421 of 2016).

Figure 1: National performance score of local government in Indonesia.

East Java, West Java, East Kalimantan, DKI Jakarta and Central Java provinces experienced improved performance from 2013 to 2015 for provincial government performance appraisal with a performance score of 3. Only East Java Province always achieved performance with a score of 3. Provincial government still dominated by performance scores that have not reached a score of 3. In 2013, North Maluku and Papua Provinces achieve performance scores in the numbers 1-1.5 the score is very far compared to the average

Each local government has different financial capabilities in exploring and managing financial resources, such as exploring regional wealth seen from Local Revenues (LR) through collection of regional taxes and retribution and, measuring the level of regional financial dependence from the government or balancing funds as financial assistance in implementing the region. Not all provincial governments in Indonesia can finance their regional needs by using LR, having a large regional size based on the number of regional assets owned by local governments and making expenditure decisions independently according to the actual needs of the region each.

There are several studies related to the local government performance in Indonesia, especially in terms of the association between local government characteristics and financial performance (Mustikarini & Fitriasari, 2012), (Kusumawardani, 2012), (Sudarsana & Rahardjo, 2013), (Rustiyaningsih & Immanuela, 2014), (Artha, 2015), (Sedyaningsih & Zaky, 2015), (Meilina & Hapsari, 2016), (Setyaningrum & Martani, 2018). Previous studies have found that the size of local government, local government wealth, and level of dependency on central government have positive effects on performance (Nugroho & Prasetyo, 2018).

Mustikarini & Fitriasari, 2012 conducted research using wealth variable that had an influence on government performance. The results of these studies are similar to the results of research conducted by (Meilina & Hapsari, 2016). In contrast to (Sudarsana & Rahardjo, 2013) conducted research with wealth variable by showing that wealth does not affect government performance. A study using the balancing fund variable, namely there was no influence between balancing funds and government performance (Rustiyaningsih & Immanuela, 2014). Regional expenditure variable that did not significantly influence the performance of local governments (Mustikarini & Fitriasari, 2012).

The difference the local government ability is assumed to have an influence on the performance of the local government in managing its finances and the results of previous research encouraged researcher to re-examine the influence of regional wealth, intergovernmental revenue, regional size and regional expenditure on the performance of local government provinces in Indonesia. This study aims to determine the partial and simultaneous effect of regional wealth, intergovernmental revenues, regional size, and regional expenditure on the local government performance in Indonesia.

Overall, this paper begins with a brief explanation of the problem and the research context that is described in the introduction. After that, it is followed by an explanation of the theoretical framework used, research method, evaluation results and discuss the findings research. The final section of this paper explains the conclusions, implications, and suggestions for further research.

## **2 LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT**

### **2.1 Stewardship Theory in Public Sector**

The grand theory used in this research is that Stewardship theory, views management (local government) as a party that can be trusted to act as well as possible for the public interest or stakeholders, for the interests of the principal (community and government). Stewardship theory describes a situation or condition in which management is not motivated by individual goals but rather prioritizes the interests of the organization (Davis, Schoorman, & Donaldson, 1991).

The theory assumes that there is a strong relationship between organizational satisfaction and success. Organizational success describes maximization utility of principals and management groups. The utility maximization of this group will ultimately maximize the interests of individuals within the group of organizations.

### **2.2 Local Government Performance (LGP)**

Home Affairs Ministerial Regulation number 73 of 2009 (Indonesia, Procedures for Implementing

Performance Evaluation for Regional Government Ministerial Regulation, 2009) reveals that the performance of regional administration is the achievement of the implementation of regional government affairs as measured by input, process, output, results, benefits and/or impacts. The LGP is measured using Key Performance Indicators for the operationalization of evaluations on general aspects agreed upon by policy makers are key performance indicators that reflect the successful implementation of governmental affairs which include alignment and effectiveness of relations between regional government and the government and between regional government in the framework of developing regional autonomy, harmony between local government policies and government policies, effectiveness of relations between local government and Parliament, effectiveness of decision making processes by Parliament along with follow-up implementation of decisions, adherence to government regulation, transparency in utilization of allocation, disbursement and absorption of General Allocation Fund (GAF), Special Allocation Fund (SAF) and sharing of funds, effectiveness and transparency of collection of sources of LR, regional loan, and regional assets, effectiveness of planning, preparation, implementation of administration, accountability and regional government budget and new breakthroughs/innovations in the administration of regional governance.

The performance of the regional government will be followed up by conducting a Local Government Performance Evaluation (LGPE). LGPE is a systematic process of collecting and analyzing data on the performance of regional governance, the ability to implement regional autonomy, and the completeness of aspects of governance in newly formed regions.

### 2.3 Regional Wealth (RW) and LGP

The economic wealth of a municipality is to a large extent dependent on the income level of its citizens (Cohen, 2008). Personal income is an important measure of citizens' ability to pay taxes. A high level of personal income generally means higher property, sales and business taxes. Thus, the affluence of a municipality is expected to be positively related to its capacity to generate revenues. A local authority with wealthy citizens is able to levy, at least theoretically, higher local taxes and charge higher prices for the services rendered. This prospect is also expected to be positively

related to its asset turnover; the invested capital would and generate more revenues.

LR was a very appropriate variable to indicate that a high LR affected wealth (Nugroho & Prasetyo, 2018). Wealth is the ability to full fill need. According to Minister of Home Affairs Regulation number 13 of 2006 (Indonesia, Guidelines for Regional Financial Management, 2006) states that the LR is divided according to the type of income which consists of regional taxes, regional retributions, separated wealth management results, other legal revenue

Research on wealth was carried out by (Mustikarini & Fitriyani, 2012) which revealed that LR had a significant positive effect on the performance of local governments. The results of these studies are in line with (Meilina & Hapsari, 2016) by proving that LR has a significant positive effect on the performance of local governments. There is a difference as evidenced by (Sudarsana & Rahardjo, 2013) that the wealth of local governments does not affect the performance of local governments.

Based on above arguments, the hypothesis proposed in this research is as follows:

H<sub>1</sub>: Regional wealth affect local government performance.

### 2.4 Intergovernmental Revenue (IR) and LGP

IR as budget transfers from central government and federal government to local governments (Halim, 2012). In Indonesia, balancing fund is in the form of IR which is a transfer from central government to local government for maintaining fiscal balance between the central government and regional governments including of tax share/non tax share, GAF and SAF.

The fiscal gap that occurs between the government and the regions and between regions can be reduced by the existence of a balance fund. Balancing funds are also used to increase regional capacity in exploring regional economic potential (Nugroho & Prasetyo, 2018). The high percentage of balancing funds shows that local governments are not independent in managing their income and can lead to lower assessment of performance accountability because the high percentage of

balancing fund indicates if the government is unable to plan and run programs/activities to optimize LR.

Previous research using the balancing fund variable (Tama & Adi, 2018) is requiring that the level of dependence on the government has a positive effect on the performance of local governments. The research was supported by (Mustikarini & Fitriasaki, 2012) which revealed that the high balancing fund received would have an impact on the better service of the local government to the community so that the performance of the regional government would increase.

Based on above exposure and previous research, the following hypothesis is summarized:

H<sub>2</sub>: Intergovernmental revenue affect local government performance.

## 2.5 Regional Size (RS) and LGP

The size of local government can be seen from how much total assets it has. The main purpose of the work program established by the local government is to provide the best service to the community (Sudarsana & Rahardjo, 2013). In providing the best service must be supported by good assets too. Therefore, very adequate resources and facilities are needed to provide optimal service. Thus, the greater the size of the region is marked by the large amount of assets of the regional government, it is expected that the performance of local governments will also be higher.

In Indonesia, size of regional government is measured by amount of regional government assets which has influence to financial performance (Nugroho & Prasetyo, 2018). Large regional size in the government will facilitate operational activities which will then facilitate the provision of adequate community services. In addition to the convenience in the operational field, which will facilitated the provision of fluency in obtaining LR for regional progress as evidence of improved performance (Kusumawardani, 2012).

This opinion is supported by research conducted by (Mustikarini & Fitriasaki, 2012) and (Tama & Adi, 2018) requiring that the size of local government has a significant effect on the performance of local governments. The variable size has also positive and significant impact on the financial independence of local government (Siregar & Pratiwi, 2017).

Based on above exposure and previous research, the following hypothesis is summarized:

H<sub>3</sub>: Regional size affect local government performance.

## 2.6 Regional Expenditure (RE) and LGP

According to Republic of Indonesia Law number 32 of 2014 Article 1 (Indonesia, Regional Government, 2014) describes regional expenditure as all regional obligations that are recognized as a deduction of net worth in the period of the relevant fiscal year. Home Affairs Ministerial Regulation number 13 of 2006 (Indonesia, Guidelines for Regional Financial Management, 2006) expenditures consist of: indirect expenditure is budgeted expenditure not directly related to the implementation of programs and activities. Indirect expenditures consist of: employee expenditure, interest, subsidies, grants, social assistance, profit sharing, financial assistance, and unpredictable expenditure. Direct expenditure is budgeted expenditure directly related to the implementation of programs and activities.

The higher the regional expenditure reflects the higher level of service provided to the community. Furthermore, the increasing services provided will also affect the high performance of local governments. However, there are differences in the results of research conducted by (Sudarsana & Rahardjo, 2013) which proves that regional expenditure does not affect the performance of local governments. This is supported by (Meilina & Hapsari, 2016).

Based on above exposure and previous research, the following hypothesis is summarized:

H<sub>4</sub>: Regional expenditure affect local government performance.

## 2.7 RW, IR, RS, and RE and LGP

The description of each variable has been explained in the previous hypothesis. Based on the description that has been explained, the variables used in this study were also used in previous studies. Previous research that has been proven by researchers, it is known that the independent variables used significantly influence.

Based on the description above, the research hypothesis is formulated as follows:

H<sub>5</sub>: Regional wealth, intergovernmental revenue, regional size and regional expenditure affect the local government performance.

### 3 RESEARCH METHODOLOGY

The population in this study consists of all local government in Indonesia. The provinces that were used as sample were 29 with 3 years budgeted. Purposive sampling was used to select the sample, with the criteria of the provincial government that has a score and status for the implementation of Regional Government Performance in 2013-2015, and has complete financial information data. Financial information data was presented in the Budget Realization Report and Balance Sheet in 2013 to 2015.

This study used regression analysis with panel data, and the equation as follow:

$$LGP = \alpha + \beta_1RW + \beta_2IR + \beta_3RS + \beta_4RE + \epsilon$$

Notes: LGP = LGIPE score; RW = total own-source revenue divided by total revenue; IR = total transfer revenue divided by total revenue; RE = total non-routine expenditure (expenditure other than employee expenditure) divided by total expenditure.

Data analysis techniques in this study use statistical tools Eviews 10.

## 4 RESULT AND DISCUSSION

### 4.1 Result

#### 4.1.1 Multiple Linear Regression Analysis

After selecting the panel data regression model, the chosen fixed effect model in this study. Regression results are using the fixed effect model method obtain the regression equation as follows:

$$LGP = -12.01 + 0.74RW - 0.53IR - 0.29RS + 0.08RE + \epsilon$$

Based on the Fixed Effect regression model, shows the value of the correlation coefficient obtained from the adjusted R<sup>2</sup> value of 0.7262 means the change in RW, IR, RS and RE have a correlation or relationship performance of provincial government implementation of Indonesia of 72.62

percent while the remaining 27.38 percent is explained by other factors that are not observed or examined in this study.

### 4.1.2 Hypothesis Testing

**F-Test Result.** The F-statistic test is basically used to determine whether the variables of RW, IR, RS and RE simultaneously affect performance of provincial government implementation of Indonesia. Decision will be taken by looking at the probability of F-statistics. The probability value (F-statistic) is 0.00 where the probability value is smaller than the value of  $\alpha = 0.05$  that can be concluded that the variables of RW, IR, RS and RE simultaneously have an influence on LGP of Indonesia.

**T-Test Result.** Partial testing aims to see the difference between each independent variable by using the t-test, which is a test conducted to determine or not significantly from the wealth, the level of regional finances, the size and cost. The partial test results are presented t-statistic is greater than 0.05, H<sub>0</sub> is accepted, which means that there are no properties. Whereas if prob. T-statistic) is smaller than 0.05, H<sub>0</sub> is rejected, which means there is a significant difference.

This study prove that RW has a significant influence on the LGP. The IR does not significantly influence the performance of regional government. Size of the provincial government in Indonesia has no effect on the LGP. Regional expenditures made by the provincial government in Indonesia have no effect on the LGP.

### 4.2 Discussion

#### 4.2.1 The Impact of RW on LGP

Proven regional wealth has a significant influence on local government performance of Indonesia. Local government wealth has positive effects on local government performance (Setyaningrum & Martani, 2018). The wealth of a regional government is proxied by the amount of local revenue. LR is one source of revenue that has local government sourced from contribution of society consisting of local taxes, regional retribution and other revenues aimed at financing regional development so that it will impact on community services. When an area has large local revenue and is always increasing every year, then the area has been able to maximize the ability of the region and reflect the state or economic capacity that is good and stable. However, when an

area has difficulty in maximizing LR sources, there will be unstable economic problems. If the LR received is greater, then it can be said that the high level of society participation in paying regional taxes and levies. This will increase the motivation of local governments in improving the quality of service to the society. Good quality public services will reflect the performance of a good local government.

The large amount of LR must be accompanied by a high performance of regional government performance which is also seen from the LGIPE which results in local government performance scores. This is evidenced by the DKI Jakarta Province and East Java Province having a large number of the LR influencing the received performance score, which is very high with a range of 3-4 while North Maluku Province receives a low LR also has an impact on the performance score of the local government compared to other provincial governments.

The average LR that has been received by the provincial government in Indonesia is classified as good in optimizing or exploring the potential wealth of each region. The high number of LR proves that the government has played an active role in improving the performance of the implementation of the provincial government in Indonesia.

#### 4.2.2 The Impact of IR on LGP

Hypothesis 2 in this study was rejected, balancing funds are the proceeds from tax and non-tax funds, special funds, and funds sourced from the central government to finance regional administration needs. Tax and non-tax revenue sharing funds are the revenue sharing from taxes that have been obtained from the country's natural resources. Tax and non-tax revenue sharing funds are one of the benchmarks to see the performance of regional government.

The greater the area that receives funds for tax results and Income Tax as well as natural resources derived from waste, gas, natural gas and others. This will affect what has been done in the region. It was proven by the performance score which stated that the provincial governments of DKI Jakarta and East Java benefited for very high funds.

Unlike the special funds and funds used by the government, these funds are government taxes to assist in the administration of government with certain considerations and calculations. Balancing

funds are also used to fund tasks, decrease provisions and burdens.

Regional governments are not active in collecting funds that are used for costs that are greater than optimal. If this condition continues, the local government will always influence which will affect the performance produced by the regional government. This will affect the performance of government, supported by the very high performance required by local governments by the provincial governments of DKI Jakarta and East Java.

Not only provides funds that can be used for governance, but more balancing funds in the context of regional government costs that will be used at the end of the fiscal year. A higher refund will cause a deficit that must be closed with a balance fund. The development of the above hypothesis explains why there is no greater influence.

#### 4.2.3 The Impact of RS on LGP

Hypothesis 3 in this study was rejected. Accrual-Based Government Accounting Standards of PSAP 01 in paragraph 66 state that future economic benefits embodied in affiliate assets are the potential to contribute, both directly and indirectly, to government operational activities, which are branches of expenditure for local governments. Provisions that allow people who can benefit from local government. However, the results of this study are large or small the total assets used by local governments in Indonesia cannot be accessed as a factor that influences the LGP.

The cause is the provincial government in Indonesia who are unable to utilize and manage assets that allow you to provide income to the local government (Nugroho & Prasetyo, 2018). Large amounts of assets are not sufficient to contribute to local government employees if not supported by good management by the local government.

The ability to manage assets is needed so that companies can provide maximum results for the government concerned. The results of a system that will be calculated for the performance carried out by the regional government.

#### 4.2.4 The Impact of RE on LGP

Hypothesis 4 in this study was rejected. The most dominant component of regional expenditure issued

by the provincial government in Indonesia is the expenditure of goods and services. Expenditures of goods and services carried out by the local government are aimed at improving services to the community which have an impact on improving the performance of local governments. However, in reality the regional governments that make greater expenditures on goods and services do not affect the performance of local governments (Nugroho & Prasetyo, 2018) and (Martini, et al., 2019).

It caused by limited local government financial capacity and high community demands for accountability for government performance require local governments to spend goods and services efficiently and effectively. Through the process of spending goods and services, local governments are required to avoid waste. The process of spending goods and services in local government institutions is more directed at accelerating absorption and the budget is measured based on the amount of realization of goods and services expenditure compared to the selection of types of goods or services needed by the local government. Often, these purchases are made so that the available funds can be disbursed, without considering whether the goods and services purchased can be useful in supporting the performance of local governments.

As a result, the amount of goods and services that are not so important can be excessive while other items that are needed are not sufficiently available. The Directorate General of Regional Financial Development states that goods and services spending is often carried out by local governments such as: motor vehicle maintenance, printing/copying, building/parking rental, vehicle rental mobility, heavy equipment rental, office equipment and equipment rental, food and drinks, clothing and official attributes, work clothes, special clothing and certain days, official travel, official travel, transfer of duties focused more on what is needed by the apparatus rather than the needs of the community (<http://keuda.kemendagri.go.id>, 2013).

#### **4.2.5 The Impact of RW, IR, RS, and RE on LGP**

RW, IR, RS, and RE have a significant effect on the performance of provincial government implementation of Indonesia. It is proven by the results of the study that the probability value (F-statistic) is 0.0000 where the probability value is smaller than the value of  $\alpha = 0.05$ .

Performance measurement is used to measure the accountability of public institutions in terms of use of resources, innovation, and public service quality (Globadian & Ashworth, 1994) in (Martini, Sari, & Wardhani, 2015) and (Setyaningrum & Martani, 2018). The result of this study in line with (Rustiyaningsih & Immanuela, 2014) which prove the size, LR, and regional expenditure have a simultaneous influence on the performance of local government. (Meilina & Hapsari, 2016) proved that a simultaneous influence between LR, regional spending and the level of government dependence on LGP.

This confirms that the provincial governments in Indonesia have been able to improve the performance of the implementation of local governments by fulfilling and managing regional wealth, the level of regional financial dependence, regional size, and regional expenditures owned effectively and efficiently. It is evident from the research results that there is a contribution of 72.62 percent that has been given from the independent variable to the dependent variable.

## **5 CONCLUSIONS**

Management of regional wealth, the level of regional financial dependence, regional size, and regional spending effectively and efficiently for the benefit of local governments to better and/or maximize development in order to improve service to the community will have an impact on the high performance of local governments that have been carried out. Provision of good services to the community in the operational activities of local governments can be one of the drivers of the high performance status of local government operations.

This study prove that wealth has a significant influence on the performance of the local government due to the large number of LR received has illustrated of the performance carried out by the local government in exploiting or extracting the region's original income.

This study revealed too intergovernmental revenue does not significantly influence the performance of regional government because the provincial go vernment in Indonesia is still dominated by general allocation funds from the central government so that the regional government does not play an active role in obtaining its income.

Regional size of the provincial government in Indonesia has no effect on the performance of the regional government because the amount of assets of the regional government is not a major factor in measuring the performance of the regional government but management of the asset management carried out by the local government. Regional expenditures made by the provincial government in Indonesia have no effect on the performance of local governments due to the realization of goods and services expenditures that are still dominant compared to capital expenditure or personnel expenditure which will have an impact on improving the performance of local governments for community services.

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