

## **Local Government Financial Performance: Good Governance, the Effectiveness Internal Control and Competence**

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**Abstract:** Good governance is an important foundation in creating transparency, accountability, and integrity in organizational management. This study aims to analyze how the principles of good governance, internal control and competence of the financial performance of the Bekasi City local government are moderated by internal control. This study uses a quantitative methodology with a sample of 41 respondents who are financial employees in the Bekasi City government with statistical testing using Smart PLS 3.0. The results of the study found that (1) good governance, internal control and competence have a positive effect on the financial performance of the local government. (2) Good governance contributes to creating transparency and accountability. (3) Internal control in good financial reporting can prevent deviations. In addition, this study also found that the competence of human resources in the financial sector plays an important role in effective budget management. This study provides recommendations that the importance of improving governance, internal control, and human resource competence as a strategic effort to improve the financial performance of the local government.

**Keywords:** Competence, Good Governance, Internal Control, Local Government Financial Performance

### **A. Introduction**

The public finance literature emphasizes the financial performance of local governments in developing countries (Kapidani, 2018). Public sector reforms are carried out by governments in various countries to encourage privatization of the public sector through increased financial autonomy (Thoa & Nhi, 2022). Local autonomy allows local governments to improve public services, improve responsiveness and efficiency, and strengthen their role in the economy and intergovernmental systems (Prabowo & Rafli, 2020). Sustainability, financial responsibility, and quality of public services will improve with local authorities, especially in terms of finance (Hartley et al., 2016).

**Table 1. Bekasi City Local Government Effectiveness Ratio**

Year	Effectiveness
2019	74,60%
2020	67,91%
2021	99,94%
2022	92,52%
2023	87,74%

Source: (SIKD Pemkot Bekasi, 2024)

The budget is made by the local government after the implementation of regional autonomy according to their capabilities and potential (Christia & Ispriyarso, 2019). As the fiscal year draws to a close, budget absorption is one of the topics that is often discussed. The budget absorption rate in this area is low. Table 1 shows that, based on the effectiveness ratio, from 2019 to 2023, it was classified as ineffective because the percentage was less than 100%. As the resulting performance realization was less than expected, the effectiveness level also dropped. As a result, the goals and performance targets of the local government of Bekasi City have not been achieved. After receiving a Fair with Exception (WDP) opinion from the Audit Board (BPK) on the Audit Report (LHP) of the 2022 Bekasi Regency Regional Government Financial Statements (LKPD), the performance of Bekasi Regent Dani Ramdan is increasingly becoming a concern. Soleman, Deputy Chairman of the Bekasi Regency DPRD, was disappointed with the opinion of the WDP from the BPK RI, which according to his assumption showed the poor performance of the Regent of Bekasi (Sadat, 2023).

A strategy to improve performance is good governance, according to (Zhang, 2019). This study shows that good governance is crucial for the government to regain public trust. In addition, good performance is crucial for local governments to regain public trust, which has declined due to the many cases of mismanagement related to local governments. According to (Said et al., 2016; Sevigo & Lathifah, 2024; Babinski et al., 2018), organizations must understand clean and authoritarian governance mechanisms along with public sector governance systems if they want to improve the performance of local governments. The high demands of the public for state administrators, both in the government, legislature, and judiciary, to run good government reflect the prominent problem in the management of public administration (Hartanto et al., 2021; Setyaningrum et al., 2017).

According to (Indriana & Nasrun, 2019) found that financial performance is influenced by good governance. This is different from the findings of other studies (Setyaningrum et al., 2017; Wardhani et al., 2017), which found that the performance evaluation indicators of local governments are still not appropriate to measure the quality of government. The ability to manage risks and organizational governance systems depends on internal control. It creates, enhances, and protects stakeholder value and guarantees the achievement of organizational goals (IFAC, 2012). If an organization wants to succeed and achieve its goals, the main problem is internal

control. Internal controls can be clarified as actions taken by organizations to increase the likelihood of actualization of their goals. According to a study that investigated the relationship between performance and internal control systems (Waromi et al., 2024), some parts of the control system were not implemented properly. Internal control helps the utilization of resources and helps management achieve the company's goals, according to other researchers (Koeswayo et al., 2024); (Knechel & Vanstraelen, 2007); (Mattoasi et al., 2021) investigated the relationship between internal control elements and local government financial performance, which has a positive impact.

Competence refers to the expertise or knowledge demonstrated by professionalism in a particular domain. This ability is considered the most significant or superior in the domain (Augustine, 2009). Ability refers to an individual's capacity to excel at work, which includes the application of skills and knowledge in new contexts to optimize improving mutually recognized excellence. Another study shows that competence does not affect the performance of local government (Rosnidah et al., 2022). Based on this background, a formulation of the problem can be submitted, namely: (1) Does good governance affect the financial performance of local governments? (2) Does internal control affect the financial performance of local governments? (3) Does competence affect the financial performance of local governments?.

This study has several important benefits, both theoretical and practical: (1) This study helps the development of research on the relationship between good governance, internal control, and competence and local government financial performance. It is important to improve academic understanding of how good governance principles and functioning internal control systems can improve the financial performance of the public sector. (2) This research can help local governments, especially the City of Bekasi, improve their financial performance by applying the principles of good governance, better internal control, and improving the capabilities of employees. Other local governments can also use these findings as a reference to improve their financial management performance. (3) This study can also be useful as a basis for formulating policies related to improving the financial performance of local governments. By understanding the influencing factors, policymakers can design effective strategies to maximize governance and efficient use of local budgets.

## **B. Methods**

This study uses a quantitative methodology rooted in positivist philosophy. This method is used to test a certain population or sample, supported by the use of research instruments for data collection, which is then processed quantitatively and statistically to evaluate the hypothesis that has been determined. According to positivism theory, reality, symptoms, and phenomena can be categorized as causal, relatively permanent, concrete, observable, and measurable (Sugiyono, 2017). The questionnaire survey was distributed to financial employees of the Bekasi city local

government. The data collection method is through an online questionnaire sent via email. The questionnaire uses a measurement interval scale to collect data. The instrument of each variable is measured using five (5) Likert scale points as below: 1 - Strongly disagree 2 - Disagree 3 - Neutral 4 - Agree 5 - Strongly agree.

The population and sample in this study are several employees (heads and staff) of the finance department in the local government of Bekasi city. The number of samples used was 41 local government employees. As explained (Sugiyono, 2017), the appropriate sample size in this study, which is 30 to 500, then the number of samples can still be used.

Variables in this study include: (1) Good Government Governance is the safeguarding of reciprocal relationships between organizational elements formed by the government, which is aimed at achieving policy objectives efficiently and effectively, as well as communicating openly and providing accountability to stakeholders (Pelu et al., 2023). The Questionnaire on the Application of Good Government Governance Principles includes 20 questions adopted from the research (Wardhani et al., 2017). The application of Good Government Governance principles is developed from indicator items: transparency, independence, accountability, accountability, and fairness, measured on a likert scale of 1-5 (strongly disagree - strongly agree). (2) Internal Control: Government Regulation of the Republic of Indonesia No. 60 of 2008 concerning the Government Internal Control System (SPIP) conveys that SPIP is a comprehensive process of actions and activities that are carried out continuously by the leadership and all central and regional government apparatus. The goal is to provide adequate certainty regarding the achievement of organizational goals through effective and efficient operations, reliability of financial reporting, security of state assets, and compliance with laws and regulations. The Internal Control Questionnaire obtained from the study (Reding et al., 2013) included 25 questions, which the researcher measured using a likert scale of 1 to 5 (strongly disagree - strongly agree). (3) Human resource competence refers to the ability of employees to carry out their responsibilities, thus requiring growth to obtain satisfactory performance. The human resource competency indicator as presented (Rosnidah et al., 2022), has four items that are assessed on a Likert scale of 1-5 (strongly disagree to strongly agree). (4) The financial performance of local governments is determined by the extent to which government apparatus achieves organizational goals and objectives so as to indicate the success or failure of the implementation of activities. The performance proxy concerned is managerial performance, which is assessed through the instruments used in the study (Carmeli, 2002) including nine indicator items: planning, coordination, evaluation, supervision, staffing, negotiation, representation, and investigation, which is assessed using a likert scale of 1-5 (strongly disagree - strongly agree).

This study uses the structural-partial least square equation (SEM-PLS) model by utilizing SmartPLS for data analysis. Structural equation modeling (SEM) is divided

into two types: covariance-based SEM (CB-SEM) and variance-based SEM, which is often referred to as the partial least squared (SEM-PLS). CB-SEM originated as software as a result of Lisrel's development in the 1970s, although SEM-PLS was later developed and designed by Herman Will, Karl Joreskog's academic mentor (Sugiyono, 2017).

SEM-PLS operates effectively when using limited sample sizes and complex models. The assumption of data distribution in SEM-PLS tends to be looser than CB-SEM. CB-SEM estimation requires adherence to certain assumptions, including multivariate data normality, minimum sample size, and homoscedasticity. The estimation findings of the two methods are similar, which shows that SEM-PLS can function as an effective proxy for CB-SEM. SEM-PLS is able to obtain estimates despite the limited number of samples and the assumption of distorted multivariate normality (Sugiyono, 2017).

SEM-PLS can thus be considered a nonparametric methodology for CB-SEM. Furthermore, when it is not able to meet the CB-SEM assumptions, SEM-PLS can serve as a suitable approach for theoretical testing. If the data meets the CB-SEM assumptions, including the minimum sample size and is normally distributed, CB-SEM is chosen. If it is inadequate, you can choose SEM-PLS. SEM-PLS is a nonparametric methodology that works effectively even with abnormal data (Sugiyono, 2017).

Convergent validity is a component of the measurement model or external model in SEM-PLS and as a confirmatory factor analysis (CFA) in a covariance-based SEM. There are two conditions in evaluating whether the outer model (measurement model) meets the convergent validity requirements for reflective construction: (1) the loading must exceed 0.7, and (2) the p-value must be significant ( $<0.05$ ). However, under certain conditions, the requirements for loading more than 0.7 are often not met, especially for newly conducted surveys. As a result, a loading that ranges from 0.40 to 0.70 is considered acceptable.

Loading indicators less than 0.40 need to be removed from the model. However, for indicators with loading ranging from 0.40 to 0.70, it is important to evaluate the effect of the decision to remove these indicators on the average extracted variance (AVE) and composite reliability. Indicators with a load between 0.40 and 0.70 can be eliminated if their removal maximizes the average extracted variance (AVE) and composite reliability exceeds the respective thresholds. The threshold for AVE is 0.50, while the reliability of the composite is 0.70. Another factor to consider in eliminating indicators is their effect on the validity of the construct content. Indicators with minimal loading are sometimes maintained due to their contribution to building content authenticity (Hair et al., 2020).

Influence Significance Test (Bootstrapping) (Hypothesis Test) (Inner Model) (Hair et al., 2020) showed that the evaluation of the structural model (inner model) can be done

by testing the r-square value that connects the latent variable construct. This test intends to find out the extent to which the independent variable model is able to explain the bound variable. The r-square value assesses the degree of variation of the bound variable resulting from the change of the independent variable. A higher R<sup>2</sup> indicates a superior prediction model within the recommended research framework. The limiting parameters of the R<sup>2</sup> value are categorized into three classifications, namely 0.67 (substantial), 0.33 (moderate), and 0.19 (weak). This study utilizes an adjusted R-Square value (R<sup>2</sup>) due to the existence of several independent variables (Hair et al., 2020). The last stage is to test the hypothesis with the SmartPLS application by analyzing the bootstrapping findings. Testing is carried out by accessing the compute menu, followed by selecting the bootstrapping option, which will then display the desired data.

### *Hypothesis Development*

#### H1: Good Governance Affects the Financial Performance of Local Governments

In order to meet the objectives of establishing a public sector organization, effective management seeks to apply the principles of private sector management into public sector operations. Key characteristics of public sector management include transparency and diligence in the execution of duties, as well as a strong dedication to integrity, ethical standards, and legal compliance. The main goal of good governance is to ensure that public sector organizations consistently operate for the benefit of society (Indriana & Nasrun, 2019). Studies (Maimanah & Nurdiono, 2024) show that effective governance runs efficiently. This makes it clear that the concept of effective governance, including participation, transparency, and accountability, has been successfully implemented. Improving good governance is positively correlated with maximizing local government financial performance.

#### H2: Internal Control Affects the Financial Performance of Local Governments

An active action called internal control allows for remediation if something goes wrong with plan occurs. It is used to increase productivity and efficiency, prevent assets from being lost, improve the accuracy and reliability of financial statements, and ensure everyone complies with laws and regulations (Triono & Dewi, 2020). Through the findings of (Mattoasi et al., 2021), it was found that the government's internal control system is very helpful for the financial performance of local governments.

#### H3: Competence Affects Local Government Financial Performance

According to (Sukarno et al., 2020) apparatus competence is the ability to complete tasks that are based on knowledge and skills and supported by the work behavior and attitude required by the task. There are three indicators of competence: knowledge,

skills, and behavior (Sukarno et al., 2020). Apparatus competence and local government financial performance are positively correlated, according to behavioral indicators. Only one of the four variable indicators of apparatus competence at the beginning of the test, behavioral indicators, reached the value of external load; Other indicators, knowledge, abilities and skills, achieve values under external loads. Behavior is a term that refers to the way government officials carry out their duties and responsibilities.

### **C. Results and Discussion**

The results of the research were obtained through primary data processing, namely the distribution of questionnaires in Bekasi City. The questionnaire that the researcher processed in this study amounted to 41 questionnaires. The research variables used amounted to four variables: good governance variables, internal control, competence, and government financial performance variables. The number of indicators in this study is 58 indicators.

#### **Description of The Research Respondents**

Respondents Based on Gender: In the Bekasi City Regional Apparatus Organization, male respondents amounted to 21 people (51.22%), while female respondents amounted to 20 people (48.78%). Respondents Based on Education Level: The diversity of education of respondents to the Bekasi City Regional Apparatus Organization included seventeen people with accounting majors of 41.46%, 22 people with management majors representing 51.66%, and 22 people with law majors. Two respondents, namely 4.88%. Respondents Based on Position: The Bekasi City Regional Apparatus Organization amounted to 6 respondents with the position of head of accounting amounting to 14.63%; 14 respondents held senior accounting positions, representing 34.15%; and 21 respondents in junior accounting positions, accounting for 51.22%.

#### **Evaluation of the Outer Model (Measurement Model): Validity and Reliability Test**

The outside loading validity test in Figure 1 shows that if the total outer loading value exceeds 0.7, it shows that it meets the validity criteria based on the outer loading value. Next, a validity test was carried out based on the average variance extract (AVE) value. Recommends an AVE value exceeding 0.5. All AVE values exceeded 0.5, indicating that they met the validity criteria based on the AVE. Furthermore, a reliability test was conducted based on the composite reliability (CR) value. Table 2 illustrates the reliability test based on composite reliability (CR), where the recommended CR value is more than 0.7. All CR values are known to exceed 0.7, which indicates compliance with reliability standards based on cronbach's alpha (CR). Next, a reliability test is carried out using the CA value.

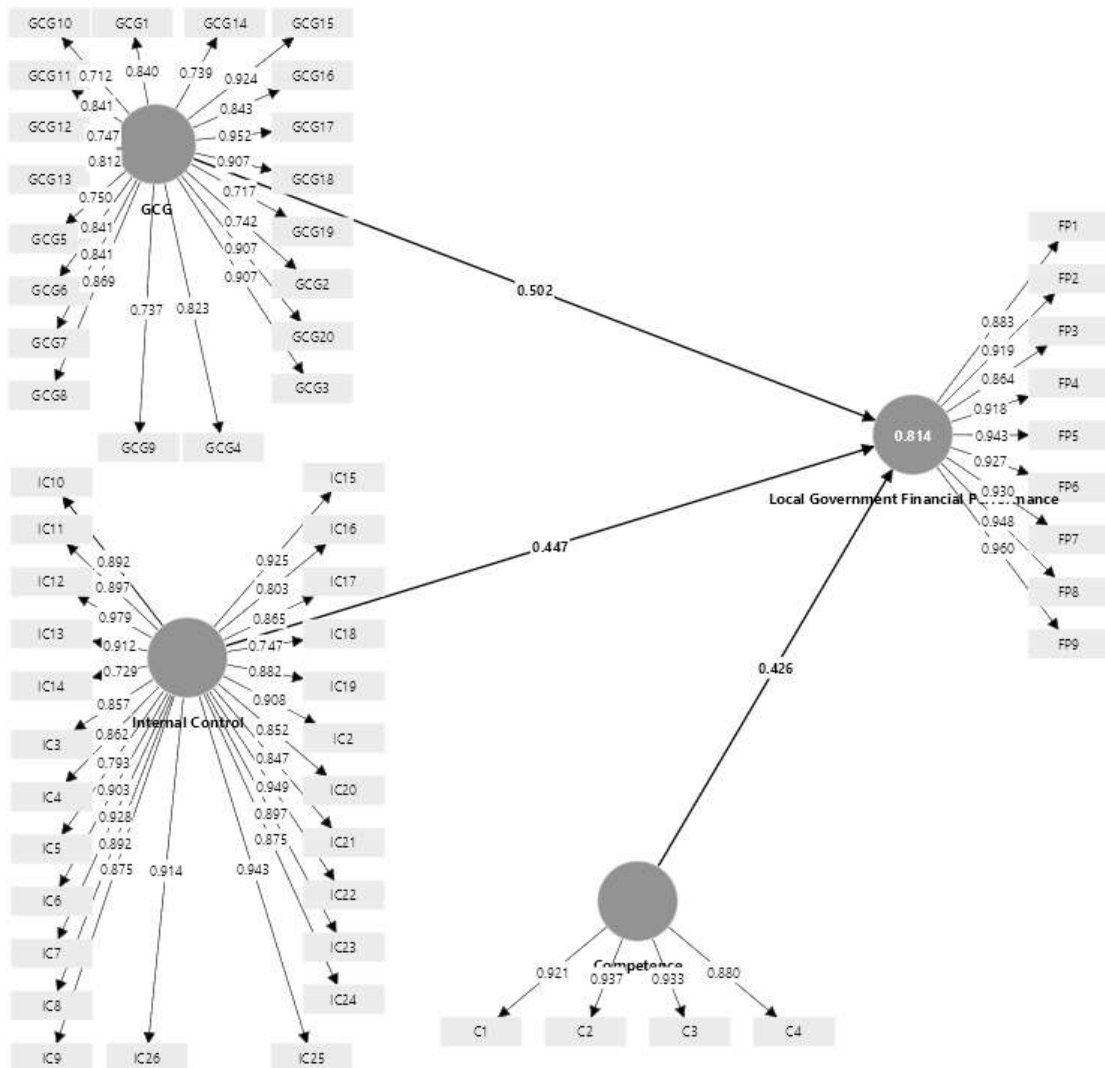


Figure 1. Validity Test

Table 2. Reliability test as per Cronbach's Alpha (CA)

	Cronbach's alpha
Competence	0,939
GCG	0,975
Internal Control	0,988
Local Government Financial Performance	0,978

**Influence Significance Test (Bootstrapping) (Hypothesis Test) (Inner Model)**

Table 3. Path Coefficient Test & Significance of Influence

	Original sample (O)	Sample mean (M)	Standard deviation (STDEV)	T statistics ( O/STDEV )	P values
Good Governance	0,349	0,335	0,138	2526,000	0.012
Internal Control	0,310	0,272	0,138	2241,000	0.025
Competence	0,296	0,272	0,137	2170,000	0.030



Based on the above results, the findings were obtained: (1) Good governance positively affects local government financial performance, with coefficient values (original sample column) = 0.502, and significant, with T-Statistics = 2.526 > 1.96 and p-values = 0.012 < 0.05 (accepting hypothesis). (2) Internal control positively affected local government financial performance, with coefficient values (original sample column) = 0.447, and significant, with t-statistics = 2,241 > 1.96 and P-values = 0.025 < 0.05 (accepting hypothesis). (3) Competence positively affected local government financial performance, with coefficient values (original sample column) = 0.426, and significant, with t-statistics = 2,170 > 1.96 and p-values = 0.030 < 0.05 (accepting hypothesis).

### **Good Governance Affects the Financial Performance of Local Governments**

The regression analysis carried out in this study shows that effective governance significantly improves the financial performance of local governments. The principles of good governance have a significant impact on the performance of government employees. As a result, the response to effective governance has increased rapidly, and government employees have shown great concern about this. The implementation of good governance aims to improve the financial performance of local governments. According to the findings of a study (Indriana & Nasrun, 2019), the independent variable of good governance separately has a considerable positive influence on the financial performance of local governments.

### **Internal Control Affects the Financial Performance of Local Governments**

The regression analysis carried out in this study shows that internal control substantially maximizes the financial performance of local governments. Internal control is a proactive action that can carry out corrective actions in reaction to non-conformities. These internal controls are established to reduce deviations from the plan, increase efficiency and effectiveness, prevent asset loss, improve the reliability and accuracy of financial reporting, and encourage compliance with laws and regulations to achieve the goals that have been set. This is expected to affect the financial performance of the Bekasi City Regional Government. According to a study (Mattoasi et al., 2021), the government's internal control mechanism significantly improves local government performance.

Internal control functions as a proactive monitoring mechanism to ensure that every organizational activity runs according to plan. With quick corrective action on non-conformities, internal control can prevent deviations that can harm the organization, such as errors in financial reporting, budget waste, or even fraud. Thus, internal control is an important element in improving the quality of local government financial management. Good internal control supports efficiency and effectiveness in the use of financial resources. For example, through budget monitoring and supervision of program implementation, local governments can ensure that the budget is used

optimally according to predetermined priorities. In the Bekasi City Local Government, the implementation of internal control can reduce inefficiency and increase productivity in financial management.

One of the main objectives of internal control is to improve confidentiality and financial reporting. Local governments with a strong internal control system are able to present transparent and reliable financial reports. In addition, internal control ensures compliance with laws and regulations, which is important to maintain legitimacy and public trust. The Bekasi City Local Government needs to strengthen its internal control system by ensuring that each component of the system (environmental control, risk assessment, control activities, information and communication, and monitoring) is implemented thoroughly. This includes training employees to understand the importance of internal control, developing technology to support financial oversight, and enforcing an independent audit system. Internal control serves to prevent asset losses and budget irregularities, which are often challenges in government financial management. With internal control, these risks can be minimized through strict monitoring procedures, periodic evaluations, and follow-up on audit findings. The implementation of good internal control not only impacts financial performance but also increases public accountability. The public tends to have greater trust in a government that is able to demonstrate transparent and responsible financial management.

### **Competence Affects the Financial Performance of Local Governments**

The regression analysis carried out in this study makes it clear that competence significantly improves the financial performance of local governments. Competence is related to the ability or talent of employees to carry out their work obligations or responsibilities. Optimal competence is shown by abilities and knowledge based on work attitudes and their application in carrying out duties and responsibilities in the workplace, in accordance with predetermined work standards. In the Bekasi Regional Government, the workforce has qualifications that are relevant to their job descriptions so as to maximize their competence and skills. They are assigned according to their expertise, by guaranteeing the principle of “the right man in the right place” that facilitates optimal performance in achieving organizational goals. This group is responsible for improving the financial performance of the Bekasi City Regional Government. According to the findings of a study (Rosnidah et al., 2022), the competence of government employees significantly improves local government performance.

The results of this study emphasize that employee competence has a significant influence on the financial performance of local governments. Competence, which includes employee abilities, knowledge, and work attitudes, is an important element in supporting the achievement of organizational goals, especially in the context of the Bandung City Regional Government. (1) Employee competence is not only related to

technical abilities, but also includes knowledge and work attitudes that are applied in accordance with established standards. This shows that improving the financial performance of local governments is greatly influenced by the ability of employees to carry out their duties effectively and efficiently. Optimal competence allows employees to make the right decisions, increase budget efficiency, and maximize the use of resources. (2) Placing employees according to their expertise and qualifications is an effective strategy to improve organizational performance. In the context of the Bandung City Regional Government, the application of this principle ensures that employees work in positions that match their competence, which in turn makes it easier for them to make maximum contributions to regional financial performance. This also shows the importance of strategic human resource management in public organizations. (3) Good employee competence also contributes to increased accountability and transparency in financial management. Competent employees tend to have a better understanding of financial rules and regulations, thus being able to avoid errors or irregularities in financial reporting. This is important to build public trust in local government.

#### **D. Conclusion**

According to the results of the analysis and discussion, it can be concluded that good governance, internal control and competence positively affect the financial performance of the local government of Bekasi city. Good governance, which includes the principles of transparency, accountability, and participation, plays an important role in strengthening financial performance. A good internal control system allows local governments to maintain financial administration, ensure that every transaction is recorded accurately, and prevent possible errors. The competence of human resources who have relevant knowledge, skills, and expertise is a very important element in maintaining and improving the financial performance of local governments. Subsequent researchers are encouraged to use larger samples with greater diversity of characteristics from different local governments and to extend the duration of the study. In this study, 3 variables are used, other independent variables must be added in the next research that also affects financial performance.

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