

Analysis of Correlation between Levels of Local Government Compliance with Legislation and Opinion on Local Government Financial Statements

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Abstract

This study aims to analyze the correlation between the level of local government compliance with laws/regulations and opinions on the Local Government Financial Statements (LGFS) and identify the causes of failure in detecting non-compliance, including non-compliance that contains elements of fraud, in LGFS audit. The method used is explanatory sequential mixed methods with a content analysis approach on 54 LGFS samples and interviews with the Audit Board of Indonesia (Badan Pemeriksa Keuangan/BPK) auditors. The results showed that there was indeed a correlation between the level of compliance of the local government and the opinion on the LGFS, but there was a risk of detection failure and the risk of errors in opinion caused by different concepts in determining fraud, differences in the concept of materiality among BPK auditors, failure to update programs audit, potential threats/dangers experienced by the auditors, and failure to reduce the auditors' negative perception of work protection. The limitation of this study was that the interview sample only involved auditors from three representative offices originating from Java and did not conduct confirmation to the unit responsible for the preparation of guidelines/guidelines for the audit and units that deal with legal issues. This research implied that BPK must increase the effectiveness of audit quality assurance to improve audit quality and BPK auditors should be able to apply the principle of due professional care in carrying out the LGFS audit so that audit quality is maintained. This study also considers materiality in analyzing the findings of non-compliance and attempts to identify the factors causing the correlation.

Keywords: Public Sector Audit, The Audit Board of Indonesia, BPK, Supreme Audit, Compliance

1. INTRODUCTION

To realize the successful implementation of state governance, state finance must be managed in an orderly manner, complying with laws and regulations, efficient, economical, effective, transparent and responsible. Therefore, each local head (governor/mayor) is required to submit accountability for the management of the state finances (APBN/APBD) to the House of Representatives (DPR/DPRD) in the form of financial reports that have been audited by the Supreme Audit Board (The Audit Board of Indonesia/BPK) no later than six months after the fiscal year ends (Republic of Indonesia, 2003). Accordingly, BPK must conduct an audit of the management of state finances as also mandated by the Law of the Republic of Indonesia Number 15 of 2004 concerning the Inspection of Management and Responsibility of State Finances. One of the most anticipated results of BPK audits is the opinion on government financial reports.

However, in the last two years, BPK has been in the public spotlight. The reason is, there are several numbers of local heads who are entangled in legal problems due to violations of the laws and regulations even though the financial statements of the local government that they lead get an unqualified opinion (WTP) from BPK. Some of them have even been named as suspects of corruption. Indonesia Corruption Watch (ICW) states that ten local heads are suspected of corruption after the local government's financial reports were rewarded by the WTP opinion by BPK.

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Then, does the opinion given by BPK not reflect the level of compliance of the local government with the applicable legislation? Moermahadi Soerja Djanegara, as chairman of BPK, stated that the WTP's opinion did not guarantee that the entity in question did not have corruption because the audit of financial statements was not specifically aimed at detecting corruption. However, BPK is obliged to disclose if there is non-compliance or disobedience whether it influences the opinion on the financial statements or not.

However, the statement is not entirely correct. The State Financial Audit Standard (SPKN) regulates that the auditors must design an audit to provide adequate assurance to detect non-compliance with the provisions of the legislation and other legal products that have a direct and material effect on the main points/information on the subject matter being audited. The auditors must also identify risk factors for fraud and assess the risk of non-compliance with statutory provisions caused by fraud. This risk must be considered a significant risk. If there is a risk of non-compliance with statutory provisions indicating fraud that significantly affects the subject matter/information on the subject matter audited, the auditors must modify the procedure to identify the occurrence of fraud and/or non-compliance, and determine its impact on the subject matter/information on the subject matter checked (BPK, 2017).

Thus, the opinion given by BPK on the financial statements of local governments should be able to reflect the level of compliance of the local government with the legislation. Therefore, the authors are interested in researching the correlation between the level of compliance of the local government with the legislation and the opinions given by BPK. The author hopes that this research can contribute to the auditors and users of the audit report related to the process of determining opinion in the audit of local government financial statements, particularly related to the level of compliance with state financial management with laws and regulations.

2. LITERATURE REVIEW

In the process of auditing state finances, there are three parties involved, namely the auditors of state finances, those responsible, and users of audit reports (BPK, 2017). Each party in the organization is filled with people whose duties and responsibilities are clearly defined, usually in written form (Siegel and Marconi, 1989). In the case of an audit of state finances, the roles and responsibilities of each party are briefly described as follows (BPK, 2017):

- a. State financial auditors
BPK is a state institution that the duty and authority of which are to audit the management and responsibilities of state finances.
- b. Responsible party
The responsible party is the audited party consisting of the president, ministers, and local heads. This party is responsible for information on the subject matter, managing the subject matter, and following up on the results of the audit. The main things are the audited things and/or those that are of concern in an audit assignment, which can be in a form of information, conditions, or activities able to be measured/evaluated based on certain criteria.
- c. Audit results report users
Users of audit reports (LHP) are representative institutions, the government, and other parties who have an interest in the LHP.

In this study, the researchers focus the discussion on the first party, namely the state financial auditors. In his book, Siegel and Marconi (1989) and Supriyono (2015) define roles as someone's part that is played in their interactions with others. Furthermore, both of them also define social roles as rights, duties, obligations, and proper behavior of people who hold certain positions in particular social contexts. In official organizations, such as BPK, this role is defined explicitly in the form of guidelines or regulations.

The actual behavioral component of the role is called the norm. Norms are expected and needed behaviors that are appropriate for specific roles (Siegel and Marconi, 1989). For example, the auditors are expected to carry out his audit duties properly, following the standards and ethics set for him. Based on role theory, an auditor can be seen as a status or profession in the social system (Oseni and Ehimi, 2012). Since they are in a position in a profession, the auditors must comply with a resolution or decision made by the public to them. Failure in carrying out the provision of social roles cannot be tolerated. Sanctions or penalties can be imposed on people who violate these provisions (Siegel and Marconi, 1989; Davidson, 1975, in Oseni and Ehimi, 2012).

In Indonesia, the public has set a set of standards, in the form of Public Accountant Professional Standards (SPAP) which contain audit standards (SA), which must be obeyed by auditors in carrying out audits. In the context of auditing state finances, BPK has set SPKN as a standard and guideline that must be adhered to. Based on SPKN,

BPK must carry out its main duties, functions, and authorities economically, efficiently and effectively based on statutory regulations. Furthermore, each BPK member and state financial audit must maintain the dignity, honor, image, and credibility of BPK in carrying out its duties (BPK, 2017).

To realize this, besides being independent and having integrity, BPK must also be professional in carrying out audits. The SPKN defines professionalism as an ability, expertise, and professional commitment in carrying out tasks accompanied by due care, thoroughness, and carefulness, and is guided by the standards and provisions of legislation (BPK, 2017). The same thing is also regulated in SPAP (SA 200); competence and professional precision are two of the basic principles in terms of code of ethics and must be obeyed by auditors. In addition, auditors must also use professional judgment in planning and carrying out audits of financial statements.

Thus, it becomes clear that in the social order of society, a state financial auditor has a social role in a profession and must obey the norms set for him. These norms are specified in SPAP (general) and SPKN (specifically). Both regulate specifically that the auditors, in carrying out the planning and implementation of the audit, must act professionally, by exerting all efforts carefully (due care), thorough, and careful, and based on the rules and standards set.

This intends to make the audit and its results as outlined in the audit report have high quality, including the quality of the opinion given. The high quality of audit is certainly expected in the midst of the government's efforts and general objectives of BPK in creating a clean and free government from corruption, collusion and nepotism (BPK, 2017). Conversely, the failure of the auditors in obeying the norm can result in the low quality of the audit report which means that the state's objectives and BPK, in general, cannot be achieved.

The SPKN regulates that auditors must design audits to provide sufficient confidence to detect non-compliance with statutory provisions and other legal products that have a direct and material effect on the subject matter/information of the subject matter audited. The auditors must also identify fraud risk factors and assess the risk of non-compliance with statutory provisions caused by fraud. These risks must be considered as significant risks. If there is a risk of non-compliance with statutory provisions indicating fraud that significantly affects the subject matter/information on the subject matter audited, the auditors must modify the procedure to identify the occurrence of fraud and/or non-compliance, and determine its impact on the subject matter/information on the subject matter checked (BPK, 2017). Thus, the opinion given by BPK on the financial statements of local governments should be able to reflect the level of compliance of the local government against the legislation.

Several researchers had conducted studies on this issue, although they did not specifically study the correlation between compliance levels and BPK opinion. Studies conducted by Safitri and Darsono (2015) and Widodo and Sudarno (2017) show that the findings of non-compliance with laws and regulations significantly influence audit opinion. The direction of the correlation is negative, which means that the more the number of findings on non-compliance with laws and regulations, the less the probability of giving a WTP opinion by BPK RI auditors to the local government financial statements. Also, Ningsih (2015) in her research found that accounts that are often excluded in BPK's opinion are mainly caused by a weak internal control system, non-compliance with laws and regulations, and inefficiency and ineffectiveness. Unfortunately, the studies that have been carried out still ignore the concept of materiality value findings and only focus on the frequency of occurrence. Ignorance in the concept of materiality can be fatal because materiality is a very important factor in the formulation of opinion.

2.1 Hypothesis

Based on role theory, the auditors must carry out the audit task by applying the principle of due professional care. Thus, the audit must be carried out following the audit standards and established codes of ethics so that the results of the audit report produced are expected to have high quality, including the opinions given. The failure of the auditors in carrying out this matter can mean the failure of the audit process carried out. The logical consequence is that the audit results are of low quality.

One of the criteria set out, both by law and audit standards, is that the opinion given must consider the problem of local government compliance with laws and regulations. Thus, the auditors should plan and design an audit program to be able to detect non-compliance, whether it is caused by fraud or errors. WTP opinion should not be given to LGFS which still contains material misstatements originating from the non-compliance of the local government with the laws and regulations. The higher the level of local government non-compliance with laws and regulations (which is reflected by the findings of non-compliance in the audit report), the lower the opinion obtained by LGFS.

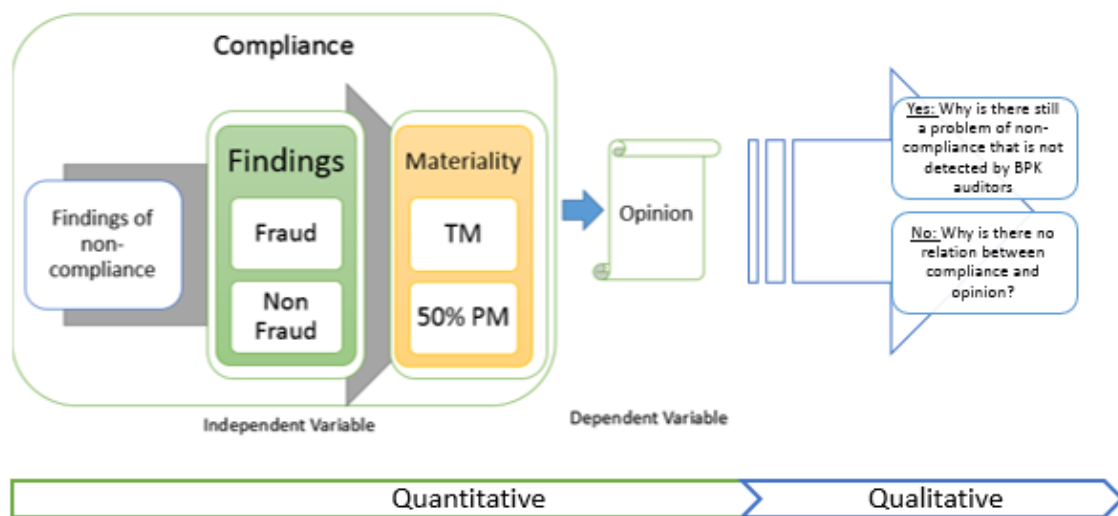
Therefore, based on the previous description, the researcher proposes an alternative research hypothesis as follows:

Ha: BPK auditors considers the findings of the local government's non-compliance with laws and regulations in the process of determining opinion on the local government's financial statements

3. RESEARCH METHOD

In accordance with the research design in figure 1, the research model that is used by the researcher is explanatory sequential mixed methods. Explanatory sequential mixed methods are the methods used by researchers to first conduct quantitative research, analyze the results, and then arrange the results to explain them in more detail with qualitative research (Creswell, 2014). Figure 1 also shows that the researcher wants to explain the results of quantitative testing with qualitative data. Quantitative analysis techniques are used to analyze the correlation between the level of compliance with the opinions given by BPK on the financial statements of local governments. Furthermore, such techniques are used to elaborate furtherly on the factors causing the correlation.

Figure 1 Research Design



3.1 Operational Definition of Variables

Figure 1 shows that there are two variables used, namely the level of compliance and BPK opinion. In detail, the definitions of the two variables are as follows:

a. Compliance Level

The level of compliance is reflected by the findings of non-compliance found in the BPK audit report. In accordance with the nature of the materiality, the types of non-compliance findings are divided into two groups, namely findings that indicate fraud and non-fraud. Types of fraud findings have a materiality score of tolerable misstatement (TM) accounts while non-fraud type findings have a materiality score of 50% planning materiality (PM). This means that if there is a misstatement on an account whose value exceeds the materiality score, the misstatement is declared subject to material misstatement (BPK, 2016). In addition, the auditors also consider the impact of pervasiveness. A misstatement is stated to have a pervasiveness effect if the misstatement can affect the financial statements as a whole.

In the process of determining materiality for the compliance variable, researchers use the following assumptions:

- 1) Materiality is only determined quantitatively and does not take into account qualitative factors. This is caused by each local government's different characteristics so that the qualitative factors possessed vary greatly.
- 2) Pervasiveness is determined by quantitative measures, i.e. misstatements are stated to have a pervasiveness effect if the value of misstatement exceeds PM.
- 3) In addition, regarding the determination of the types of fraud and non-fraud findings, the types of fraud findings are determined by using criteria developed by researchers based on SPKN, the criminal law code of Indonesia (KUHP), and ACFE. This is done because BPK does not have certain guidelines/criteria to determine whether a problem falls into the category of fraud or not. In detail, fraud criteria developed by researchers can be seen in Table 1.

Based on the description above, the researcher provides the code for materiality using the ordinal scale as can be seen in table 2.

b. **BPK Opinion**

There are four types of opinions that BPK can give to the LGFS, namely unqualified opinion (WTP), qualified opinion (WDP), adverse opinion (TW), and disclaimer of opinion (TMP). Therefore the researcher gives the code to the opinion on an ordinal scale starting from the highest to the lowest which can be seen in Table 2.

Table 1. Criteria for Determining the Type of Fraud TP

No	Fraud Criteria	Criteria Source
1	Against laws/regulations	SPKN, KUHP, and ACFE
2	Take/defraud goods/money	
3	Benefit individual/ group	
4	Harm other people/local government	
5	Deliberately carried out (there is an attempt to fake/hide evidence/document of transaction)	

Table 2. Code of Materiality and Opinion in the Ordinal Scale

Materiality	No Material	Material but not Pervasive	Material and Pervasive Misstatement	Material and Pervasive Limitation of Scope
Code	1	2	3	4
Opinion	WTP	WDP	TW	TMP

3.2 Population and Samples

In the sample selection process, the researcher uses the assumption that the audit quality of all representative BPKs is the same. By using purposive sampling, 54 LGFSs samples are selected with 18 LGFSs obtained WTP opinion, 18 WDP, and 18 TMP. In addition, to elaborate the results of quantitative research, interviews were also carried out on 10 BPK auditors from three representative offices, namely BPK Representatives of Central Java, Yogyakarta and East Java Provinces, with qualifications for the role of audit as team leader (KT), supervisor (PT), and the auditor in charge (PJ).

3.3 Data Analysis Technique

Creswell (2014) states that in sequential mixed methods explanatory research models, researchers conduct quantitative research, analyze the results, and then compile the results to explain them in more detail with qualitative research.

4. RESEARCH RESULTS AND DISCUSSION

4.1 Correlation between Compliance Level and LGFS Opinion

Table 3 provides some information, such as the value of N or the total number of observations on each variable which is 54 LGFS in the 2017 testing period. In detail, the explanation for table 3 is described as follows:

- 1) Opinion code 1 (WTP) should only contain compliance level code 1. However, compliance level code 1 does not always occur in FSLGs showing opinion code 1, as seen in 18 FSLGs being observed. There were 16 LGFSs that had a level of compliance 1 and there were 2 LGFSs that had a level of compliance code 2. The results of further search for these conditions indicate that an anomaly occurred in South Halmahera Regency and Kerinci Regency with the following explanation.
- 2) South Halmahera Regency. There was a fraud problem in the Grant Shopping account amounting to Rp1,887,000,000 (TM Rp408,089,927.89) and Unexpected Expenditures Rp166,266,500 (TM Rp34,144,696.98) so they obtain a materiality score of 2 (PM Rp62,344,535,777.70).
- 3) Kerinci Regency. There was a fraud problem in the Local Retribution Income account of Rp318,500,000 (TM Rp78,047,728.96) so they obtain a materiality score of 2 (PM Rp58,815,905,672.92).

Table 3. Descriptive Statistics of Variables Level of Compliance and Opinion

	Opinion Code				Total
	1	2	3	4	
Compliance Test	1	16	8	0	24
	2	2	8	0	18
	3	0	0	0	0
	4	0	2	0	12
Total	18	18	0	18	54

- a. Code of opinion 2 (WDP) should contain the compliance level code 2. However, from 18 LGFSs, there were only 8 LGFSs that had a level of compliance 2. The remaining 8 LGFSs had a level of compliance 1 and 2 LGFSs had a level of compliance 4. The conditions could be explained as follows:
 - 1) 8 LGFSs that have compliance code 1 may experience exceptions to the internal control system.
 - 2) 2 LGFSs that have compliance code 4 are Batu Bara Regency and Karo Regency.
 - a) In Batu Bara Regency there was a dispute over PT Inalum's Unfinished Local Tax - LRA (Road Lighting Tax) amounting to Rp205,172,961,203.9 (PM Rp38,928,211,722.78) so they obtain a materiality score 4. The value has been recorded in the Balance Sheet as of December 31, 2017, in the Local Tax Receivable account. Also, there were fraud problems (lack of volume) in the Road, Irrigation and Network Capital Expenditure account worth Rp3,191,740,431.79 (TM Rp1,914,951,963.08) so they obtain a materiality score of 2. Both of these problems have been considered as exceptions in the giving opinion (some which lacked volume in the capital expenditure account have not been restored).
 - b) In Karo Regency, there were audit findings on the Goods and Services Expenditure account worth Rp75,751,883,538 (PM Rp.15,208,267,591.18) so they obtain a materiality score of 4. The findings were administrative in the form of realization of expenditures on activities that had not been budgeted before. In addition, there was fraud on the Equipment and Machine Capital Expenditures account worth Rp5,603,472,955 (TM Rp.224,739,303.79), Road Capital, Irrigation and Network Capital Expenditures worth Rp3,154,267,860.21 (TM Rp1,096,231,467.68), and Cash in the Expenditure Treasurer valued at Rp. 189,930,300 (TM Rp. 751,623.16) so they obtain a materiality score 2. Findings on the Cash account in the Treasurer Expenditure have become one of the exceptions in opinion.
- b. The opinion code 3 (TW) does not have a sample item because no LGFS has TW opinion in 2017.
- c. Opinion code 4 (TMP) has 8 LGFSs that have a compliance score of 2 and 10 LGFSs that have a compliance score of 4. 8 LGFSs that have a compliance code 2 are likely to experience exceptions to the internal control system.

Hypothesis testing in this study used Somers' D correlation test and Kendal Tau C. Testing was done using IBM SPSS Statistics application tools 25. Somers' D test results showed that the correlation between the variable level of compliance and opinion had a value of 0.696 with a significance level of 0,000 (p-value <0.0005). Based on the direction of the correlation, the correlation between the level of compliance as an independent variable and opinion as the dependent variable showed a value of 0.709 with a significance level of 0,000 (p-value <0.0005). Thus H_0 in this study was rejected. This means that there is a positive directed correlation between the level of compliance and opinion with a significant level of correlation strength.

The test results using Kendal Tau C showed that the correlation between the variable level of compliance and opinion had a value of 0.683 with a significance level of 0,000 (p-value <Tb) so that H_0 in this study was rejected. This means that there is a fairly strong correlation between the level of compliance and opinion with a significant level of correlation strength.

To strengthen the test results, the researcher conducted a test to determine the existence of statistically significant differences between the averages of two or more independent groups (not interrelated) using the Kruskal Wallis nonparametric test. This type of testing was chosen because the research data had an abnormal distribution so it could not be done parametrically. Based on Kruskal Wallis test results which obtain a significance value of 0.00 (p <0.05), means that there are differences in the average between opinion groups, namely the average level of compliance of the WTP opinion group which different from the WDP opinion group and TMP opinion group.

The results of statistical tests showed that BPK Auditors had considered the findings of the non-compliance of local governments with the laws and regulations in the process of determining opinion on local government financial statements. Thus there is a correlation between the level of local government compliance with laws and regulations and opinions on LGFS. The direction of the correlation is positive, meaning that the better the level of compliance of the local government is reflected by the smaller value of findings of non-compliance (including those containing elements of fraud), the better the opinion that is obtained by the local government.

The results of this study are in line with the research conducted by Safitri and Darsono (2015) and Widodo and Sudarno (2017) which show that the findings of non-compliance with laws and regulations have a significant effect on audit opinion. The direction of the influence correlation is negative, which means that the more findings of non-compliance with laws and regulations, the less the probability of giving a WTP opinion by BPK RI auditors to the local government financial statements.

However, some things deserve attention, namely the existence of LGFS which obtained WTP opinion but obtained compliance score 2 (material not pervasive) and LGFS which obtained WDP opinion but obtained compliance score 4 (limitation of material and pervasive scope) as can be seen in table 3. Although these differences are generally caused by differences in the concept of fraud between researchers and auditors, the researchers assume that the findings contain elements of fraud while the auditors do not say so. Nevertheless, this has the potential to cause problems in the future. Among the indications of the problem, there are differences in the understanding of fraud and materiality related to fraud among BPK auditors as described in the next section in this article.

Then, why is there still a problem of non-compliance that is not detected by BPK auditors when carrying out LGFS audits as indicated by the existence of a number of local heads who are caught in a problem of corruption (fraud) even though the financial statements of the local government they lead obtain unqualified opinion (WTP) from BPK? For this problem, the researcher found several reasons and conditions for BPK auditors which are described in the following sections.

4.2 Identification of Correlation Causing Factors

4.2.1 BPK Auditors' Perception of the Correlation between the Level of Compliance with Opinions on the LGFS

BPK auditors agree that there is a correlation between the level of compliance of the local government and the opinion of the LGFS. This is mainly related to the criteria for formulating opinions, namely compliance with government accounting standards, adequate disclosure (compliance), compliance with laws and regulations, and the effectiveness of internal control systems. More specifically, the auditors stated that compliance that affected opinion was compliance related to the fairness of the account in the financial statements of the local government. Thus, in general, BPK auditors focus more on compliance checks on matters that have relevance to the fairness of accounts in financial statements. So if the auditors encounter two conditions of non-compliance, namely the first problem which can affect the fairness of the account and the second problem which may not affect the fairness of the account, therefore auditors will focus on the first problem.

4.2.2 Compliance

One of the objectives of the financial audit is to obtain adequate confidence so that the auditors are able to provide an opinion that the financial statements present fairly, in all material respects, the compliance with accounting standards, the adequacy of disclosures, compliance with laws and regulations, and the effectiveness of the internal control system (BPK, 2017). Thus, compliance with laws and regulations becomes a matter that must be tested by BPK auditors. However, in the LGFS audit, BPK does not provide conclusions regarding the level of compliance of the local government and also there is no limit on the extent, type, and nature of compliance that must be tested by BPK auditors. As a result, the nature of compliance that must be tested by BPK auditors becomes too broad.

4.2.3 Fraud

The Technical Guidelines (Findings Code) stated that there were five subgroups of findings of non-compliance, namely findings of state/local losses, potential losses of state/regions, lack of revenue, administration, and indications of criminal acts. Generally, findings of state/local losses, potential state/local losses, and indications of criminal offenses are closely related to fraud. The SPKN states that auditors must identify fraud risk factors and assess the risk of non-compliance with statutory provisions caused by fraud. If there is a risk of non-compliance indicating fraud that significantly affects the subject matter/information of the subject matter audited, the auditors must modify the procedure to identify the occurrence of fraud and/or non-compliance. BPK auditors agree with the concept, but there are several obstacles faced by auditors in the effort to detect fraud in LGFS audits. Some of these constraints are described as follows:

a. There are no standard fraud criteria/requirements yet at BPK

In particular, there is no standard guidance on the criteria/conditions for fraud set by BPK. Terms of fraud are only mentioned generally in the SPKN; Acts that contain intentional intentions, intentions, benefit oneself or others, fraud, concealment or embezzlement, and abuse of trust that aim to gain unauthorized profits that can be in the form of money, goods/property, services, and not paying services, which are carried out by one or more individuals from parties responsible for governance, employees, or third parties (BPK, 2017). As a result, the auditors used professional judgment in determining whether a finding of non-compliance met the criteria for fraud or not. The criteria used by the auditors also varied, as expressed by participants R7, R8, and R10 as follows:

"Our judgment and evidence on the field." (R.8.18)

"A finding of non-compliance is categorized as fraud if it meets the following elements: there is an intention from the responsible parties, loss of state/region, real and certain amount, and there is an act against the law" (R.7.6)

"...so far the easiest fraud criteria are (financial) losses in the area" (R.8.12)

"So I think compliance will mean fraud if it meets the elements of fraud, what is that? The first is hidden two, he broke the rules. Third, there are those who benefit, there are those who are disadvantaged, if they have fulfilled it, then it is fraud..." (R.10.10)

b. BPK tends to be careful in determining fraud findings

Some auditors revealed that BPK tended to be very careful in fraud findings. Some of the reasons are that there was still a dualism of the assertiveness of BPK leadership's opinion on fraud. Some leaders stated that fraud must be stated expressly while other leaders were still hesitant to state explicitly. In addition, there are fears of future lawsuits for fraud findings. These concerns are generally related to the strength of evidence obtained by auditors in the field. As a result, BPK tended to avoid audit terms that can lead to fraud in writing findings of non-compliance. For example, the BPK tended not to use the term indication of state losses/potential state losses/state losses in audit findings and replace them with over payment terms.

c. Collusion makes fraud difficult to detect/prove

Collusion factors make fraud difficult to detect, especially if collusion involves the third party that is often used by BPK auditors in confirming an issue of non-compliance.

d. There are threats/dangers in fraud examining experienced by auditors

Another factor that makes fraud even more difficult to detect is the threat or danger experienced by the auditors. Some auditors tend to avoid exploring fraud when there is a threat or danger.

e. The willingness of auditors to detect fraud is low

The auditors' willingness to detect fraud is also an obstacle. This is quite surprising because the auditors should carry out his role professionally following audit standards. Some of the reasons that might be attributed to this factor are the security factors as described above and the work protection factors that are explained in the next section.

4.2.4 Audit Program

The majority of auditors stated that the audit program had been designed to detect non-compliance and that the program was quite effective. However, several things deserve attention with the following details.

- a. The audit program is generic/normative/standard. The audit program is a guideline used by the auditors in carrying out the audit in the field. The audit program should be designed at the planning stage based on the results of the preliminary audit. Unfortunately, in general, the auditors only copy the audit program from the audit preparation team or the audit program in the previous years.
- b. In general, the audit program has not been designed to detect fraud.
- c. At the planning stage, the standard audit program should be modified by the audit team following the conditions of the auditee. The modification also needs to be done so that the audit program can be used to detect fraud if there is a risk of fraud. However, auditors tend not to update/modify the audit program and continue to use the standard audit program.

Different conditions were expressed by several participants who stated that the audit program had been designed to detect fraud, both directly and through modifications to the standard audit program based on the results of the fraud risk assessment matrix (FRAM) analysis at the preliminary audit. This showed that there are variations in the field. Some audit teams had tried to adjust the audit program according to the auditee's condition based on the results of the assessment at the time the preliminary audit was carried out but some others did not do so.

4.2.5 Skill and Experience

To be able to detect non-compliance and fraud, the auditors' skills and experience are necessary, including the ability to establish conditions of non-compliance/fraud in the audit findings. The lack of these two competencies

can reduce the auditors' detection ability, specifically related to the ability to write audit findings. If the auditors do not have this ability, it can make readers of the findings, including the opinion review team, misunderstand the real conditions experienced by the auditee. To bridge this, a tiered review mechanism when examining in the field becomes very important, especially for inexperienced auditors, so that the quality of the audit is maintained.

4.2.6 Limitations on the Amount of Time and Human Resources (HR)

It is undeniable, that the problem of the amount of time and HR is an important factor in the audit process, including in efforts to detect non-compliance. Both of these factors can determine the depth and extent of audits in the field, including coverage, samples, and types of testing that can be done. The limitations of these two things force the audit team to be able to organize and plan audits properly, including by applying the risk based-audit. Regarding the timing of audits at the planning stage, BPK auditors stated that the determination of the time of the audit, generally, was not carried out through the results of an adequate analysis/assessment. Determination of the length of the audit is carried out with a budget allocation approach so that the length of the audit process does not depend on the conditions of the auditee but rather on the available budget allocations. This was revealed by participant R1 as follows:

"Yes. So, to be honest, the determination of the length of the audit day in the field was not based on the results of the assessment or analysis before the audit, but more to the budget. So in my opinion sometimes it's not fair.... So the starting point is how much budget we have and then how we can fulfill it backward. So in fact, in my opinion, it is rather unfair and less true...." (R.1.20)

4.2.7 Materiality

In terms of materiality, especially materiality in the findings of fraud, there were differences of opinion among the auditors even though in the end the auditors agreed to follow the *Local Government Financial Statement Audit Implementation Guidelines* in determining materiality. Some auditors stated that if there were findings of fraud, any value should be considered material. This refers to the *Technical Guidelines for Establishing Materiality Limits* which state that the level of government compliance with laws and regulations has a high importance value, so violations of laws and regulations, such as transactions that indicate corruption of any nominal value, whether they have a direct or indirect impact on the reasonableness of financial statements can affect the assessment of materiality qualitatively. In line with this, the *Local Government Financial Statement Audit Implementation Guidelines* state that the qualitative factor is considered by the auditors in determining PM and TM by looking at its effect on the fairness of the financial statement accounts, including the fraud committed by management in the presentation of financial statements. Even though the value of fraud is below materiality, it is qualitatively material if management intentionally manipulates a particular purpose. Following the fraud tree developed by the ACFE, we know that corruption and manipulation of financial statements are branches of fraud.

On the other hand, several other auditors stated that a fraud finding was declared material if it had exceeded the TM value set at the time of the audit. This statement refers to the *Local Government Financial Statement Audit Implementation Guidelines* in section Annex IX.2 stating that for a problem of non-compliance if the auditors believe there are some elements of fraud, the materiality limit is set at TM. Regarding this problem, participant R1 stated that the determination of the materiality of fraud findings by TM was to ensure uniformity and fairness in the determination of the audit opinion mainly related to the comparison of values between the findings of fraud and the assets managed by the local government. In addition, the determination of TM materiality of fraud also allows BPK to be able to account for and prove more accountably if there are future lawsuits.

4.2.8 Opinion Considerations

BPK auditors are very careful in setting opinions on LGFS, especially if there is a condition that can result in a decrease in opinion on LGFS. One of these precautions is the granting of concessions to the auditee to finalize findings, both by restoring state losses and with other action plans. One of the reasons for recovering state losses which can be considered as the process of formulating an opinion is when findings of compliance generally resulting in the state losses are not categorized as a fraud. Furthermore, they are not even classified as (potential) state losses but rather as an overpayment.

4.2.9 Work Protection & Negative Protection Stigma

It has been stated that there are potential threats and dangers experienced by the auditors when dealing with fraud problems. This caused some auditors to be reluctant to explore findings that indicated fraud. This reluctance is

stronger when there is a perception among the auditors that the protection of work provided by BPK to the auditors is also inadequate. Actually, BPK has tried to provide legal assistance through the Legal Subdivision in each representative office, but the practice of legal aid provided seems to be less uniform/adequate. However, some participants stated that the auditors should continue to work professionally in all conditions and that the potential threats/dangers experienced by the auditors in the field constitute a work risk that must be faced.

5. CONCLUSION

This study showed that there is indeed a correlation between the level of compliance of the local government with legislation and opinions on the LGFS. The correlation has a positive direction which means that the more obedient the local government is, the better the opinion is on the LGFS given by BPK. However, there is a risk of auditing that may occur, both in the implementation process and in the audit reporting, including in the opinion formulation process. Risks that might arise can be divided into two aspects. First, risk of failure to detect problems of non-compliance and fraud. Some of the causes are differences in concepts related to fraud criteria, failure to update the audit program, potential threats/dangers experienced by the auditor, and failure to reduce the auditors' negative perceptions of work protection. Second, risk of errors in setting opinions. Some of the causes are the risk of failure to detect material non-compliance and fraud problems. Also, differences in the concept of materiality among BPK auditors can increase the risk of errors in setting opinions. Thus, BPK needs to increase the effectiveness of audit quality assurance to improve audit quality.

This study has several limitations. The interview sample for qualitative research only involved auditors from three representative offices from Java. This study did not involve auditors from outside Java who could experience different conditions. Also, the researcher did not conduct interviews with personnel from the Main Directorate of Planning, Evaluation, and Development of the State Financial Audit and Legal Representation Subdivision to confirm, especially related to internal audit guideline/regulatory issues related to fraud and work protection issues for auditors.

Based on the findings in this study, several research developments can be carried out as described below:

- a. Research related to what factors can be considered in determining the time of the LGFS audit.
- b. Research on types of threats experienced by BPK auditors in LGFS audits, whether they are related to fraud or other problems.
- c. Research on how BPK auditors perceive the work protection provided by BPK.

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