

## WHY DO AUDITOR SEE AN ASSET MANAGEMENT AS THE IMPACT ON THE QUALITY OF THE FINANCIAL REPORTING OF THE LOCAL GOVERNMENT: RESEARCH IN BANDUNG CITY GOVERNMENT

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### ABSTRACT

*The impact of asset management on the quality of financial report of the local government in Indonesia has been studied by several Indonesian scholars. The purpose of this study to examine whether the quality of financial reporting is affected by an asset management in Bandung City Government. Usefulness of research as input for the government to improve asset management practices and the quality of the financial reporting. The sample in this research is 35 unit tool (SKPD) with respondents as many as 78 civil servants. Data collection using primary data. Method data testing conducted by validity and reliability. With structural equation model approach partial least square, confidence level 95% and  $\alpha = 0.05$ , the hypothesis 1 (H1), hypothesis 2 (H2) and hypothesis 3 (H3) rejected H0. The result showed that asset inventory and legal audit have significant effect on the Quality of The Financial Reporting in Bandung City Government. Otherwise, asset valuation has a not significant effect on the Quality of The Financial Reporting. Asset inventory, audit legal, and asset valuation simultaneously impact of 65.2% on the quality of financial reporting, while the remaining 34.8% is effected by other factors that were not studied. The conclusion is the implementation of asset management especially for asset inventory, audit legal, and asset valuation impact on the quality of the financial reporting. To enhance the quality of assset management practices, all audit findings from auditor must be finished completely. The same findings also not to repeatedly.*

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### 1. Introduction

Regional autonomy is the right, authority and obligation of autonomous region to regulate its own affairs according to the laws and regulations (Law number 32 The Year 2004, article 1 point 5). The Government of Bandung City has also applied the principle of autonomy. The Government of Bandung City acquire asset from Local Government Budget (APBD) funding source to support government performance and society services. Acquiring asset needs good asset management from planning to reporting (Mahmood et al., 2014) and also useful to users. The preparation of financial reporting is a form of accountability of the implementation of APBD (Law Number 17 The Year 2003, Article 10 point 2) and resources management such as asset. The four normative prerequisites required for government financial reporting to meet the desired quality are relevant, reliable, comparable, and understandable (PP 71 of 2010). Financial reporting compiled by the Regional Government are delivered to the Head of Regional Government for The Audit Board (BPK) to be audited not more than three months after the end of the fiscal year (Permendagri 13 The Year 2006, Article 297 paragraph 1). The quality of regional government financial reports will be assessed by BPK. Based on the results of BPK audit on Financial Reports in Bandung City Government in the last four Fiscal Year, Bandung City Government obtains an unsatisfactory result. It is because the mismanagement of regional property (BMD) that occurred repeatedly from 2012 until now. For example, there are still unrecorded assets, and assets with the unknown location, value, and certificate. The unsatisfactory result is due to BPK being unable to obtain sufficient and proper evidence of the value and the legality of fixed assets because there is no data and information available. As a result, these issues form the basis for BPK providing low assessment result. Until now, The Government of Bandung City still gains qualified opinion from BPK. The problem of inadequate data availability is a challenge for Local Governments in managing assets (Hanis, Trigunarsyah, Susilawati, 2011). Siregar (2004) states that asset management activities consist of five stages: (1) inventory assets; (2) legal audit; (3) asset valuation; (4) asset optimization; and (5) SIMA development (asset management information system). Based on the phenomenon found in BMD management, asset management is weak, especially in the stage of asset inventory, legal audit, and asset valuation which affect the result of BPK assessment on the quality of financial reporting. Anshari (2016) states that BMD inventory has a positive and significant effect on the quality of financial reporting, while Febrianti (2016) states that inventory partially negatively affects the quality of financial reporting. According to Anshari (2016), Simamora and Halim (2013), legal audits (proof of ownership) and BMD assesment affect the quality of financial reporting. Through the study of asset management and previous research, this study aims to examine whether the quality of financial reporting is affected by an asset management in Bandung City Government.

### 2. Theoretical Review

The term asset in Government Regulation Number 27 The Year 2014 on the State / Regional Property Management, is a State / Regional Property. Asset management is a science and art to guide asset management process consisting of asset planning, inventory, audit legal, valuation, use, waste until removal and transfer of the asset (Sugiana, 2013, Hadinata, 2011, Kaganova and McKellar in Hariyono, 2007). Asset management in PP 27 of 2014 is known as the regional property management. Management of State / Regional Property Article 3 of Government Regulation no. 27 of 2014 include asset needs planning and budgeting, procurement, use, utilization, security and care, assessment, alienation, destruction, removal, administration,

coaching, supervision and control. Hastings (2010) says "Asset management is the set of activities associated with identifying what assets are needed, identifying funding requirements, acquiring assets, providing logistic and maintenance support system for assets disposing or renewing assets". Siregar (2004) divides asset management into five work stages, involves inventory, legal audit, asset valuation, asset optimization and SIMA development (asset management information system). Good asset management is expected to assist in making the right decision to make the assets managed effectively (Sugiama, 2013, Summerell, 2005). Jim (2007) mentions the main objectives of management and it is accompanying components to assist in: (1) knowing exactly what assets they have, (2) finding out exactly what assets are, (3) knowing the condition of assets in each time, (4) understanding the design asset criteria and with appropriate performance and conditions, (5) development program that assures the performance of each asset is reliable when required, (6) the overall performance of activities at the optimal cost. Asset management becomes very important and complex, so the government can be well managed (Mahmood, Dhakal, Brown, 2014). To implement good asset management is a challenge for the government (Hanis, Bambang, and Connie, 2011, Rayya, 2015). Practices on asset management need to be evaluated for improvement in the development of asset management programs (Rebecca, Richard, 2006).

The first point in asset management cycle by Siregar (2004) is asset inventory. Asset inventory is a series of activities to collect data collection, recording and reporting of asset data collection (Chabib Sholeh and Heru Rochamnsjah, 2010, Sugiama, 2013, Government Regulation No. 27 of 2014). Siregar (2004) divides the asset inventory consists of two aspects, inventory of the physical and legal. Physical features consist of shape, area, location/volume /quantity, type, address, and others. While legal aspect is the status of mastery, legal issues owned, the ultimate limit of mastery and others. The work process undertaken is data collection, coding/labeling, grouping, and bookkeeping/administration in accordance with asset management objectives. Second, legal audit is the scope of asset management work to obtain a clear and comprehensive picture in the form of an inventory of asset control status, systems and procedures for asset control or transfer, identification and finding solutions to legal issues, and strategies for solving legal problems related to the acquisition or transfer of assets (Siregar, 2004, Sugiama, 2013). Third, asset valuation is commonly performed to know asset cost or value. Siregar (2004: 519) highlight asset valuation as a work process for appraise asset which is generally done by appraisal. The asset valuation result will be used to find out the value of an asset and to determine the value of assets to be sold. Asset valuation is a work process to know the value of organization wealth (Siregar, 2004). Asset valuation estimates the value of an asset based on the analysis of objective and relevant facts using the applicable valuation methods and principles (Sugiama, 2013). Fourth, optimization, Siregar (2004) defines the optimization of assets as a potential work process to optimize the physical, location, value, volume, legal and economic potential of the asset. Siregar (2004) also states that at this stage the asset must be investigated and grouped into potential assets and not. Meanwhile, according to PP 27 of 2014, in the framework of optimizing the utilization of BMN / D assets can be utilization and alienation. Utilization of assets in PP 27 The Year 2014 consists of the relend-use, build operate and transfer, and provision infrastructure cooperation. While the transfer according to PP 27 of 2014 is a transfer of State / Region Property which consists of sales, exchange, and grant. Fifth, SIMA (Asset Management Information System) is an effective way to improve supervision and control performance (Siregar, 2004). Siregar (2004) also stated that manage asset clearly from handling to responsible could minimize corruption, collusion, and nepotism. PP27 of 2014 state that the Regional Secretary as the manager of property must supervise and control the property through monitor and investigation by requesting the internal control apparatus of the Government to audit the use, Utilization and Transfer of State /Regional Property. Ulum (2008) noted that one of the indicators to know the honest and performance of local government can be seen through its financial report. The financial report are a form of government financial accountability that is a structure in realizing transparency and accountability. In presenting the financial report, the head of state/regional government must assure that its asset and all account in its financial report are complete, accurate, and accountable. Financial report submitted by the Head of Region is compiled as a responsibility for the resources entrusted must the qualified financial. PP 71 of 2010 on Government Accounting Standards (SAP) establish the normative prerequisites required for government financial reports to meet the desired quality, consisting of relevant, reliable, comparable, and understandable. Based on the phenomenon as described above, financial report present asset information incompleteness (there are still unrecorded assets), the land assets have not been certified and there are assets which can not be known its existence and value. Researcher supposes that the problem is suspected by the ineffectiveness of asset management. M. Yusuf (2010: 8) in Ansari (2016) states that asset management is a very important component to realize the better financial report. Based on the findings/problems which are found in the BPK's Audit Report, the researcher assumed that asset management component consisting of asset inventory, legal audit, and asset valuation has not been implemented well to become a factor which causing the qualified opinion on Bandung City Government Financial Report. Therefore, research use three variable independent consisting of asset inventory, legal audit, and asset valuation, one dependent variable is financial report. This paper discuss about three construct (hyphothesis) that impact on the financial report. Research on an asset management as the impact on the Quality of Financial Report of the Local Government carried out by Anshari (2016), Febrianti (2016), and Simamora and Halim (2013) who argued that the implementation of asset management effect the quality of financial report. Based on this phenomenon and previous research, the framework description in this research as below:

#### **Hypothesis of asset inventory has a significant effect on the quality of financial reporting**

Working process of asset inventory by Siregar (2004) is data collection, coding/labeling, grouping, and bookkeeping/administration in accordance with asset management objectives. The main objectives of the asset inventory are orderly administration, asset security, control and supervision for an asset (Sugiama, 2013: 175). If Bandung City Government managed asset inventory well, the database which is fully informative of the quantity and quality of fixed asset can be owned by the Regional Government. The financial report can get an unqualified opinion if they present complete information. Anshari (2016) noted that if asset inventory is managed well or better, it will improve the quality of financial report. This study aims to prove whether the asset inventory has a significant effect on the quality of financial report in Bandung City Government as the first statistical hypothesis (H1). The number of indicators used in measuring asset inventory variables is 16 indicators denoted by X1.1 to X1.16.

**Hypothesis of legal audit has a significant effect on the quality of financial reporting**

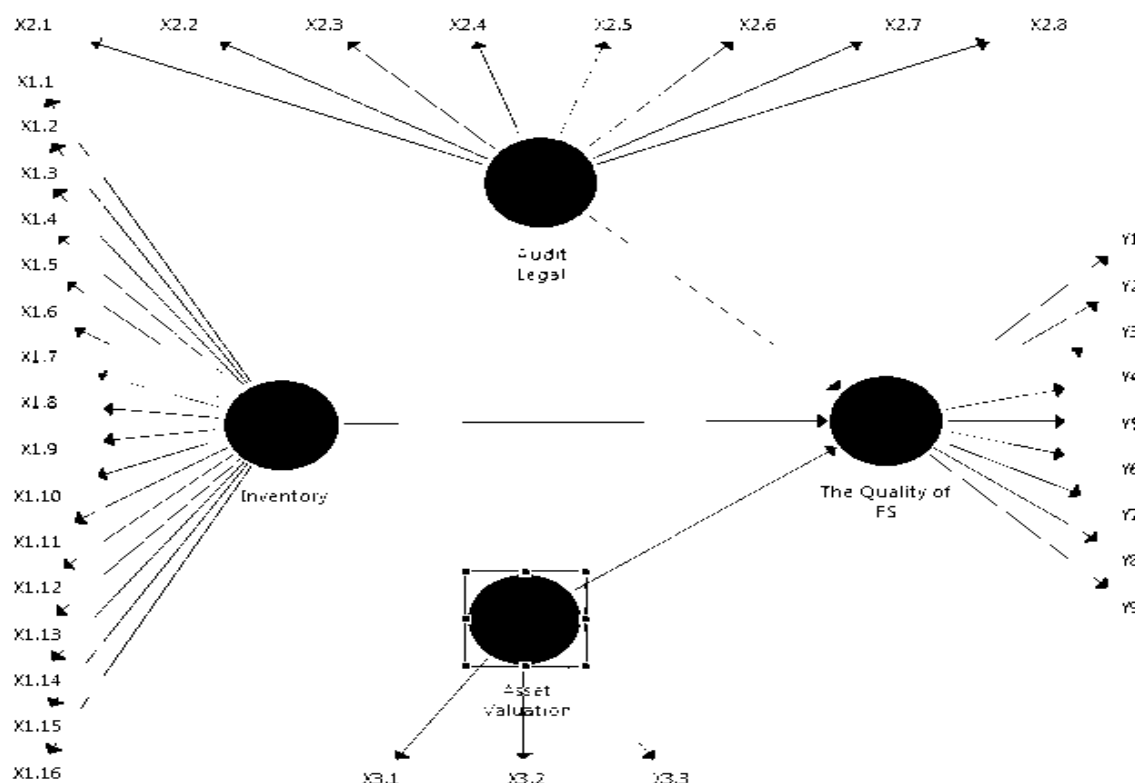
Legal issues are often encountered by Local Government include weak asset ownership status, assets owned by other parties, alienation of unmonitored assets, and others (Siregar, 2004: 519). The benefit of the legal audit include 1) minimizing legal risk, 2) optimizing the using and utilization of assets, 3) identifying potential problems, 4) resolving various issues that may arise concerning legal aspects (Sugiama, 2013: 189). A well-executed legal audit will present asset information in an honest, verifiable, and neutral financial report that has been guaranteed its legality. Anshari (2016) noted if the legal audit is doing well or better, it will improve the quality of financial report. This study aims to prove whether the audit legal has a significant effect on the quality of financial report in Bandung City Government as the second statistical hypothesis (H2). The number of indicators used in measuring the legal audit variables is 8 indicators denoted by X2.1 through X2.8.

**Hypothesis of asset valuation has a significant effect on the quality of financial reporting**

Asset valuation is a process of working to appraise the organization's asset to know the value of asset wealth (Siregar, 2004: 519). If the asset valuation is well done, all assets must have its value or cost. Anshari (2016) noted that if the asset valuation is well done or better, it will improve the quality of financial report. Simamora and Halim (2013) also noted that the factors affecting asset management include the proof of ownership and valuation of assets. This study aims to prove whether the asset valuation also affects the quality of financial report in Bandung City Government as the third statistical hypothesis (H3). The number of indicators used in measuring asset valuation variables is as much as 3 indicators denoted by X3.1 to X3.3.

The quality of the financial report will be measured using 9 indicators denoted by Y1 to Y9. From the description above can be concluded that the asset management consisting of asset inventory, audit legal, and asset valuation can improve the quality of the financial report. Figure 1 shows the conceptual framework whether asset inventory, audit legal, and asset valuation partially and simultaneously effect the Quality of Bandung City Government's Financial Report.

Figure 1: Conceptual Framework



**4. Research Methodology**

The type of this research is descriptive and verification research by using quantitative approach. A sample in this study is 35 unit tool (SKPD) with respondents as many as 78 civil servants were selected by using purposive sampling method. Method of data analysis structural equation model. SEM is used in order to answer the problem formulation and testing hypothesis (Kewo, 2017). (Chin and Wested,1999) in (Ghozali, 2014) argued that PLS is not only used to explain the presence or absence of relationships between latent variables (prediction), but also to confirm the theory. The goal of SEM is predictive oriented (Ghozali, 2014). Data collection using primary data. Primary data is data/information collected by researchers through questionnaires and interviews for the purpose of obtaining the facts and factual information from respondents. (SEM) approach partial least square (PLS) with consideration of the number of a sample under 100 and data used is primary data. Method data

testing conducted by validity and reliability. Test the validity of this questionnaire is done by correlating each question with a total score for each variable. Test the validity of this research use the formula of product moment correlation is as follows:

$$r_{ix} = \frac{n \sum ix - (\sum i)(\sum x)}{\sqrt{(n \sum i^2 - (\sum i)^2)(n \sum x^2 - (\sum x)^2)}}$$

To ascertain how each indicator block relates to its latent variables, researcher performe an outer model analysis. The objective is to ensure that the measurements used are valid as a measurement by testing convergent validity. Testing convergence validity can be known from loading factor value for each indicator construct. Ghozali (2014) states that convergent validity is related to the principle that the manifest variable of a construct should be highly correlated. In general, the rule of thumb for confirmatory research must have loading factor value greater than 0,7. However, the loading factor value from 0,5 to 0,6 is still considered sufficient for early-stage research of measurement scale development (Chin: 1998).

Reliability statistics that are still in use today is Cronbach's alpha. The reliability test is performed to find out which instrument measurement results can be trusted (Azwar:2011). Test of reliability in this research using cronbach alpha test technique. If the reliability of each variable studied is greater than 0,7, the responses from the respondent can be reliable.

Hypothesis testing is done by using SEM-PLS software. Null hypothesis (H0) is rejected if the Bootstrapping calculate  $T_{value}$  grater than  $T_{table}$  in each construct. To determine whether the impact of each construct is significant refers to  $T_{value}$ . The impact is significant when  $T_{value}$  grater than  $T_{table}$ . The possitive value of path coefficient means dependent variable has a positive impact on dependent variable.

### 5. Result and Discussion

The measurement results of confirmatory factor analysis showed all indicators are valid a measure for each variable >0,50 (Figure2). The composite reliability each variable >0.70 (Table 1) indicates that the indicators have consistency in measuring the variable of each.

Figure 2: PLS Algorithm Result

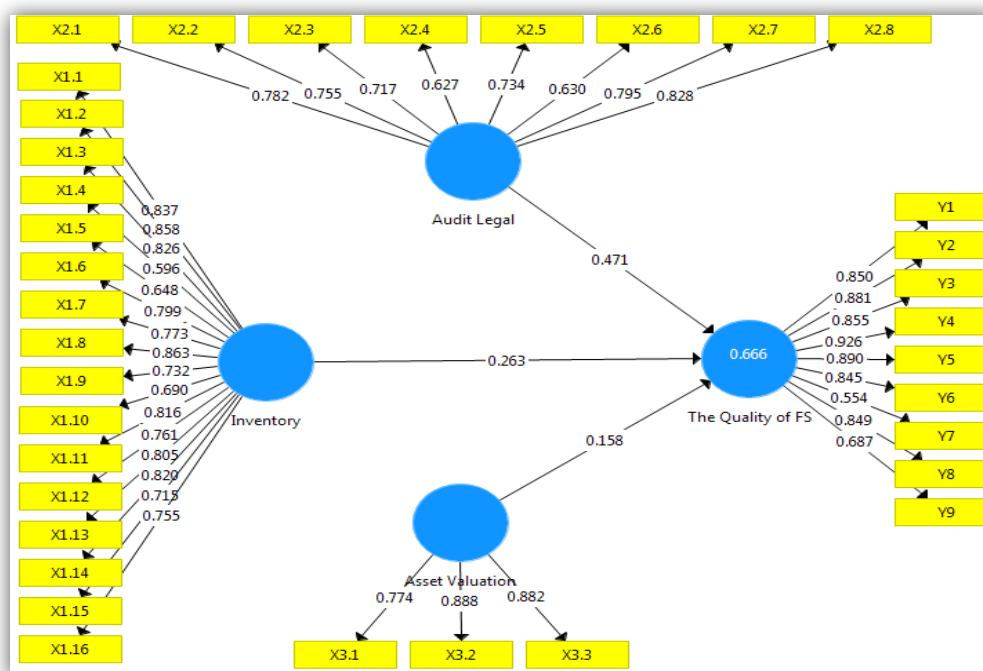


Table 1: Bootstrapping Result

Variable	R <sup>2</sup>	Error Variance	CR	Cronbach's alpha	AVE
Inventory		0,243	0,959	0,954	0,597
Audit Legal		0,330	0,904	0,878	0,544
Aset Valuation		0,228	0,949	0,813	0,677
Financial Report	0,652	0,381	0,887	0,938	0,724

Table 2: Testing results the effect inventory on the quality of financial reporting

Path coefficient	T <sub>value</sub>	T <sub>table</sub>	Ho
0,237	2,094	1,960	Reject

Table 3: Testing results the effect legal audit on the quality of financial reporting

Path coefficient	T <sub>value</sub>	T <sub>table</sub>	Ho
0,465	2,917	1,960	Reject

Table 4: Testing results the effect asset valuation the quality of financial reporting

Path coefficient	T <sub>value</sub>	T <sub>table</sub>	Ho
0,178	1,193	1,960	Accept

Table 2 show that T<sub>value</sub> inventory that is equal to 2,094 > 1,96. Because T<sub>value</sub> grater than T<sub>table</sub>, degree of error rate of 5% was decided to reject H0. It can be concluded that inventory partially effect the quality of financial report. The results of this study provide empirical evidence that the betterthe inventory will enhance the quality of financial report. The first hypothesis (H1) of asset inventory effect the quality of financial report is proven in Bandung City Government. Path coefficient of the inventory variable is 0.237. Positive path coefficients showed that the better the inventory will improve the quality of financial report in Bandung City Government.

Table 3 shows T<sub>value</sub> audit legal is 2,917 greater than value T<sub>table</sub> 1,960. This means that we decide to reject H0. Based on the test results, it can be concluded audit legal partially effect the quality of financial report. The results of this study provide empirical evidence that the better the audit legal will enhance the quality of financial report. The second hypothesis (H2) of audit legal effect the quality of financial report is proven in Bandung City Government. Path coefficient of the audit legal variable is 0,465. Positive path coefficients showed that the better the audit legal will improve the quality of financial report in Bandung City Government.

Table 4 shows T<sub>value</sub> asset valuation is 1,193 lesser than value T<sub>table</sub> 1,960. Because T<sub>value</sub> lesser than T<sub>table</sub>, degree of error rate of 5% was decided to accept H0. T<sub>value</sub> 1,193 means that T<sub>value</sub> is not significant. The results of this study does provide empirical evidence that the better the asset valuation will enhance the quality of financial report but not significant. The third hypothesis (H3) of asset valuation effect the quality of financial report supported the statistic hypothesis. Path coefficient of the asset valuation variable is 0,178. Positive path coefficients showed that the better the asset valuation will improve the quality of financial report in Bandung City Government. Because T<sub>value</sub> is not significant, we can conclude that asset valuation effect the quality of financial report but not significant.

Asset inventory, audit legal, and asset valuation simultaneously impact of 65.2% on the quality of financial report, while the remaining 34.8% is effected by other factors that were not studied.

## 6. Conclusion

The asset management (inventory, audit legal, asset valuation) impact the quality of financial report in Bandung City Government. This research result show the value of R-square is 0,652 or 65,2% which means independent variable (asset inventory, legal audit, and asset valuation) able to explain the variance of the quality of financial report equal to 65,2%. The result testing of three statistical hypotheses obtained the positive value of parameter coefficient for all hypothesis. Whereas T-value only significant for H1 and H2, not H3. The positive value of parameter coefficient for all hypothesis means each construct has a positive effect to the financial report. The better the application of inventory, audit legal, and asset valuation will make the quality of the Bandung City Government's financial report is also getting better. This research evidence is not support that asset valuation has a significant effect on the financial report.

Overall application of inventory in Bandung City Government is already quite good, even though there are some things that still need to be improved, for example, the inventory must be practiced not only to gather data but also validated the data. Besides inventory practice to the asset physics, it must be also to asset legalization and administration. Inventory can be conducted every year, not just for occasionally or like once in 5 years as described in PP 27 The Year 2014 or as a follow-up for audit findings. Suggestion for State Government to revise PP 27 The Year 2014 especially the point of inventory. The next concept of new rules maybe can be revised the implementation of inventory which can be done every year not "minimum once in 5 years".

The application of audit legal in Bandung City Government is still not good and need to be improved. All land asset must be certified. The agreement of asset utilization by other parties must be updated, the database of asset and the users must be validated, complete, and always updated. Bandung City Government must design the audit legal program and activity to identify asset problem and state the solution which is also allocated in Local Government Budget. Furthermore, the next activity of asset is asset valuation.

The application of asset valuation in Bandung City Government still need to be improved though the result obtained asset valuation has not a significant effect on the quality report. Even though Bandung City Government uses the appraisal to appraise asset land, the auditor dubious for the result of valuation. The important things of asset management are document and data available. Archive management and providing storage space is urgently needed to do. The challenge to revaluation asset in Bandung City Government is unavailable document and information. The better asset valuation makes the quality of the financial report of the higher or more qualified. Good asset valuation performance will affect the quality of financial report and minimize incompleteness asset information in the presentation of financial report. On those matters, the Mayor of Bandung needs to evaluate the performance of all SKPD heads in managing assets and finishing all audit findings. Without supervision and evaluation from top management, the users and managers of assets do not aware the importance of duties and performances in managing the asset. For all audit findings from auditor must be finished completely and monitor the progress.

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