

Determinant: Follow-up of Audit Result Recommendations on the Quality of Regional Government Financial Reports

Empirical Study Regional Government-LKPD Period 2015-2019

*Auditing and
Government
Financial Reports*

431

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ABSTRACT

This study aims to determine the Follow-up of Recommendations for Examination Results, the Quality of Financial Statements and the Effect of Follow-up Recommendations on the Quality of Financial Statements. This research was conducted at the Regional Government-LKPD for the 2015-2019 period. This study used a quantitative approach with descriptive design and associative research. The research data used the technical census of 542 LKPD for the 2015-2019 period. Data analysis using binary logistic regression analysis. The results showed that in the 2015-2019 period local governments had followed up on the Examination Results Recommendations according to the recommendations by 61.6%, followed up but not according to the recommendations by 30.5%, had not followed up by 7.8%, and could not follow up by 0.1%. Furthermore, in the same period 100% WTP opinion has been achieved by all provincial governments, in district governments it reaches 88%, while in city governments it reaches 94%. The results showed that the Follow-up Recommendation of the Examination Results had a positive effect on the quality of the Local Government's financial statements. Thus, it means that follow-up recommendations on audit results can improve the quality of financial statements, if local governments follow up on the recommendations given by auditors, it will be able to improve the quality of financial statements for the next period.

Keywords : *Follow-up Recommendations of Examination Results, Quality of Financial Statements*

INTRODUCTION

The quality of financial statements accurately represents the performance of the entity in order to facilitate users of financial statements to predict cash flows (Miller, 2002) . The quality of financial statements overcomes the problem of information asymmetry so that fund owners have perfect information on the risks of investment projects and company risks (Hubbard, 2013) . High-quality information is important because it can influence the decisions of capital providers and other stakeholders in making investments, credit, and other resource allocations so that overall market efficiency increases (Beest & Boelens, 2009) .

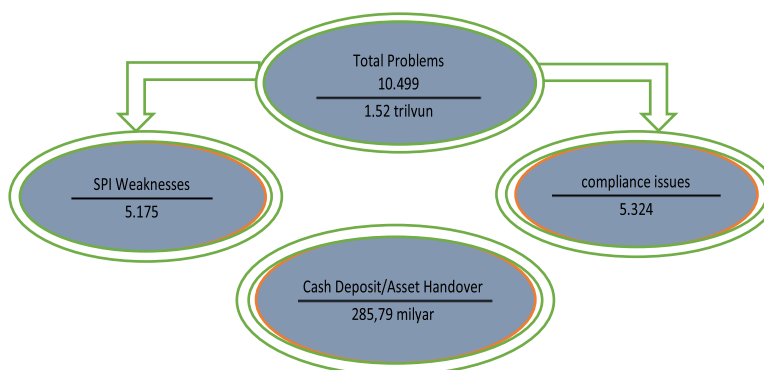
In order to know that the financial report of a government agency is of good quality, an authorized institution is required to assess it, in this case the Audit Board of Indonesia (BPK). There are four assessment opinions that can be given by the BPK on the Financial Report (LK) of a government agency, namely: first, Unqualified Opinion (WTP), which means that all LK is considered completely fair. Second, Fair with Exceptions (WDP), which means that there are only certain items that are considered unreasonable. Third, a disclaimer is given because there is a state of uncertainty. Fourth, adverse is issued because the LK is unreasonable, either due to non-compliance with regulations, not in accordance with accounting standards or misleading figures in the report. Audit report results by auditors are generally an indicator of the reliability of financial reports for most users of financial reports, because audit result information is assumed to be complete, accurate, and unbiased (A. Arens et al., 2012) , especially financial reports that receive an

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unqualified audit opinion (unmodified auditor's report) will be able to increase the trust of the legislative council and other stakeholders in the entity (ANAO, 2015 in (Jati, 2019)

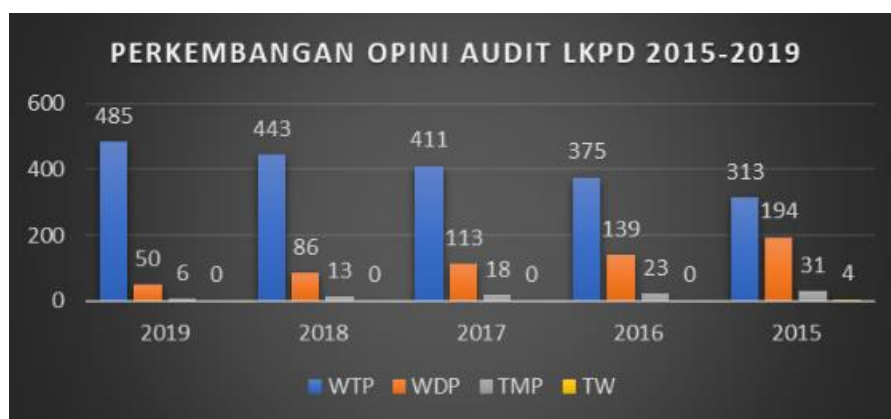
In preparing the Financial Report, each government agency strives to present the Financial Report properly and correctly to achieve the best predicate, namely WTP. However, in the public sector financial report, there are still many weaknesses, for example based on (IHPS I, 2020) the results of the BPK audit of the Regional Government Financial Report (LKPD) revealed 6,160 findings containing 10,499 problems consisting of 5,175 Internal Control System (SPI) problems and 5,324 problems of non-compliance with the provisions of laws and regulations amounting to IDR 1.52 trillion.



Source: IHPS I, 2020

Figure 1 BPK's Findings on Regional Government Financial Reports

Related to the weaknesses that are still found, it also affects the quality of government agency financial reports. The report (IHPS I, 2020) contains the results of the examination of 541 of the 542 Regional Government Financial Reports (LKPD) from the 542 LKPDs in 2019 that must be submitted. For the 541 LKPDs in 2019, the BPK gave 485 WTP opinions (90%), 50 WDP opinions (9%), and 6 TMP opinions (1%).



Source: IHPS I, 2020

Figure 2 : The increase in the quality of LKPD

Based on graph 1.1, there is an increase in the quality of LKPD every year, an average increase of 12% per year. This increase occurred because the local government continues to make efforts to improve the weaknesses that occurred in previous years. Although there has been an increase in the quality of LKPD, there are still 10% or 57 LKPDs out of a total of 542 LKPDs that have not received a WTP opinion.

In addition, there are still financial reports that have not received an WTP opinion due to the low number of recommendations followed up by ministries/institutions. Based on the Follow-up Report on Audit Results-TLHP I 2019, for the period 2015-2019 the number of Audit Recommendations was 148,762, of which 91,262 had been followed up according to the recommendations, 45,496 were followed up but not according to the

recommendations, 11,750 had not been followed up/follow-up process, while 254 recommendations could not be followed up. This shows that the audited entity has not paid attention to the results of the BPK audit. The results of the study (Sari et al., 2015) show that the more BPK recommendations that are followed up according to the recommendations will improve the quality of financial reports as represented by a high level of disclosure. If the BPK audit recommendations are followed up, then ministries and institutions can improve the findings of the previous period, thereby reducing the findings in the next period, thus increasing the chances of obtaining an WTP opinion.

Research (Chen et al., 2011) found that the efforts of entities or other related parties in following up on audit recommendations can improve government transparency and accountability. Research (Tresnawati & Nur Apandi, 2016), (Wulandari & Bandi, 2015), (Sari et al., 2015) and (Djanegara, 2017) show that follow-up of audit results has a positive effect on audit opinion. The more recommendations are followed up, the better the financial management becomes so that the opportunity to obtain the best opinion in the next period is greater, which means that the financial report is also of higher quality because the audit report by the auditor is generally an indicator of the reliability of the financial report, because the audit information is assumed to be complete, accurate, unbiased (A. Arens et al., 2012)

LITERATURE REVIEW

Follow-Up On Recommendations From The Results Of The Examination

Recommendations are suggestions from the auditor based on the results of their audit addressed to the person and/or body authorized to take action and/or improvements. Officials are required to follow up on recommendations in the LHP and are required to provide answers or explanations to the BPK regarding follow-up to the recommendations. Officials who are found not to have fulfilled their obligation to follow up on recommendations in the LHP may be subject to administrative sanctions in accordance with the provisions of laws and regulations in the field of personnel and/or criminal sanctions.

Regulation No. 2 of 2017 concerning monitoring of follow-up of BPK audit results, stipulates that BPK reviews the answers or explanations from officials to determine whether follow-up has been carried out in accordance with Article 6 paragraph 1, the classification of review results based on Article 6 paragraph 4 includes:

1. Follow-up has been in accordance with recommendations
2. Follow-up is not in accordance with recommendations
3. Recommendations not yet followed up
4. Recommendation cannot be followed up for valid reasons

A BPK recommendation is declared to have been followed up in accordance with the recommendation if the BPK recommendation has been followed up adequately by officials and the follow-up is in accordance with the recommendation and action plan accompanied by supporting evidence. BPK recommendations are expected to improve the management and accountability of state/regional/company finances in the relevant entity.

Quality Of Financial Reporting

In general, users of financial statements assess the auditor's report as an indicator of the quality of financial statements, because information that has been audited by an independent auditor is assumed to be complete, accurate, and unbiased (A. Arens et al., 2012). In line with the IASB and FASB Standards Boards agree that information that can be independently verified is generally more useful (IASB, 2008). By using the A. Arens model, the quality of financial reporting can be measured by the financial statements that receive the auditor's opinion. The types of audit opinions applied by the BPK, according to the Decree of the BPK RI Number 4/K/1-XIII.2/7/2014 concerning the Guidelines for the Implementation of Financial Audits, include four types of opinions, namely unqualified audit opinions (WTP) or unqualified opinions, because the financial statements present fairly in all material respects in accordance with government

accounting standards (SAP); Fair with exceptions (WDP) or qualified opinions, namely when the financial statements present fairly in all material respects in accordance with SAP, except for the impact of matters related to those excluded; Unfair (TW) or adverse opinion, because the financial statements do not present fairly in all material respects in accordance with SAP; and Statement of refusal to provide an opinion or disclaimer of opinion (TMP) or disclaimer opinion.

Among all auditor opinions, an unqualified opinion (unmodified auditor's report) can increase the trust of parliament, legislative councils and other stakeholders in the entity (ANAO, 2015 in (Jati, 2019) . For users of financial statements, financial statements with an unmodified or unqualified audit opinion are an important signal about the reliability of financial information (IAASB, 2014)

METHODS

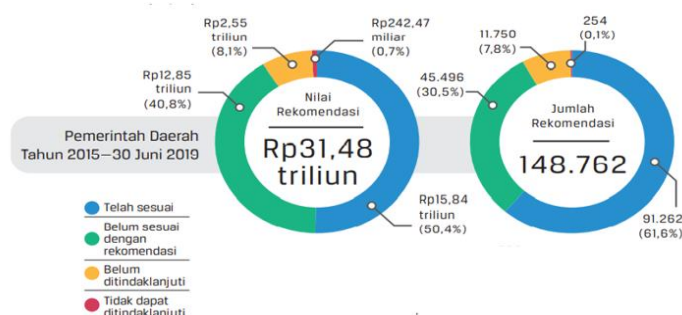
This study uses descriptive and causal-explanatory methods by conducting hypothesis testing. The data collected are secondary data, namely the BPK-RI IHPS Report Document for the 2015-2019 period which contains a list of Recommendations, Follow-up to Audit Results (TLHP) and Audit Opinions. The data was obtained from the BPK RI Information and Communication Center. The data was analyzed using descriptive statistics and Binary Logistic Regression analysis to test the hypothesis of the effect of Follow-up to Audit Result Recommendations on the Quality of Financial Reports. The test results are determined by the probability value, namely at a significance level of 5%. The criteria for accepting and rejecting the hypothesis are if the p-value > 5% then the hypothesis is rejected. Conversely, if the p-value < 5% then the hypothesis is accepted.

In this study, the Follow-up to Audit Result Recommendations as an independent variable is proxied into the number of Follow-up to Audit Result in accordance with the Recommendations using a ratio scale, while the Quality of Financial Reports as a dependent variable is a categorical or dummy variable proxied into the audit opinion using a nominal scale (WTP is coded 1 and other than WTP is coded 0).

RESULTS AND DISCUSSION

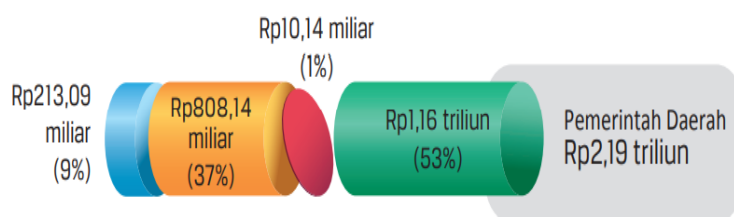
Follow-up on Recommendations from the 2015-2019 LKPD Audit Results

BPK monitored 148,762 recommendations on the results of the 2015-30 June 2019 audit period amounting to Rp31.48 trillion to 542 regional governments. The results of the monitoring of follow-up recommendations are as follows. Recommendations that have been followed up in accordance with the recommendations are 91,262 recommendations (61.6%) amounting to Rp15.84 trillion. A total of 45,496 recommendations (30.5%) amounting to Rp12.85 trillion are not in accordance with the recommendations. A total of 11,750 recommendations (7.8%) amounting to Rp2.55 trillion have not been followed up. A total of 254 recommendations (0.1%) amounting to Rp242.47 billion cannot be followed up. Regarding these recommendations, the entity has followed up by submitting assets/deposits to the state/regional treasury amounting to Rp6.33 trillion.



Source: IHPS I, 2020

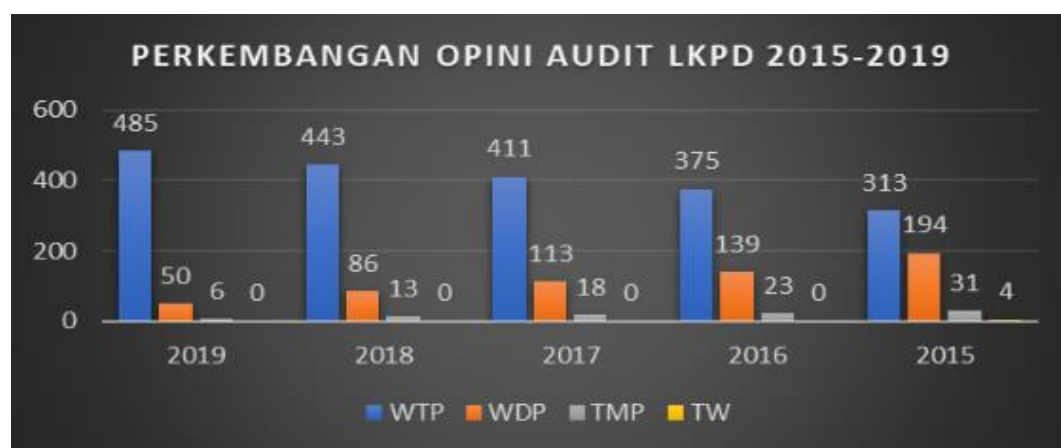
The results of monitoring in the regional government showed that there was a regional loss of Rp2.19 trillion with a settlement rate consisting of installments of Rp213.09 billion (9%), repayment of Rp808.14 billion (37%), and write-off of Rp10.14 billion (1%). The remaining loss in the regional government was Rp1.16 trillion (53%).



Source: IHPS I, 2020

Quality of Regional Government Financial Reports for the 2015-2019 period

The development of opinion from 2015 to 2019 has increased by an average of 12% per year as presented in the graph below:



Source: IHPS I, 2020

In 2019, the quality of the Regional Government Financial Report (LKPD) increased when compared to the 2018 LKPD, this can be shown by an increase in WTP opinions of 8%, namely from 443 (82%) of 542 LKPDs in 2018 to 485 (90%) of 541 in 2019.

The increase in opinion occurred because the local government has made efforts to improve the weaknesses that occurred in previous years as recommended by the BPK Auditor. Based on IHPS I 2020. The local government has improved and corrected the school operational assistance (BOS) treasurer's cash records in accordance with the confirmed source documents, then recalculated the balances and made corrections to the inventory presented in the financial statements. The local government has gradually traced and updated assets on the goods inventory card (KIB) and capitalized assets, both buildings, buildings, road assets, and irrigation and network assets, to then correct the calculation of the current year's depreciation expense and its accumulated depreciation.

In addition, the regional government has also conducted an inventory of other assets in the form of roads and land areas under the road where the results are capitalized into the parent asset, and the transfer of assets to the village. Issuing a letter of request for assessment and/or determination by the BPK for cash deficits, absolute responsibility letters (SKTJM), temporary release letters, and in installments returning cash deficits to the regional treasury. In the APBD, the regional government budgets BOS fund expenditures and reports them in the financial report, the regional government also recovers excess payments for goods and services expenditures by depositing them into the regional treasury. Recovering excess capital expenditures by depositing them into the

regional treasury and taking civil legal action for excess payments and has been processed by the court.

Follow-up on Audit Result Recommendations and their Impact on the Quality of Regional Government Financial Reports

The results of the Hosmer and Lemeshow Test measured using Chi-square produce a probability of 0.252 where 0.252 is greater than 0.05, then the null hypothesis is accepted meaning the model is able to predict its observation value or it can be said that the model is acceptable because it fits the observation data therefore this regression model is feasible to be used in conducting further analysis. (Ghojali, 2013).

Hosmer and Lemeshow Test

Step	Chi-square	df	Sig.
1	10.194	8	.252

The test results when the independent variables were not included in the model with a sample size of 542, the output results (table 4.2) obtained an initial -2 Log Likelihood (LL) value (Block number = 0) of 355,892, this is significant with an alpha of 5% so that the null hypothesis is rejected, this indicates that the model with only constants does not fit the data.

Table 4.2
Block 0 : Beginning Block
Iteration History^{a,b,c}

Iteration	-2 Log likelihood	Coefficients Constant
Step 0		
1	375,777	1,594
2	356,474	2,074
3	355.893	2.177
4	355.892	2.181
5	355.892	2.181

- a. Constant is included in the model.
- b. Initial -2 Log Likelihood: 355.892
- c. Estimation terminated at iteration number 5 because parameter estimates changed by less than.001.

Tabel 4.3
Block 1 : Method Enter
Iteration History^{a,b,c,d}

Iteration	-2 Log likelihood	Constant	Tindak Lanjut
Step 1			
1	355.699	2.343	-.004
2	328.166	3.386	-.007
3	326.511	3.752	-.008
4	326.500	3.784	-.008
5	326.500	3.784	-.008

- a. Method: Enter
- b. Constant is included in the model.
- c. Initial -2 Log Likelihood: 355.892
- d. Estimation terminated at iteration number 5 because parameter estimates changed by less than.001.

Furthermore, after the independent variables are entered into the regression model, the final -2 Log Likelihood (LL) value (Block number = 1) is 326,500 (table 4.3). There is a

decrease between the initial and final -2 Log Likelihood of 29,392, the decrease in LL proves that this regression model is running well. Because, the decrease in likelihood shows that the hypothesized model fits the data (Ghozali, 2011:340)

Table 4.5

Model Summary

Step	-2 Log likelihood	Cox & Snell R Square	Nails R Square
1	326,500 ^a	.053	.110

a. Estimation terminated at iteration number 5 because parameter estimates changed by less than .001.

Table 4.5 shows the Cox & Snell R Squared value of 0.053 and Nagelkerke R of 0.110, which means that the ability of the independent variable to explain the dependent variable is 11.0% and there are 89.0% other factors outside the model that explain the dependent variable.

The predictive power of the regression model to predict the chances of obtaining a WTP opinion (quality financial report) by the local government can be shown in the classification matrix.

Tabel 4.5

Classification Table^a

Observed	Predicted	Kualitas Laporan Keuangan		Percentage Correct
		Tidak Berkualitas	Berkualitas	
1	Tidak Berkualitas	4	51	7.3
	Berkualitas	3	484	99.4
Overall Percentage				90.0

a. The cut value is .500

The output results (Table 4.5) show that in the prediction column there are 487 quality Regional Government Financial Reports, the actual observation results of quality Regional Government Financial Reports are 484 with a percentage of 99.4% (484/487), while for non-quality Regional Government Financial Reports there are 55, and in the actual observation results there are 4 non-quality with a percentage of 7.3% (4/51). Overall, the accuracy of the model in this study is 90.0%.

Tabel 4.6

Variables in the Equation

Step	Tindak Lanjut	B	S.E.	Wald	df	Sig.	Exp(B)	95% C.I. for EXP(B)	
								Lower	Upper
1 ^a		.046	.009	28.71	1	.000	1.048	1.030	1.065
	Constant	-.445	.470	.895	1	.344	.641		

a. Variable(s) entered on step 1: Tindak Lanjut.

Test Results (table 4.6), the significance value (Sig.) of the Follow-up to Audit Result Recommendations variable is 0.000 and has a beta coefficient value (B) of 0.046 which indicates that the Follow-up to Audit Result Recommendations variable has a positive effect on the quality of Regional Government financial reports because Sig. 0.000 is smaller than the significance level of 0.05.

The constant value of -0.445 indicates that if the follow-up value is 0 or the audit recommendation is not followed up, the quality of the financial report will decrease by -

0.445. Furthermore, the Beta coefficient of β .046 indicates that by following up on the audit recommendation, the quality of the financial report will increase, in other words, the follow-up of the audit recommendation can improve the quality of the financial report, the higher the follow-up of the recommendation, the better the quality of the financial report

The BPK conveys audit findings and provides recommendations for improving financial management and accountability in the regional government environment. The audit findings contain problems including problems of weaknesses in the internal control system (weaknesses in the accounting and reporting control system, weaknesses in the budget implementation control system and weaknesses in the internal control structure), problems of inefficiency, ineffectiveness, and problems of non-compliance with the provisions of laws and regulations. Findings containing these problems can result in losses, potential losses, and shortfalls in revenue. For these problems, the BPK has provided recommendations for follow-up.

The local government seeks to follow up on the recommendations of the audit results, it is realized that by following up on the recommendations it will be able to improve the financial management system, increase compliance with laws and regulations, and internal control will be more effective, programs/activities can be implemented more economically, effectively and efficiently, losses can be prevented/recovered immediately, state/regional revenues can be increased. The Indonesian Institute of Accountants stated that significant internal control deficiencies (material weaknesses) are caused by management's failure to take corrective action appropriately (IAPI, 2013). (Aikins, 2012) found that inaccurate document maintenance of control weakness issues does not strengthen the accountability of public entities.

Follow-up of previous year's audit results will be the auditor's consideration in determining audit risk. Follow-up of previous period's audit results is an effort to improve audit findings based on auditor recommendations, so that the same findings do not recur in the following period. Effective internal control in the current year can provide stakeholders with an overview that programs/activities can be implemented more economically, effectively and efficiently and the possibility of misstatements in the financial statements in the following year is also relatively small.

Accuracy, precision, and accuracy in the input process, transaction processing, and document verification are very important in improving the accuracy of account balances in financial statements. The more effective internal control is, the more factors related to fraud in financial statements and misuse of assets can be minimized. If the effectiveness of internal control increases, it means that the entity's records are guaranteed to be accurate and reliable so that the entity's assets can be protected. Thus, the risk of misstatement can be avoided and the financial statements presented can be ensured to be more accurate, or in other words, the quality of the financial statements produced will be better and the criteria for providing an opinion will be met so that the greater the opportunity to obtain a WTP opinion.

The results of this study confirm the results of the study (Djanegara, 2017) that the higher the level of completion or follow-up of improvements to weaknesses in internal control, the higher the quality of LKPD. The more follow-up audits carried out, the better the financial management so that the opinion obtained in the next period is better. This result is also in line with the results of the study (Sari et al., 2015), (Tresnawati & Nur Apandi, 2016) which obtained the results that follow-up audit results have a positive effect on audit opinions where good audit opinions reflect the quality of financial reports. The results of this study confirm the statement (SPKN-BPK RI, 2017) that Follow-up on recommendations can improve accountability, transparency, economy, efficiency, and effectiveness in the management and responsibility of state finances.

CONCLUSION

Based on the results of the research conducted regarding the Follow-up to Recommendations and the Quality of Regional Government Financial Reports for the

2015-2019 period, the following conclusions can be drawn: BPK monitored 148,762 Recommendations worth IDR31.48 trillion to 542 Regional Governments in the 2015-2019 period, Recommendations that have been followed up in accordance with the recommendations are 91,262 (61.6%) of IDR15.84 trillion, 45,496 recommendations (30.5%) of IDR12.85 trillion are not in accordance with the recommendations, 11,750 recommendations (7.8%) of IDR2.55 trillion have not been followed up, 254 recommendations (0.1%) of IDR242.47 billion cannot be followed up. Regarding these recommendations, the entity has followed up by submitting assets/deposits to the state/regional treasury of IDR6.33 trillion.

The development of opinions for the 2015-2019 period experienced an increase of an average of 12% per year. From the government side, the WTP opinion has been achieved by 100% by all provincial governments, in district governments the WTP opinion was achieved by 364 (88%) of 415 district governments, while in city governments the WTP opinion was achieved by 87 (94%) of 93 city governments. The increase in the quality of the opinion is an indicator of the increase in the quality of the financial report because the quality of the opinion reflects that the financial report has been presented completely, accurately, in accordance with accounting principles and no material misstatements were found.

The results of the binary logistic regression test obtained a significance value (Sig.) of the Follow-up to Audit Result Recommendations variable of 0.000 and had a beta coefficient value (B) of 0.046, indicating that the Follow-up to Audit Result Recommendations had a positive effect on the quality of the Regional Government's financial reports. Thus, it means that the Follow-up to Audit Result Recommendations can improve the quality of financial reports. The higher the follow-up to audit result recommendations, the better the quality of the financial reports.

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