

The Mediation of Financial Report Information Quality on Governance Based on Apparatus Competence and Internal Control Systems

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This study aims to examine the intervening influence of the quality of financial report information on governance based on the competence of personnel and the internal control system in the Makassar City Government. The objective of this research is to analyse the direct and indirect effects between the independent, dependent, and intervening variables. The data collection techniques (instruments) used include observation, questionnaires, and documentation. The population in this study comprises 44 regional work units (SKPD) in the Makassar City Government, consisting of 687 individuals selected purposively. The sample size of 268 respondents was determined using the Solving formula. Data analysis was conducted using Structural Equation Modelling (SEM) with the SmartPLS program. The results of the study indicate that competence has a significant effect on the quality of financial report information. The internal control system also has a significant effect on the quality of financial report information. However, competence does not significantly contribute to government governance. Similarly, the internal control system does not significantly enhance government governance. The quality of financial report information has a positive and significant impact on government governance. The findings suggest that improvements are needed in the competence area, particularly in enhancing independence in performing core duties and functions. Regarding the internal control system, there is a need for better implementation to identify the added value in each aspect of governance.

1. Introduction

The development of government in Indonesia has led to the implementation of good governance at both central and regional levels (Mondo, 2023). Financial information plays a crucial role in achieving good governance (Tahar et al., 2023). The need for quality information is relevant and essential in assessing financial information for the purpose of good governance (Nur Fadji et al., 2023). Financial reports provide various pieces of information considered in accordance with reporting standards, which are produced based on fundamental characteristics of relevance and representativeness (Hong Nurng & Hanh Dao, 2022).

The quality of financial information needed by both central and regional governments reflects an entity adhering to applicable financial standards (Firmansyah, 2022). Generally, the quality of financial reports serves as basic information in decision-making in economic transformation, encompassing intrinsic, contextual, representative, accessibility, and responsibility factors linked to data usage in generating various pieces of information and diverse measurement characteristics for assessing information quality (Osadchy et al., 2022). The determination of integrated financial reports typically includes assets, liquidity, income, expenses, and profits (Mashuri, 2023). This quality of information is necessary for influencing the five principles of governance implemented by the government.

Improving good governance is inseparable from the contribution of the quality of financial reports (Solihin et al., 2020). This contribution affects the application of good governance principles to civil service regulations (Muhammad, 2019). The five principles of good governance include transparency, accountability, responsibility, independence, and fairness in achieving effective governance (Ruth, 2021). Therefore, good governance requires quality financial report information, which is considered in evaluating governance that can be well implemented in financial governance (Azhar, 2020).

It is evident that the quality of financial report information affects the actualization of good governance (Safkaur et al., 2019). To support this influence, the competence of officials and a robust internal control system are needed to ensure the quality of financial report information for good governance (Anto, 2023). The competence of officials is a major consideration in influencing the quality of financial report information prepared by institutions or individuals (Dang Ngoc et al., 2023). Competence elements play a significant role in performing one's main duties and functions based on knowledge, skills, experience, and attitude (Ahmad et al., 2021).

Usually, the role of officials' competence in government directly and indirectly contributes to improving work quality and governance (Karyatni, 2020). Strengthening competence based on knowledge can provide clarity of information according to the required reporting standards (Puspitasari, 2021). Skills are crucial in actualizing quality work (Ahmad et al., 2021). Experience drives the realization of work quality according to standards, variations, and qualifications (Bawono et al., 2021). Attitude is important in decision-making to determine good work quality (Maneewan & Kittipol, 2022). Thus, the competence of officials influences the quality of financial report information and good governance.

In addition to competence, a guaranteed internal control system is also needed. The internal control system directly and indirectly affects the quality of information and good governance (Xaverius & I Made, 2022). The internal control system is actualized in an organization in such a way to ensure goal achievement (Twaha et al., 2021). In government, the internal control system involves organized and orderly control or regulation of activities, information, and financial monitoring (Kathleen & Devon, 2021). It is proven that the internal control system directly and indirectly affects the quality of financial report information and governance.

Considering the importance of officials' competence and the internal control system implemented by the government in improving the quality of financial report information for good governance, it is necessary to find a novelty that differs from previous research results by examining differences and similarities between this research and previous studies. Therefore, it is important to observe the competence of officials and the internal control system concerning the quality of financial report information as an intervening variable that connects its influence on governance in the government.

2. Methodology

The research location was conducted at the Makassar City Government as the research object. This study observes the intervening variable of the quality of financial report information on governance as the ending variable, based on the competence of officials and the internal control system as independent variables. This survey research uses a quantitative approach. Primary and secondary data are the data sources used for weighting data tabulation. Data collection techniques (instruments) from observation and questionnaire distribution are based on a population of 44 Regional Work Units (SKPD) consisting of 687 people, and a sample of 268 respondents determined using the Slovin formula (Singarimbun & Effendi, 2017). The research hypothesis was answered based on inferential statistical data analysis using

SEM with SmartPLS software, starting from model measurement (outer model), structural model (inner model), and hypothesis testing. Mediation effect testing can be done by calculating the variance accounted for (VAF) with the formula indirect effect/total effect. The total effect is the direct effect plus the indirect effect. Thus, VAF is a measure of how much the mediating variable can absorb the previously significant direct effect from the model without mediation.

3. Results and Discussion

The research results show that after evaluating the outer model, all indicators of each research variable are applied. The outer model evaluation includes two aspects: validity testing and construct reliability testing. Validity testing includes: (1) Factor Loadings Test, (2) Fornell-Larcker Criterion Test, and (3) Cross Loadings Test. According to Cooper and Schindler (2006), reliability can be measured by looking at the values of Cronbach's Alpha, rho_A, Composite Reliability, and Average Variance Extracted (AVE). Construct validity shows the degree of appropriateness of the use of a measurement with the theories used to define a construct. Construct validity is tested by measuring the strength of the correlation between the construct and its items. Construct validity is achieved if there is a strong correlation between the construct and its items and a weak relationship with other variables. In this study, the variables of officials' competence (X1), internal control system (X2), quality of financial report information (Y), and governance (Z) are first-order constructs. Furthermore, for the purpose of analysing construct validity and reliability, it is considered necessary to display the output results of the SEM Algorithm data processing using PLS software as presented in Figure 1.

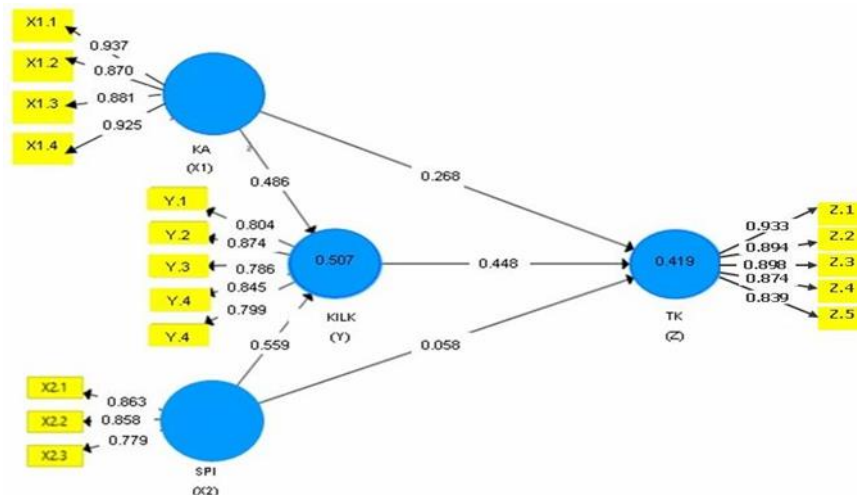


Figure 1. Output Loading Factor and Path Confection Smart PLS Algorithm

There are several methods for testing the validity of an indicator, including the Outer

Loading test, the comparison of values \sqrt{AVE} with correlation (Fornell-Larcker Criterion), and the Cross Loadings test. According to Chin (2018), an indicator is considered valid if it has a loading factor above 0.7, or at the very least 0.5, with respect to the intended construct. The table below presents the loading factor values for all indicators of the variable.

Table 1. Construct Loading Factor

	Original Sample (O)
x1.1 X1	0.937
x1.2X1	0.870
x1.3X1	0.881
x1.4X1	0.925
x2.1X2	0.863
x2.2X2	0.858
x2.3X2	0.779
y.1Y	0.804
y.2Y	0.874
y.3Y	0.786
y.4Y	0.845
y.5Y	0.799
z.1Z	0.933
z.2Z	0.894
z.3Z	0.898
z.4Z	0.874
z.5Z	0.839

In Table 1, all indicators for each construct exhibit loading factors (original sample) exceeding 0.7. This indicates that all indicators are valid in reflecting their respective constructs. Fornell and Larcker (2018) also present a method for testing discriminant validity among two or more factors/constructs. This involves comparing the average variance extracted \sqrt{AVE} for each construct with the shared variance between constructs. A measurement model demonstrates good discriminant validity if the \sqrt{AVE} for a variable exceeds the correlations with other variables. The results of the Fornell-Larcker Criterion test are presented in Table 3.

Table 2. Testing of Fornell-Larcker Criterion

	X1	X2	Y	Z
X1	0,869			
X2	-0,056	0,882		
Y	0,541	0,628	0,851	
Z	0,459	0,371	0,637	0,970

Table 2 demonstrates that the square root values of the AVE for each variable are greater than the correlations with other latent variables. Consequently, based on the results of the Fornell-Larcker Criterion test, the constructs can be considered valid. The Cross Loadings test is utilized to assess the discriminant validity of the measurement model indicators. If the correlation of an indicator with its own construct is higher than its correlation with other constructs, the construct is said to possess high discriminant validity.

Table 3. Cross Loading in Testing of Discriminant Validity

	X1	X2	Y	Z
X1.1	0,937	0,049	0,398	0,426
X1.2	0,870	-0,034	0,338	0,410
X1.3	0,881	-0,039	0,344	0,386
X1.4	0,925	-0,051	0,258	0,368
X2.1	-0,023	0,863	0,340	0,477
X2.2	-0,040	0,858	0,214	0,467
X2.3	-0,074	0,779	0,053	0,350
y.1	0,378	0,412	0,804	0,329
y.2	0,401	0,483	0,874	0,537
y.3	0,318	0,380	0,786	0,485
y.4	0,302	0,537	0,845	0,463
y.5	0,422	0,333	0,799	0,361
z.1	0,286	0,313	0,329	0,933
z.2	0,381	0,208	0,537	0,894
z.3	0,305	0,199	0,485	0,898
z.4	0,258	0,185	0,544	0,874
z.5	0,348	0,139	0,388	0,839

Table 3 shows that each indicator has the highest cross-loading value on its latent variable. This indicates that all indicators meet the discriminant validity in the Cross Loadings test. Therefore, all indicators are suitable for inclusion in further analysis.

The reliability of a construct indicates the consistency of results in measuring a concept or variable (Cooper and Schindler, 2018). Reliability can be measured by examining the values of Cronbach's Alpha and Composite Reliability. Cronbach's Alpha measures the lower bound of a construct's reliability value, while Composite Reliability measures the actual value of a construct's reliability (Salisbury et al., 2022). The rule of thumb is that Cronbach's Alpha, rho_A, or Composite Reliability values should be greater than 0.7. However, if the results are close to 0.7 (such as 0.6), and the AVE is greater than 0.5, this is still acceptable in exploratory studies (Hair et al., 2019). Based on the data processing results, Table 5 presents the values of Cronbach's Alpha, rho_A, Composite Reliability, and AVE.

Table 4. Cronbach's Alpha and Composite Reliability Score

	Cronbach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)
X	0,938	0,945	0,945	0,739
1	0,785	0,825	0,872	0,694
X	0,892	0,890	0,928	0,810
2	0,881	0,888	0,915	0,680
Y				
Z				

Table 4 demonstrates that the values for Cronbach's Alpha, rho_A, and Composite Reliability for each construct are all greater than 0.70, while the Average Variance Extracted (AVE) for each construct is greater than 0.50. Consequently, all the measurements used in this study are deemed reliable.

The evaluation of the inner model encompasses two main aspects: the assessment of model fit (goodness of fit) and the evaluation of the influence of exogenous variables on endogenous variables through hypothesis testing. The influence assessment includes both direct and indirect effects. The evaluation of model fit and the influence of exogenous variables on endogenous variables are based on the SEM PLS bootstrapping output, as illustrated in Figure 2.

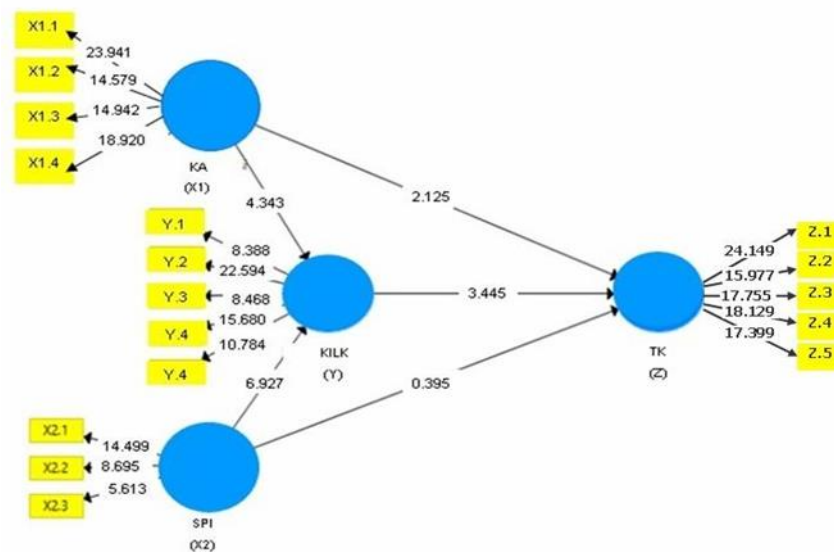


Figure 2. Output Loading Factor and Path Coefficient Smart PLS Algorithm

In Figure 2, there are two exogenous variables, namely, civil servant competence (X1) and internal control systems (X2), one intervening variable, which is the quality of financial reporting information (Y), and one endogenous variable, governance (Z). The endogenous variable governance (Z) has three predictors including civil servant competence (X1), internal control systems (X2), and the quality of financial reporting information (Y). Meanwhile, the intervening variable quality of financial reporting information (Y) has two predictors including (X1) and internal control systems (X2). In Figure 2, the quality of financial reporting information (Y) acts as an intervening variable.

The structural model resulting from PLS processing needs to be evaluated using R-square for each dependent variable, and Q square predictive relevance to observe the effects of exogenous latent constructs on their endogenous variables. For the purpose of evaluating the Goodness of Fit Inner Model, Table 6 is presented, which contains the R-square coefficients

for each endogenous variable.

Table 5. R-Square Score

Variables	R Square
Financial Reporting Information Quality (Y)	0,507
Governance(Z)	0,409

Table 5 displays an R-square value of 0.507 for the variable of financial reporting quality (Y) and 0.409 for governance variable (Z). This indicates that the variation in the financial reporting quality variable (Y) can be explained by the combined competencies and motivations by 50.7 percent. The remaining 49.3 percent is accounted for by factors other than competencies of officials and internal control systems. Furthermore, the governance variable (Z) can be explained by competencies of officials, internal control systems, and IT utilization by 40.9 percent. The remaining 59.1 percent is attributed to factors other than these three variables.

Based on the two R-squared coefficients in Table 6, the magnitude of the Q2 coefficient or the Stone Geiser Q-Square test (Stone, 1974; Geisser, 1974, and Ghazali, 2011) can also be calculated:

$$Q2 = 1 - \{(1 - R12) (1 - R22)\}$$

$$Q2 = 1 - \{(1 - 0,507) (1 - 0,409)\}$$

$$Q2 = 1 - \{(0,493)(0,591)\}$$

$$Q2 = 1 - (0,291) = 0,709$$

The calculation results obtained a Q2 of $0.709 > 0.35$, indicating that this model exhibits strong predictive prevalence. This implies that a significant portion of the variation in the dependent variable can be explained by the variables included in this research model. A value of 0.709 or strong predictive prevalence suggests that the resulting model is suitable for prediction purposes.

During hypothesis testing, it is crucial to consider the direct influence and significance indicated by the directional arrows between exogenous latent variables towards the endogenous variable. The exogenous variables encompass the competency of the apparatus (X1) and internal control systems (X2). The quality of financial report information (Y) serves as an intervening variable. The endogenous variable is governance (Z). For the purpose of hypothesis testing, Table 7 is presented, containing path coefficients, t-statistics, and P-values.

Table 6. Path Coefficient, T-Statistics, P-Values

	Original Sample (O)	T Statistics (O/STDEF)	P Values	Significant
X1Y	0,486	3,242	0,001	Significant
(β_1)	0,559	5,916	0,000	Significant
X2Y	0,268	1,025	0,155	Not
(β_2)	0,058	0,283	0,385	Significant
X1Z	0,448	2,334	0,010	Not
(β_3)				Significant
X2Z				Significant
(β_4)				
YZ (β_5)				

Hypothesis Testing 1:

The improvement of civil servant competence contributes to the quality of financial report information. This hypothesis suggests a positive influence denoted by $\beta_1 > 0$, thus a one-tailed test will be conducted on the right side. H_a is accepted or H_0 is rejected if the t-value $>$ critical t and $P < \alpha$. Referring to the t-table in Ghazali (2019) for a one-tailed test with $df > 40$ at a significance level (α) of 5%, the critical t-value is obtained as 1.684. The hypothesis testing on the positive influence of civil servant competence on financial report information quality is based on the results of SEM PLS data processing, as presented in Table 2. Further, in Table 3 for the influence of civil servant competence on financial report information quality (X1 to Z), it is observed that the coefficient $b_1 = 0.486$, T-statistics = 3.242, and P-value = 0.001. The magnitude of T-statistics = 3.242 $>$ critical t = 1.684, and P-value = 0.001 $<$ $\alpha = 0.05$, thus statistically at $\alpha = 5\%$, H_a is accepted or H_0 is rejected. This indicates that the increased civil servant competence affects the quality of financial report information, demonstrating its significance. This proves that competence in terms of knowledge, skill, experience, and attitude has a significant positive relationship and influence in enhancing the quality of financial report information.

Hypothesis Testing 2:

Internal control systems contribute to the quality of government financial report information. The hypothesis stating a positive influence denoted by $\beta_2 > 0$, thus a one-tailed test will be conducted on the right side. H_a is accepted or H_0 is rejected if the t-value $>$ critical t and $P < \alpha$. Referring to the t-table in Ghazali (2019) for a one-tailed test with $df > 40$ at a significance level (α) of 5%, the critical t-value is obtained as 1.684. The hypothesis testing on the positive influence of internal control systems on financial report information quality is based on the results of SEM PLS data processing, as presented in Table 2. Further, in Table 3 for the influence of internal control systems on financial report information quality (X2 to Z), it is observed that the coefficient $b_2 = 0.559$, T-statistics = 5.916, and P-value = 0.000. The magnitude of T-statistics = 5.916 $>$ critical t = 1.684, and P-value = 0.000 $<$ $\alpha = 0.05$, thus statistically at $\alpha = 5\%$, H_a is accepted or H_0 is rejected. This proves that internal control systems in the form of financial activities, information, and monitoring have a significant positive relationship and influence in affecting government financial report information quality.

Hypothesis Testing 3:

Civil servant competence contributes to governance. The hypothesis stating a positive influence denoted by $\beta_3 > 0$, thus a one-tailed test will be conducted on the right side. H_a is accepted or H_0 is rejected if the t-value $>$ critical t and $P < \alpha$. Referring to the t-table in Ghazali (2019) for a one-tailed test with $df > 40$ at a significance level (α) of 5%, the critical t-value is obtained as 1.684. The hypothesis testing on the positive influence of civil servant competence on governance is based on the results of SEM PLS data processing, as presented in Table 2. In Table 3, for the influence of civil servant competence on governance (X1 to Z), it is observed that the coefficient $b_3 = 0.268$, T-statistics = 1.025, and P-value = 0.155. The magnitude of T-statistics = 1.025 $<$ critical t = 1.684, and P-value = 0.155 $>$ $\alpha = 0.05$, thus statistically at $\alpha = 5\%$, H_0 is accepted or H_a is rejected. This indicates that competence in terms of knowledge, skill, experience, and attitude has a positive relationship and influence but is not significant in affecting governance. The lack of significance indicates that civil servant competence still needs improvement and enhancement, especially in relation to the autonomy of civil servants in implementing good governance.

Hypothesis Testing 4:

Internal control systems contribute to governance. The hypothesis stating a positive influence denoted by $\beta_4 > 0$, thus a one-tailed test will be conducted on the right side. H_a is accepted or H_0 is rejected if the t-value $>$ critical t and $P < \alpha$. Referring to the t-table in Ghazali

(2019) for a one-tailed test with $df > 40$ at a significance level (α) of 5%, the critical t-value is obtained as 1.684. The hypothesis testing on the positive influence of internal control systems on governance is based on the results of SEM PLS data processing, as presented in Table 2. In Table 3, for the influence of internal control systems on governance (X2 to Z), it is observed that the coefficient $b4 = 0.058$, T-statistics = 0.283, and P-value = 0.385. The magnitude of T-statistics = $0.058 < \text{critical } t = 1.684$, and $P\text{-value} = 0.385 > \alpha = 0.05$, thus statistically at $\alpha = 5\%$, H_0 is accepted or H_a is rejected. This proves that internal control systems in the form of financial activities, information, and monitoring have a positive relationship and significant influence in affecting governance.

Hypothesis Testing 5:

The quality of financial report information contributes to governance. The hypothesis stating a positive influence denoted by $\beta_5 > 0$, thus a one-tailed test will be conducted on the right side. H_a is accepted or H_0 is rejected if the t-value $>$ critical t and $P < \alpha$. Referring to the t-table in Ghazali (2019) for a one-tailed test with $df > 40$ at a significance level (α) of 5%, the critical t-value is obtained as 1.684. The hypothesis testing on the positive influence of financial report information quality on governance is based on the results of SEM PLS data processing, as presented in Table 2. In Table 3, for the influence of financial report information quality on governance (Y to Z), it is observed that the coefficient $b5 = 0.448$, T-statistics = 2.334, and P-value = 0.010. The magnitude of T-statistics = $2.334 > \text{critical } t = 1.684$, and $P\text{-value} = 0.010 < \alpha = 0.05$, thus statistically at $\alpha = 5\%$, H_0 is rejected or H_a is accepted. This means that the quality of financial report information in terms of intrinsic, contextual, representational, accessibility, and responsibility aspects should be considered in governance practices.

The influence of the competency of personnel (X1) and internal control systems (X2) on the quality of financial report information (Y) is guided by the magnitude of the path coefficients (b). In Figure 2 Table 3, the magnitude of the path coefficients for the influence of personnel competency (X1) ($b1 = 0.486$) and the influence of internal control systems (X2) ($b2 = 0.559$) is evident. Referring to path coefficients $b1$ and $b2$, the structural equation for the competency of personnel and internal control system's influence on the quality of financial report information can be formulated as follows:

$$Y = b1X1 + b2X2 + e1$$

$$Y = 0.486X1 + 0.559X2 + e2$$

There is a positive influence of personnel competency on the quality of financial report information, and there is a positive influence of internal control systems on the quality of financial report information. This implies that if personnel competency and internal control systems are good, the quality of financial report information can be achieved. Since the coefficient $b1 = 0.486$ and $b2 = 0.559$, this means that the achievement and quality of financial report information are more dominantly influenced by the internal control system. This implies that in the quality of financial report information, the internal control system is 1.18 times more influential than personnel competency.

The influence of personnel competency (X1), internal control systems (X2), and the quality of financial report information (Y) on governance (Z) is guided by the magnitude of the path coefficients (b). In Figure 3, the magnitude of the path coefficients for the influence of personnel competency (X1) ($b3 = 0.268$), the influence of internal control systems (X2) ($b4 = 0.058$), and the influence of the quality of financial report information (Y) ($b5 = 0.448$) is apparent. Referring to path coefficients $b3$, $b4$, and $b5$, the structural equation for personnel competency, internal control systems, and the quality of financial report information's influence on governance can be formulated as follows:

$$Z = b_3X_1 + b_4X_2 + b_5Y + e_2$$

$$Z = 0.268X_1 + 0.058X_2 + 0.448Y + e_2$$

There is a positive influence of personnel competency, internal control systems, and the quality of financial report information on governance. This means that if personnel competency, internal control systems, and the quality of financial report information increase, governance will also improve. Conversely, if there is a decrease, governance will decrease as well. Since the quality of financial report information has the largest path coefficient ($b_5 = 0.448$), it means that the contribution of the quality of financial report information is most dominant in enhancing governance compared to other variables.

4. Conclusion

Based on the analysis and discussion above, it can be concluded that the competence of civil servants significantly influences the quality of financial reporting information. Internal control systems also have a significant impact on the quality of financial reporting information. However, the competence of civil servants does not significantly contribute to governance. Likewise, internal control systems have not significantly improved governance. The quality of financial reporting information has a positive and significant effect on governance.

It is recommended that both competence and internal control systems need to be improved to enhance governance, as the results indicate that their influence on governance is not significant. Competence enhancement should focus on fostering the independence of civil servants in performing their duties effectively. Additionally, improvements in internal control systems should include assessments of systems that have not been well-implemented, particularly to ascertain the value addition necessary for every aspect of governance.

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