



Social perception on corruption and its influence on public legitimacy and open government (Indonesia)

Percepción social sobre corrupción y su influencia en la legitimidad pública y gobierno abierto

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Contents

- [1. Introduction](#)
 - [2. Literature review and hypotheses](#)
 - [3. Research method](#)
 - [4. Results and discussion](#)
 - [5. Conclusion](#)
- [Bibliography](#)

ABSTRACT:

This study attempts to analyze the extent of the effect of audit findings and transparency on corruption perception index in local government in Indonesia based on legitimacy theory. This study uses STATA-12 and Ordinary Least Square (OLS) by analyzing the data of 95 observations of Corruption Perception Index (CPI) of Transparency International Indonesia. The findings indicate that the transparency positively impacts on the index; and the audit findings contained in the audit reports published by Audit Board of the Republic of Indonesia has no significant effect on the index. These results reveal the important function of transparency in reducing corruption practices and enhancing public trust and legitimacy on the local governments.

Keywords: Corruption Perception Index, Local Government, Audit Findings, Transparency, Indonesia

RESUMEN:

Este estudio intenta analizar el alcance del efecto de los hallazgos de la auditoría y la transparencia en el índice de percepción de la corrupción en el gobierno local de Indonesia basado en la teoría de la legitimidad. Este estudio utiliza STATA-12 y Ordinary Least Square (OLS) al analizar los datos de 95 observaciones del Índice de Percepción de la Corrupción (IPC) de Transparencia Internacional Indonesia. Los hallazgos indican que la transparencia tiene un impacto positivo en el índice; y los hallazgos de auditoría contenidos en los informes de auditoría publicados por la Junta de Auditoría de la República de Indonesia no tienen un efecto significativo en el índice. Estos resultados revelan la importante función de la transparencia para reducir las prácticas de corrupción y mejorar la confianza y legitimidad del público en los gobiernos locales.

Palabras clave: índice de percepción de la corrupción, gobierno local, resultados de la auditoría, transparencia, Indonesia

1. Introduction

Indonesia, as many developing countries do, faces an enormous social, economic and political problems related to the widespread corruption and bribes throughout the

government services and private business, characterized by increasing corruption cases, as data released by the Corruption Eradication Commission (2014). Until August 31, 2014, the number of corruption cases handled by Indonesia's Corruption Eradication Commission (Indonesian: *Komisi Pemberantasan Korupsi*), from 2004-2014 kept increasing, i.e. consisting of 645 cases of preliminary investigation, 393 cases of full investigation, 309 cases of prosecution, 270 permanent legal force cases, and 282 cases of execution (KPK, 2014). These facts do not include the corruption cases handled nationally and locally by prosecutors and police department amounting to 9.868 cases.

Olken's (2007) study shows the effectiveness of the government auditor's surveillance and the influence of the two control strategies i.e top-down supervision performed by the government auditors and bottom-up supervision through public participation in reducing the level of misuse of funds in development projects in the rural areas. However, these studies do not specifically analyze the effect of audit report on the corruption index and the extent of transparency of that. Meanwhile, despite the presence and function of accounting and governance auditing that has been recognized and improved since the enactment of the package of national financial acts in 2003-2004, the functioning of accounting has not yet been able to demonstrate its optimum contribution in reducing corruption cases in Indonesia (Furqan, 2011).

The purpose of this study is to extend the applicability of legitimacy theory in the public sector especially in the local government, by analyzing Act No. 14 of 2008 on Public Information Openness. The law, which consists of 64 articles, essentially gives an obligation to every Public Agency to open access for every applicant for public information to obtain public information, except for certain information classified as state secrets (Suhartono, 2018). Despite the fact that legitimacy theory is more applicable in private context, and corruption and CPI are studied much in public sector, some studies have attempted to combine these both variables. Furthermore, although CPI is not actually able to measure the level of absolute corruption, it can be used to determine the level of public trust as a basis for public sector legitimacy. For instance, a study of Xin and Rudel (2004), Kurniawan (2017) show that the perception on experienced corruption is more likely to reduce citizens' trust in legitimacy of the government. Hence, low CPI is perceived as a threat of legitimacy, while the transparency is a way to regain the public trust and government legitimacy by providing more transparent financial report. Moreover, O'Donovan (2002) reveals the importance of the role of annual report disclosures to gain, maintain, and repair legitimacy. Furthermore, this study also examines the impact of audit findings as an object of transparency on CPI. Therefore, this study contributes to empirically analyze the extent of the relationship between the audit findings on corruption cases in the local governments and corruption perceptions index (CPI) in Indonesia.

2. Literature Review And Hypotheses

The legitimacy of the local government relies heavily on its performance that meets the expectation of the people. Particularly, the public can judge the government's behavior by using the results of the auditor report in assessing the performance of financial management. Ferraz and Finan (2008) find that the audit report of local government discloses the corruption activities, which would then affect the outcome of elections or electoral votes as the source of government legitimacy. Similarly Malagueño et al. (2010) reveal that the accounting and auditing quality significantly affect the perceived level of corruption in a country. The study also implies that the higher the quality of accounting and auditing report, the lower the level of corruption perceived by society. Thus, we propose the following hypothesis:

H1 The audit findings negatively affect the corruption perception index.

Setyaningrum et al. (2014) finds that the publication of audit findings significantly affects audit findings of the following year. Similarly, DiRienzo (2007) emphasizes the role of transparency on the decrease in corruption. Reinikka and Svensson's (2005) study on the government of Uganda further explains that transparency is the determining factor on the size of the role of the government's auditing report. Moreover, they state that Ugandan

government's publication and socialization regarding education funds allocated to primary schools, resulting in a significant decline in embezzlement of education funds, leading to an increased public trust in the education in Uganda. Davis (2004) and Lindstedt and Naurin (2010) reveal the link between the reduction of corruption and the accountability of institution. Bertot et al. (2010) state that the access for information indicates public response of corruption cases. Hence, it can be said that the transparency of the audit report impacts the public perception. Thus, the following hypothesis is proposed:

H2 The transparency positively affects the corruption perception index

H3 The transparency increases the negative influence of audit findings on the corruption perception index.

3. Research Method

By using purposive sampling, this study used a sample amounting to 95 samples of municipalities and cities in Indonesia obtained from two main sources, i.e auditing reports of Financial Investigation Bureau of Indonesia and survey results of Indonesian Corruption Perception Index (CPI) published by Transparency International Indonesia (TII) in 2006-2014. The survey of the Corruption Perception Index (CPI) conducted by Transparency International Indonesia (TII) during 2006-2014 has now been carried out 3 times. In 2006, the survey was conducted in 32 municipalities/regencies, in 2008 conducted in 50 municipalities/regencies and in 2010 conducted in 50 municipalities/regencies. While related to the Audit Board of the Republic of Indonesia (*Badan Pemeriksa Keuangan/BPK*) audit report on Local Government Financial Reports, because the BPK published the reports on the previous financial year in 2 stages, namely in semester 1, it published in September of the current year, and semester 2, it published in March of the following year. Accordingly, the audit findings for the 2006 fiscal year and the audit opinion on the 2006 reports were published in full, not later than March 2008. Therefore, it can be said that the CPI in 2008 was assumed to be based on information on the audit report on the 2006 fiscal year report, while the CPI in 2010 was assumed to be based on information on the audit report on the 2008 fiscal year report. However, because there are data that are not complete then the sample that can be used in this study is only 95 samples.

Therefore, it can be said that the CPI in 2008 was assumed to be based on information on the audit report on the LKPD for the fiscal year 2006, while the CPI in 2010 was assumed to be based on information on the 2008 financial year LKPD audit report. complete then the sample that can be used in this study is only 95 samples.

This study used the auditor report as the independent variable, the corruption level as the dependent variable and the size of asset value of region (city or municipality) as the control variable.

The independent variable in this study is the auditor's report which was proxied by the number of audit findings, as used by Setyaningrum (2014) and Liu and Lin (2012). The variable that was interacted with the auditor's report was transparency. The measurement of the transparency variable was using dummy based on the issuance of Law Number 14 of 2008 concerning Public Information Openness, which, assuming after the issuance of the Law, has already had access to greater public information, including audit reports. In detail, for the CPI in 2008 and the previous year using a scale of "0" or not yet transparent, and the CPI above in 2008 using a scale of "1" or transparent.

The dependent variable in this study was the degree of corruption as measured by the Corruption Perception Index (CPI) of the local governments. The level of corruption of the Regional Government measured in this study is with the Corruption Perception Index referring to the scale used by DiRienzo, et al. (2007), Malagueño, et al. (2010), and Hartanto and Probohudono (2013). The corruption perception index ranges from 0 to 10, where 0 means that it is perceived as very corrupt, 10 is very clean.

The control variable used in this study is the variable size of local government. This variable is used based on the results of research by Liu and Lin (2012) and Hartanto and Probohudono (2013).

The data was analyzed by using the following equation. Since there is a potential for multicollinearity between the two variables examined, we analyze the proposed hypotheses by this regression:

$$CPI_i = \beta_0 + \beta_1 AR_i + \beta_2 TRD_i + \beta_3 LASSET * TRD_i + \beta_4 LnASSET_i + \epsilon_{i1} \quad (1)$$

Where:

CPI_i = Corruption Perception Index;

AR_i = Auditing Report (proxied by the number of audit findings of the bureau);

TRD_i = Transparency (Dummy, 1= after 2008; 0= 2008 and the previous years);

$LnASSET_i$ = Ln Asset Size of Local Government;

β_0 = intercept (constant)

β_{1234} = slope (coefficient);

ϵ_{i1} = residual error

4. Results And Discussion

4.1. Descriptive Analysis

This descriptive statistics analysis gives an overview of the sample used in the study with a description of the mean, the minimum and maximum value, standard deviation and variance of each variable examined. Based on the research sample of the 95 observed regions, the statistical description of the variables of corruption perception index and audit findings was obtained.

Table 1
Descriptive statistics

Variable	N	Mean	Min	Max	Stand. Dev	Variance
Corruption Perception Index (CPI)	95	4,74	2,97	6,71	0,72	0,52
Number of Audit Findings	95	86,34	28,00	163,00	31,38	985,02

This result reveals that the mean of CPI is 4.74 with the standard deviation of 0.72 and variance of 0.52, the minimum value of 2.97 and maximum of 6.71. This implies that the public perception of corruption in the local government in Indonesia is still very high, which is still below 7. In other words, the public perceives that corruption is still prevalent in the local government and none of the local governments are considered free of corruption, especially during the observation period in 2006-2014. The audit findings reveal the mean of the findings of 86.34 at the maximum value of 163, the minimum of 28, the standard deviation of 31.38 and the variance of 985.02.

4.2. Data Analysis

This study used the software of STATA-12 in analyzing the data. Before testing the hypotheses, the study firstly used the testing of assumption of Ordinary Least Square (OLS) toward regression model to estimate the unknown parameters in the above-mentioned linear model.

Table 2
Testing Result Of Assumption Of Ols

						Unadjusted p-
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Variable	n	Prob>z	VIF	1/VIF	Chi2	values
Corruption Perception Index	95	0.98	-	-	0.58	0.44
Audit Findings	95	0.57	1.39	0.718	0.19	0.64
Transparency	95	1.00	1.35	0.742	0.01	0.38
Asset/Size	95	0.00	1.06	0.941	0.03	0.58

The result shows that the variables of corruption perception index data, audit findings and transparency as the main variables used in this study are all normally distributed, except for the variable of asset size of the local government as the control variable that shows the probability value of <0.05 . Due to the normality problem of the control variable, then it is not able to be further analyzed in testing the hypotheses.

By using VIF and tolerance testing (1/VIF), the values of VIF for all the independent variables are <5 and the tolerance values are > 0.20 . Hence, it can be stated that there are no problems of multicollinearity in the regression model. Moreover, the testing of Szroeter's demonstrates the value of unadjusted p-values of > 0.05 in all the variables, so there is no problem of heteroscedasticity of the regression model variance since all the variables have constant values of variance.

Table 3
Hypothesis Testing (Without Interaction)

Variable	Coefficient	Stand. Err	t	P> (t)	Sig.
Constant	4.7291	0.2882	16.41	0.000	-
Audit Findings	-0.0019	0.0026	-0.73	0.718	-
Transparency	0.3485	0.1646	2.12	0.037	**
Corruption Perception Index = Dependent					
Prob > F = 0.016 **					
R-squared = 0.085					
Adjusted R-squared = 0.065					
Root MSE = 0.699					
** = 5%					

The result shows that the variables' effects are statistically significant at the level of 5% i.e. 0.01 or below <0.05 , although the audit findings and transparency variables together are only able to explain the corruption perception index in a weak effect 6.5%. The small value of the adjusted R square occurs since this study only focuses on accountability, and does not consider other factors such as monopoly and discretion as previously stated by Klitgaard (1998).

The test shows that the variable of audit findings negatively influences the Corruption

Perceptions Index (T value -0.73). However the p value shows the value of 0.718 or above the level of significance (0.05). Thus, statistically the first hypothesis stating that the audit findings negatively affect the corruption perception index is not supported.

The variable of transparency has the t-statistic value of 2.12 and p value of 0.037 or below the level (0.05), then statistically the hypothesis stating that the transparency positively affects the corruption perception index is accepted. This means that Act No. 14 of 2008 regarding public disclosure that provides a measurement of transparency of public financial management of local government has a better impact on corruption index, indicated by the positive value of coefficient of this variable than that before the enactment of the Act on Public Information Openness in 2008.

By using the above-mentioned equation, the testing of the third hypothesis was conducted by measuring the interaction between transparency and audit findings.

Table 4
Hypothesis Testing (With Interaction)

Variable	Coefficient	Stand. Err	t	P> (t)	Sig.
Constant	4.1525	0.2882	10.37	0.000	***
Audit Findings	0.0037	0.0037	0.98	0.718	-
Transparency	1.2788	0.4843	2.64	0.010	**
Transparency* Audit Findings	-0.0106	0.0051	-2.04	0.044	**
Corruption Perception Index	= Dependent				
Prob > F	= 0.007 ***				
R-squared	= 0.124				
Adjusted R-squared	= 0.096				
Root MSE	= 0.688				
** , ***	= 5%, 1%				

The testing reveals that the interaction between the transparency and audit findings provides a better explanation to the variation of the index that is reflected in the increase in the value of the adjusted R square to 0.096. The interaction brings a negative and significant impact on the index. Thus, the third hypothesis stating that the transparency increases the negative influence of the audit findings on corruption perception index is accepted. It means that the publication of the audit findings would be perceived by the public that the level of the corruption of the local government is high.

5. Conclusion

This result confirms the theory of the legitimacy, in which the local government would increase the performance of public finance management by reducing the negative findings of the audit report, to get legitimacy from the public. The study demonstrates the importance of transparency in reducing corruption practices that occur in the local government.

Transparency has a positive effect on better public perception of local government that is marked by the increase in the corruption index. On other hand, the transparency of the audit findings has a negative effect on the corruption perception index. When the audit

findings are published, it could lead to public perceptions on an increasing corruption in the local governments, which is characterized by a lower value of the index. However, the transparency has an important role in reducing corruption practices that occur in local government officials.

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[\[Index\]](#)

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