THE ROLE OF GOOD VILLAGE GOVERNANCE IMPLEMENTATION TOWARDS REDUCING FRAUD POTENTIAL AND ENSURING EFFECTIVE GOVERNMENT PERFORMANCE

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Purpose of the study: This research aimed to examine the effect of Good Village Governance (GVG), external supervision, and citizen participation on the fraud potential in village funds management and its consequent impact on village government performance.

Methodology: The sample studied involved 60 respondents including village officials in Demak Regency, Central Java, Indonesia. The data was collected. We use Structural Equation Model (SEM) and use WarpPLS tools to examine causality test among variables.

Main Findings: The results showed the implementation of GVG did not have a significant effect on the fraud potential in fund management while external supervision and citizen participation have a negative and significant effect. Furthermore, the GVG implementation and citizen participation were found not to have a significant influence on village government performance while external supervision and fraud have a negative and significant effect. Moreover, fraud has a very strong influence and it is the most dominant determinant of village government performance, therefore, it should be handled with serious attention.

Applications of this study: External supervision of village fund management is needed to reduce fraud and improve performance. In addition, the implementation of GVG can also support improved village government performance.

Novelty/Originality of this study: This research builds a model and examines the GVG concept model that can be a solution to the problem of fraud and the low performance of local governments in Indonesia.

Keywords: fraud; village government performance; good village governance; external supervision; citizen participation

INTRODUCTION

The Indonesian Government through Law number 6 of 2014 on Villages authorized village governments to manage certain funds for the development of villages. This led to the disbursement of IDR 20.7 trillion in 2015, IDR 46.9 trillion in 2016, and IDR 60 trillion in 2017 to 74,910 villages (Merdeka, 2017). The aim was to ensure effective, fair, and equal village-based programs (Law No. 6 of 2014, Article 72).

However, empirical facts have proven the misuse of this fund leading to the unfulfillment of this objective. According to the deputy chairman of the Corruption Eradication Commission (KPK), Laode, the irregularities observed in the management of village funds include fictitious procurement of goods and services, inflated budget, exclusion of the community in village deliberations, the use of village funds for personal gain, as well as weak supervision and embezzlement of village officials' salaries (Viva, 2017). Another method used is through the collaboration between the officials and law enforcement officers, especially the police. The data provided by ICW showed there has been a significant increase in the cases of village funds misuse since it was provided.
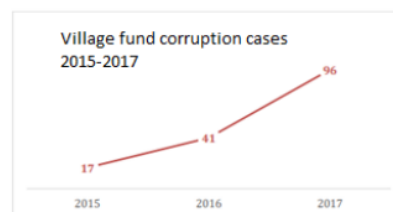

Figure 1. Village Fund Corruption Case

Source : (Indonesia Corruption Watch, 2018)

Some studies have reported the high rate of fund misuse is due to the low competence and quality of human resources and lack of supervision from the community (Mondale, Fahlevi, & Aliaman, 2017; Wibisono & Purnomo, 2017). Effective understanding and supervision have a positive impact on improving village financial accountability (Mondale et al., 2017; Wibisono & Purnomo, 2017). Moreover, based on the fraud theory, one of the causes of corruption in public organizations is pressure while it is mostly due to bad corporate governance in the private sector (Kadir, Kiswanto, Widarini, Gunawan, & Puspitasari, 2017).

Several works of research have also established a strong relationship between corporate governance and the occurrence of fraud (Kadir et al., 2017; Chen, Firth, Gao, & Rui, 2006; Mangala & Kumari, 2017; Eferakeya, Enaibre, & Offor, 2016). Activities of fraud were found to be dominant in companies with poor management systems (Dunn, 2004; Farber, 2005; Rezaee & Tuo, 2017). Therefore, there is a need for the establishment of an honesty culture in corporate organizations by

the management to reduce fraud potential (Halbouni, Obeid, & Garbou, 2016). This, however, means companies with good management also known as Good Corporate Governance (GCG) tend to have good finance (Jan, 2018).

This led to the possibility of implementing GCG as one of the solutions to reduce fraud in village funds in line with the 2015 Semarang State University Strategic Plan concerning the empowerment of the community's economy through the improvement of economic institutions to prosper and improve the welfare of the rural communities. Moreover, the village fund management involves social interaction between several stakeholders such as the central, regional and village governments, as well as the community.

Therefore, GCG implementation is needed by the village government to protect the interests of stakeholders and, more specifically, to ensure the funds are managed in accordance with the objectives without any misuse. This research was used to empirically prove the influence of GCG implementation on fraud potential in village fund management (In'airat, 2015; Larelle Chapple, Ferguson, & Kang, 2005; Lutui & 'Ahokovi, 2017; Matoussi & Gharbi, 2011; Shi, Connelly, & Hoskisson, 2017; Wilhelm, Communications, & Bilbao, 2016).

LITERATURE REVIEW

Literally, fraud means cheating and according to the Chartered Institute of Management Accountants (2009), it is a dishonest fraudulent act conducted for personal gain thereby causing harm to others. Webster's New World Dictionary also explains it as a fraudulent or deception activity performed for personal gain while the International Standards of Auditing Section 240 defines it as "... intentional actions by deceiving members of company management playing a role in corporate governance, employees, or third parties to obtain unfair or illegal profits".

Fraud is closely related to theft, corruption, conspiracy, embezzlement, money laundering, bribery, and extortion. This further led to the formulation of a map called fraud tree with three branches including corruption, asset misappropriation, and fraudulent statements by the Association of Certified Fraud Examiners (ACFE) (Baader & Krcmar, 2018). In the government sector, fraud is mostly in the form of corruption and it is often observed in developing countries, including Indonesia (Prabowo, Cooper, Sriyana, & Syamsudin, 2017). To analyse the occurrence of corruption in public organizations, there are several perspectives developed three and they include schemata, corruption normalization, and moral development theories (Prabowo et al., 2017).

Meanwhile, the development of a strong internal control system was recommended by COSO to guarantee a company's wealth, accuracy and correctness of accounting data, reliable financial statements, efficient and effective operation, and obedience to management policies, laws and regulations.

This research was, however, based on the use of the governance system as an effort to reduce the occurrence of fraud. This is necessary considering the fact there is no management structure in place to avoid fraudulent acts since the issuance of the regulation in 2014 which has created several challenges in implementing Village Fund Allocation (Abidin, 2015). Moreover, the fraudulent activities have been reported to be due to the ineffectiveness of village facilitators, inadequate coaching and supervision from the subdistrict head, government, Development Supervisory Team (TP4), and the BPD or village council as well as the lack of community participation (Wibisono, 2017; Aziz, 2016).

The Good Village Governance (GVG)

This concept was developed from Good Corporate Governance (GCG) which is defined as a company's internal control system directed towards managing significant risks, securing company assets and increasing shareholder investment value in a long term to realize the business objectives. Moreover, it is the relationship between shareholders, creditors, financial markets, institutions, workers and companies. This, therefore, means GCG involves a set of rules and policies to guarantee the interests of stakeholders through appropriate supervision of company assets and efficient risk management process. Furthermore, this concept is needed to support the achievement of the goals set by the village government.

It is needed due to the inefficiencies of the government in conducting its duties in the village as regards financial management (Aziz, 2016; Suparman, Kusnadi, & Harono, 2014). It was even reported, in some areas, that funds were embezzled by village officials and this was found to be due to weak accountability (Supriyadin, 2017; Sohuturon, 2017).

In several studies, the implementation of corporate governance has been able to improve company performance and avoid fraud (Chen et al., 2006; Mangala & Kumari, 2017; Eferakeya et al., 2016; Halbouni et al., 2016; Tan, Chapple, & Walsh, 2017). Other pieces of evidence found there was a difference in management between highly fraudulent companies and safe ones (Matoussi & Gharbi, 2011).

There is a frequent occurrence of fraudulent activities in village funds and, according to President Joko Widodo, there were 900 village heads involved in the misuse of funds (Supriyadin, 2017) and fraud is mostly in the form of corruption in Village Fund Allocation (ADD), Village Funds, and Village Cash (Indonesia Corruption Watch, 2018).

Indonesia Corruption Watch (2018), Mondale et al. (2017), and Wibisono & Purnomo (2017) found weak supervision from several stakeholders as well as the low community involvement in the management of village funds are the main causes of high fraud potential (Mondale et al., 2017).

Therefore, Good Village Governance (GVG) was developed based on the concept of GCG in the private sector which has been proved by several empirical studies to have the ability to reduce fraud and achieve corporate performance (Chen et al., 2006; Mangala & Kumari, 2017; Eferakeya et al., 2016; Halbouni et al., 2016; Matoussi & Gharbi, 2011; Tan et al., 2017). Based on this, background, the following hypotheses were formulated:

H1   GVG Implementation, Internal Control, and Citizen Participation have a significant effect on fraud potential.

H2   GVG Implementation, Internal Control, Citizen Participation, and Potential Occurrence of Fraud have a significant effect on Village Government Performance.

METHODOLOGY

This research was conducted quantitatively with a causality design to examine the factors influencing the possibilities of fraud in village funds. The population was made of village officials in Demak Regency, Central Java directly responsible for the management of village funds and a total of 60 respondents were selected using incidental sampling method. All respondent are village government officials who receive village funds.

The research variables used include GVG implementation, External Supervision, Citizen Participation as the independent ones, Village Government Performance as the dependent variable while Fraud Potential was both an independent and dependent variable. The GVG implementation variable is measured by 11 question indicators, the external monitoring variable is measured by 7 indicators, citizen participation is measured by 4 indicators, the potential for fraud is measured by 5 indicators, and village government performance is measured by 7 indicators. All variables are measured on a Likert scale with 5 levels.

Primary data was obtained from the use of questionnaires retrieved from previous researchers and provided to the respondents. Moreover, the data obtained were analysed using descriptive analysis and a causality test was conducted on the variables. The causality test among variables using the Equation Model Structure (SEM) with the WarpPLS tool

RESULTS/FINDINGS

Table 1 presents the descriptive data of the respondents. The results showed most of the officials were male with only 8 represented by 13% being women. The most predominant age range was 30-39 years old and the majority of the respondents have quite a long work experience as observed in the 57% that have worked for more than 5 years. Moreover, it is also important to note that only 4 of the village heads representing 7% were willing to be respondents in this research.

Table 1. Research Respondents Description

Respondents Description		Total	Percentage
Gender			
Male		52	87
Female		8	13
	Total	**60**	**100%**
Age			
20 – 29 years old		8	13
30 – 39 years old		20	34
40 – 50 years old		18	30
> 50 years old		14	23
	Total	**60**	**100%**
Position			
Village head		4	7
Village secretary		12	20
Head of the development division		6	10
Others		38	63
	Total	**60**	**100%**
Work Experience			
< 1 year		6	10
2 – 3 years		12	20
4 – 5 years		8	13
> 5 years		34	57
	Total	**60**	**100%**

Source: Research Analysis Data

Descriptive statistics of the research variables are presented in Table 2. The results showed the mean value for the Village Government Performance was 28.03 which is in the high category. This means the respondents believe the performance of each village government has been good and in accordance with the expectations of the citizens. Moreover, Fraud

Potential was found to be 8.61, which is a low category. This indicates the possibility of fraudulent activities in the management of the fund is very small. The GVG Implementation has a mean value of 47.15 which is in the high category while External Supervision and Citizen Participation were in the medium category and considered good enough.

Table 2. Descriptive Statistics of Research Variables

Research Variables	Minimum	Maximum	Mean	Std. Deviation
Village Government Performance	19	32	28.03	3.1387
Fraud Potential	5	20	8.61	3.6881
GVG Implementation	40	55	47.15	3.9164
External Supervision	25	35	29.78	2.4849
Citizen Participation	12	20	16.58	1.6526

Source: Research Analysis Data

The hypotheses formulated were tested for validity and reliability using SEM analysis and assisted by WarpPLS software. The results showed the composite reliability coefficients of GVG Implementation, External Supervision, Citizen Participation, Fraud Potential, and Village Government Performance were 0.858, 0.878, 0.849, 0.914, and 0.839 respectively. Meanwhile, the values of Cronbach's alpha coefficients were 0.811, 0.835, 0.761, 0.873, and 0.786, respectively. This, therefore, means the research instruments fulfilled the requirements of validity and reliability.

Several criteria in WarpPls also showed the research model fulfilled requirements and declared it to be fit. The Average path coefficient (APC) value was 0.235 with P = 0.013, Average Adjusted R-squared (AARS) value was 0.332 with P <0.001, Average R-squared (ARS) value was 0.371 with P <0.001, Average block VIF (AVIF) value was 2.170 while the Average full collinearity VIF (AFVIF) value was 2.397. A model is declared acceptable if all these values are less than or equal to 5 and, ideally, 3.3.

The causality test results between variables using the Structural Equation Model method, we present in the figure and table below:
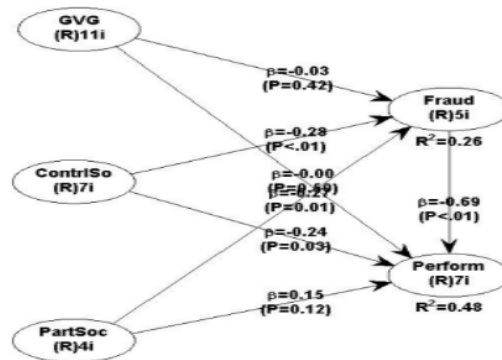

Figure 2. Output of WarpPLS

Source : Result of Analysis Data

Table 3. Hypothesis Test Results

	GVG	External Supervision	Citizen Participation	Fraud Potential
P values				
Fraud Potential	0.419	0.010	0.013	
Village Government Performance	0.495	0.026	0.119	<0.001
Path coefficients				
Fraud Potential	-0.026	-0.282	-0.269	
Village Government Performance	-0.002	-0.235	0.146	-0.687

Source: Research Analysis Data

DISCUSSION / ANALYSIS

Table 3 shows the path analysis of the hypotheses test and the first was the relationship between Fraud Potential as a dependent variable and GVG, External Supervision and Citizen Participation as an independent variable. The second includes village government performance as the dependent variable with GVG, external supervision, citizen participation, and the fraud potential as the independent variables.

The results showed different values for the influence of dependent variables on Fraud Potential. The P-value of GVG was 0.419 with a path coefficient of -0.026 and this indicates there was no significant relation. Moreover, External Supervision was 0.010 with a path coefficient of -0.282 which indicates a negative and significant effect while Citizen Participation was 0.013 with a path coefficient of -0.269 which means there was a negative and significant influence.

Subsequently, varying results were also observed with the influence of the dependent variables in the second test on Village Government Performance. The P-value of GVG was 0.495 with a path coefficient of -0.002 to show the absence of any significant effect. External Supervision was 0.026 with a path coefficient of -0.235 indicating the existence of a negative and significant effect. Furthermore, Citizen Participation was 0.119 with a path coefficient of 0.146 which means there was no significant relationship while Fraud Potential was <0.001 with a path coefficient of -0.687 showing a significant and negative effect. The findings also showed Fraud Potential has the greatest path coefficient than other independent variables and this means it has a more dominant influence on Village Government Performance.

The results showed there was no significant effect of GVG on fraud potential while external supervision and citizen participation have a negative and significant effect. This means the implementation of GVG is not a determinant to control the occurrence of fraud in village fund management but rather through the use of effective supervision from external parties as well as the active participation of citizens in the management process.

The supervising role of different parties, as well as the involvement of citizens, has the ability to make village officials become more careful in managing funds and also in the prevention of fraud. This is because the active participation of more citizens has the capacity to ensure transparency and accountability in the fund management activities of the officials.

These findings are not in line with the report of previous studies that governance has the ability to prevent fraud (Chen et al., 2006; Mangala & Kumari, 2017; Eferakeya et al., 2016; Halbouni et al., 2016; Matoussi & Gharbi, 2011; Tan et al., 2017). It is, however, believed the implementation of GCG is a solution to reduce fraud in village funds since the management process involves social interaction between several stakeholders such as central, regional and village governments as well as the community.

Several studies have associated the high misappropriation of village funds to the lack of supervision from the community (Mangala & Kumari, 2017; Wibisono, 2017). As earlier stated, effective understanding and supervision have a positive impact on the improvement of financial accountability (Widarnawati et al., 2018). These previous findings confirmed the importance of external supervision as well as the active participation of citizens in preventing fraud.

The results showed only external supervision and fraud potential had a significant effect on village government performance while no influence was found with GVG and citizen participation. This finding showed the implementation of GVG is not effective in ensuring good performance of the village government and the same was observed with citizen participation. Furthermore, external control was found to have a negative instead of positive influence because good supervision is expected to provide a better performance, therefore, it is recommended this variable is re-investigated.

Fraud Potential was also found to have a negative and significant effect on Village Government Performance. This means a smaller potential of fraudulent activities is good for the performance of the government and vice versa. It also showed cheating and misappropriate of funds make it impossible for village officials to conduct the required programs for development.

Summarily, these findings are contrary to the results of previous studies that the implementation of corporate governance has been able to improve company performance (Tan et al., 2017; Dalwai, Basiruddin, & Rasid, 2015; Aggarwal, 2013; Cheema & Din, 2013; Kamardin & Haron, 2011; Pathan & Faff, 2013; Rahman & Bremer, 2016). This shows good village governance has not been an important instrument in some districts of Central Java while government performance was more influenced by other factors like the Javanese culture.

CONCLUSION

The implementation of GVG was found not to have a significant effect on the potentials of experiencing fraudulent activities in village fund management while external supervision and citizen participation have a negative and significant effect. Furthermore, it also indicated the implementation of GVG and citizen participation were not proven to have a significant effect on village government performance while external supervision showed negative influences. Meanwhile, the potential for fraudulent activities was found to have the most significant effect on the performance of the government. Therefore, there is a need to put appropriate attention to the possibilities of fraud in order to ensure the efficient conduct of governmental activities.

It is suggested all related parties focus on preventing fraud in the village fund management and this is expected to be most effective with the strengthening of supervisory activities as well the level of citizen participation. This should be conducted to reduce the possibilities of fraud to improve village government performance.

LIMITATION AND STUDY FORWARD

This study uses few respondents. The theme of research on fraud is the cause of the low participation of village officials to become research respondents. We suggest different data search methods, cooperating with local governments in finding data so that respondents have an increased respond rate.

ACKNOWLEDGEMENT

AUTHORS CONTRIBUTION

Ahmad Nurkhin contributes significantly to designing the instrument, and data collection. Hasan Mukhibad provides data analysis and contributes to additional literature review and performs proof- reads the final manuscript. Dr. Agus Wahyudin as conceptor and analysis the quality of the manuscript. In addition, Fachrurrozie contributes significantly to developing the instrument.

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