FINANCIAL MANAGEMENT REFORM PROCESS IN THE INDONESIAN VILLAGE GOVERNMENT

Andy Dwi Bayu Bawono¹, Heppy Purbasari², Suyatmin Waskito Adi³

¹, ²Lecturer, Department of Accounting, Universitas Muhammadiyah Surakarta, Surakarta, Jawa Tengah, Indonesia, ³Senior Lecturer, Department of Accounting, Universitas Muhammadiyah Surakarta, Surakarta, Jawa Tengah, Indonesia.

Email: ¹andy.bawono@ums.ac.id, ²heppy.purbasari@ums.ac.id, ³yatin.waskitoadi@gmail.com

Article History: Received on 25th July 2019, Revised on 31st August 2019, Published on 06th October 2019

Abstract

Purpose: The study aimed to examine contingency factors influencing the village reform especially the financial management process.

Methodology: Primary data was obtained through interviews, while the supporting data was gathered from an examination of Indonesian government documents, organizational reports, and academic literature.

Result: The present study found that the primary motive for FMS Reform in the Indonesian village government was the need that was expressed by the Indonesian Ministry of Home Affairs (MoHA) as a regulator of Indonesian village government for modernizing the village financial management and reporting system.

Applications: This research can be used for the universities, teachers, and students.

Novelty/Originality: The first FMS reform was marked by the enactment of Indonesian Government Regulation (GR/PP) 72/2005 on ‘Village’ followed by the MoHA regulation on the ‘guidance of financial management system’. These regulations were denoted as a reform from the old village administration system regime to the new village financial management system.

Keywords: Financial Management Reform Process, Lüder FMR Model, the Indonesian Village Government.

INTRODUCTION

The new public management (NPM) reform has emerged in both developed and developing countries in response to adaption of private-sector practices. The NPM notion aimed to reform public sector organizations to align their management practices with private sector organizations emphasizing the idea of developing the government’s public management system in consideration of citizens as customers (Denhardt and Denhardt, 2000). There are four aspects of NPM reform, namely finance and budgeting; personnel management; public sector organization; and performance measurement systems (Pollitt and Bouckaert, 2011; Ingavale, 2013).

Proponents of NPM argue that traditional institutional systems are not suitable anymore to fulfill current governmental needs that require voluminous and multifarious formats. Several researchers also stated that the NPM notion explained the pattern of transformation concerning how the public sector was governing. This new paradigm is used to solve problems of high degrees of trust in the private sector and low degree of trust in the public sector by its stakeholders (Yazdekhasti et al, 2015).

However, adoption and implementation of the NPM notion have attracted much criticism as there is a contradiction between the above-mentioned aim of NPM reforms and their outcome. Paradoxes refer to contradictions between hopes or promises for regulations and what is achieved by reforms. For instance, traditional bureaucracies are often retained and augmented formality and regulation during the NPM implementation period. NPM may produce a bureaucracy with more rule-based system and process-driven routines than characteristics of the traditional bureaucracy that is intended to be removed by NPM. A reform, which does not achieve the stated objective, can be categorized as the goal displacement. It is a phenomenon by the paradoxical effect of the NPM (Prabowo et al, 2017; Muyambiri & Chabaefe, 2018; Peres et al, 2018).

Despite the debatable “relevance” and “real use” of NPM reform, the Indonesian government has endeavored to use NPM ideas to reform its political, structure and financial management reforms since early 1999 after the fall of Soeharto regime in 1998 (Bawono, 2015).

Furthermore, the notion for NPM reform also rose in the village management system, which resulted in an implementation of a new financial management system since the reconstruction of the Government Regulation (GR) 72 in 2005 for the Village.

However, there are few studies on the extant literature examining the reason for the implementation of NPM notions through the new financial management practice in the Indonesian village government. To this end, the present study sought to raise the research question: How and why the changes in the village financial management system were made from 2005 to 2014?

The present paper used the Lüder Financial Management Reform (FMR) model as a conceptual framework to analyze the financial management reform in the Indonesian village government as the case study. According to the prior model (Lüder,
Contingency Model), the FMR model modified and emphasized on the behavioral context as an extension of the classical contingency theory approach. The model assumed that a certain arrangement of institutional modules affected the attitudes and behavior of various members (in public life, politics, and administration) in the financial reform process.

RESEARCH METHOD

The present research used a case study approach to examine the financial management reform in the Indonesian village government. Case studies approved the personal or organization examination within definite situations utilizing the collected data from documents, archival records, interviews, direct or participant observations, and physical artifacts (Leedy and Ormrod, 2012).

The approach was suggested by several researchers in the examination of financial management reform including budgeting and accounting changes in the government. The research data were collected from semi-structured interviews through Indonesian MoHA officers, technocrats and academics with knowledge on the village financial management; Indonesian government archival documents (laws, government regulations, decrees, and reports); publications; and newspaper articles. The Lüder FMR model was used to support the design of interviews including questions based on the relevant literature review.

RESULTS AND DISCUSSION

The present section contextualized research findings and enriched our understanding of the Indonesian village government and its position in the Indonesian government structure, the financial management reform process within the Indonesian village government system, and an analysis of this reform from the Lüder FMR model as a conceptual framework.

A Historical Overview of Indonesian Village Government Financial Management

Prior to the Indonesian Republic's independence in 1945, villages were established in entire Indonesia from Sumatera to Papua since eras of numerous kingdoms. The village was named by various local terms such as desa, huta, gampong, nagari, kampung, or tiuh and it was started as a small republic or self-governing community or tribe that was recognized by the prior local kingdom. In the Dutch colonial and Japanese occupation era, several regulations were also imposed to rule villages and village management in Indonesia based on their local wisdom, tribe cultures and origins (Etucuban & Pantinople, 2018; Mussabekov et al., 2018).

Since 1945, villages had special positions as parts of the Indonesian Government recognized by the central government through the enactment of the Law No. 22/1948 on the ‘Local Government’ (UU RI No. 22 Tahun 1948 tentang Pemerintah Daerah). This law regulated the Indonesian local government consisting of province, district (big city) and village (small city/negeri/marga).

In 1965, the Indonesian government enacted the second regulation for village known as the Law No. 19/1965 on ‘The Village Government’ (UU RI No. 19 Tahun 1965 tentang Desapraja sebagai Bentuk Peralihan Untuk Mempercepat Terwujudnya Daerah Tingkat III di Seluruh Wilayah Republik Indonesia). This law emphasized regulating villages in Indonesia as the third level of local government according to the Indonesian local government structure that considered the province as the first level and city/district as the second level. As the third level of government, the village had a right to self manage its household authority and local democracy. According to this law, the village had certain regulations for managing its financial management system that imposed village to prepare its annual budget for village government and development. However, several local rules in village financial system such as village leader and staff salary from village land (e.g. tanah bengkok) and feudalism system were inherited from the prior era and forbidden from implementation. Therefore, the revenue from village's own land management should be paid to the village bank account before using for salary.

However, before this law was well implemented in entire Indonesia, 1965 revolution began resulting in the regime change from Soekarno (Old Order) to Soeharto (New Order). Therefore, several mentioned old practices of village financial management still existed.

In the New Order era, the new regulation on the village began with enactment of the Law No. 5/1979 on ‘The Village Government’ (UU RI No. 5 Tahun 1979 tentang Pemerintahan Desa). According to this law, there was a uniformity of village name, status, and structure. The village position in the Indonesian government structure was also repositioned below the sub-district (Kecamatan) and had vertical accountability to above articulated level of government under which the village autonomy status was removed. In this era, the village status was downgraded only as an administrative institution rather than the prior sovereign government. This village system was implemented for more than twenty years until the 1997 financial crisis in Indonesia resulting in the political reform and a new reform era.

As a result of a reform era in 1998, the Indonesian government imposed a regional autonomy for local government that was denoted by an enactment of the Law No. 22/1999 on the 'Local Government' (UU RI No. 22 Tahun 1999 tentang Pemerintahan Daerah). This rule regulates the local government's responsibility to manage its territory and associated affairs including its financial management especially budget management practices. Furthermore, the consideration must be also taken on the Law No. 25/1999 on 'Central and Regional Financial Balance' (UU RI No. 25 Tahun 1999 tentang Perimbangan Keuangan Pusat dan Daerah) on which further rules are based. This regulation is expected to balance the
transparency and accountability in the distribution of authority, finance, and financial management systems to achieve more effective implementation of regional autonomy. Using these regulations, the local government accountability is directly distributed among the public through their legislative members. Therefore, the local government's financial management is also changed from a traditional budget and accounting system to performance-based budgeting and accrual approach to respond the local autonomy implementation (Harun and Robinson, 2010). Correspondingly, these laws repositioned village back in prior recognition as special territory that had its own autonomy in the district/city.

Therefore, the village regulation also included changes by an enactment of the Government Regulation No. 76/2001 on 'General Guidance for Village Government' (Peraturan Pemerintah [PP] No. 76 Tahun 2001 tentang Pedoman Umum Pengaturan mengenai Desa) following by the MoHA decree No. 47/2002 on the guidance of the village administration (Kepmendagri No. 47/2002 tentang Pedoman Administrasi Desa). Despite the fact that the local government (province and district/city) implemented the new financial management system, the village management was ruled by this MoHA decree to use a traditional village administration system consisting of several administrations with a financial administration system of routine and development budget. This budget model was known as a part of traditional budget that was inherited and implemented in the prior era (both old and new orders).

As the law 22/1999 and law 25/1999 created too much freedom in the local government that affected several frauds and corruption cases, the central government began to enact new regulations on the local government to retract several authorities for controlling the local government by an enactment of new Laws namely the Law No. 32/2004 on the 'Local Government' (UU RI No. 32 Tahun 2004 tentang Pemerintahan Daerah) and the Law No. 33/2004 on 'Central and Regional Financial Balance' (UU RI No. 33 Tahun 2004 tentang Perimbangan Keuangan Pusat dan Daerah). Based on these laws, the village management was also changed by an enactment of the GR No. 72/2005 on 'Village' (PP No 72/2005 tentang Desa) that provided much explanation for the village and its management system. Based on this GR, village or other local communities, which were previously named in the first page, were positioned and defined as the "unity of law-based community that had exact territorial and right to regulate its authority on the community based on local culture and origin, this local authority is also recognized and respected by the Indonesian government".

Therefore, it was clear that the village within the frame of GR No. 72/2005 had an autonomy based on its culture and origin. This GR also stated the allocation of transfer namely the Village Fund Allocation (Alokasi Dana Desa [ADD]) from the district/city and other funding from the Central Government and province for financing the village government financial management. The idea of ADD was introduced far before 2008 for the implementation by several local governments, for instance in the implementation of DAUN (Dana Alokasi Umum Nagari) in Solok, West Sumatera and scholars from Brawijaya University since the early millennium era. This best practice in Solok was also spread and implemented in several districts such as Jayapura, Magelang, and Sumedang during 2001-2004. This notion aimed to help the equity of development in entire Indonesia through an allocation of general grants for village. This idea was finally accepted by MoHA and enacted as a common system as a part of village funding through the district/city allocation.

To control the accountability of all aforementioned funds, the MoHA enacted the Regulation 37/2007 on the 'Guidance of Village Financial Management' (Permentdagri No. 37 Tahun 2007 tentang Pedoman Pengelolaan Keuangan Desa) based on the financial management system derived from local government (province and district/city) system that was previously successfully implemented. Therefore, the GR 72/2005 and MoHA regulation 37/2007 were marked as significant village management reforms from the old administration system to the more modern financial management system. This new financial management system introduced new financial principles such as transparency, accountability, participative principle, and budget order and discipline.

The village government should have the medium-term planning for five years and short-term (annual) planning, which were implemented based on participative principles, to answer the implementation of those principles. Those documents were used to provide the annual budget formulation. Furthermore, the village government was also regulated to formulate its budget based on the direct and indirect expenditure classification and also operational and capital budget. Despite the fact that the village financial management system did not follow any exact accrual accounting system as the local government, the treasury system, account recording, and reporting system followed the cash accounting model that was also rigid and detailed in the account classification and reporting document.

However, this financial management system was finally changed in 2014 as the Law No. 6/2014 on 'Village' (UU RI No. 6 Tahun 2014 tentang Desa) and the MoHA Regulation No. 113/2014 on the 'Guidance of Village Financial Management' (Permentdagri No. 113 Tahun 2014 tentang Pedoman Pengelolaan Keuangan Desa) were enacted (Eko, 2014).

CONCEPTUAL FRAMEWORK
The Lüder's FMR model was adapted, modified and used as a conceptual framework for analyzing the financial management reform process in the Indonesian village government as well as examining factors that formed this reform process. The framework delivered a contingency model for recognizing and analyzing pertinent contextual aspects and key players in financial management reform in the Indonesian local government. It is important to analyze and detail the Indonesian village financial management reform process using the Lüder's FMR model in order to provide the knowledge about the financial management process in the Indonesian village government and gaining the benefit of the broader accounting field.
According to the Lüder's FMR model, different innovations or reforms are seen in many governments, for instance implementation of financial management system contingent on the environmental factors in which the system operates. Conducive environment factors occurred like economic, political, administrative and culture stimulus reforms. According to figure 1, The Lüder's FMR model consists of two contextual variables, namely stimuli and institutional arrangements; three behavioral variables, namely reform drivers, political reform promoters, and stakeholders; and two instrumental variables, namely the reform concept and implementation strategy. (McCarthy, J. F. (2004).)

![Figure 1: An Adaptation of the Financial Management Reform Process (FMR)](image)

1. The stimulus is defined as a condition occurring in the early phase of innovations and point to the need for new financial management system. It then affects political reform promoters to change their expectations and behavior. In the case of the Indonesian village financial management reform (FMR), the dominating doctrine from the superior country financial management system through the implementation in the Indonesian local government was the stimulus for village FMR. This system was imposed as a public sector requirement of village FMR following the successful story of financial management reform in the local government as an impact of decentralization (local autonomy) (Leedy and Ormrod, 2012; Harun and Robinson, 2010). However, several local values such as the ADD and central government, which were recognized on village origin and culture, were also maintained as a local policy based on local government and village requirements.

2. Reform drivers are the recognized institutions or professionals that act as drivers for the reform. These drivers are cores of behavioral variables that together with stimuli provide the cause for political reform promoters to build the reform concept. In this study, several MoHA officers, local government officers, technocrats and scholars acted as the reform drivers that supported the formulation of regulations and implementation of the new financial management system. Consultant and donor (e.g. the World Bank) also supported the further implementation in the village in several local governments through the joint project with MoHA (e.g. Initiative for Local Governance Reform [Prakarsa Khusus Pembangunan Tata Pemerintahan Daerah]).

3. The political reform promoters are parts of government or parliament that promote the institutional arrangement and all administrative reforms. In this case, MoHA officers were the political reform promoters who imposed this financial management system to be implemented in the Indonesian village system. This effort was also continued in the application of Law 6/2014 on Village 9 (Djogo, T., & Syaf, R. (2003, June).

4. The institutional arrangement is a contextual variable, which is promoted by political reform driver and also affects the stakeholder, and it consists of five variables namely, legal system, state structure, administrative structure, the
qualification of civil service and the country culture. The present study identified several prior-mentioned institutional arrangement attributes of the Indonesian village system that might have empowered or delayed village FMR. First, Indonesia is a unitary of state government that implemented the local autonomy. However, autonomy was fully implemented as several authorities and was still in the central government. Therefore, a similar case occurred in the village government; and several revenues were still in the central or local government's authority that created village and was still in the weak position for decision making. Secondly, the Indonesian legal system followed the civic law that was inherited from the colonial era. According to Lüder, the law system was a barrier to the implementation of financial management system. Finally, the qualification of village staff was still weak in order to implement the new system.

5. A stakeholder is a person or an institution that gets positively or negatively influenced by the reform. In this regard, stakeholders do not refer to people that are involved in reform driver and political reform promoters. Given the village financial management, there were few stakeholders involved in the implementation and dissemination of village financial management based on MoHA regulation No. 37/2007. Most of involved people were MoHA staff, local government officers from finance department, and consultants from donor projects. (Ito, T. (2006).)

6. The reform concept is the reform design before implementation. This concept leads to the implementation strategy and also contains the reform outcome plan. MoHA was a party that had a responsibility to develop the reform concept by supporting several scholars.

7. The implementation strategy is the process and strategy of the implementation reform. In the village financial management reform, the selected strategies of the Indonesian government were still authoritarian with a single command and central guidance from MoHA. This strategy combined one and more steps in the local government implementation by scaling the training and dissemination in several phases (Fauzi, N., & Zakaria, R. Y. (2002, June.).)

8. The outcome is the consequence/result of reform or its stage. It means that the outcome could be a step of reform and dynamically return back as stimuli to the next reform. After a long process of dissemination and implementation, the implementation of this financial management system began diffusion with other programs such as PPK, PNPM that resulted in an idea to combine the system with the new Law namely, the Law 6/2014 on 'Village' (UU RI No. 6 Tahun 2014 tentang Desa). Therefore, this new reform for the dynamical loop to the new stimuli proved that there was a need for system reform to develop and achieve an ideal phase that was necessary for the community.

CONCLUSION
The present research aimed to investigate motives for the financial management reform in the Indonesian village government as well as factors influencing its implementation from 2005 to 2014. Based on findings and according to the village FMR, several conclusions can be made about research questions.

The procedure of village management of Indonesia can be traced from its regulations and rules that are inherited from the kingdom era. Numerous regulations were imposed to rule villages as a part of an Indonesian government system. Focusing on the conceptual framework village FMR, this first stimulus was a dominating doctrine for the requirement of new financial management system that changed the village management system from the administration regime to financial management system. The village financial management reform process in 2005-2014 was driven by key persons from MoHA, local government, technocrats, and scholars. Despite the fact that this reform was not fully implemented in all villages in Indonesia, this reform was denoted to teach the village staff about the need for a modern financial system resulting in the next financial management reform based on new laws and regulations.

Furthermore, the present study indicated the usefulness of the Lüder's FMR model as a conceptual framework for understanding the village financial management system in Indonesia.

ACKNOWLEDGMENT
The author confirms that the data do not contain any conflict of interest.

REFERENCES
1. Bawono, Andy Dwi Bayu. (2015). “The Role of Performance-Based Budgeting in the Indonesian Public Sector.” Ph.D Thesis, Macquarie University.
2. Eko, Sutoro. (2014). Desa Membangun Indonesia [Village Develops Indonesia]. Sleman: Forum Pengembangan Pembaharuan Desa (FPPD).
3. Etcuban, J. O., & Pantinople, L. D. (2018). The Effects of Mobile Application in Teaching High School Mathematics. International Electronic Journal of Mathematics Education, 13(3), 249-259. https://doi.org/10.12973/iejme/3906
4. Harun, Harun, and Sydney Peter Robinson. (2010). “The Adoption of Accrual Accounting in the Indonesian Public Sector.” Research in Accounting in Emerging Economies 10: 233–250. https://doi.org/10.1108/S1479-3563(2010)000010014
5. Ingavale, D. (2013). An impact of advertisements on purchase decision of youth with reference to consumer goods. *Advances in management*, 3(1), 18-22.

6. Leedy, Paul D., and Jeanne Ellis Ormrod. 2012. Practical Research: Planning and Design. New Jersey: Pearson Education, Inc.

7. Mussabekov, G., Auyezov, B., Tavoma, A., Sultanbekova, Z., Akhmetova, Z., & Kozhakhmetova, G. (2018). Formation of readiness of future teachers to creative activity in school. *Opción*, 34(85-2), 569-599.

8. Muyambiri, B., & Chabaefe, N. N. (2018). The Finance–Growth Nexus in Botswana: A Multivariate Causal Linkage. *Dutch Journal of Finance and Management*, 2(2), 03. https://doi.org/10.20897/djfm/2634

9. Peres, P., Moreira, N., & Mesquita, A. (2018). Are Really Technologies at the Fingers of Teachers? Results from a Higher Education Institution in Portugal. *Journal of Information Systems Engineering & Management*, 3(1), 08. https://doi.org/10.20897/jisem.201808

10. Pollitt, Christopher, and Geert Bouckaert. (2011). Public Management Reform. A Comparative Analysis: New Public Management, Governance, and The Neo-Weberian State. New York: Oxford University Press.

11. Prabowo, Tri Jatmiko Wahyu, Phlomena Leung, and James Guthrie. (2017). “Reforms in public sector accounting and budgeting in Indonesia (2003-2015): confusions in implementation.” *Journal of Public Budgeting, Accounting & Financial Management* 29(1): 104–137. https://doi.org/10.1108/JPBAFM-29-01-2017-B005

12. Yazdekshast, A., Erfan, N., & Nazari, N. (2015). Investigating the Relationship between Spiritual Intelligence and Social Adaptation among Girl High School Students in Shahreza City. UCT Journal of Social Sciences and Humanities Research, 3(1), 20-23.

13. Djogo, T., & Syaf, R. (2003, June). Decentralization without accountability: power and authority over local forest governance in Indonesia. In Issues of decentralization and federation in forest governance: proceedings from the Tenth Workshop on Community-based Management of Forestlands (pp. 9-25).

14. Ito, T. (2006). The dynamics of local governance reform in decentralized Indonesia: Participatory planning and village empowerment in Bandung, West Java. Asian and African Area Studies, 5(2), 137-183.

15. Fauzi, N., & Zakaria, R. Y. (2002, June). Democratizing decentralization: Local initiatives from Indonesia. In Paper submitted for the International Association for the Study of Common Property 9th Biennial Conference, Zimbabwe.

16. McCarthy, J. F. (2004). Changing to gray: decentralization and the emergence of volatile socio-legal configurations in Central Kalimantan, Indonesia. *World Development*, 32(7), 1199-1223. https://doi.org/10.1016/j.worlddev.2004.02.002

17. Salim, A., Bulan, W. R., Untung, B., Laksono, I., & Brock, K. (2017). Indonesia’s Village Law: enabler or constraint for more accountable governance?.

18. Bünte, M. (2008). Indonesia’s protracted decentralization: Contested reforms and their unintended consequences. In Democratization in Post-Suharto Indonesia (pp. 122-143). Routledge. https://doi.org/10.4324/9780203934760

19. Nordholt, H. S. (2005). Decentralisation in Indonesia: less state, more democracy? In Politicising Democracy (pp. 29-50). Palgrave Macmillan, London. https://doi.org/10.1057/9780230502802_2

20. Kurauchi, Y., La Vina, A., Badenoch, N., & Fransen, L. (2005). Decentralization of natural resources management: lessons from Southeast Asia. *Synthesis of decentralization case studies under the resources policy support initiative (REPSI).*

21. Syri, H. Y. (2011). In search of appropriate approaches to coastal zone management in Indonesia. *Ocean & coastal management*, 54(6), 469-477. https://doi.org/10.1016/j.ocecoaman.2011.03.009

22. Miller, M. A. (2008). Rebellion and reform in Indonesia: Jakarta's security and autonomy policies in Aceh. Routledge. https://doi.org/10.4324/9780203888193