

UDC 336

FINANCIAL PERFORMANCE: AN ANALYSIS OF LOCAL REVENUE AND BUDGETING IN BANTEN PROVINCE

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ABSTRACT

This study aimed at examining the effect of local revenue (seen from the amount of Regional Revenue) and local budgeting (expenditure) on the financial performance of the local government. This study took place in cities and regencies of Banten. A purposive sampling technique was applied in the selection of research samples including eight (8) cities/regencies, The Office of Finance and Assets Management (Badan Pengelola Keuangan dan Aset Daerah – BPKAD), The Office of Local Revenue (Badan Pendapatan Daerah - BAPENDA), and <http://otda.kemendagri.go.id>. Data were analyzed using IBM Statistical Package for Social Science (SPSS) version 25. Results showed that local revenue and budgeting positively and significantly affected the financial performance of the local government of Banten.

KEY WORDS

Local revenue, local budgeting, financial performance, local government.

The financial performance of the local government indicates its success in managing the local budget; it can be seen from the local (original) revenue. The economic crisis has affected the local taxes (retribution) and regional wealth—two main components of the local budget. The crisis has disrupted the economic activities of the people leading to a decrease in income; this in turn has affected local revenue resulted in lower and uncertain local revenue. The pressure faced by the local government due to decreasing local revenue has led to a shift in the planning and management of local budgeting.

A state is a nation or territory considered as an organized community under one government. For the government of Indonesia, the reformation was considered one of the efforts to regain trust from the citizens of the archipelagic country; the government has been trying to realize good governance and an authoritative government to restore the economic, social, and political conditions of Indonesia. The economic crisis of Indonesia was the beginning of the transfer of authority and responsibility in financial management from the central government to regional (local) governments.

The transfer of authority was done with the aim of the local governments later being able to manage their budget, to minimize the interference of the central government on local affairs, and to reduce the budget dependency of local governments towards the central government. Thus, the central government expected that the local governments could find and develop their potential that they could do their best in serving the public (local people). The central government believes that by doing so the local people's needs and interests will be fulfilled better. Besides, the local governments are also expected to show higher performance because the public has demanded it since the reformation era started and since the stipulation of TAP MPR Number XV/MPR/1998 on regional autonomy, regulation, distribution, and utilization of national resources, and a balanced central and regional finance within the framework of the Republic of Indonesia.

Previous research conducted by Sunaryanto & Syah (2018) reveals the use of the Lean Government Algorithm with DMAIC and LCM to process documents and provide services in Badan Pengelola Keuangan dan Aset Daerah (BPKAD) of South Tangerang—the use of the algorithm has helped to make financial statements transparent, objective, and accountable. This present study focused on the financial performance of the local government of Banten related to local revenue and budgeting. Thus, this was different from

the previous study as it did not examine the application, but it examined the effect of local revenue and budgeting on financial performance.

Another previous study by Ginanjar & Syah (2019) examines the use of the Lean Government Concept in the making of ID cards in government organizations. The use of the concept has helped the effective and efficient use of funds and has benefit to the community.

A study by Limbong *et al.* (2019) focuses on risk management for newly established and growing companies. It found that risk management must be carried out for both commercial and government companies or the public sector—this includes financial risk, marketing and technical risk, and other operational risks that the organization can achieve its goals effectively and efficiently.

Local governments need to evaluate their performance. Performance measurement is important because it provides feedback on plans implemented (Wibowo, Syah, Darmansyah, & Pusaka, 2018). The Government Regulation Number 6/2008 mentions that one of the evaluations on the administration of local governments is Evaluasi Kinerja Penyelenggaraan Pemerintahan Daerah (EKPPD)¹. The regulation is supplemented by the Regulation of the Minister of Home Affairs Number 73/2009 concerning the procedures for evaluating the performance of local governments and the Regulation of the Minister of Home Affairs Number 74/2009 on guidelines for awards to local government administrators. Article five of the first minister regulation states that Laporan Penyelenggaraan Pemerintah Daerah (LPPD)² becomes the main source of information to evaluate the performance of local governments.

EKPPD is done by calculating and assessing the composite index of the two main variables of the performance of local governments. The total composite index is the sum of the assessment that includes the performance achievement index and material suitability index. The performance achievement index measures the performance of local governments at the level of policymakers. In addition to the characteristics of the local government of Banten, we also used the audit results of the Audit Board of the Republic of Indonesia in measuring the financial performance of the local government to avoid fraud in the implementation of government activities.

In budget management, independence is the basis for the local government to optimize revenue from its region, known as local revenue. According to the Law Number 32/2004, local revenue originates from the region itself; it may come from the local tax revenue, local retribution, the results of management of local assets, and other legitimate local revenue (Horoshkova *et al.*, 2018). The local governments are given the authority to manage their revenue following the regulation on local autonomy as a manifestation of decentralization. One of the most important criteria to examine the ability of local governments in managing their region is the financial capacity.

An increase in local revenue is expected to increase investment of the local governments on their spending that they can provide good quality public services. Tabellini (2018) also explains that the increase in local revenue is a supporting factor of macroeconomic performance. Growth encourages investment that, at the same time, the investment will encourage improvements in local infrastructure. Good local infrastructure and high investment in the region will increase local revenue. Tabellini (2018) asserts that the increase in local revenue should be supported by an increase in the quality of public services because the good quality of public services reflects the good performance of the local government.

Based on the Law of the Republic of Indonesia Number 15/2004 concerning the State Financial Management and Accountability Audit, an audit is a process of problem identification, analysis and evaluation carried out independently, objectively, and professionally based on inspection standards to assess the truth, accuracy, credibility, and reliability of information regarding the management and responsibilities of state finances.

A previous study discloses that the government could achieve financial stability if the local revenue could cover all the expenses of the government in England (Allen, Carletti,

¹ Evaluation of the Performance of Local Government Administration.

² The Report on the Implementation of Local Governments.

Goldstein, & Leonello, 2018). The other study by Tabellini (2018) argues that local revenue and local government expenditure in the United States are influenced by racial heterogeneity factors such as the level of education, cultural background, and awareness of each individual in completing their obligations as citizens.

Our study is different from previous studies since the object was local revenue, local budgeting, and financial performance in local governments. Our subject was the local government of Banten Province. The study took place from 2015 to 2018.

We hope that our findings become a reference for scientific studies on financial performance, local revenue, and budgeting in Banten Province, and can provide information and description specifically to the local government on the importance of local revenue and budgeting for increasing local financial performance.

LITERATURE REVIEW

Local Revenue

The economic development of a region requires some funds derived from various sources managed by the region. Based on the principle of regional autonomy, economic development in a region is carried out based on the ability of local revenue since the central government transferred the authority to do so to the local governments, which include the regency or city government. Local revenue can be interpreted as funds sourced from fees and levies imposed by the local government on any person or a business entity owned by the government or private based on applicable regulations. According to the Law Number 33/2004, local revenue refers to revenue coming from sources within its region collected based on regional regulations as well as applicable laws and regulations. According to the Government Accounting Standards, revenue is all receipts of the State or local governments in the form of general cash accounts that add to the equity of current funds in the current fiscal year period—these receipts become the right of the government and the government does not need to pay back. Meanwhile, according to PSAK 23 (revised in 2009), revenue is the gross inflow of economic benefits during the period arising from the course of the ordinary activities of an entity when those inflows result in increases in equity, other than increases relating to contributions from equity participants.

Local revenue is a rationally measurable estimate that can be achieved for each source of income. Local revenue includes all cash receipts through local cash accounts that add equity funds to the local right in one fiscal year [PSAK 23 (revised in 2009)].

Local Budgeting

Local budgeting is government expenditure that can contribute to financial performance. Lam & Wang (2018) argue that local budgeting is one of the activities of local government spending that can increase fixed assets and can provide benefits in the long term. Local budget is also intended to finance projects aimed at improving the welfare and interests of the community (Muda, Yahya, Nasution, & Utara, 2018). Local budgeting can also be said to be an investment activity carried out by the regional government, but even so, it does not seek profits. The success of local expenditure budgeting is reflected in the quality of services given (it meets the expectation), in the things produced (it meets the number expected), in the time allotment (it is suitable with the plan), and in the amount of fund spent (it does not exceed the limit previously set). One of the activities related to local budgeting that can produce income is the development of infrastructure in an area—the built infrastructure must be able to encourage investment in the region so it will have an impact on the financial performance of the region in the future; finally, the regional economy is growing and it can create jobs for the local community.

Local Financial Performance

Performance refers to achievements (Indonesian Dictionary, 2001). According to Robbin (1994), performance is a measure of the results of work using mutually agreed criteria. Performance measurement is a process of continuous monitoring and reporting of

achievements of activities, particularly progress on planned goals (Sumarjo, 2010). The Government Regulation Number 6/2008 mentions that one of the evaluations on the administration of local governments is EKPPD. The regulation is supplemented by the Regulation of the Minister of Home Affairs Number 73/2009 concerning the procedures for evaluating the performance of local governments and the Regulation of the Minister of Home Affairs Number 74/2009 on guidelines for awards to local government administrators. Article five of the first minister regulation states that Laporan Penyelenggaraan Pemerintah Daerah (LPPD) becomes the main source of information to evaluate the performance of local governments.

EKPPD is a process of collecting and analyzing data systematically on the performance of local government by using a performance measurement system—a system used to measure, evaluate, and compare systematically and continuously the performance of local government administration. Article five of the Regulation of the Minister of Home Affairs Number 73/2009 states that Laporan Penyelenggaraan Pemerintah Daerah (LPPD) becomes the main source of information to evaluate the performance of local governments focusing on performance achievements at the level of policymakers and policy implementers using Indikator Kinerja Kunci (IKK)³. According to Mardiasmo (2006), IKK is a set of indicators considered as key performance measures for both financial and non-financial aspects in the operation of business units. Article five of the Regulation of the Minister of Home Affairs Number 73/2009 states that IKK is a unity in the performance measurement system starting from Organisasi Perangkat Daerah (OPD)⁴, local governments, among regions within a province, and up to the national level. Local budgets are financial plans as the basis of public service delivery. In Indonesia, the local budget document is called Anggaran Pendapatan dan Belanja Daerah (APBD)⁵—the term is used in the provincial, city/regency, and district level. The budget planning according to Law 22/1999 (and Law 32/2004) involves two parties: the executive and the legislative, each has a budget team or committee.

Before preparing APBD, an agreement is made between the executive and the legislative regarding general objectives, policies, and budget priorities, which will serve as guidelines in preparing APBD. The executive makes the APBD draft following the general objectives, policies, and budget priorities, which are then submitted to the legislative to be discussed before being established as a Peraturan Daerah (PERDA)⁶. In the agency perspective, this is a form of contract (incomplete contract), which becomes a tool for the legislative to oversee the executive in implementing budgeting.

The executive has advantages in terms of mastery of information over the legislative (information asymmetry). This advantage stems from the factual condition that the executive is the executor of all functions of the local government and deals directly with the community. The executive understands bureaucracy and administration as well as laws and regulations that underlie all aspects of governance. Therefore, the budget for public services is allocated based on assumptions that make it easier for the executive to provide good services. The executive will tend to propose a bigger budget than the needed one (the maximum principle). In contrast, the executive tends to propose lower targets (the minimum principle) so the target is achieved more easily. Such proposed budgets illustrate the asymmetry of information between the executive and the legislative. This occurs because the agent (executive) wants a relatively safe and comfortable position in executing their duties and functions.

The legislative may show opportunistic behavior in two positions: as a principal and as an agent. As a principal for the executive, the legislative realize its interests by making policies appearing to be an agreement between the two parties, but benefit the legislative in the long run, both individually and institutionally. Through its discretionary power, the legislative can propose policies difficult to reject by the executive, even though the proposal

³ Key Performance Indicators.

⁴ Local Apparatus Organization.

⁵ The Local Revenue and Budgeting.

⁶ Local Regulation.

is not directly related to public services and legislative functions. As an agent for the public (voters), the opportunistic behavior of the legislative is even more apparent.

In budgeting, the legislative should defend the interests of voters by accommodating public needs. Activities to be financed with a budget should be based on the identified problems and needs of the community.

The executive uses two conditions to realize their opportunistic behavior in budget preparation. First, they do it explicitly related to the legislative budget and, second, they do it through the budget for public services in the form of safekeeping. In the first condition, the legislative proposes a budget that increases their income to fulfill their self-interest in the short term; this has led to political corruption (Halim & Abdullah, 2006). In the second condition, the focus is to achieve long-term self-interests. The proposed budget is the one that benefits politicians in certain regions, so the proposal is all about making visible results from the perspective of the public. As a result, politicians tend to choose development projects in a region as it becomes a powerful constituency for them. The public finds it difficult to understand this tendency.

Relationship Between Variables

Local Revenue and Financial Performance

The ability of the region to explore and exploit its potential can certainly generate and increase local revenue. The local revenue generated by the region contributes to financial performance, as stated by Jumingan & Kasidin (2017) that local revenue consisting of income from local taxes and all incomes entitled to the region is expected to improve the financial performance of local governments.

Furthermore, Syam, Lisandri, Rizani, & Oikawa (2018) and Allen *et al.* (2018) argue that local revenue has a significant positive effect on the financial performance of local governments.

H1: Local revenue has a significant positive effect on the local financial performance of Banten Province.

Local Budgeting and Financial Performance

According to Regulation of the Minister of Home Affairs Number 13/2006, local budgeting is one of the regional government expenditures that can increase and provide benefits in the long run. Infrastructure development in the form of public facilities is one of the capital expenditures expected to be able to increase the growth of local revenue and will ultimately improve the local economy.

H2: Local budgeting has a significant positive effect on the local financial performance of Banten Province.

Based on the above hypothesis, the research model is illustrated in Figure 1:

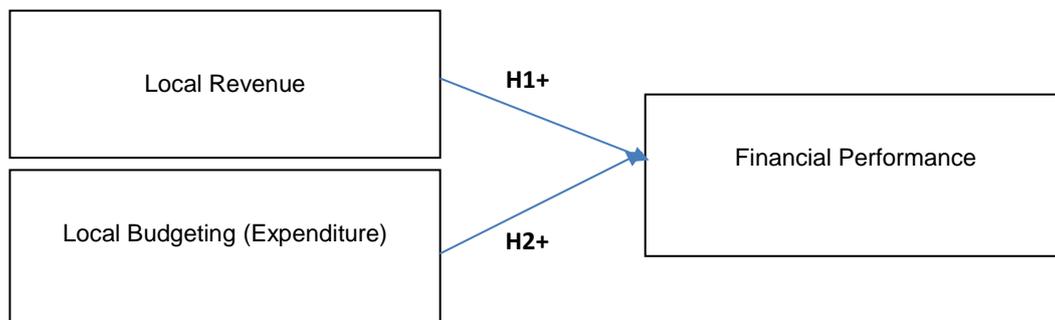


Figure 1 – Research Model

Tabellini (2018) suggests that allocating more funds to local expenditure will later assist regions to obtain more financial resources that will help to improve the financial performance of local governments. One of the activities related to local budgeting that can produce more financial resources is the development of infrastructure in an area—the built infrastructure

must be able to encourage investment in the region so it will have an impact on the financial performance of the region in the future; finally, the regional economy is growing and it can create jobs for the local community. According to Muda *et al.* (2017), infrastructure is expected to be able to create efficiencies in various sectors and to increase community productivity so it creates a better financial performance of local governments. Local government expenditure including capital expenditure is thought to be one of the variables that can affect the financial performance of local governments (Kuntari, Chariri, & Prabowo, 2019).

METHODS OF RESEARCH

This study aimed to examine the effect of local revenue and local budgeting (expenditure) on financial performance in Banten Province. Jumingan & Kasidin (2017) prove that local revenue derived from taxes, routine income, and other local income has a positive effect on improving the financial performance of local governments. Furthermore, the size of the local government with total assets as the proxy and the level of dependence of the local governments on the central government with Dana Alokasi Umum (DAU)⁷ as the proxy compared to the total realization of expenditure proved to not significantly affect the performance score of the local government (Syam *et al.*, 2018). Audit by the Audit Board of the Republic of Indonesia with the audit findings as the proxy compared to the total expenditure and the local wealth level variable with local revenue as the proxy compared to the total revenue significantly influences the performance score of the local government.

Eriadi, Erlina, Muda, & Abdullah (2018) argue that the quality of local financial performance is influenced by the effectiveness and efficacy of local revenue and budgeting for expenditures mediated by assets of local governments. The present study examined the influence of local revenue and budgeting on financial performance in Banten Province.

The present study was quantitative because it required a systematic approach to reveal the relationship between variables focusing on testing hypotheses using statistical tools. There were two (2) independent variables (local revenue and budgeting or expenditure) and one (1) dependent variable (financial performance). Operational definitions were made and measurements were done on each of the research variables. Samples were chosen purposively including four (4) cities and four (4) regencies in Banten Province from 2015 to 2018, so we had 32 samples.

SPSS Version 25 was used for data analyses. Hypotheses were tested using multiple linear regression tests and pre-tests involved a normality test, classic assumption test, and t-test.

RESULTS AND DISCUSSION

Samples were chosen purposively including four (4) cities and four (4) regencies in Banten Province from 2015 to 2018, so we had 32 samples. The normality test, classic assumption test, and t-test were performed using SPSS Version 25.0. In the data normality test and classical assumption test, each variable had a significance level above 0.05, meaning that the data were normally distributed and could be used in further testing.

Regression models are used for significant and representative estimates if they do not deviate from the classical basic assumptions. To meet these classic assumptions, a classic assumption test consisting of the normality test, the multicollinearity test, the heteroscedasticity test, and the autocorrelation test must be done.

The normality test is used to find out whether data taken from populations are normally distributed or not. In this study, we employed the Kolmogorov Smirnov test and it showed that the data used in this study were normally distributed since the asymptotic significance of 0.853, which was greater than the significance level of 0.05. Because the data used in this study were normally distributed, the data could be used in the regression model.

⁷ General Allocation Fund.

The Multicollinearity test is used to test whether a correlation between independent variables is found in a regression model. We employed a tolerance value and Variance Inflation Factor (VIF). The multicollinearity test results showed that the tolerance value for all variables in each regression model was greater than 0.1 and the VIF value for all variables in each regression model was smaller than 10; thus, it can be said that there were no symptoms of multicollinearity in the regression models used in this study.

The Heteroscedasticity test aims to test whether in the regression model occurred inequality variance from one observation to another observation. The heteroscedasticity test in this study showed that the probability (sig) in each regression model was greater than 0.05 or 5%; thus, it could be stated that no symptoms of heteroscedasticity in all regression models of this study.

The results of the partial test on the effect of local revenue on financial performance showed a significance value of 0.014 or smaller than 0.05 and a positive slope of 0.24; thus, it can be said that local revenue has a significant positive effect on financial performance.

The results of the partial test on the effect of local budgeting (expenditure) on financial performance showed a significance value of 0.023 or smaller than 0.05 and a positive slope of 0.004; thus, it can be said that local budgeting (expenditure) has a significant positive effect on financial performance.

From the calculation of multiple linear regressions, the relationship between the independent variables and the dependent variable is formulated as follows:

$$\text{Financial Performance} = 1.714 + 0.024 \text{ Local Revenue} + 0.004 \text{ Local Budgeting}$$

The equation can be interpreted as follows. A constant of 1.714, this means if the independent variable considered constant ($x_1 = 0$, $x_2 = 0$), then the financial performance of each region would be 1.714. The coefficient on local revenue increased by 0.024, meaning that a change in local revenue by 1% would increase capital expenditure by 0.024 or 0.24%. The coefficient on local budgeting increased by 0.004, meaning a change in local budgeting by 1% would increase capital expenditure by 0.004 or 0.04%.

DISCUSSION OF RESULTS

Local revenue has a significant positive effect on financial performance. Our findings differ from the one by Muda *et al.* (2017) and Eriadi *et al.* (2018) that local revenue will improve financial performance if supported by the good, effective and efficient recording of local assets.

However, the results of this study are consistent with or similar to the research conducted by Jumingan & Kasidin (2017) and Syam *et al.* (2018) that local revenue has a positive and significant effect on regional financial performance. High local revenue will lead to a better level of financial performance.

Local budgeting has a significant positive effect on regional financial performance. The results of the present study also contradict the one presented by Allen *et al.* (2018) that local budgeting does not necessarily provide efficiency for financial performance because every budgeting should be accompanied by good performance as a response to the expenditure.

However, the findings support the research conducted by Tabellini (2018) that any local budgeting carried out by local governments will provide a stimulus for improving financial performance. This study also responds positively to previous research conducted by Kuntari *et al.* (2019) that local budgeting (expenditure), Dana Alokasi Umum (DAU), and Dana Alokasi Khusus (DAK)⁸ have a significant positive effect on local budgeting (expenditure).

CONCLUSION

Research data originating from eight (8) cities and regencies in Banten Province observed from 2015 to 2018 showed that local revenue has a significant positive effect on

⁸ Special Allocation Funds

local financial performance. The results of this study are consistent with the research hypothesis that local revenue has a significant positive effect on financial performance.

Local budgeting (expenditure) has a significant positive effect on local financial performance. The results of this study are consistent with the research hypothesis that local budgeting (expenditure) has a significant positive effect on financial performance.

Local governments, especially Banten covering the eight (8) cities or regencies studied, need to pay more attention to the components of local revenue and budgeting, such as local tax returns, levies on the use of local wealth, and other legal taxes because the local revenue is proven to have positive and significant effects in improving the financial performance of the local government.

Further research needs to examine comprehensively factors other than local revenue and budgeting that can improve the financial performance of local governments, such as Dana Alokasi Umum (DAU), and Dana Alokasi Khusus (DAK), and so forth.

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