

Effect of Budgeting Models and Characteristics Local Government on Local Government Performance with Leadership Style as A Variable Moderating

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Abstract. This research aims to empirically prove whether the budgeting model and regional government characteristics influence regional government performance. Apart from that, the study also aims to analyze whether leadership style can moderate this relationship. The samples are taken from the district or city governments in Central Java and DIY Provinces. There were 41 regional governments with 5 respondents from each regional government, so there were 205 respondents. The sampling model was based on purposive sampling. The results found that in the leadership style budgeting model, regional government characteristics influence regional government performance. All regional government characteristics including regional government size, dependence on central funds, regional government wealth, and capital expenditure influence regional government performance positively. Meanwhile, leadership style does not moderate all variables on local government performance.

Keywords: Budgeting Model, Leadership Style, Regional Government Characteristic, Local Government Performance

1 Introduction

The shift in the governance paradigm from a process-oriented approach to a results-oriented approach has driven reforms in the national financial management system in both developed and developing countries, including Indonesia. Local governments are expected to leverage their regional potential to reduce dependency on the federal government by increasing Regional Original Revenue (PAD), which indicates the extent of a region's wealth [1]. PAD can also serve as an indicator of local government autonomy.

In this study [2], the researcher adds an independent variable, namely the budgeting model, along with leadership style as a moderating variable. The purpose of these additions is to examine how effective governance can be achieved by analyzing the local government budgeting model. "This budgeting model represents the objectives set by the local government for a 12-month period and is utilized in government activities, including expenditures on land

acquisition, equipment and machinery, buildings and structures, roads, irrigation systems, networks, and other fixed assets" (Article 53, Paragraph (1) of Permendagri 13/2006).

2 Literature Review and Hypothesis Formulation

2.1 The Influence of Regional Government Size on Regency/City Regional Government Performance Scores in Central Java and DIY

The main objective of local government programs is to deliver the highest quality of service to the community. High-quality support relies on robust assets. Consequently, delivering public services necessitates adequate facilities and infrastructure. Local government performance is expected to improve as the area expands, as indicated by an increase in local government assets [3].

Local governments can deliver optimal services when supported by high-value assets [4]. Therefore, adequate facilities and resources are essential to effectively serve the public. Consequently, larger local governments are expected to exhibit better performance compared to smaller ones. This is reinforced by findings from this study [4] and [5], which indicate that the size of a local government has a positive impact on the financial outcomes of district and city governments in Indonesia.

H1: Regional government size has a positive effect on the performance of district/city regional governments in Central Java and DIY

2.2 The Influence of Regional Wealth Levels on the Performance of Regency/City Governments in Central Java and DIY

Regional wealth can be measured by the amount of Regional Original Revenue (PAD) [1]. According to [6], PAD is a source of regional income derived from local resources, serving as the primary capital for local governments to finance regional development and activities, thereby reducing dependency on central government funds. PAD includes regional taxes, user charges, revenue from separated regional assets, and other legitimate regional income sources. Regional revenue originates from intergovernmental transfers as well as internal sources, specifically PAD and other legitimate income. As noted by [8], PAD consists of income from legitimate regional taxes, user charges, profits from regional enterprises, and other revenue. This aligns with [6], which explains that PAD consists of regional taxes, user charges, revenue from separated regional assets, and other legitimate original income sources, allowing regions greater flexibility to secure funding to support regional autonomy and implement the principle of decentralization. Studies [8], [9], [3], and [10] find that a local government's level of PAD positively influences its financial performance. Based on this explanation, the first hypothesis of this study can be formulated.

H2: The level of regional wealth influences the performance of Regency Regional Governments in Central Java and DIY.

2.3 The Influence of the Level of Dependence on the Central Government on the Performance of District Governments in Central Java and DIY

The level of dependence of local governments on the central government varies, as reflected in the receipt of the General Allocation Fund (DAU). PAD and DAU are two primary sources of regional income that play a significant role in the implementation of regional autonomy, aiming to enhance public services and promote regional economic development [11]. According to [12], intergovernmental revenue reflects the level of dependence of local governments on the central government. High levels of dependence tend to increase the level of disclosure. Based on stewardship theory, humans are inherently trustworthy, capable of acting responsibly, and possess integrity and honesty toward others. This indicates that local governments have a significant responsibility to perform their duties and functions, particularly in managing finances entrusted to them by the central government, with the aim of achieving optimal public service and community welfare. Therefore, the higher the DAU from the central government, the better the local government's service to the community, which in turn enhances local government performance. In line with this explanation, research by [13] indicates that DAU correlates with local government performance.

According to the study by [8], the Intergovernmental Transfer Fund (Dana Perimbangan) has a positive impact on the financial performance of local governments. This is supported by research from [14] and [15], which concluded that the level of dependence of local governments on the central government positively affects the performance of local governments in Indonesia.

H3: The level of dependence on the central government influences the performance of Regency/City Regional Governments in Central Java and DIY4.

2.4 The Influence of Capital Expenditures on the Performance of Regency/City Governments in Central Java and DIY Provinces

[16] defines capital expenditure as spending made to form capital, aimed at increasing inventories and fixed assets that provide benefits across multiple accounting periods. This includes maintenance costs that not only extend the useful life of assets but also enhance their capacity and quality. Capital expenditure is intended to acquire fixed assets for local governments, such as equipment, buildings, infrastructure, and other fixed assets. Theoretically, there are three methods to acquire these fixed assets: by building them, exchanging them for other fixed assets, or purchasing them. However, in government practice, the most common method is through purchasing. The purchasing process is typically carried out through complex bidding or tender procedures [1]. The amount of capital expenditure reflects the provision of facilities and infrastructure. The more development undertaken by local governments (stewards), the better the service provided to the public (principals). The more development undertaken by local governments (stewards), the better the service provided to the public (principals), which results in better performance by the local government. According to [9], this explanation is backed up, which found that the size expenses incurred by a region Positively impacts local government performance. Nevertheless, this contrasts with the findings of [3], which suggest that local governments with larger total expenditures tend to perform worse. This is further supported by the study of [10], which examined capital expenditure in isolation and concluded that capital expenditure does not have a significant effect on local government

financial performance. Based on this explanation, the third hypothesis in this study can be formulated:

H4: Capital expenditure influences the performance of Regency/City Regional Governments in Central Java and DIY Provinces.

2.5 The relationship between the Participatory Budgeting Model and the Performance of Government Agencies with Leadership Style as a moderating variable

The involvement of groups or individuals in the budgeting process is highly influenced by the leader's interaction style with subordinates and the extent to which the situation grants control and influence to the leader. According to [17], a leader's style can be determined based on whether it is task-oriented or relationship-oriented, which can be assessed using the LPC (least preferred coworker) instrument developed by the author. With a relationship-oriented leadership style, budget participation enhances opportunities for subordinates to perform their tasks more effectively. This is because harmonious interactions between superiors and subordinates motivate and provide a sense of security for subordinates in their work, which subsequently impacts the performance of superiors. The study conducted by [18] demonstrates that leadership style has a positive impact on the motivation to engage in the budgeting process.

A relationship-oriented leadership style encourages managers to engage in open communication with their subordinates, fostering strong social bonds between them. This approach makes subordinates feel valued and accountable for performing their duties. With such a leadership style, participation in the budgeting process is likely to occur, ultimately leading to improved performance within government institutions.

Considering the explanation above, it can be inferred that a task-oriented leadership style tends to weaken the relationship between participation in budget planning and performance outcomes, as the primary focus is on task completion or achieving work goals rather than on the development of subordinates' abilities. This means there is a lack of motivation or encouragement from the leader to the subordinates. In contrast, a relationship-oriented leadership style enhances the opportunities for subordinates to achieve good performance, as it fosters a harmonious relationship between the leader and subordinates. Furthermore, the leader will strive to provide enthusiasm and motivation to the subordinates, ultimately improving the performance of government institutions.

Leadership style refers to the manner in which a leader influences others or subordinates to carry out the leader's desires in order to achieve organizational goals, even if such actions may not be personally preferred. [18] suggests that a leader's style can be identified as either task-oriented or relationship-oriented through the use of the LPC (least preferred coworker) instrument developed by the author.

A leadership style focused on relationships can enhance participation in budgeting, providing subordinates with opportunities to improve their performance. This is due to the harmonious interaction between leaders and subordinates, which offers motivation and a sense of security in their work, ultimately leading to a positive impact on the leader's performance.

H5: The Participatory Budget Preparation Model significantly improves the performance of local government.

H6: Leadership Style Moderates the relationship between the Participatory Budget Preparation Model and the performance of regional/city governments in Central Java and DIY Provinces.

3 Research Methods

3.1 Method of Collecting Data

This study utilizes primary data obtained directly from respondents, with a target sample size of 205 respondents. Data collection was carried out using a survey method with a questionnaire containing a series of questions posed directly to the respondents. The questionnaire was distributed online using Google Forms, and respondents who met the survey criteria were provided with free beverages. A total of 205 valid samples were obtained from the responses collected through Google Forms.

3.2 Measurement of Variabel

3.2.1 Size Institution

The study [19] states that the size of a company can be measured by total assets, sales, and market capitalization. The larger the total assets, sales, and market capitalization, the larger the size of the company. These three variables are used to determine the company's size as they reflect the scale of the company. The greater the assets, the larger the invested capital; the higher the sales, the greater the cash flow; and the larger the market capitalization, the greater the recognition of the company in the market.

The value of assets tends to be more consistent than market capitalization and sales when measuring the size of a company.

The study by [4] suggests that the characteristics of local governments can be explained by their size, which is measured by total assets. A larger government size facilitates operational activities, thereby improving the provision of public services. Furthermore, operational ease also supports the generation of Local Revenue (PAD), contributing to regional development and serving as an indicator of improved performance [5]. This aligns with [4], the greater the scale of local government, the more likely it is to achieve stronger financial outcomes.

Larger local governments tend to face greater pressure to disclose their financial performance. In reporting their performance, local governments are more likely to highlight "good news" that reflects positively on their operations. This positive information may include reports on the government's good performance, which can contribute to improving their performance score.

3.2.2 Regional Wealth Level

Financial performance analysis can be conducted using financial ratios, which serve as tools to assess financial performance [16]. [3] measures regional wealth by comparing Local Revenue

(PAD) to total revenue. According to Law No. 33 of 2004, PAD is the revenue obtained by a region from internal sources within its jurisdiction, collected based on regional regulations in accordance with applicable laws and regulations. PAD includes local taxes, local levies, proceeds from the management of separated regional assets, and other legitimate regional revenues [20]. The level of regional wealth can be measured using the following formula:

$$\text{Regional Wealth Levelerah} = \frac{PAD}{\text{Total Income}}$$

3.2.3 Level of Dependency with the Central Government

The level of dependence on the central government is measured by comparing the amount of the General Allocation Fund (DAU) to the total revenue [3]. According to [20], the General Allocation Fund (DAU) is a transfer from the central government to regional governments aimed at addressing horizontal inequalities, with the primary goal of equalizing financial capabilities across regions. The amount of DAU for each district/city can be found under the balance fund section in the APBD Realization Report. This variable is measured using the following formula:

$$\text{Level of Dependency with the Central government} = \frac{DAU}{\text{Total Income}}$$

3.2.4 Capital Expenditure

The Ministry of Finance of the Republic of Indonesia, through [21], states that capital expenditures within the total realization of regional spending reflect the proportion of regional spending allocated or realized for capital expenditures. This realization of capital expenditures will have a multiplier effect in driving the local economy. Therefore, in this study, capital expenditures are measured using the following formula:

$$\text{Level of Capital Expenditure} = \frac{\text{Capital Expenditure}}{\text{Total Realized Expenditure}}$$

3.2.5 Budgeting Model

Participation in budget preparation refers to the level of involvement and influence of individuals in determining and formulating the budget for a specific division or department, whether periodically or annually. From the definition of budget participation, it can be concluded that the performance of local government officials will improve when budget participation is implemented. Effective participation brings several benefits, including positively influencing initiative, morale, and enthusiasm, producing better results from a plan due to the integration of knowledge from multiple individuals, enhancing collaboration between departments, and enabling employees to better understand future situations related to goals and other considerations [22]. The questionnaire used to measure this variable is adapted from [23]. A Likert scale is used to assess this variable, with scores of 5 (SL=Always), 4 (SR=Frequently), 3 (KD=Occasionally), 2 (P=Never), and 1 (TP=Never).

3.2.6 Leadership Styles

Leadership style refers to the manner in which a leader influences individuals or subordinates to willingly carry out the leader's desires in order to achieve organizational goals, even if such actions may not be personally favored.

Leadership style will be assessed using a questionnaire instrument adapted from the study [24]. This questionnaire aims to determine whether the leadership style in an organization is transformational, transactional, or laissez-faire. The use of this instrument is based on its prior use by other researchers and its proven reliability.

The questionnaire consists of 36 questions that will be answered by the respondents. Each answer will be scored on a scale from 1 to 5, and the responses to each question will be grouped and summed to obtain a score for each leadership style.

The grouping of leadership styles is as follows:

- 1) The transformational leadership style includes 5 dimensions, each with 4 questions, totaling 20 questions.
- 2) The transactional leadership style consists of 3 dimensions, each with 4 questions, totaling 12 questions.
- 3) The laissez-faire leadership style has only one dimension, consisting of 4 questions.

3.2.7 Performance of Regency Regional Government

The dependent variable in this study is the performance rating of local governments in regencies/cities, as issued by the Directorate General of Regional Autonomy under the Ministry of Home Affairs. The total composite index of local government performance is the sum of assessments, which include the performance achievement index and the material compliance index. The performance achievement index is measured by evaluating the Key Performance Indicators (IKK) at the policy formulation and policy implementation levels. The range of local government performance scores is 0-4, divided into four categories: 0-0.999 = low, 1-1.999 = moderate, 2-2.999 = high, and 3-4 = very high (Minister of Home Affairs Regulation No. 73 of 2009).

3.3 Data Processing and Analysis

The data collected through Google Forms will be converted into Microsoft Excel format for further analysis. Subsequently, several tests will be conducted using SEM PLS software to obtain the required test results.

4 Results and Discussion

4.1 Outer Model (Measurement Model)

4.1.1 Outer Weight Test

In this study, data analysis is conducted using the Partial Least Squares (PLS) approach, which focuses on a single component of the variable. According to [25], PLS is an approach that shifts from the covariance-based SEM approach, typically used to test causality or theory. In contrast, PLS is a more predictive model. PLS is considered a powerful analysis method because it is not reliant on many assumptions. In addition to confirming theories, PLS can also be used to explain the existence of relationships between latent variables. PLS can simultaneously analyze constructs built with both reflective and formative indicators.

Table 1. Outer Weight Test Results

Variable	Original Sample (O)
Asset -> Performance	2.367
Cost of Capital -> performance	2.089
General Allocation Fund_ -> Performance	3.049
Leadership Style -> Performance	3.354
Budgeting Model -> Performance	3.409
Moderating Effect 1 -> Performance	-1.118
Locally-generated revenue -> Performance	2.528
Cost Realisation -> Performance	2.904
Total Income -> Performance	2.246

4.1.2 Inner Model (Measurement Model)

The results of the structural model estimation using all PLS bootstrapping estimation methods indicate that the path coefficient values obtained through t-statistic testing (>1.68) and p-value (<0.05) between construct variables are significant, as shown in the following figure.

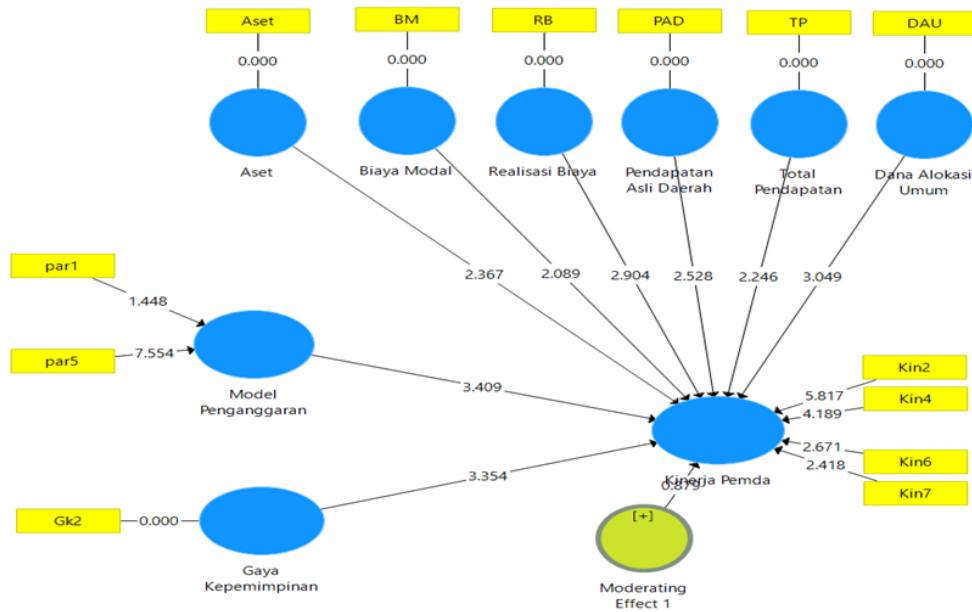


Fig. 1. Measurement Model

Table 2. Test-Path Coefficients

Variable	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	t Statistics	P Values
Asset -> Performance	4.409	4.435	1.863	2.367	0.009
Cost of Capital -> Performance	-3.382	-3.930	1.619	2.089	0.019
General Allocation Fund_ -> Performance	10.739	10.213	3.522	3.049	0.001
Leadership Style -> Performance	0.573	0.627	0.171	3.354	0.000
Budgeting Model -> Performance	-0.414	-0.374	0.121	3.409	0.000
Moderating Effect 1 -> Performance	-1.118	-0.164	1.273	0.879	0.190
Locally-generated revenue -> Performance	4.471	4.378	1.769	2.528	0.006
Cost Realisation -> Performance	-8.837	-7.781	3.043	2.904	0.002
Total Income -> Performance	-7.434	-7.339	3.310	2.246	0.013

From the data in Table 2 it is explained as follows:

a. The influence number of assets has a positive effect on local government performance

The results of this study indicate that the main goal of local government work programs is to provide optimal service to the community. High-quality service requires strong asset support. Therefore, to effectively serve the public, adequate facilities and resources are essential. As a result, local government performance is expected to improve with an increase in the region's size, which is often marked by a larger asset base for the government. Effective service provision by local governments relies on having strong resources. Thus, adequate facilities and resources are crucial for serving the community. Consequently, local governments with larger territories are expected to perform better compared to those with smaller jurisdictions. This is further supported by studies [4], [10], and [5], which show that the size of a local government's area has a positive effect on the financial performance of district and city governments in Indonesia.

b. The Effect of Capital Expenditure on Regional Government Performance

The findings indicate that a high capital expenditure reflects the provision of facilities and infrastructure. Increased development efforts by local governments (stewards) enhance services to the public (principals), thereby improving local government performance. This explanation is supported by research [9], which found that higher regional spending positively impacts local government performance. However, these findings contrast with [9], which reported that local governments with higher total spending actually perform worse. Further support comes from research [10], which examined capital expenditures separately and concluded that capital expenditures significantly affect local government financial performance.

c. The influence of General Allocation Funds on Regional Government Performance

The study results indicate that the General Allocation Fund (DAU) positively influences local government performance. The level of dependency of district and city governments on the central government varies, reflected in their receipt of DAU funds. Both Local Own-Source Revenue (PAD) and DAU are key revenue sources that play an important role in supporting regional autonomy, with the ultimate goal of improving public services and advancing the local economy [25]. According to [12], intergovernmental revenue highlights the degree of dependency on higher levels of government, where high dependency tends to increase disclosure levels. Stewardship theory posits that individuals are inherently trustworthy, capable of acting responsibly, and uphold integrity and honesty toward others. This suggests that local governments have a significant responsibility to carry out their duties in financial management entrusted by the central government, with the expectation that public services and community welfare will be optimally achieved. Accordingly, a higher DAU allocation from the central government leads to better local government services and, consequently, enhanced local government performance. Supporting this, research by [13] found a correlation between DAU and local government performance, noting that the Balance Fund positively impacts local financial performance. Additionally, studies by [9] and [15] suggest that the degree of reliance on the central government positively influences local government performance in Indonesia.

d. The Influence of Leadership Style on Local Government Performance

The research findings indicate that leadership style has a direct impact on local government performance. These findings suggest that a task-oriented leadership style tends to weaken the relationship between budget participation and performance, as it focuses primarily on task completion rather than developing subordinates' skills. This implies a lack of motivation or

encouragement from leaders to subordinates. Conversely, a relationship-oriented leadership style increases subordinates' opportunities to achieve strong performance due to a positive relationship between leaders and subordinates, with leaders striving to provide encouragement and motivation. Thus, a relationship-oriented leadership style enhances the performance of government institutions.

Leadership style is the approach a leader takes to influence others or subordinates in such a way that they are willing to carry out the leader's directives to achieve organizational goals, even if the task may not be personally appealing. According to [17], a person's leadership style can be identified as task-oriented or relationship-oriented through the use of the LPC (least preferred coworker) instrument that has been developed for this purpose.

With a leadership style that tends to be relationship-oriented, budget participation increases subordinates' opportunities to perform their tasks more effectively. The harmonious interaction between superiors and subordinates provides motivation and a sense of security for subordinates in their work, which, in turn, positively impacts the performance of the superiors themselves.

e. The Influence of Budgeting Models on Local Government Performance

The research findings demonstrate that the budgeting model has a positive impact on local government performance. Participation in budget preparation significantly and positively influences the performance of government agencies, with this effect becoming weaker when the leadership style is task-oriented, and stronger when the leadership style is relationship-oriented.

A participatory budgeting process is an effective method for enhancing the performance of organizational work units. Participation in budget preparation involves both leaders and subordinates in the process, allowing their performance to be evaluated based on the criteria set within the budget. The achievement of budget targets reflects the overall performance of the organization's work unit.

f. The Effect of Regional Original Income on Regional Government Performance

The findings reveal that Local Own-Source Revenue (PAD) is a source of income derived from local resources within the region, which is used as a foundational capital for local governments to finance development and regional initiatives, thus reducing dependency on central government funds. PAD consists of local taxes, local levies, revenues from the management of separated regional assets, and other legitimate local income. Regional income comes from the receipt of balance funds from the central and local governments, as well as from local sources such as PAD and other legitimate income. According to Sugiarto (2007), PAD refers to income obtained by local governments from legitimate local taxes, levies, profits from regional enterprises, and other sources. This aligns with the explanation in Law No. 33 of 2004, which states that PAD is intended to provide local governments with the flexibility to raise funds from local taxes, levies, the management of specific regional assets, and other legitimate sources to finance regional autonomy and support decentralization. Studies by [8], [9], [3], and [10] found that the level of PAD in local governments has a positive impact on the financial performance of local governments..

5 Conclusion

The performance of local governments is influenced by the wealth of the local government, which is reflected in the amount of local government assets, total capital costs, total general allocation funds from the central government, leadership style (mayor, regent, and governor), budgeting model, and local own-source revenue. Leadership style cannot moderate all of these variables in improving local government performance.

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