International Journal of Civil Engineering and Technology (IJCIET)
Volume 10, Issue 02, February 2019, pp. 310-319, Article ID: IJCIET_10_02_034
Available online at http://www.iaeme.com/ijciet/issues.asp?JType=IJCIET&VType=10&IType=02
ISSN Print: 0976-6308 and ISSN Online: 0976-6316
 Scopus Indexed

THE MODEL OF SUCCESSFUL RISK MANAGEMENT IMPLEMENTATION IN LOCAL GOVERNMENT

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ABSTRACT

This study was examined and analyzed the factors that influence the success of risk management implementation in the local government. Risk management implementation can reduce fraud in the North Sumatra provincial government. Risk management is not an option but a necessity in public sector organizations especially local governments. The government is expected to make large investments to implement risk management. The population in this study were all internal auditors and budget users in Sumatera Utara Province. This study used all population as samples. Data were collected by questionnaire. Data were analyzed using the Structure Equation Model using the PLS application. The results of this study indicate that Management commitment, quality of human resources and conflicts of interest influence the successful implementation of risk management in local governments. The top managements didn't commit to implementing risk management because of their lack of understanding of the benefits of risk management. There is a tendency for top management to avoid implementing risk management. This can be attributed to the facts nowadays, precisely top management who make fraud.The higher conflict of interest in local government is also a barrier to the successful implementation of risk management. There is a tendency for the executive and the legislature to have different interests with the of the local government objectives, so that the existence of risk management will actually hinder their goals. In addition, human resources in local government have low understanding risk management at all, so as internal auditors. If the expected internal auditor who will supervise units in local government does not understand risk management, how can they be expected to help organizational units to implement risk management? Based on the results of the interview, the regional government hopes that there will be cooperation between the regional government and the Educational Institution to conduct research on the right *strategies in implementing risk management. So far the strategy has been applied specifically to banking and financial companies and there is nothing specifically applied to the public sector, especially the regional government.*

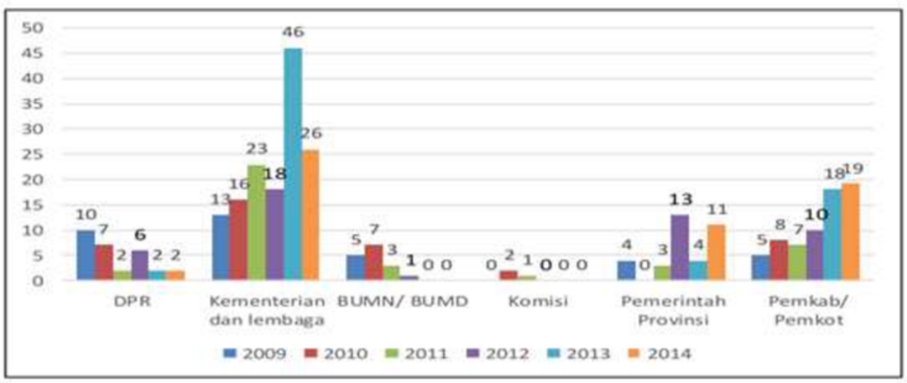
Keyword: Risk Management Local Government, Conflict of Interest, Human resources Quality, Management Commitment, Fraud

Cite this Article: Erlina, Devi Rosyana Putri, Iskandar Muda and Harnovinsah, the Model of Successful Risk Management Implementation in Local Government, International Journal of Civil Engineering and Technology, 10(02), 2019, pp. 310–319

http://www.iaeme.com/IJCIET/issues.asp?JType=IJCIET&VType=10&IType=02

1. INTRODUCTION

Nowadays, there has been a lot of fraud committed by government officials in implementing regional financial management. This can be seen from the number of government officials who are caught in corruption cases. Cases of fraud in local governments have been in the public spotlight. Based on data from the Corruption Perception Index (CPI) in Indonesia shows that Indonesia is the 80th most corrupt countries in the world while in ASEAN, Indonesia is a country that is prone to corruption or 2nd most corrupt compared to neighboring countries (Transparency International Indonesia, 2015). The number of cases of corruption in Indonesia during 2009 until 2014 can be seen in Figure 1.



Source: Report on the corruption eradication commission 2009-2014

Notes: DPR= National Council

BUMN/BUMD=State Owned Enterprises/Regional Owned Enterprises

Pemerintahan Provinsi= Province Government

Pemkab/Pemkot = Local Government

Figure 1. The number of cases of corruption in Indonesia during 2009 until 2014

Ministries and institutions also local government have indicated corruption but their financial statements received unqualified opinion. During the audit process from both internal and external auditors, fraud committed by some individuals cannot be detected by the auditor. Some government agencies affected by corruption cases include the Ministry of Energy and Mineral Resources of the Republic of Indonesia, the Corruption Eradication Commission has set the Minister of Energy and Mineral Resources as a suspect in alleged extortion cases related to their authority in operational ministries for fiscal year 2011-2013 (voaindonesia, September 3, 2014), previously the Ministry of Energy and Mineral Resources (ESDM) of the Republic of Indonesia was also involved in bribery cases (Republika Online, March 19, 2014). The Ministry of Religion was also a suspect by the Corruption Eradication Commission with cases of corruption in the procurement of goods and services in 2012-2013 and the process of organizing the Hajj was alleged to have committed corruption (BBC.com, May 22, 2014).

The Corruption Eradication Commission also designated the former Director General of Horticulture of the Ministry of Agriculture as a suspect related to the procurement of cultivation facilities in the Plant Pest Organizations at the Directorate General of Horticulture at the Ministry of Agriculture in the Fiscal Year 2013 (Okezone, February 9, 2016). There are more cases of fraud that occur in ministry agencies in Indonesia.

Fraud should be detected by the internal auditor. But in reality the Corruption Eradication Commission found fraud in financial management both in ministries, institutions and local governments. Effective internal audit should reduce the likelihood of fraud but in reality, the internal audit carried out cannot detect fraud. The reason, in conducting audits, internal audits still use a process approach. Private sector organizations have made a change of approach in carrying out internal supervision. The change of approach starts from system based internal audit to process based internal audit and now uses risk based internal audit.

Risk-based internal audit can be implemented if organization have implemented risk management in each organizational unit. Risk management is a strategy that can be applied by local governments in order to minimize the potential effects of risk like fraud. The forms of fraud commited in governments include corruption, bribery and others. Goal of Risk management is to avoid not achieving the intended local government goal.

The number of human resources from internal auditors are relatively small so audit of local government financial management cannot be carried out properly. A good strategy is needed so that internal audit becomes effective in preventing fraud. One strategy that is carried out is the risk management implementation.

Implementation of risk management in the public sector of government organizations is not an option but is a necessity if they want to achieved their strategic goals and objectives (Ahmeti & Kosovo, 2017). Risks has been defined as the posibility of loss, disadvantage, or destruction from local government operation day to day.

In addition, managing risk in the public sector has become more challenging than risk management in the private sector, due to the many regulations of the central and regional governments, bureaucracy, and various conflicts of interest of the stakeholders involved. Although in reality, there is no good theory of risk management strategies in the local government and research related to risk management in the local government lessly

However, adjustments can be made from the private sector risk management theories and strategies to improve the accuracy of the models and principles used. According to Solveig & Olsen, (2018) in their paper emphasize the fact that local governments handle many requirements and objectives, have high-level bureaucracy and regulations, risk management in the public sector becomes more complex and challenging. Leung & Isaacs, (2008) also support the idea that risk management in the public sector is very complex, mainly from various interests involved (mostly conflicting interests), political influence, etc. (Braig & Sellgren, 2011) also agree that managing risk in the public sector is more complicated than in the private sector.

They identified the main challenges identified in risk management in the public sector, which are as follows:

1. Mission objectives that override other considerations.
2. Frequent changes in leadership and vacant leadership positions.
3. Leaders who lack knowledge about risk management and business.
4. Separation of the operating budget from the program budget.
5. Lack of clear risk metrics.
6. Complex procedural requirements.
7. Limited risk culture and risk mindset.

There are several studies that apply risk principles and standards in public organizations. Countries that have implemented risk principles and standards include Australia, New Zealand, Canada, the United Kingdom and the United States. All G20 countries are committed to risk management in the public sector but not many publications are available regarding their risk practices and approaches in public sector organizations. Most countries currently fail to establish national risk management plans and strategies, or even if they have them, they cannot implement them in an effective way.

There are possible obstacles that will occur if the local government wants to implement risk management in each regional organization. Regional readiness in risk management is still relatively weak. In addition, according to (Erlina & Muda, 2018), the understanding of human resources in the local government regarding risk management is relatively low. the understanding Internal audits that are expected to help in implementating risk management are also very low.

Governments around the world must do a lot of research on risk management in their public sector. A highly recommended suggestion is to establish cooperation between the government and higher education institutions and research centers. Public-private partnerships in risk management will require a more qualitative commitment to risk management in the public sector. However, for this to happen, there is an increased awareness of the importance of risk management in public sector organizations. As a closing note, most emerging research must promote and support risk management in the public sector. Ask the central and regional governments for more commitment to implementation risk management (ahmeti)

Based on the results of previous research, the factors that are thought to be very influential on the successful implementation of risk management in the local government are management commitment, quality of human resources, research & development and regional head regulations. Besides these factors, a stakeholder conflict of interest will weaken the success of implementing risk management.

2. LITERTURE REVIEW

2.1. Risk Management

A risk is a set of conditions that hinder the achievement of objectives. Risk is possibility of loss, injury, disadvantage, or destruction resulting from organization operations. Risk management is a term used for the analysis of the process of analyzing, organizing, planning, directing and controlling organizational resources to overcome potential risks. Risk management, in general, is proactive, and includes all activities directed by management aimed at achieving optimal results professionally.

Making remarkable progress risk management must be applied using a defined strategy appropriate for the identified risks. The strategy must also be in line with the organization's goals and objectives. Risk management should be incorporated in the strategic planning process. some study concludes that organizations have multiple risks therefore management must develop portfolios of risks and sieve out only those that have significant impact on the achievement of their goals and objectives (Amulyoto, 2014)

Risk management is more beneficial in public sector than private companies. According to some previous researchers, the regional government more needs implementation of risk management. Nevertheless, there is still much progress to be made in learning from previous research, fine-tuning its process and recognizing the level of risk taking that is appropriate for a local government research organization, including how it can best manage its various operational and strategic risks. Mechanisms and means for greater sharing of institute experiences across the organization will allow better decision making around risk and opportunity. Currently, risk management is an optional decision making and management support tool at the institute level, although it is a management expectation for all departments and agencies as a whole. Looking ahead, further research will continue to build better understanding across local government to encourage the practice and use of risk management, integrating it into other local government management activities such as planning and project management. The process, related thinking and mindset still need to percolate more broadly to some groups.

2.2. Factors Affect Risk Management Implementation

2.2.1. Commitment Management

Diversity in the conceptualization and measurement of organizational commitment has made it difficult to interpret the results of previous research. Commitment, as a psychological state, has at least three separable components reflecting (a) a desire (affective commitment), (b) a need (continuance commitment), and (c) an obligation (normative commitment) to maintain employment in an organization. Every component is considered to develop as a function of different antecedents and to have different implications for on-the-job behavior. The aim of this reconceptualization is to aid in the synthesis of existing research and to serve as a framework for future research (Meyer & Alien, 1991). Rahmatika (2016) found that top management support had a negative and significant influence on the level of fraud. The study of the influence of top management commitment on risk management implementation has never been done. Top management commitment will have an influence on the successful implementation of the system, the method, as well as the success of risk management. The se evidence show one of the strategies for the successful implementation of risk management is through commitment from management. When management commitment increases, the quality of financial statements also increases (Tambingon et al., 2018). Researchers suspect the top management commitment will influence the success of the implementation of risk management so that fraud detection can be done earlier. Strong regional head commitment will encourage all elements in the organization to work harder in order to obtain maximum results (Mahlil & Yahya, 2017). The findings of this study reinforce the opinion of COSO (2009) which states that if the performance of leaders is good, then all components will be integrated and mutually in the management process. To achieve the goals of COSO emphasize leaders to take a central role in leading.

2.2.2. Self-Efficacy

In carrying out their work, a person does not work independently. It is important to understand how interactions between people, tasks, and the environment will affect one's performance. Bandura (1977) suggested that individual behavior is a result of interactions between environment and personal factors. Although self-efficacy is a subjective view of a person on his ability, it greatly influences his actions, motivation, perseverance, and behavior (Bandura 1991). Gist and Mitchell (1992) state that self-efficacy is an important motivational construct. This affects individual choices, goals, emotional reactions, effort, coping, and perseverance. Self-efficacy is related to individual task performance. Self-efficacy has a positive impact on performance because high self-efficacy allows humans to regulate effective behavior through a series of cognitive, motivational, and affective decision processes (Bandura 1997).

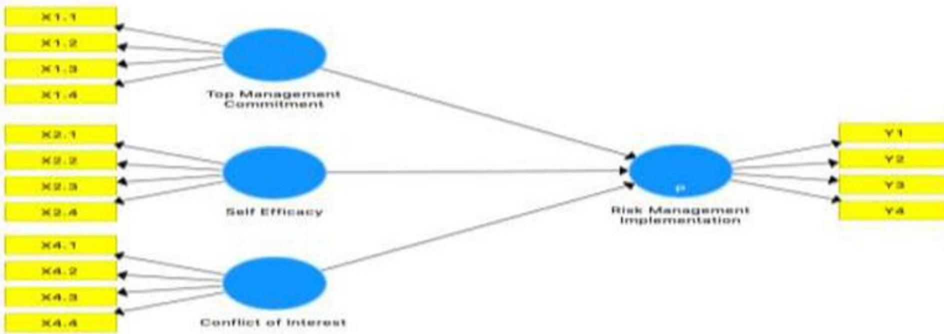
Self-efficacy is an important construct, it can increase energy, provide direction, and stimulate persistence (Porter et al., 1974). In fact, self-efficacy plays an important role for all professionals. Hayati et al. (2014) stated that five job characteristics included variations in skills, task identity, task significance, feedback and authority played an important role in fostering work motivation. Because auditing is a profession that provides services based on knowledge and experience with human resources as key elements, the motivation and ability of an auditor to achieve a goal is a strong advantage. Auditors with higher self-efficacy tend to motivate themselves to achieve goals. Therefore, self-efficacy will influence behavior by influencing motivation and self-confidence to overcome difficulties and improve performance. Someone who has high self-efficacy will increase the success of implementing risk management in the organization (Erlina, Putri, & Sopanah, 2018)

2.2.3. Conflict of Interest

In fact, agency relations in government organizations are an important concept. This is because the daily activities of these organizations are always related to delegation of authority, such as the provision of health services, education, and various other services related to the community, all delegated to the lower levels. The problem is, so far there has not been a real concept (theory) that embodies the agency relations model in the government sector. Studies relate to executive-legislative agency relationships conducted by researchers (see Thompson and Jones, 1986; McCubbins et al., 1987; Christensen, 1992; Lupia, 2001; and Fozzard, 2001) have grouped accounting sector public relations with models agency relations into the supervision system, budget manipulation, information asymmetry, and incentive systems between the executive and the legislature. Therefore, it is very interesting to examine further the executive and legislative agency relationships in the budget process of regional government. This study is motivated by research conducted by Niskanen (1971, 1975) and Weingast (1983). Niskanen's research (1971, 1975) says that executives are responsible for government budget inefficiencies. He focuses more on the executive role in the agency relationship. While on the other hand, Weingast's research, Moran (1983) shows that the legislature is responsible for the chaotic government budget caused by weak supervision. In his research in the local government of Great Britain, he viewed that agency relations in the government were dominated by the legislature. This is because, empirically, the legislature is the executive boss in the hierarchy of government authority he is the principal and the executive is the agent. Conflicts of interest in the government make it difficult to implement risk management. each has conflicting interests and many political interests. The main purpose of implementing risk management is to achieve government goals and reduce the risk of fraud and others. But in reality, it is precisely the authorities in the government who commit fraud. this is like the example presented in the introduction.

2.4. Research Framework and Hyphotesis

Based on the previous description, it is assumed that the successful implementation of risk management will be influenced by top management commitment, self-efficacy, conflict of interest. Based on the previous explanation, the framework of this research is as follows.



Sources: SmartPLS Result (2019).

Figure 2. Research Framework

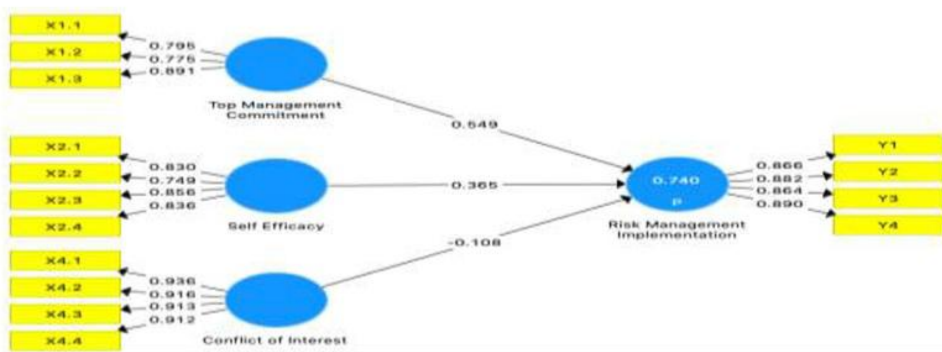
4. RESEARCH METHOD

This research was conducted to determine and analyze the influence of top management commitment, self-efficacy, and conflict of interest on the success of risk management implementation. The population of this study is internal auditors and all human resources involved in regional financial management in North Sumatra Province. The hypothesis is tested using PLS data processing program

5. RESULT AND DISCUSSION

5.1. Test Results of Measurement Model (Outer *Model*)

The test of the *outer model* begins with estimating or estimating parameters, namely by calculating the PLS *algorithm*. Based on the output analysis, the measurement model (outer*)* can be evaluated *model*) by testing convergent validity, validity as validity and reliability, all items are valid and reliable questions. The test results can be seen in figure 3 below



Sources: SmartPLS Result (2019).

Figure 3. Measurement Model

5.2. Path Coefficient Analysis Results *(Path coëficient s)*

The structural model in PLS is evaluated using *R-square* for the dependent variable and *path* coefficient value for the independent variable, then the significance is based on the *t- statistic* value *of* each *path* . *Smart* program PLS *Algorithm* results PLS in assessing the value of *path* and *R-square* coefficients can be seen in Table 1 in the following:

Table 1. *t* statistic

	Original Sample	Standard deviation	T statistics	P Value
Top Management -> Risk Management Implementation	0,549	0,103	5,338	0,000
Self-Efficacy -> Risk Management Implementation	0,365	0,099	3,670	0,000
Conflict of Interest -> Risk Management Implementation	-0,108	0,056	1,971	0,049

Sources: SmartPLS Result (2019).

Based on table 1, it can be concluded that top management commitment and efficacy efficacy have a positive and significant effect on the success of risk management implementation. Whereas conflict of onterest has a negative and significant effect on the success of the application of risk management. This means that if top management commitment and high self efficacy will increase the success of risk management implementation. While the greater the conflict of interest in the local government, the more difficult to implement risk management.

5.3. Discussion

Top leadership commitment has a positive effect on the successful implementation of risk management. Currently, there are no l local governments in Indonesia have implemented risk management. This is probably because top management and all the elements in the local government have not realized the importance of implementing risk management. As explained by previous researchers that local governments must implement risk management because risk management is not an option but a necessity. The risk in local government is far higher compared to banking and financial companies because there are many regulations that must be followed by both central regulations and regional regulations, political interests, conflicts of interest and the risk of not achieving the objectives of regional governments, namely improving people's welfare.

There are not many local government human resources who understand risk management. This lack of understanding causes them not to know the benefits of risk management. on the other hand, consultants, academics also only understand the application of risk management for banking and financial companies, so that the difficulties in using strategies that are in accordance with the conditions of local governments. The difficulties faced by human resources, consultants and academics require a certain approach. to reduce these difficulties it is necessary to increase the self-efficacy of each individual involved in risk management implementation. the self-efficacy human resources of the regional government in North Sumatra province are relatively high so that the difficulties in implementing management risks can be reduced (Erlina, Tarigan, Mulyani, Maksum, & Muda, 2018). We conclude that self-efficacy have a positive effect in affecting the risk management implementation. The result of this study support the result of the previous research. Confidence is an individual's belief in his ability to mobilize motivation, cognitive resources and actions needed to deal with the situation. Self-Efficacy is an individual's belief in his ability to mobilize motivation, cognitive resources and actions in situations faced by a person. Self-efficacy impact on the performance of management and auditors. Kuang's research (2009) shows that there is a significant and positive relationship between self-efficacy and the performance of internal auditors. If auditors have a high self-efficacy, he will be able to develop a strong personality, reduce stress and not easily affected so he can perform his task well. The results support the institutional theory. Its core idea is the establishment of an organization by the institutional environment pressure and it causes the occurrence of institutionalization. Another concept on institutional theory according to Donaldson (1995) is loose-coupling in the theory of institutional with open systems. Confidence is related to the individual's beliefs about his ability. Self-efficacy can specifically demonstrate the auditor's confidence in its ability to complete a given task. Individuals with a high level of self efficacy will feel confident about their performance capabilities (Erlina, Putri, et al., 2018)

The results of our research found that there was a high level of conflict of interest in the regional government. The higher the level of conflict of interest, the higher the difficulty in implementing risk management. The benefits of implementing risk management include saving government funds but in reality there are many political interests so that both the executive and legislative regional governments are suspected of being reluctant to implement risk management.

6. CONCLUSION

The success of implementing risk management in local government is strongly influenced by top management commitment, the high self-efficacy of individuals involved in the application of risk management and the low level of conflict of interest. In addition, there are several factors that are thought to influence its implementation, namely the improvement of the quality of human resources through training and the need for regional regulations regarding risk management.

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