

Strategy for increasing Internal Audit Capability on Inspectorate of Jember Regency

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ABSTRACT

One of Indonesia's Government way to eradicate corruption throughout the region is to increase Internal Audit Capability Model at the Provincial/District/City Inspectorate. Petraşcu dan Tleanu (2014) stated that internal audit has various responsibilities to support management in building anti-fraud/corruption mechanisms, assessing fraud risks at the organizational and business process levels, assessing connections between fraud risks and internal control, supporting auditor efforts in fraud investigations and reporting to the audit committee. The East Java Province BPKP Representative's assessment of the business processes of the Jember Regency Inspectorate until the end of 2022 concluded that the Jember Regency Inspectorate only obtained level 2 IACM (Internal Audit Capability Model). This research aims to analyze several factors that influence internal audit capability, evaluate business processes and formulate strategies that the Jember Regency Inspectorate can use to improve its internal audit capability. Strategy formulation is carried out by analyzing key organizational factors using the IE, SWOT and QSPM matrices. The research results show to improve supervisory governance, share knowledge regarding supervision, develop policies/SOPs related to independence, monitor follow-up results of supervision and recruit auditors.

A. INTRODUCTION

The Indonesia Corruption Eradication Commission (KPK) considers that the Regional Inspectorate as a supervisory agency at the Regional Government level is considered not optimal in preventing the occurrence of KKN (Corruption, Collusion and Nepotism) at the regional level. During 2004-2022, KPK handled 641 local government corruption crimes or 53.44% of the total 1,351 corruption crimes handled by KPK (KPK, 2023). Regional inspectorates as internal government audit institutions at the regional level, play a role in eradicating corruption through investigative audits (Dudy et al., 2023). Apart from investigative audits, regional inspectorates also have a whistleblowing system mechanism to reveal suspected criminal acts of corruption (Nickolan et al., 2018).

The Regional Inspectorate as the government's internal audit agency is also known as APIP. The definition of Government Internal Supervision Apparatus (APIP) according to Peraturan Pemerintah Nomor 60 Tahun 2008 about Government Internal Control Systems (SPIP) Pasal 49 is a government agency formed with the task of carrying out internal supervision within the central government and/or regional government.

The Indonesia government, through Undang-undang Nomor 1 Tahun 2022 about Financial Relations between the Central Government and Regional Governments, Pasal 152 emphasizes strengthening Inspectorate Capabilities to support improving the quality of local government budgeting (APBD) management. The APIP (Government Internal Audit Apparatus) Capability Assessment Process can be assessed using the IACM (International Audit Capability Model) method published by The Institute of Internal Auditors Research Foundation (IIARF).

The IACM standards were then adopted in Indonesia by the BPKP (Financial and Development Supervisory Agency) as the supervisor of APIP and used as a guideline for assessing the level of internal audit capability. The IACM method categorizes the quality of internal audit institutions into 5 progressive levels, meaning that higher the level, the internal audit capability better. Level 1 (initial) internal audit capability indicates that the Regional Inspectorate does not yet have permanent monitoring practices and is very dependent on individual performance. Level 2 (Infrastructure) shows that there are routine and repeated monitoring practices but only some of them are in accordance with internal audit standards, while Level 3 (integrated) shows that professional practices are uniform and in accordance with internal audit standards and Institution has also carried out 3E consultancy and assessment activities (efficient, economical and effective) (Safitri N & Halim A, 2017).

The number of Provincial/Regency/City Inspectorates in the East Java Province region are 39 Institution. By the end of 2022, 24 Inspectorates or 20.51% had successfully reached level 3 (integrated). However, there are still Regional Inspectorates in the East Java Province region which is still at level 2, namely 15 Institution or 20.51%. The results of IACM levels mapping for East Java Province in 2022 can be seen in Table 1.

Table 1
Mapping of IACM Levels at East Java Province Level in 2022

No.	IACM Level	Number of APIP	Percentage
1	1 (<i>initial</i>)	0	0,00
2	2 (<i>infrastructure</i>)	15	20,51
3	3 (<i>integrated</i>)	24	79,49
Total		39	100,00

Source: Processed from The Performance Report 2022 of East Java Province BPKP Representative

According to the Performance Report 2022 of East Java Province BPKP Representative as shown in Table 2, the IACM level of the Jember Regency Inspectorate is still lower than that of Inspectorates in surrounding Regencies (Bondowoso Regency, Lumajang Regency and Banyuwangi Regency). This shows that the Jember Regency Inspectorate has not been optimal in supervising the management of the APBD. The Jember Regency Inspectorate needs improvements to its business processes (supervision) and supporting elements (personnels, finances and infrastructures).

Table 2
Comparison of IACM Level between the Jember District Inspectorate and the surrounding District Inspectorates

No.	Regional Inspectorate	IACM Level
1	Jember Regency	2 (<i>infrastructure</i>)
2	Lumajang Regency	3 (<i>integrated</i>)
3	Banyuwangi Regency	3 (<i>integrated</i>)
4	Bondowoso Regency	3 (<i>integrated</i>)

Source: Processed from The Performance Report 2022 of East Java Province BPKP Representative.

Based on this, this research aims to (1) identify the business process of supervision and supervisory support at the Jember Regency Inspectorate, (2) analyze the factors that influence the assessment of IACM level at the Jember Regency Inspectorate, (3) formulate a strategy for increasing IACM level at the Inspectorate Jember Regency.

B. METHOD

This research was conducted at the Jember Regency Inspectorate, East Java Province, with the research objects being Functional Auditor Officials (PFA) and Administrative Department Officials (Personnel, Finance and General Affairs). The research was conducted between January – March 2023.

The types of data used in this research are primary data and secondary data. Primary data is used in the research questionnaire to determine the factors that influence IACM level. Apart from that, primary data can be obtained by direct interviews (In depth interviews) using guided questions with officials at the Jember Regency Inspectorate. Secondary data was collected through a literature review on internal auditors in the form of IACM Evaluation Guidelines from BPKP, Indonesian Government Internal Auditor Standards (SAIPI), JFA (Functional Auditor Position) Implementation Guidelines published by the BPKP JFA Development Center.

The population in this study were all employees at the Jember Regency Inspectorate. The sample selected for the SEM PLS quantitative analysis which identified variables influencing IACM level was simple random sampling with a minimum of 30 respondents consisting of Functional Auditor Officials (PFA) as implementers of supervisory activities and administrative employees as supporters of supervisory activities. A minimum sample of 30 respondents was taken because according to Zuhdi et al. (2016) the minimum number of samples required to carry out SMART PLS analysis is 30 samples.

Descriptive analysis and strategy formulation using purposive sampling with BPKP auditor informants who have been assisting in increasing IACM level, Jember Regency Inspector, Jember Regency Inspectorate Secretary, Inspectorate and P2UPD auditors, and employees of the Program and Reporting section of the Jember Regency Inspectorate.

The analysis used in this research is descriptive analysis to determine the business processes of the Jember Regency Inspectorate with analytical tools in the form of Peraturan Kepala BPKP Nomor 8 Tahun 2021 about the assessment of the Capability of Government Internal Supervisory Apparatus (APIP) in Ministries/Institutions/Regional Governments. SEM (Structural Equation Modeling) analysis is also used to determine the factors that influence IACM level. SEM analysis is a multivariate analysis method that can be used to simultaneously describe linear relationships between observed variables (indicators) and variables that cannot be measured directly (latent variables) (Prihandini & Sunaryo, 2011). Strategy formulation to increase IACM level at the Jember Regency Inspectorate using a strategic formulation framework (David, 2017) in the form of IFE and EFE, SWOT and QSPM matrices.

C. RESEARCH FINDING AND DISCUSSION

Factors Analysis Affecting IACM level at the Jember Regency Inspectorate

In this research, a description of the respondents was obtained from the results of distributing questionnaires to respondents, namely 30 questionnaires. These respondents are representatives of Jember Regency Inspectorate employees consisting of Functional Auditors/Government Supervisors and secretarial employees. According to Zuhdi et al. (2016) the minimum number of samples required to carry out SMART PLS analysis is 30 samples while Hair et al. (2017) said that small samples are not an issue when using Partial Least Square (PLS) SEM analysis.

Validity and Reliability Test (Outer Model)

Table 3 shows the results of convergent validity testing and reliability testing. The validity test is assessed using loading factors. Based on Table 3, all items have a loading factor value of >0.50 . This means that it meets the criteria of Hair et al. (2017). The reliability test uses values from composite reliability (CR) and Cronbach's alpha (CA). Items are considered reliable if the CR and CA values are >0.70 (Hair et al., 2017).

Based on table 3, it is known that all research items (Independence, Compliance with Auditing Standards, Adequate Human Resource Management, Effectiveness of Internal Audit Function) have a loading factor value of >0.50 , so all of these research items are valid. Then the composite

reliability (CR) and Cronbach's alpha (CA) values of all research items have values >0.70, so all research items are reliable.

Table 3 Validity (Loading Factor) and Reliability (CR and CA) Test Results

Item	Loading Factor	Composite Reliability	Cronbach's Alpha
Independence		0,840	0,764
IO1	0,668		
IO3	0,825		
IO4	0,827		
IO5	0,688		
Compliance with Auditing Standards		0,811	0,668
SA1	0,738		
SA2	0,861		
SA3	0,698		
Adequate Human Resource Management		0,837	0,757
SD1	0,663		
SD2	0,616		
SD3	0,736		
SD4	0,768		
SD5	0,769		
Effectiveness of Internal Audit Function		0,868	0,824
EF1	0,617		
EF2	0,665		
EF3	0,599		
EF4	0,781		
EF5	0,841		
EF7	0,812		

Source: Data Processed (2023)

Structural Model Evaluation (Inner Model)

1) Collinearity Test

The collinearity test is used to test the relationship between latent variables. Multicollinearity can cause the model to experience problems that can cause data redundancy. Hair et al. (2017) stated that the collinearity test can be seen using the Variant Inflation Factor (VIF) value. Results that meet the criteria can be obtained if the VIF value is <5.00. The results of the collinearity test can be seen in Table 4.

Table 4 Variable Collinearity Test Results

Variable	Independence	Compliance with Auditing Standards	Adequate HR Management	Effectiveness Internal Audit Function
Independence				1,113
Compliance with Auditing Standards				1,306

Variable	Independence	Compliance with Auditing Standards	Adequate HR Management	Effectiveness of Internal Audit Function
Adequate HR Management				1,193
Effectiveness of Internal Audit Function				

Source: Processed from SmartPLS V3.2.9 (2023)

Table 4 informs that no VIF value is greater than 5.00. This means that there is no collinearity between variables.

2) Coefficient of Determination (R-Square)

The coefficient of determination test value (R-square) is used to assess the influence of the substance of the exogenous latent variable on the endogenous variable. The influence category is substantial if the R-square value is at least 0.75, moderate if the R-square value is at least 0.50, and weak if the R-square value is at least 0.25 (Hair et al., 2019).

Table 5 Determination Coefficient Test Results (R-square)

Variable	R-square
Effectiveness of Internal Audit Function	0,549

Source: Processed from SmartPLS V3.2.9 (2023)

Table 5 shows that the R-square value is 0.549, which means that the variable effectiveness of the internal audit function can be explained by variables in the model of 54.9%, and the remaining 45.1% is explained by other variables outside the model. The internal audit function effectiveness variable with an R-square value of 54.9% indicates that the model can be categorized as a moderately predictive model.

3) Hypothesis Test

The results of hypothesis testing on the influence of independence variables, compliance with audit standards, and adequate human resource management on Internal audit function effectiveness are in table 6.

Table 6 Hypothesis Test Results

	Original Sample (O)	T Statistic (O/STDEV)	P Values	Results
Adequate HR Management ----> Effectiveness of Internal Audit Function	0,417	3,009	0,003	H1 accepted
Independence ----> Effectiveness of Internal Audit Function	0,152	0,987	0,324	H2 rejected
Compliance with Auditing Standards -> Effectiveness of Internal Audit Function	0,402	2,273	0,023	H3 accepted

Source: Processed from SmartPLS V3.2.9 (2023)

Testing of research hypotheses is measured by t statistics and p values. The hypothesis is supported and significant if the t statistic value is greater than 1.96 and the p value is less than 0.05.

Table 6 shows that the t statistics value for adequate HR management and compliance with internal audit standards is more than 1.96 and the p value is less than 0.05. This means that adequate human resource management and compliance with internal audit standards positively and significantly influence the effectiveness of internal audit functions. The t statistics value of the independent variable is less than 1.96 and the p value is more than 0.05. This means that independence does not have a significant effect on the effectiveness of internal audit functions. This finding is different from previous research which examined the relationship between independence and the effectiveness of internal audit functions. Alzeban and Gwilliam (2014) stated that an independent audit function will encourage the achievement of audit objectives and have a positive impact on the effectiveness of internal audit.

Descriptive Analysis of IACM Level at the Jember Regency Inspectorate

Qualitative descriptive analysis is a term used in qualitative research for a study that is descriptive in nature. Qualitative descriptive analysis is focused on answering research questions related to who, what, where and how an event or experience occurs until finally it is studied in depth to find patterns that emerge from the event (Kim H, et.al., 2016).

Qualitative analysis in this research uses tools in the form of Peraturan BPKP Nomor 8 Tahun 2021 about Capability Assessment of Indonesia Government Internal Audit Apparatus (APIP) in Ministries/Institutions/Regional Governments. The purpose of this descriptive analysis is to obtain an overview of the condition of internal audit capability through IACM level at the Jember Regency Inspectorate. The results of observations regarding internal audit capability at the Jember Regency Inspectorate are that there are 2 elements with 6 topics that are still at level 2 of IACM with the following description:

1) Elements of Professional Practice

- Internal Audit Planning

The policy for preparing the Annual Internal Audit Work Program (PKPT) has been included in the Internal Audit Charter (IAC) in accordance with the decision of the Peraturan Bupati Jember Nomor 188.45/139/1.12/2019 about the policy for internal audit implementation of the Regional Government of Jember Regency, but there are no guidelines for preparing a monitoring plan based on risk.

The Jember Regency Inspectorate already has a risk-based internal audit planning but it has not been approved by the Regent of Jember and is not in accordance with the standards in the Peraturan Deputy Kepala BPKP Nomor 8 Tahun 2020 about risk-based internal audit planning.

- Quality Assurance and Improvement Program

The Jember Regency Inspectorate does not yet have guidelines regarding the quality assurance and improvement program (QAIP). The Jember Regency Inspectorate has also not carried out an internal review (peer review between auditors) and has not attached documentation of a tiered review of internal audit assignments.

2) Role and Services Elements

- Compliance Audits

The Jember Regency Inspectorate has included compliance audits in the audit charter issued by Bupati Jember Nomor 188.45/139/1.12/2019, however the Jember Regency Inspectorate does not yet have guidelines for implementing compliance audits and SOPs (Standard Operating Procedures) for following up on monitoring results.

The Jember Regency Inspectorate has carried out compliance audit assignments, one of which is a compliance audit for the management of waste/cleaning service levies at the Environmental Service in 2021 and Quarter 1 of 2022 but has not attached documentation of its implementation starting from the planning, implementation, reporting and follow-up to the results of the compliance audit.

- Performance Audits

The Jember Regency Inspectorate has included performance audits in the audit charter issued by Bupati Jember Nomor 188.45/139/1.12/2019, however the Jember Regency Inspectorate does not yet have guidelines for implementing performance audits.

The Jember Regency Inspectorate has carried out performance audits including performance audits on service quality for the issuance of practice licenses recommendations for health workers

in 2022 but has not attached documentation starting from the planning, implementation, reporting and follow-up process of the results.

- Assurance of Governance, Risk Management, and Organizational Control

The policy regarding Assurance for Governance, Risk Management and Organizational Control is included in the Audit Charter but does not yet have guidelines for independent assessment of the maturity of the implementation of the internal control system.

The Jember Regency Inspectorate has carried out an independent assessment of the maturity of the integrated internal control system, but has not yet attached documentation including assignment orders, quality control, quality assurance work papers, self-assessment of the maturity of the internal control system, review report sheet and report on the results of the self-assessment of the maturity of the internal control system in the Jember Regency Government.

- Consultancy Services

Consultancy services carried out by the Jember Regency Government based on audit charter Number 188.45/139/1.12/2019 are mentoring, assistance and socialization. The Jember Regency Inspectorate has carried out consultancy services but has not yet accompanied the assignment supporting documents.

Strategy to increase internal audit capability at the Jember Regency Inspectorate

The first stage in developing a strategy to increase internal audit capability at the Jember Regency Inspectorate is to identify key internal and external factors at the Jember Regency Inspectorate. The weight and rating values for each identified internal and external factor are shown in Tables 7 and 8.

Table 7. Internal Factor Evaluation Results Matrix (IFE)				Table 8. Eksternal Factor Evaluation Results Matrix (EFE)			
Internal Factor	Weight	Rating	Score	Eksternal Factor	Weight	Rating	Score
Strengths				Opportunities			
Support resources sufficient	0,11	3,86	0,42	Development auditors cooperation with third parties	0,10	3,57	0,35
Availability of an adequate budget	0,11	3,86	0,42	Joint Audit with other inspectorates	0,10	3,43	0,33
Availability of implementation and reporting guidelines	0,08	3,71	0,30	Support from the Regent of Jember to increase the level of IACM	0,12	3,86	0,47
Employee Income	0,08	3,86	0,31	Professional certification program free with STAR funding	0,10	3,43	0,33
Utilizing Information technology for internal audit work	0,11	3,14	0,34	Assistance in increasing internal audit capabilities by BPKP	0,10	3,71	0,36
Weaknesses				Threats			
Lack of auditors	0,14	1,29	0,17	Public Policy Changes that affect business processes	0,10	2,86	0,28
Internal audit planning is not risk based	0,08	1,43	0,12	Moratorium on procurement of civil servants	0,12	2,86	0,35
Internal review between auditors has not been carried out	0,08	1,43	0,12	Relationship between the Jember Regency Inspectorate and the Internal Auditor Professional Organization not yet well established.	0,07	3,14	0,23
Auditors rarely collect credit figures according to applicable regulations	0,11	1,86	0,20	Conflict of Interest with Auditee	0,10	3,14	0,31
Consultancy activities and performance audits are not well documented.	0,11	1,29	0,14	Audit findings were not followed up by the Auditee.	0,10	3,43	0,33
Total	1,000		2,53	Total	1,000		3,35

The total score obtained from the IFE matrix was 2.53 and the EFE matrix was 3.35. Then these values are entered into the IE matrix. The IE matrix is obtained from the plot of the total score of the IFE matrix as the x-axis and the EFE matrix as the y-axis. The plot results show that the position of the Jember Regency Inspectorate is in quadrant II. The right strategy for the institution to implement is grow and build.

Next, carry out a matching stage between internal and external factors by combining the IFE matrix and EFE matrix into a SWOT matrix to determine strategic alternatives while monitoring the relationship between strategies. The SWOT matrix describes how the external opportunities and threats faced by an agency can be adjusted to its internal strengths and weaknesses (Siregar, 2020). There are 9 alternative strategies for increasing internal audit capability at the Jember Regency Inspectorate that can be implemented as shown in Table 9

Table 9. SWOT Matrix and Alternative Strategies

Strategy S-O	Strategy W-O
1. Sharing knowledge about internal audit (S1, S2,S3, S4, S5, O1, O2, O3, O4, O5).	1. Recruitment Auditor path of first appointment, transfer, adjustment and promotion (W1, O3).
Strategy S-T	Strategy W-T
1. Monitoring follow-up results of internal audit assignments (S3,S5, T5). 2. Develop policies related to Auditor Independence (S1, S3, T4).	1. Improvement of internal audit governance (W2, W3, W4,W5, T1, T5).

Source: data processed (2023)

The final stage is decision making to determine priority strategies in an effort to increase internal audit capability at the Jember Regency Inspectorate by using QSPM analysis. QSPM is designed to determine the relative attractiveness and evaluate alternative strategic options that can be implemented objectively, based on internal and external factors that have been identified in the previous EFE and IFE matrices. QSPM is the final stage matrix in the strategy formulation analysis framework (Dewi, 2019). The results of the QSPM analysis are shown in Table 10.

Table 10. QSPM Matrix

No	Strategy	TAS	Priority
1.	Sharing knowledge about internal audit	6,00	2
2.	Recruitment Auditor path of first appointment, transfer, adjustment and promotion	5,10	5
3.	Improvement of internal audit governance	7,00	1
4.	Monitoring follow-up results of internal audit assignments	5,53	4
5.	Develop policies related to Auditor Independence	5,91	3

Source: data processed (2023)

Based on the results of the strategic priority analysis using the QSPM matrix, improving internal audit governance became the main strategy chosen and then a program design was prepared in the context of technical implementation of the proposed priority strategy as shown in Table 11.

Tabel 11. Implementasi Strategi Peningkatan Kapabilitas APIP

No.	Strategy	Program	Executor
1.	Improvement of internal audit governance	<ul style="list-style-type: none"> Improvement of facilities and infrastructure Use of information technology in internal audit Improvement of internal audit procedures 	<ul style="list-style-type: none"> Inspector Inspectorate Secretary Inspectorate Auditors

No.	Strategy	Program	Executor
2.	Sharing knowledge about internal audit	• Assistance in improving internal audit capabilities	• BPKP • Inspectorate Auditors
		• Auditor training and certification	• BPKP • ADB STAR • Inspectorate Auditors
		• Joint audit	• Inspectorate Auditors
3.	Develop policies related to Auditor Independence	• Technical guidance on auditor independence	• BPKP • Inspectorate Auditors
		• Creation of standard operating procedures (SOPs) for auditor independence	• Inspectorate Secretary
4.	Monitoring follow-up results of internal audit assignments	• Assistance in monitoring follow-up results of internal audit assignments	• BPKP • Inspectorate Auditors
		• Monitoring follow-up results of internal audit assignments	• Inspectorate Auditors
5.	Recruitment Auditor path of first appointment, transfer, adjustment and promotion	• Recruitment of Auditors from various channels	• Regional Personnel Agency (BKD) • Inspector

D. CONCLUSION AND RECOMMENDATION

Conclusion

Adequate human resource (HR) management and compliance with audit standards have a positive effect on the effectiveness of the internal audit function at the Jember Regency Inspectorate, but independence does not have a significant effect on the effectiveness of the internal audit function at the Jember Regency Inspectorate.

There are 2 elements and 6 topics that are still at level 2 of internal audit capability based on IACM, namely element (1) professional practice with the topics of monitoring planning, assurance programs and quality improvement and element (2) roles and services with the topics of compliance audits, performance audits, consultancy services, assurance on governance, risk management and organizational control.

Increasing the level of internal audit capability at the Jember Regency Inspectorate can be achieved by using a grand strategy, namely grow and build, which can be reduced to 5 specific strategies which then become programs and are proposed to the Jember Regency Government to be implemented in policies to increase internal audit capability at the Jember Regency Inspectorate.

Recommendation

The support of the Regent of Jember is highly expected in improving the internal audit capability of the Jember Regency Inspectorate. Forms of support can be in the form of budgets, office facilities and infrastructure, and recruitment of government employees with the formation of auditors.

Competency development of employees/auditors must be carried out continuously in accordance with developments in science and changes in government regulations/policies so that the

implementation of internal audits carried out by Jember district Inspectorate auditors is in accordance with professional ethical standards and norms.

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