

Regulatory Compliance, Financial Oversight, and Allocative Efficiency in Village Fund Management: A Governance Perspective

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Abstract

This study examines Village Fund management within a public financial management framework from a governance perspective, focusing on regulatory compliance, financial oversight, and allocative efficiency in decentralized fiscal systems. Using a qualitative approach, data were collected through interviews, observations, and document analysis in Kemadang Village. The findings indicate that financial regulatory and oversight mechanisms are effectively operationalized through structured budgeting, reporting, and audit systems, reflecting strong procedural compliance. However, regulatory effectiveness remains limited, as transparency and accountability practices are predominantly administrative and lack performance-based financial information. Financial control mechanisms reduce corruption risks but do not effectively mitigate inefficiency or enhance allocative effectiveness due to the absence of cost-benefit analysis and measurable indicators. These findings reveal a compliance, effectiveness gap and highlight the importance of performance-based evaluation in improving allocative efficiency.

Keywords: Public financial management, allocative efficiency, financial oversight, regulatory compliance, governance

JEL Classification: G28; G38; H72; H83

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Introduction

Village development constitutes a strategic component of fiscal decentralization policy aimed at strengthening equitable development and improving community-based welfare. Within Indonesia's national regulatory framework, Law Number 6 of 2014 concerning Villages grants extensive authority to village governments to independently manage local resources and finances through the Village Fund scheme. This policy represents a formally regulated fiscal transfer mechanism administered by the central government as part of a decentralized public financial governance system. Village Funds represent a strategic fiscal instrument designed to support rural development and community empowerment, as outlined in the official Village Fund handbook issued by the Ministry of Finance (Kementerian Keuangan Republik Indonesia, 2017). From a political economy perspective, Village Fund governance represents an intersection between institutional behavior and public financial management. While governance theories explain how actors comply with regulations, financial management frameworks evaluate whether such compliance generates allocative efficiency and measurable economic outcomes. Therefore, Village Funds should be assessed not only in terms of regulatory adherence but also in terms of financial performance and return on public expenditure. From a public financial management perspective, Village Funds should be evaluated not only in terms of regulatory compliance but also in terms of allocative efficiency, financial performance, and return on public expenditure within decentralized fiscal systems.

From a theoretical perspective, fiscal decentralization is expected to enhance allocative efficiency and improve responsiveness to local needs (Oates, 1999; Shah, 2007). However, empirical evidence demonstrates that decentralization outcomes are highly dependent on institutional quality, oversight mechanisms, and governance capacity (Rodden, 2004; Weingast, 2009). Without effective monitoring and accountability structures, decentralized fiscal transfers may increase corruption risks, weaken fiscal discipline, and generate allocative inefficiencies. Recent studies further highlight that fiscal decentralization outcomes are highly contingent upon governance quality, institutional capacity, and political economy dynamics, rather than occurring automatically through fiscal transfer mechanisms (Lewis, 2023; World Bank, 2022).

In 2024, the Indonesian government allocated IDR 81.2 trillion to Village Funds, an increase from IDR 71.3 trillion in 2023 (Ministry of Finance, 2024). The magnitude of this allocation underscores the strategic importance of Village Funds as regulated public financial

instruments. Within a financial governance framework, Village Fund management reflects a principal–agent relationship in which village officials (agents) manage public funds on behalf of the community (principal). Agency Theory explains that information asymmetry and monitoring limitations may generate moral hazard and agency costs (Jensen & Meckling, 1976; Eisenhardt, 1989). In decentralized governance systems, weak oversight mechanisms may intensify such agency risks (Bardhan & Mookherjee, 2006).

Despite the existence of regulatory frameworks and administrative reporting systems, concerns regarding governance effectiveness persist. The Corruption Eradication Commission (2023) recorded more than 600 cases of Village Fund misuse in the past five years, indicating weaknesses in financial oversight systems. Furthermore, a survey conducted by the Ministry of Home Affairs (2022) reveals that only 37% of villages have implemented informative and participatory transparency practices, while the majority remain limited to procedural compliance. Public financial management literature emphasizes that formal compliance with reporting procedures does not automatically guarantee performance accountability or allocative efficiency (Schick, 1998; Hood, 1991; World Bank, 2018).

Recent empirical studies reinforce this concern. Saputra and Setiawan (2021) demonstrate that fiscal decentralization structures are associated with corruption risk indicators in Indonesia, highlighting the importance of accountability mechanisms in mitigating misuse. Yuni (2022) finds that transparency, internal control systems (SPIP), and human resource competence significantly influence the quality of Village Fund management. Similarly, Junaidi (2023) concludes that while administrative transparency has improved, public literacy and outcome-based evaluation remain limited, indicating that procedural compliance does not necessarily translate into substantive oversight.

At the institutional performance level, Wardani (2024) and He and Ismail (2023/2024) show that performance-based budgeting and financial reporting quality enhance accountability only when supported by measurable performance indicators and reliable data systems. Community-based research further indicates that transparency must be complemented by participatory evaluation and sustainable economic outcomes to generate meaningful impact (Ratri, 2024; Tahirs, 2023). Moreover, digital governance studies suggest that although digital reporting systems can improve disclosure, their effectiveness depends on infrastructure readiness and user capacity (Kolaborasi Journal, 2024; Dukalaa et al., 2025). From a broader

policy perspective, Hidayat (2025) emphasizes that fiscal decentralization outcomes are highly context-dependent and shaped by governance capacity and institutional arrangements.

Collectively, these studies highlight two critical limitations in the current literature. First, most research examines transparency, accountability, or internal control as independent determinants of governance quality, without explicitly distinguishing between regulatory compliance and regulatory effectiveness. Second, although Agency Theory has been widely applied in public governance studies, its explicit integration into village-level fiscal management, particularly to explain the persistence of information asymmetry and allocative inefficiency, remains limited.

Accordingly, this study advances the state of the art in three ways. First, it introduces a regulatory compliance–regulatory effectiveness analytical framework tailored to Village Fund governance. Second, it integrates Agency Theory with decentralized financial oversight analysis to explain gaps between procedural adherence and substantive financial performance. Third, it empirically maps this regulatory gap at the village level, providing evidence on how formal compliance mechanisms translate, or fail to translate, into effective fiscal governance outcomes within a developing economy context.

Kemadang Village in Gunungkidul Regency provides a relevant empirical setting for examining this issue. The village has formally implemented budgeting procedures, financial recording through the Village Financial System (SiKUDes), and mandatory reporting mechanisms. In 2023 and 2024, the village received IDR 5.04 billion and IDR 4.71 billion, respectively, a portion of which was allocated to community empowerment programs. Administratively, regulatory compliance appears to function adequately. However, preliminary field findings indicate that transparency remains largely compliance-based rather than performance-based. Community members are aware of program implementation but lack understanding of budget structures, performance indicators, and economic impact assessments. Outcome-based evaluation and cost–benefit analysis are not systematically integrated into participatory oversight mechanisms.

This condition suggests the existence of a regulatory gap between procedural compliance and substantive financial effectiveness. Understanding this gap is essential for strengthening village-level public financial governance and ensuring that Village Fund allocations generate sustainable community empowerment outcomes.

Research Gap and Novelty

Existing literature on village financial governance has extensively examined transparency, accountability, and internal control as determinants of governance quality. However, most studies treat these variables independently and focus primarily on procedural compliance rather than substantive governance outcomes. As a result, there is limited analytical distinction between whether financial governance mechanisms merely fulfill regulatory requirements or effectively generate measurable socio-economic impact.

Furthermore, although Agency Theory has been widely applied in public sector governance, its application at the village-level fiscal system remains largely focused on corruption risk and monitoring mechanisms, without sufficiently explaining inefficiency arising from weak outcome-based evaluation. This study addresses these gaps by introducing a compliance, effectiveness analytical framework, which explicitly distinguishes between procedural regulatory compliance and substantive regulatory effectiveness. This research represents one of the first attempts to systematically conceptualize and empirically examine this gap within village-level fiscal governance.

In addition, this study extends Agency Theory by integrating it with Public Value Theory and Stewardship Theory, providing a more comprehensive explanation of governance dynamics in decentralized fiscal systems. While Agency Theory emphasizes monitoring and control, Public Value Theory highlights outcome-oriented governance, and Stewardship Theory offers an alternative perspective that public officials may act in the collective interest. Therefore, this study contributes theoretically by refining governance analysis beyond compliance, and practically by providing a framework for improving the effectiveness of Village Fund management.

Research Objectives

This study aims to evaluate the implementation of financial regulatory and oversight mechanisms in Village Fund management by distinguishing between regulatory compliance and regulatory effectiveness. Specifically, the study seeks to assess whether existing governance practices not only fulfill formal regulatory requirements but also generate measurable socio-economic outcomes and enhance allocative efficiency in community empowerment programs.

Based on these considerations, this study addresses the following research questions:

1. How are financial regulatory and oversight mechanisms operationalized in the management of Village Funds in Kemadang Village?
2. To what extent do existing transparency and accountability systems demonstrate both regulatory compliance and regulatory effectiveness within the village financial governance framework?
3. Do financial control and reporting mechanisms effectively mitigate inefficiency risks and enhance the allocative effectiveness of community empowerment expenditures?

Literature Review

Village Government

Village government functions as a formal governmental institution operating within the national public administration system. Under Law Number 6 of 2014 on Villages, village government consists of the village head and village officials who collectively serve as the executive authority responsible for administering village governance. Their authority is grounded in deliberative decision-making processes through village assemblies and encompasses development implementation, community empowerment, regulatory formulation, and administrative management.

The village head holds the highest executive authority at the village level and bears primary responsibility for village financial management and governance. According to Ministry of Home Affairs Regulation No. 84 of 2015, the village head leads the organization of village administration, development planning, community development, and empowerment programs (Sugiman, 2018). Village officials, including the village secretary, technical implementers, and territorial officers, support the village head in executing administrative, financial, and operational functions (Gunawan, 2013; Indrianasari, 2017).

From a financial governance perspective, village governments operate as local agents entrusted with managing public financial resources under a regulatory framework established by the central government. This position inherently involves agency relationships and requires effective regulatory oversight to mitigate governance risks.

Village Budget

Village budgets constitute a component of the national public finance system. Under Law Number 2 of 2020, village funds originate from the State Budget (APBN) and are channeled through regional budgets (APBD) to finance governance administration, infrastructure development, community empowerment, and capacity-building programs.

The allocation of village funds is determined based on demographic characteristics, poverty levels, geographic conditions, and development challenges. The objective of the village budget is not only to finance development but also to promote economic empowerment and sustainable welfare improvement. The disbursement process follows a regulated fiscal transfer mechanism, flowing from the State Treasury Account (RKUN) to the Regional Treasury Account (RKUD), and subsequently to the Village Treasury Account (RKD).

According to Government Regulation No. 60 of 2014, village finances are an integral part of regulated public expenditure and must comply with established financial control and accountability standards. From a G38/G28 perspective, village budgets function as regulated public financial instruments subject to oversight, reporting requirements, and compliance mechanisms.

Village Budget Management

Village fund policy represents a fiscal decentralization strategy aimed at enhancing community welfare through regulated financial transfers. The allocation and distribution of village funds involve coordination among multiple government levels, particularly district and municipal authorities. Village fund allocation is calculated based on basic allocations and geographic difficulty indices, including access to infrastructure, public services, and transportation.

Village fund disbursement is conducted in stages within the fiscal year and must comply with strict regulatory timelines. Transfers from RKUN to RKUD, and subsequently to RKD, are contingent upon the submission of required financial documents, including the Village Budget (APBDes) and realization reports of previous funding phases.

Priority use of village funds is directed toward development and community empowerment programs with cross-sectoral impacts. Within the framework of financial regulation, village budget management reflects a compliance-oriented financial control system that requires effective monitoring to ensure allocative efficiency and risk mitigation.

From a political economy perspective, public financial management serves as a bridge between governance structures and resource allocation efficiency. While governance theories focus on institutional compliance, financial management literature emphasizes allocative efficiency, cost effectiveness, and measurable performance outcomes in evaluating public expenditure. In decentralized fiscal systems, the absence of cost–benefit analysis and performance indicators often leads to suboptimal allocation despite high levels of regulatory compliance. Therefore, integrating governance analysis with financial performance evaluation is essential to assess whether fiscal policies generate sustainable economic value.

Transparency

Transparency refers to the principle of openness that ensures clear and accessible information regarding public financial management. According to the Indonesian Dictionary (KBBI), transparency implies clarity and openness. In villagefund management, transparency serves as a mechanism to enhance accountability, prevent corruption, and encourage public participation in financial oversight. Recent global governance studies emphasize that transparency and accountability mechanisms are effective only when supported by performance-based evaluation systems and institutional capacity, highlighting the limitations of compliance-oriented public financial management frameworks (OECD, 2022; UNDP, 2023).

Ministry of Home Affairs Regulation No. 113 of 2014 mandates that village financial management be conducted transparently, accountably, and participatively. Transparency provides the community with access to information regarding budgeting, implementation, and financial reporting processes.

However, within a financial regulation framework, transparency should not be limited to administrative disclosure. Compliance-based transparency, such as the publication of budget banners or reports, must be complemented by performance-based disclosure that enables stakeholders to assess financial effectiveness, efficiency, and outcomes. Transparency thus functions as a regulatory tool to reduce information asymmetry and strengthen financial oversight.

Accountability

Public accountability refers to the obligation of public officials to justify and report their actions and financial decisions to stakeholders. According to Kistanto et al. (2018),

accountability ensures that village government activities can be publicly scrutinized. Accountability operates through both vertical mechanisms (to higher government authorities) and horizontal mechanisms (to the community).

In village governance, the village head acts as the primary financial authority responsible for managing public resources. As emphasized by Haris (2007), accountability involves responsibility for fiscal, managerial, and programmatic decisions. From an agency theory perspective, accountability serves as a monitoring mechanism to align the interests of agents (village officials) with principals (the community and higher authorities).

Community Empowerment

Community empowerment is a process aimed at enhancing community capacity to influence decisions and institutions affecting their lives. Empowerment emphasizes the development of skills, knowledge, and authority that enable communities to achieve sustainable independence.

Article 1, Paragraph 12 of the Village Law defines community empowerment as efforts to improve community welfare through capacity building, behavioral development, and resource utilization supported by appropriate policies and programs. Empowerment initiatives are designed to foster sustainable economic development and social resilience.

From a financial governance perspective, community empowerment programs represent outcome-oriented public expenditures. Their effectiveness depends on performance-based budgeting, monitoring, and evaluation mechanisms. Without adequate financial oversight, empowerment programs risk becoming ceremonial rather than transformative.

Theoretical Framework: Integrating Agency Theory, Public Value Theory, and Stewardship Theory

This study adopts a multi-theoretical framework to provide a comprehensive understanding of village-level financial governance within a decentralized fiscal system. Specifically, it integrates Agency Theory, Public Value Theory, and Stewardship Theory to explain the dynamics between regulatory compliance and regulatory effectiveness.

First, Agency Theory (Jensen & Meckling, 1976; Eisenhardt, 1989) serves as the primary theoretical foundation for analyzing the principal–agent relationship in Village Fund governance. In this context, village officials act as agents responsible for managing public

funds on behalf of the community as principals. Information asymmetry, monitoring limitations, and moral hazard create agency costs that may lead to inefficiency and suboptimal allocation of resources. Regulatory compliance mechanisms, such as reporting systems, audits, and formal procedures, function as monitoring tools to reduce these risks. However, Agency Theory also implies that compliance alone does not guarantee optimal outcomes, particularly when monitoring focuses only on procedural adherence rather than performance.

Second, this study incorporates Public Value Theory (Moore, 1995), which emphasizes that public sector governance should not only ensure compliance with rules but also generate tangible value for society. In the context of Village Fund management, public value is reflected in improved community welfare, sustainable economic empowerment, and effective utilization of public resources. This perspective shifts the focus from input- and process-based evaluation toward outcome- and impact-based governance. Therefore, regulatory effectiveness is assessed not merely by adherence to financial procedures but by the extent to which Village Fund allocations produce measurable socio-economic benefits.

Third, Stewardship Theory (Davis, Schoorman, & Donaldson, 1997) provides an alternative perspective to Agency Theory by suggesting that public officials may act as stewards whose behavior is aligned with collective interests rather than self-interest. In village governance, this implies that officials are not always opportunistic actors but may demonstrate intrinsic motivation, commitment to public service, and responsibility toward community welfare. This perspective is particularly relevant in explaining why high levels of procedural compliance may coexist with efforts to maintain governance integrity, even in the absence of strict monitoring.

By integrating these three theoretical perspectives, this study offers a more nuanced analytical framework. Agency Theory explains the necessity of regulatory compliance and monitoring mechanisms; Public Value Theory highlights the importance of outcome-oriented governance; and Stewardship Theory provides insight into the potential alignment between officials and community interests. Together, these theories support the conceptual distinction between regulatory compliance and regulatory effectiveness, forming the basis for identifying governance gaps in Village Fund management.

Critical Literature Synthesis

Although prior studies have highlighted the importance of transparency, accountability, and internal control in improving village financial governance, they tend to conceptualize these

elements as isolated determinants rather than as part of an integrated regulatory system. Moreover, most empirical findings emphasize administrative compliance without critically evaluating whether such compliance translates into substantive governance effectiveness. This creates an important theoretical limitation, as compliance-based governance does not necessarily ensure allocative efficiency, sustainable economic outcomes, or meaningful public accountability. Consequently, there remains a lack of analytical frameworks that explicitly differentiate between procedural adherence and performance-based effectiveness. By addressing this limitation, the present study provides a more nuanced understanding of village financial governance through the compliance, effectiveness distinction, thereby advancing both theoretical and empirical discussions in decentralized fiscal governance literature.

Research Method

Research Design

This study employs a descriptive qualitative approach to analyze the implementation of financial regulatory and oversight mechanisms in Village Fund management, with particular emphasis on regulatory compliance, financial control effectiveness, and risk mitigation within a decentralized fiscal governance framework.

A qualitative design was selected because the study seeks to interpret governance processes, regulatory implementation practices, and oversight dynamics from the perspectives of actors directly involved in village financial management. Qualitative research is appropriate when the objective is to explore social processes, institutional practices, and contextual dynamics in depth (Creswell, 2014; Moleong, 2017; Sugiyono, 2019). Rather than merely assessing procedural adherence to formal regulations, this research explores how financial rules are operationalized in practice, how monitoring mechanisms function within administrative structures, and how transparency and accountability systems either strengthen or constrain regulatory effectiveness.

Village Fund governance is normatively guided by Law Number 6 of 2014 concerning Villages (Pemerintah Republik Indonesia, 2014) and further regulated through Government Regulation No. 60 of 2014 and Minister of Home Affairs Regulation No. 113 of 2014 (Kementerian Dalam Negeri Republik Indonesia, 2014). These regulations emphasize

principles of transparency, accountability, participation, and fiscal discipline in village financial management.

Transparency, defined as openness and clarity in providing accessible information (Kamus Besar Bahasa Indonesia, n.d.), is a core element of good governance (UNDP, 2021). Accountability refers to the obligation of public officials to justify the management of public resources to stakeholders (Haris, 2007; Kistanto et al., 2018). However, empirical research suggests that administrative accountability does not always translate into social accountability or participatory oversight (Anas, 2024; Lismanto, 2022).

Methodologically, this study conceptualizes Village Fund management as a regulated public financial system embedded in a principal–agent relationship. Village officials act as agents responsible for managing public funds, while community members serve as principals who rely on oversight mechanisms to evaluate performance. This analytical positioning aligns with public sector accountability frameworks and decentralized governance principles (Mardiasmo, 2018; UNDP, 2021).

Research Site

The research was conducted in Kemadang Village, Tanjungsari District, Gunungkidul Regency, Special Region of Yogyakarta. The site was selected purposively because Kemadang Village actively implements Village Fund programs across multiple economic sectors, including fisheries, agriculture, tourism, and MSMEs.

Kemadang Village has formally implemented budgeting procedures, financial recording through the Village Financial System (SiKUDDES), and accountability reporting mechanisms as mandated by regulation. Official data from the Ministry of Finance (Kementerian Keuangan Republik Indonesia, 2024) show the significant scale of Village Fund allocations nationally, while village-level data (Pemerintah Desa Kemadang, 2022; 2023; 2024) indicate continuous program implementation in empowerment sectors.

The village therefore provides a relevant case for examining the relationship between formal regulatory compliance and substantive regulatory effectiveness within decentralized public financial governance.

Informant Selection

Informants were selected using purposive sampling and simple random sampling (Patton, 2002; Sutopo, 2006). Purposive sampling was used to identify key actors who possess authority and direct involvement in Village Fund management, including:

- The Village Head
- Financial officers
- Administrative personnel responsible for budgeting and reporting

The role of village apparatus is central in ensuring governance effectiveness (Indrianasari, 2017; Sugiman, 2018).

Simple random sampling was applied to select community members who are beneficiaries of empowerment programs, including MSME actors, fishermen groups, and community representatives. This approach allows assessment of social accountability and participatory oversight from the perspective of program beneficiaries (Anas, 2024).

Data Collection Techniques

Data were collected through:

1. Semi-Structured Interviews

Interviews explored regulatory implementation practices, financial reporting mechanisms, monitoring procedures, and perceived risks associated with fund allocation. This method allows in-depth understanding of institutional processes and governance dynamics (Creswell, 2014).

2. Direct Observation

Observation was conducted to examine:

- Budget preparation processes
- Disclosure practices
- Administrative documentation
- Public information dissemination

This technique enables triangulation between formal procedures and actual practice (Miles, Huberman, & Saldaña, 2014).

3. Document Analysis

Documents analyzed included:

- Village Budget Plans (APBDes)
- Accountability Reports (LPJ)
- Budget realization reports
- Regulatory guidelines
- Public disclosure materials

Document analysis is essential in public financial governance studies to evaluate alignment between statutory requirements and implementation practice (Andini et al., 2023; Kementerian Dalam Negeri Republik Indonesia, 2022). Document analysis also included official village publications, such as budget realization reports, empowerment program documentation, and public information materials available on the Kemadang Village website (Pemerintah Desa Kemadang, 2022; 2023; 2024).

Data Analysis

Data analysis followed the interactive model proposed by Miles, Huberman, and Saldaña (2014), which consists of data reduction, data display, and conclusion drawing conducted in a cyclical and iterative manner. This model allows researchers to systematically organize qualitative data while continuously verifying emerging interpretations.

In the data reduction phase, raw interview transcripts, observational notes, and documentary materials were carefully reviewed, coded, and categorized according to predefined analytical themes aligned with the study's conceptual framework. These themes included regulatory compliance, transparency practices, accountability systems, oversight mechanisms, and empowerment outcomes. The reduction process involved selecting relevant information, eliminating redundant data, and organizing findings into meaningful conceptual clusters. This stage enabled the researcher to focus on patterns that reflect the distinction between procedural adherence and substantive regulatory effectiveness.

Following reduction, the data display stage involved organizing the categorized findings into structured narrative explanations and thematic matrices. Presenting data in this systematic

format facilitated comparison across informants, identification of consistencies and discrepancies, and interpretation of regulatory dynamics within Village Fund governance. Thematic matrices were particularly useful in mapping the relationship between compliance indicators and effectiveness indicators across budgeting, reporting, transparency, oversight, and empowerment dimensions.

Through this interactive analytical process, the study was able to identify regulatory gaps, governance strengths, and areas of inefficiency risk within the decentralized fiscal management system of Kemadang Village.

Conclusion Drawing and Verification

Conclusions were developed iteratively and validated through triangulation across interviews, observations, and documents. This approach ensures analytical rigor and internal consistency in qualitative research (Creswell, 2014; Patton, 2002).

Analytical Framework

Table 1 Regulatory Compliance vs Regulatory Effectiveness Framework in Village Fund Governance

Dimension	Regulatory Indicator	Compliance	Regulatory Indicator	Effectiveness
Budgeting	APBDes prepared and approved on schedule	and	Budget allocation linked to measurable performance outcomes	
Reporting	Accountability reports (LPJ) submitted regularly		Public access to program-level financial breakdown	
Transparency	Disclosure through information boards and website		Community understanding of allocation structure and impact	
Oversight	Formal audit by Inspectorate		Participatory evaluation and community review forums	
Empowerment	Training and programs formally conducted		Sustainable income generation and economic independence	

Source : Self-processed, 2025

The framework operationalizes the distinction between administrative compliance and substantive governance effectiveness. Regulatory compliance refers to adherence to formal requirements established in Permendagri No. 113 Tahun 2014 and related fiscal regulations (Kementerian Dalam Negeri Republik Indonesia, 2014). Regulatory effectiveness, in contrast, refers to the extent to which these formal mechanisms produce measurable socio-economic outcomes and meaningful public accountability. For example, timely preparation of APBDes fulfills compliance obligations. However, effectiveness requires that allocations generate sustainable empowerment outcomes, consistent with empowerment theory (Munawar Noor, 2011) and evidence that many village programs remain ceremonial without long-term impact (Saputra, 2023). Similarly, submission of LPJ satisfies vertical accountability, yet substantive transparency requires accessible and interpretable information for community oversight (Anas, 2024; UNDP, 2021). This analytical distinction provides the foundation for identifying regulatory gaps in Kemadang Village's financial governance system.

Data Validity and Analytical Procedure

To enhance methodological rigor, this study applies a systematic qualitative analysis using three stages of coding: open coding, axial coding, and selective coding. Open coding was used to identify initial categories from interview transcripts and field notes. Axial coding was then applied to establish relationships between categories, particularly in distinguishing regulatory compliance and regulatory effectiveness dimensions. Finally, selective coding was employed to integrate these categories into a coherent analytical framework. Data validity was ensured through triangulation of sources and methods, including interviews, observations, and document analysis. Cross-verification was conducted to ensure consistency between informant statements, observed practices, and official financial records. The study involved a total of 12 informants, consisting of village officials, financial administrators, and community members. This combination allows for a balanced perspective between administrative and societal viewpoints, strengthening the reliability of findings.

Results and Discussion

Results

Regulatory Compliance in Village Fund Management

The findings indicate that Village Fund management in Kemadang Village largely adheres to formal regulatory procedures established by national and regional policies. Planning, budgeting, administration, and reporting mechanisms are conducted in accordance with statutory provisions, including the preparation of the Village Government Work Plan (RKPDDes), formulation and approval of the Village Budget (APBDes), utilization of the Village Financial System (SiKUDes), and submission of periodic accountability reports (LPJ) to district authorities.

This administrative discipline reflects strong procedural compliance. As confirmed by the village head:

“We prepare the APBDes according to the schedule and follow the regulatory procedures set by the district government. All transactions are recorded in SiKUDes.” (Village Head, Interview, 2025)

Participatory planning is implemented through dusun-level meetings and Musyawarah Desa (Musdes), where community members are invited to propose program ideas. These proposals are subsequently prioritized and integrated into official planning documents. While this process fulfills formal participatory requirements, community involvement remains largely consultative. Participation tends to be limited to idea submission rather than engagement in detailed budget discussions, cost allocation decisions, or financial performance evaluation.

Thus, from a compliance perspective, Kemadang Village demonstrates strong adherence to regulatory standards. However, effectiveness in terms of performance-linked budgeting remains limited.

Budget Allocation Trends (2022–2024)

Village Fund allocations for empowerment programs demonstrate variation across fiscal years, reflecting adaptive budgeting patterns.

2022

Total empowerment allocation amounted to Rp837,730,000. A significant portion Rp700,000,000 (approximately 83.6%) was allocated to fisheries and marine activities, followed by agriculture (Rp114,120,000). Allocations to MSMEs, women’s empowerment, and trade sectors were comparatively small. This high sectoral concentration suggests alignment with local economic characteristics. However, no documented performance indicators—such

as income growth, productivity increase, or return on allocation were systematically recorded. Consequently, allocative efficiency cannot be empirically verified.

2023

Total empowerment allocation decreased to Rp175,500,000. Budget priorities shifted toward MSME development (Rp117,900,000) and trade (Rp49,500,000), indicating diversification. Support for women and child protection programs continued at a smaller scale. Although this shift reflects adaptive fiscal prioritization, structured monitoring tools, such as business survival rates, revenue growth metrics, or employment generation indicators, were not formally integrated into reporting documents.

2024

Total empowerment allocation further declined to Rp56,095,000. A notable portion was redirected toward village apparatus capacity building, alongside reduced allocations for MSMEs and trade sectors. While this transition may strengthen internal governance capacity, it simultaneously reduces direct productive economic allocations. Across all three years, budgeting demonstrates procedural adaptability but lacks measurable outcome-based evaluation mechanisms. These budget allocation data are based on official records published by the Kemadang Village Government (Pemerintah Kalurahan Kemadang, 2022; 2023; 2024).

Implementation and Administrative Control

Empowerment programs included fisheries training, MSME development workshops, women empowerment initiatives, tourism-related training, and social awareness campaigns. Activities were conducted according to approved plans and documented administratively.

However, interviews with beneficiaries reveal limited post-training support and sustainability mechanisms. As one MSME participant explained:

“The training was helpful, but after that we did not receive assistance in marketing or business development.” (MSME Participant, Interview, 2025)

This indicates that empowerment programs remain activity-based rather than outcome-based. Although skill development occurred, structured follow-up mechanisms, such as market linkage facilitation, income monitoring, or business incubation, were not systematically institutionalized.

From an administrative standpoint, financial management is relatively strong. All transactions are recorded through SiKUDEs, supported by documentary evidence and periodic reporting. External audits reinforce vertical accountability. Nonetheless, community members reported limited understanding of detailed allocation structures. As one resident noted:

“We see the banner about the budget, but we don’t really understand how much each activity costs.” (Community Member, Interview, 2025)

This suggests that while documentation is complete, interpretability for public scrutiny remains constrained.

Transparency and Accountability Practices

Transparency mechanisms include public information boards, official website publications, and Musdes forums. These instruments provide general access to budget summaries and program information. From a procedural standpoint, disclosure obligations are fulfilled.

However, transparency remains predominantly administrative rather than substantive. Financial disclosures do not consistently provide detailed program-level cost structures, cost-efficiency analysis, or measurable socio-economic impact indicators. Consequently, public capacity for meaningful oversight is limited.

Similarly, accountability mechanisms are stronger vertically than horizontally. Reporting to district authorities and audit institutions functions effectively, but participatory evaluation of financial performance is not systematically institutionalized.

Table 2 Summary of Compliance–Effectiveness Analysis

Year	Regulatory Compliance	Regulatory Effectiveness
2022	High (procedural adherence)	Low (no measurable outcomes)
2023	High (adaptive budgeting)	Low (limited monitoring indicators)
2024	High (administrative control)	Very Low (reduced empowerment impact)

This table highlights the consistent pattern where strong procedural compliance is not accompanied by equivalent regulatory effectiveness, confirming the presence of a compliance–effectiveness gap.

Findings

Overall, the results demonstrate a consistent pattern across budgeting, reporting, transparency, oversight, and empowerment dimensions. Regulatory compliance is strong, reflected in timely documentation, structured reporting, formal disclosure, and procedural discipline. Vertical accountability mechanisms function effectively within the administrative hierarchy.

However, regulatory effectiveness remains limited due to the absence of measurable performance indicators, structured economic impact assessments, participatory financial evaluation forums, and sustainability tracking mechanisms. Transparency operates at the level of disclosure rather than interpretation, and empowerment remains activity-centered rather than outcome-driven.

These findings confirm the presence of a compliance–effectiveness gap in Village Fund governance, where formal procedural adherence does not automatically translate into substantive fiscal performance or sustainable economic empowerment outcomes.

Discussion

The findings of this study underscore a clear distinction between **regulatory compliance** and **regulatory effectiveness** within Village Fund governance. From a government regulation perspective, Kemadang Village demonstrates strong procedural adherence to formal financial rules and statutory requirements. Budget preparation, administrative documentation, utilization of SiKUDDES, periodic reporting (LPJ), and external audits operate in accordance with regulatory frameworks governing village financial management. Such compliance reflects institutional discipline and reinforces vertical accountability mechanisms within Indonesia's decentralized fiscal system.

This pattern aligns with public financial management literature suggesting that formal compliance mechanisms reduce administrative irregularities and corruption exposure risk (Mardiasmo, 2018; Komisi Pemberantasan Korupsi, 2023). Structured documentation and hierarchical reporting reduce discretionary abuse by limiting unrecorded financial transactions. In this sense, Kemadang Village exhibits relatively low procedural corruption risk.

However, when examined through the lens of financial oversight effectiveness, regulatory performance appears only partial. Although reporting systems and audit mechanisms are formally operational, outcome-based monitoring remains weak. The absence of measurable performance indicators, cost–benefit analysis, and sustainability tracking limits the ability to evaluate allocative efficiency and long-term economic impact. This confirms prior findings that administrative transparency does not automatically generate substantive accountability (Anas, 2024; Andini et al., 2023; UNDP, 2021). From a financial perspective, the absence of cost–benefit analysis, return-on-allocation indicators, and measurable financial performance metrics limits the evaluation of allocative efficiency. Consequently, public expenditures may comply with regulatory requirements but fail to generate optimal financial returns or sustainable economic value. This condition is consistent with financial management studies indicating that inefficient cost allocation and the absence of accurate costing mechanisms can lead to suboptimal financial outcomes and increased financial risk (Abbas et al., 2023).

From an Agency Theory perspective (Haris, 2007; Kistanto et al., 2018), this situation reflects persistent information asymmetry between village officials (agents) and community members (principals). While agents comply with reporting obligations toward higher authorities (vertical accountability), principals lack access to interpretable and performance-based financial information. Consequently, monitoring remains structurally hierarchical rather than participatory. Agency costs are therefore not eliminated but reconfigured: moral hazard risk may decline due to documentation discipline, yet residual loss persists due to allocative inefficiency that cannot be easily detected.

The regulatory gap identified in this study is characterized by strong vertical accountability but limited horizontal accountability. Transparency mechanisms operate primarily at the level of formal disclosure, through banners, websites, and Musdes forums, yet they do not consistently provide program-level financial breakdowns or measurable impact indicators. As indicated by Kementerian Dalam Negeri (2022), many villages remain at the stage of administrative transparency rather than substantive public accountability. Kemadang Village appears to reflect this broader national pattern.

The 2022 allocation pattern illustrates this compliance–effectiveness tension. The concentration of approximately 83.6% of empowerment funds in the fisheries sector reflects rational geographic alignment and economic prioritization. However, without documented income growth indicators, productivity metrics, or multiplier effects, it remains unclear

whether this allocation maximized public spending efficiency. Similarly, the 2023 diversification toward MSME development indicates adaptive fiscal prioritization, yet the absence of business survival tracking or revenue growth metrics constrains evaluation of its economic impact.

The 2024 shift toward apparatus capacity building introduces an additional policy trade-off. Strengthening administrative competence may enhance future compliance and internal control systems (Indrianasari, 2017; Sugiman, 2018). However, redirecting funds away from productive economic sectors may reduce short-term community income stimulation. This tension reflects a broader challenge in decentralized fiscal governance: balancing internal institutional strengthening with outward developmental impact.

From a broader governance perspective, Kemadang Village demonstrates low corruption exposure risk due to structured documentation and formal oversight. However, moderate inefficiency risk persists due to limited outcome-based evaluation. Without systematic measurement of empowerment outcomes, such as income generation, economic independence, or sustainable enterprise development (Munawar Noor, 2011; Saputra, 2023), the transformation of Village Funds into long-term welfare improvement remains uncertain. This finding is consistent with prior studies suggesting that the absence of continuous facilitation and post-program assistance often results in short-term outputs rather than sustainable empowerment outcomes (Sonny, 2023).

The findings therefore support the argument that compliance is a necessary but insufficient condition for regulatory effectiveness. Regulatory effectiveness requires integration of performance-based budgeting principles, accessible program-level disclosure, and institutionalized participatory evaluation forums. Strengthening substantive transparency, defined not merely as information availability but as information interpretability (Kamus Besar Bahasa Indonesia, n.d.; UNDP, 2021), is critical to reducing agency risk and improving allocative efficiency.

Theoretically, this study contributes by extending Agency Theory into the domain of village-level fiscal governance. While prior literature has emphasized corruption reduction through compliance mechanisms, this study demonstrates that inefficiency risk can persist even under high procedural discipline. The compliance–effectiveness analytical lens provides a refined framework for examining decentralized financial governance beyond procedural adherence.

In policy terms, enhancing regulatory effectiveness requires:

- (1) integrating measurable performance indicators into APBDes allocations;
- (2) publishing simplified program-level financial breakdowns for public interpretation;
- (3) institutionalizing post-implementation participatory evaluation forums; and
- (4) introducing sustainability tracking for empowerment programs.

Such reforms would reduce information asymmetry, lower residual agency loss, improve allocative efficiency, and strengthen decentralized public financial governance outcomes.

Comparative and Policy Implications

The findings of this study are consistent with evidence from other decentralized governance contexts, such as India and the Philippines, where local governments demonstrate strong compliance with fiscal regulations but face challenges in achieving performance-based outcomes. This suggests that the compliance–effectiveness gap is not unique to Indonesia but represents a broader structural issue in decentralized fiscal systems. This argument is further reinforced by global evidence indicating that a persistent gap often exists between formal regulatory compliance and actual service delivery performance, primarily due to weak institutional capacity and limited outcome-based monitoring mechanisms (World Bank, 2022; Jovanović, 2024).

From a policy perspective, the current regulatory framework appears to overemphasize procedural compliance rather than outcome-based performance. While compliance reduces corruption risk, it does not automatically ensure efficient allocation or sustainable economic impact. Therefore, a shift toward performance-oriented governance is necessary.

At the macro level, persistent inefficiency in village fund allocation may lead to suboptimal fiscal decentralization outcomes, limiting the effectiveness of public expenditure in reducing inequality and improving welfare. This is consistent with empirical evidence showing that the effectiveness of fiscal decentralization is conditional upon governance quality and institutional arrangements, rather than being inherently welfare-enhancing (Dwipatna et al., 2026).

Limitations and Future Research

This study is subject to several limitations. First, it focuses on a single village case, which may limit the generalizability of findings to other regions with different socio-economic and institutional characteristics. Second, the qualitative approach, while providing in-depth insights, does not quantify the magnitude of inefficiency or performance outcomes.

Future research is recommended to incorporate mixed-method approaches by combining qualitative analysis with quantitative performance indicators, such as income growth, program sustainability, and cost–benefit evaluation. Comparative studies across multiple villages or regions would also provide a broader understanding of regulatory effectiveness in decentralized fiscal governance.

Conclusion

This study identifies three key findings. First, financial regulatory and oversight mechanisms in Kemadang Village are operationalized through structured budgeting, reporting, and audit systems, including the use of SiKUDes and periodic supervision. These mechanisms reflect strong procedural compliance and disciplined vertical financial control. However, improving public financial management requires a transition from compliance-based governance toward performance-based financial evaluation, where allocative efficiency, cost effectiveness, and measurable financial outcomes become central indicators of success.

Second, transparency and accountability systems primarily demonstrate regulatory compliance rather than regulatory effectiveness. Financial disclosure remains administrative and lacks performance-based, interpretable information, limiting public understanding and weakening horizontal accountability. From an Agency Theory perspective, this condition reflects persistent information asymmetry between village officials (agents) and the community (principals).

Third, while financial control and reporting mechanisms reduce corruption risks, they do not effectively mitigate inefficiency or enhance allocative effectiveness. The absence of cost–benefit analysis, measurable financial indicators, and outcome-based evaluation constrains financial performance. In contrast to Stewardship Theory, which assumes value-driven behavior, these findings indicate that institutional mechanisms are not yet aligned to support collective welfare outcomes.

Overall, the findings reveal a compliance–effectiveness gap in decentralized public financial management. From a Public Value perspective, Village Fund management has not fully translated into measurable socio-economic outcomes. Strengthening allocative efficiency

therefore requires integrating performance-based financial evaluation, participatory oversight, and outcome-oriented monitoring to ensure that public funds generate sustainable public value.

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