

ABSTRACT

This study aims to analyze the influence of the effectiveness of the Internal Control System (ICS), follow-up on audit recommendations, and the implementation of Government Accounting Standards (GAS) on the audit opinion of local governments, with regional losses as a mediating variable. The background of this study is based on a contradictory phenomenon in which the quality of local government audit opinions has generally improved, while regional losses have significantly increased over the past six years. Data shows that regional losses peaked in 2023, reaching IDR 2,457,241.66 million, raising concerns about the effectiveness of financial management and accountability at the local government level.

This study uses secondary data obtained from the Audit Reports of the Audit Board of Indonesia (BPK), comprising 1,012 observations from city and regency governments across Indonesia during the 2022–2023 period. The analytical method employed is Partial Least Squares-based Structural Equation Modeling (SEM-PLS) to examine both direct and indirect relationships among variables. The results of the study indicate that: (1) The effectiveness of the internal control system does not significantly affect the audit opinion but has a significant effect on regional losses. (2) Follow-up on audit recommendations does not significantly affect either the audit opinion or regional losses. (3) The implementation of government accounting standards significantly influences both the audit opinion and regional losses. (4) Regional losses do not significantly affect the audit opinion and therefore do not serve as a mediating variable in the relationship between ICS effectiveness, follow-up on audit recommendations, GAS implementation, and audit opinion.

These findings provide several important implications. Theoretically, this study strengthens the understanding of Agency Theory, which suggests that auditors prioritize the fairness of financial statement presentation following GAS over the level of regional losses when issuing audit opinions. Practically, local governments need to balance strengthening internal controls and complying with audit recommendations with improving the quality of financial reporting to obtain better audit opinions. From a policy perspective, the findings offer insights for BPK and other oversight institutions to design more comprehensive evaluations of local government financial performance, considering not only financial statements but also the effectiveness of internal control systems and compliance with audit recommendations.

Keywords: *Internal Control System, Follow-Up on Audit Recommendations, Government Accounting Standards, Audit Opinion, Regional Losses.*