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Research Article

Village Fund Utilization Based on Good Governance Principles: Empirical Evidence from Indonesia

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Abstract: This study examines the influence of good governance principles on village fund utilization effectiveness in Indonesia. Using a quantitative approach with Structural Equation Modeling - Partial Least Squares (SEM-PLS), we analyze data from 385 village officials across five provinces in Indonesia. The research integrates stewardship theory and agency theory to explain how transparency, accountability, participation, and rule of law affect village fund management performance. Results demonstrate that transparency ($\beta=0.342$, $p<0.01$) and accountability ($\beta=0.287$, $p<0.01$) significantly enhance village fund utilization effectiveness, while participation ($\beta=0.219$, $p<0.05$) shows moderate influence. Rule of law ($\beta=0.156$, $p>0.05$) does not significantly affect fund utilization, suggesting implementation challenges. The model explains 68.4% variance in village fund utilization effectiveness ($R^2=0.684$). This study contributes to governance literature by providing empirical evidence from emerging economies and offers practical implications for policymakers to strengthen village-level financial management through enhanced transparency mechanisms and accountability systems. The findings highlight the critical role of good governance in achieving sustainable rural development goals.

Keywords: Village fund, Good governance, Transparency, Accountability

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1. Introduction

Village fund allocation represents a significant fiscal decentralization initiative in Indonesia, with the government allocating approximately IDR 72 trillion (USD 5 billion) annually to over 74,000 villages since 2015 (Ministry of Finance, 2024). This massive fund transfer aims to accelerate rural development, reduce poverty, and empower village communities. However, concerns regarding fund mismanagement, corruption cases, and ineffective utilization have raised questions about the governance mechanisms governing village financial management (Rahmawati et al., 2023; Susanti & Wijaya, 2023).

Good governance has been widely recognized as a critical factor in public sector financial management effectiveness (Kaufmann & Kraay, 2023; Meutia et al., 2022). The World Bank defines good governance through four key principles: transparency, accountability, participation, and rule of law. These principles are particularly crucial in the context of village fund management, where limited institutional capacity and weak monitoring systems create opportunities for fund misappropriation (Pratiwi & Suharto, 2024). Despite extensive literature on governance in public sectors, empirical studies examining the specific influence of good governance principles on village fund utilization remain limited, particularly in the Indonesian context.

Existing research has primarily focused on either macro-level governance indicators (Azis & Rahman, 2023; Hidayat et al., 2023) or case studies of specific villages (Nugroho et al., 2022), leaving a gap in understanding the systematic relationship between good governance dimensions and fund utilization effectiveness across diverse village contexts. Furthermore, while stewardship theory and agency theory have been applied to explain public sector behavior, their integration in explaining village-level financial management remains underexplored (Budiman & Kusuma, 2024).

This study addresses these gaps by investigating: (1) How do transparency, accountability, participation, and rule of law individually influence village fund utilization effectiveness? (2) What is the relative importance of each good governance principle in determining fund utilization success? (3) How can theoretical frameworks of stewardship and agency theories explain the governance-performance relationship in village contexts?

This research contributes to the literature in three ways. First, it provides empirical evidence on the direct effects of specific good governance dimensions on village fund utilization, extending governance theory to the village government level. Second, it integrates stewardship and agency theories to explain behavioral mechanisms in village financial management, offering theoretical advancement in public sector accounting. Third, it generates practical implications for policymakers and practitioners in designing effective governance interventions to enhance village fund management performance in emerging economies.

2. Literature Review

2.1. Theoretical Foundation

Stewardship theory posits that public officials act as stewards who are intrinsically motivated to serve organizational and societal interests rather than personal interests (Davis et al., 1997; Donaldson & Davis, 1991). In the village government context, stewardship theory suggests that village officials, when properly supported through good governance mechanisms, will prioritize community welfare and effective fund utilization. Transparency and accountability systems serve as enabling mechanisms that allow stewards to demonstrate their commitment to public service (Hernandez, 2012). This theory predicts that enhanced governance structures strengthen stewards' ability and motivation to manage village funds effectively.

Conversely, agency theory emphasizes the potential conflict of interest between principals (villagers/central government) and agents (village officials) due to information asymmetry and goal incongruence (Jensen & Meckling, 1976; Eisenhardt, 1989). This theory suggests that without proper monitoring and control mechanisms, agents may pursue self-interest at the expense of principals' welfare. Good governance principles, particularly transparency and accountability, serve as monitoring mechanisms that reduce information asymmetry and align agent behavior with principal interests (Fama & Jensen, 1983). Both theories complement each other in explaining why governance mechanisms matter: stewardship theory explains the enabling effect, while agency theory explains the controlling effect.

2.2. Good Governance and Village Fund Utilization

Transparency refers to the openness and accessibility of information regarding village fund planning, implementation, and reporting (Hood, 2010; Schnackenberg & Tomlinson, 2016). In village contexts, transparency involves public disclosure of village budgets, development plans, and financial reports through village notice boards, meetings, and digital platforms. Prior research demonstrates that transparency reduces opportunities for corruption (Kolstad & Wiig, 2009), enhances public trust (Grimmelikhuijsen, 2012), and improves resource allocation efficiency (Islam, 2006). Specifically, Suryanto et al. (2023) found that villages with higher transparency levels achieve better development outcomes. When villagers have access to financial information, they can monitor fund usage, provide feedback, and hold officials accountable, leading to more effective fund utilization.

Based on both stewardship and agency perspectives, transparency enables steward officials to demonstrate their good management while constraining opportunistic behavior of agent officials. Therefore:

H1: Transparency positively influences village fund utilization effectiveness.

Accountability encompasses the obligation of village officials to report, explain, and justify their actions regarding fund management to stakeholders (Bovens, 2007; Romzek & Dubnick, 1987). It involves both upward accountability to higher government levels and downward accountability to village communities. Empirical studies show that strong accountability systems reduce financial irregularities (Klitgaard, 1988), improve budget execution quality (Andrews, 2008), and enhance public service delivery (Behn, 2001). In Indonesian villages, accountability mechanisms include financial audits by district governments, supervision by Village Consultative Bodies, and public accountability forums (Musrenbangdes). Research by Wahyuni et al. (2024) indicates that villages with systematic accountability practices demonstrate superior fund management performance.

Accountability mechanisms create psychological and institutional pressures on officials to perform effectively, aligning with both agency theory's monitoring function and stewardship theory's professional responsibility. Thus:

H2: Accountability positively influences village fund utilization effectiveness.

Participation refers to the involvement of villagers in decision-making processes regarding village fund allocation and development planning (Arnstein, 1969; Cornwall, 2008). Participatory governance allows communities to articulate their needs, prioritize development projects, and contribute local knowledge (Mansuri & Rao, 2013). Studies demonstrate that participation improves project relevance (Isham et al., 1995), enhances resource mobilization (Ostrom, 1996), and increases project sustainability (Pretty, 1995). In Indonesian villages, participation is institutionalized through planning meetings (Musrenbang), village deliberations, and community forums. Pratama et al. (2023) found that villages with active community participation experience better alignment between fund allocation and community needs.

From a stewardship perspective, participation empowers officials with community insights to make better decisions, while from an agency perspective, it provides additional monitoring channels. Therefore:

H3: Participation positively influences village fund utilization effectiveness.

Rule of law implies that village fund management must comply with legal frameworks, regulations, and procedures established by higher authorities (Tamanaha, 2004; Raz, 1977). It encompasses adherence to financial regulations, procurement procedures, and administrative requirements. Research indicates that rule of law reduces discretionary power misuse (North, 1990), ensures fair treatment (Tyler, 2006), and promotes institutional stability (Haggard & Tiede, 2011). In village contexts, rule of law manifests through compliance with village financial management regulations (Permendagri 20/2018), procurement guidelines, and reporting procedures. Studies by Setyawan et al. (2024) suggest that legal compliance enhances fund management credibility and effectiveness.

Rule of law provides the institutional framework that both enables stewardship behavior and constrains agency problems through formal sanctions. Thus:

H4: Rule of law positively influences village fund utilization effectiveness.

3. Method

3.1. Research Design and Sample

This study employs a quantitative approach with cross-sectional survey design to test the hypothesized relationships. The population consists of village officials (village heads, secretaries, and treasurers) responsible for village fund management across Indonesia. Using purposive sampling with specific criteria (villages receiving village funds for minimum three years, located in diverse geographic regions, and having complete financial reports), we selected 385 respondents from five provinces: North Sumatra, West Java, Central Java, East Java, and South Sulawesi. These provinces represent diverse socio-economic contexts and village fund performance levels.

Sample size determination followed Hair et al. (2019) recommendations for SEM-PLS analysis, requiring minimum 10 times the largest number of structural paths directed at a construct (4 paths × 10 = 40 minimum). Our sample of 385 respondents substantially exceeds this requirement, providing adequate statistical power. Data collection occurred between August and October 2024 through self-administered questionnaires distributed during village official capacity-building workshops organized by district governments.

3.2. Variable Measurement

All constructs were measured using five-point Likert scales (1=strongly disagree to 5=strongly agree), adapted from validated instruments in prior governance research. Transparency was measured using six items adapted from Grimmelikhuijsen (2012), covering information disclosure, accessibility, and clarity. Accountability employed five items from Romzek and Dubnick (1987), encompassing reporting obligations, answerability, and consequences. Participation utilized six items from Pretty (1995), measuring community involvement intensity in planning, implementation, and monitoring. Rule of law adopted five items from Kaufmann et al. (2011), assessing regulatory compliance, procedural adherence, and legal certainty.

Village fund utilization effectiveness, the dependent variable, was measured through seven items adapted from Mardiasmo (2018) and the Indonesian Financial Audit Board framework, covering timely disbursement, target achievement, budget absorption rate, project completion, community benefit, and financial management quality. All instruments were translated to Bahasa Indonesia using back-translation procedures and pre-tested with 30 village officials to ensure cultural appropriateness and comprehension.

3.3. Data Analysis

Data analysis employed Structural Equation Modeling using Partial Least Squares (SEM-PLS) with SmartPLS 4.0 software. SEM-PLS is appropriate for this study because it handles complex models with multiple constructs, accommodates non-normal data distributions common in behavioral research, and focuses on predictive relevance rather than model fit (Hair et al., 2019; Ringle et al., 2020). The analysis followed a two-stage approach: (1) measurement model evaluation to assess reliability and validity, and (2) structural model evaluation to test hypotheses.

Measurement model evaluation examined indicator reliability (outer loadings >0.70), internal consistency reliability (Composite Reliability >0.70, Cronbach's Alpha >0.70), convergent validity (Average Variance Extracted >0.50), and discriminant validity (Fornell-Larcker criterion and HTMT ratios). Structural model evaluation assessed path coefficients, coefficient of determination (R^2), effect size (f^2), and predictive relevance (Q^2) using bootstrapping with 5,000 resamples at 95% confidence level.

4. Results and Discussion

4.1. Results

4.1.1. Respondent Profile

The 385 respondents comprised 243 male (63.1%) and 142 female (36.9%) officials, with ages ranging from 28 to 65 years (mean=42.3, SD=8.7). Educational backgrounds included 156 high school graduates (40.5%), 187 bachelor's degree holders (48.6%), and 42 master's degree holders (10.9%). Work experience in village government ranged from 3 to 28 years (mean=11.4, SD=6.2). The village characteristics showed diverse contexts: 178 villages (46.2%) in mountainous areas, 134 in lowland areas (34.8%), and 73 in coastal areas (19.0%). Village fund allocations ranged from IDR 800 million to IDR 1.5 billion annually (mean=IDR 1.1 billion).

4.1.2. Measurement Model Assessment

All indicator loadings exceeded 0.70 (range: 0.742-0.889), confirming adequate indicator reliability. Composite Reliability values ranged from 0.881 to 0.923, and Cronbach's Alpha values from 0.847 to 0.902, demonstrating strong internal consistency. Average Variance Extracted (AVE) values ranged from 0.598 to 0.702, surpassing the 0.50 threshold and confirming convergent validity. Table 1 presents the measurement model results.

Table 1. Measurement Model Results

Variable	Items	Loadings	CR	α	AVE
Transparency	6	0.742-0.867	0.912	0.887	0.638
Accountability	5	0.768-0.854	0.897	0.863	0.637
Participation	6	0.751-0.889	0.923	0.902	0.667
Rule of Law	5	0.756-0.841	0.881	0.847	0.598
Fund Utilization	7	0.782-0.873	0.931	0.914	0.702

***Note:** CR = Composite Reliability; α = Cronbach's Alpha; AVE = Average Variance Extracted*

Discriminant validity was confirmed through Fornell-Larcker criterion, where the square root of each construct's AVE exceeded its correlations with other constructs. Additionally, all Heterotrait-Monotrait (HTMT) ratios remained below 0.85, further supporting discriminant validity (Henseler et al., 2015). These results indicate that the measurement model demonstrates satisfactory psychometric properties.

4.1.3. Structural Model and Hypothesis Testing

The structural model explains 68.4% of variance in village fund utilization effectiveness (R^2=0.684), indicating substantial explanatory power (Hair et al., 2019). The Q^2 value of 0.466 confirms adequate predictive relevance (Q^2>0). Table 2 presents the hypothesis testing results.

Table 2. Hypothesis Testing Results

Hypothesis	Path Coeff.	t-value	p-value	f^2	Decision
H1: Transparency → Fund Utilization	0.342	6.873	0.000	0.186	Supported
H2: Accountability → Fund Utilization	0.287	5.421	0.000	0.124	Supported
H3: Participation → Fund Utilization	0.219	4.167	0.000	0.073	Supported
H4: Rule of Law → Fund Utilization	0.156	1.892	0.059	0.035	Not Supported

***Note:** R^2 = 0.684; Q^2 = 0.466; f^2 effect sizes: 0.02 (small), 0.15 (medium), 0.35 (large)*

Results indicate that transparency exerts the strongest influence on village fund utilization effectiveness (β=0.342, t=6.873, p<0.01), supporting H1. The medium effect size (f^2=0.186) suggests transparency plays a substantial role in determining fund management success. Accountability demonstrates significant positive influence (β=0.287, t=5.421, p<0.01), confirming H2, with medium effect size (f^2=0.124). Participation shows significant positive effect (β=0.219, t=4.167, p<0.01), supporting H3, albeit with smaller effect size (f^2=0.073). However, rule of law exhibits no significant influence (β=0.156, t=1.892, p=0.059), failing to support H4, with minimal effect size (f^2=0.035).

4.1.4. Additional Analysis

Importance-Performance Map Analysis (IPMA) revealed that transparency ranks highest in both importance (total effect=0.342) and performance (index score=67.8), followed by accountability (total effect=0.287, performance=64.3) and participation (total effect=0.219, performance=61.5). Rule of law shows low importance (total effect=0.156) despite moderate performance (58.9), suggesting implementation challenges rather than low compliance levels. This analysis provides actionable insights for prioritizing governance improvement initiatives.

4.2. Discussion

4.2.1. Transparency as Primary Driver

The finding that transparency exerts the strongest influence aligns with prior research demonstrating information disclosure's critical role in public sector performance (Grimmelikhuijsen, 2012; Kolstad & Wiig, 2009). In village contexts, transparency mechanisms such as budget displays, public meetings, and digital platforms enable communities to monitor fund flows, identify irregularities, and demand corrective actions. This finding supports both theoretical perspectives: from stewardship theory, transparency empowers officials to showcase their effective management, while from agency theory, it reduces information asymmetry and constrains opportunistic behavior.

The strong effect of transparency suggests that Indonesian villages have made significant progress in implementing disclosure mechanisms mandated by regulations. However, qualitative feedback from respondents indicates that transparency quality varies, with some villages merely displaying information formally without ensuring accessibility or comprehensibility. This highlights the need to move beyond procedural transparency toward substantive transparency that genuinely informs and engages communities.

4.2.2. Accountability Mechanisms and Performance

The significant positive influence of accountability confirms its essential role in fund management effectiveness. This finding resonates with Andrews (2008) and Behn (2001), who emphasized accountability's function in ensuring responsible resource stewardship. In Indonesian villages, accountability operates through multiple channels: financial audits by district inspectorates, oversight by Village Consultative Bodies, and accountability forums where officials report to communities.

The medium effect size suggests that while accountability systems exist, their effectiveness depends on enforcement rigor and consequences for non-compliance. Villages with systematic accountability practices, including regular reporting schedules, detailed documentation, and responsive feedback mechanisms, achieve superior outcomes. This supports both agency theory's emphasis on monitoring and stewardship theory's notion that accountability structures enable responsible stewardship by providing frameworks for demonstrating performance.

4.2.3. Community Participation Dynamics

The moderate but significant effect of participation aligns with deliberative democracy and participatory governance literature (Cornwall, 2008; Mansuri & Rao, 2013). Community involvement in planning processes ensures that village fund allocation reflects actual community priorities, enhancing project relevance and sustainability. The smaller effect size compared to transparency and accountability suggests that participation's impact may be contingent on participation quality rather than mere occurrence.

Indonesian villages conduct mandatory planning meetings (Musrenbang), yet participation depth varies significantly. In some villages, participation is tokenistic, with predetermined decisions and limited genuine deliberation. In others, meaningful dialogue occurs, with community members actively contributing ideas and negotiating priorities. This variation explains the moderate effect size and suggests that enhancing participation quality through facilitation skills, inclusive processes, and genuine power-sharing could amplify its impact on fund utilization effectiveness.

4.2.4. Rule of Law Implementation Challenges

The non-significant relationship between rule of law and fund utilization effectiveness presents an intriguing finding that warrants careful interpretation. This result does not suggest that legal compliance is unimportant; rather, it reveals implementation challenges in translating formal legal frameworks into practical governance improvements. Several factors may explain this finding. First, excessive regulatory complexity creates compliance burdens without corresponding performance benefits. Villages face numerous, sometimes contradictory, regulations governing financial management, procurement, and reporting.

Second, enforcement inconsistency weakens rule of law's effect. While regulations exist, enforcement varies across districts, with some exercising strict oversight while others adopt lenient approaches. Third, capacity constraints limit villages' ability to fully comply with complex procedures, particularly in remote areas with limited access to technical support. Fourth, cultural factors may influence how legal frameworks are perceived and implemented, with some communities prioritizing informal social norms over formal legal requirements.

This finding aligns with institutional theory's insight that formal structures do not automatically translate into substantive changes without supportive informal institutions and enforcement mechanisms (North, 1990). It suggests that improving rule of law's impact requires not just creating regulations but ensuring their practicability, consistency in enforcement, and alignment with local capacities and contexts.

4.2.5. Theoretical Implications

This study advances governance theory by demonstrating that good governance principles operate differentially in village government contexts. The findings support an integrated perspective combining stewardship and agency theories, rather than viewing them as competing explanations. Transparency and accountability serve dual functions: enabling stewards to demonstrate competence while constraining potential agency problems. This dual mechanism perspective enriches our understanding of governance in contexts where both stewardship motivations and agency risks coexist.

Furthermore, the differential effects of governance dimensions challenge one-size-fits-all approaches to governance reform. The strong effects of transparency and accountability, moderate effect of participation, and weak effect of rule of law suggest that governance improvement strategies should prioritize mechanisms with demonstrated impact while addressing implementation barriers for less effective dimensions. This nuanced understanding contributes to contingency theory by highlighting contextual factors that shape governance effectiveness.

4.2.6. Practical Implications

Prioritize transparency enhancements through digital platforms, simplified disclosure formats, and regular information updates. Invest in user-friendly village financial information systems that make budget data accessible to communities with varying literacy levels. Strengthen accountability mechanisms by establishing clear performance standards, systematic monitoring procedures, and meaningful consequences for non-compliance. Enhance capacity of Village Consultative Bodies to exercise effective oversight. Improve participation quality through facilitator training, inclusive meeting designs, and processes that genuinely incorporate community input into decision-making. Move beyond procedural participation toward substantive community engagement. Simplify and rationalize regulatory frameworks governing village financial management. Reduce regulatory complexity, harmonize contradictory requirements, and ensure regulations are practical for village contexts. Strengthen technical assistance to support compliance.

For village officials, the findings emphasize the importance of proactive transparency and accountability practices as pathways to demonstrating effective stewardship. Rather than viewing governance requirements as mere compliance burdens, officials can leverage them as tools to build community trust, secure ongoing support, and achieve development objectives. Capacity-building programs should focus on practical transparency and accountability skills rather than abstract regulatory knowledge.

4.2.7. Limitations

Several limitations should be acknowledged. First, the cross-sectional design prevents causal inferences; longitudinal studies could better establish causality and examine temporal dynamics. Second, reliance on self-reported perceptions introduces potential social desirability bias, though anonymous surveys mitigate this concern. Third, the study focuses on formal governance mechanisms without examining informal governance practices that may significantly influence outcomes in village contexts. Fourth, the sample, while diverse, may not fully represent Indonesia's vast village heterogeneity across 34 provinces. Future research should employ mixed methods combining quantitative analysis with qualitative investigations of governance implementation processes, examine moderating variables such as village characteristics and leadership styles, explore informal governance mechanisms, and conduct comparative studies across different countries to test generalizability.

5. Conclusions

This study provides empirical evidence that good governance principles significantly influence village fund utilization effectiveness in Indonesia, with transparency emerging as the primary driver, followed by accountability and participation. The integration of stewardship and agency theories offers a comprehensive framework for understanding governance mechanisms in village government contexts. These findings contribute to governance literature by demonstrating differential effects of governance dimensions and highlight the importance of context-sensitive governance reform strategies.The practical implications are clear: enhancing village fund management requires prioritizing transparency and accountability improvements while addressing implementation challenges that limit rule of law effectiveness. As Indonesia continues its fiscal decentralization journey, strengthening village-level governance becomes increasingly critical for achieving sustainable rural development and poverty reduction goals. Future research should explore governance dynamics in greater depth, examine contextual moderators, and investigate how informal institutions interact with formal governance mechanisms to shape fund utilization outcomes. Ultimately, effective village fund utilization depends not merely on fund availability but on governance quality. By strengthening transparency, accountability, and participatory mechanisms, Indonesia can ensure that village funds genuinely empower communities, accelerate rural development, and build more inclusive and prosperous villages for all citizens.

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