

# Effect of Leverage, Fiscal Distress, and Fiscal Capacity on COVID-19 Accrual Manipulation

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## Abstract

**Purpose:** This study aims to analyze the effects of leverage, fiscal distress, and fiscal capacity on accrual manipulation in provincial governments in Indonesia during 2020–2022.

**Methodology/approach:** The research data used regional government financial reports audited by the *Badan Pemeriksa Keuangan (BPK)*, with a sample size of 102 observations from 34 provinces over three years. The analysis method used was panel data regression with a Random Effects Model (REM) approach.

**Results:** The results show that leverage has no significant effect on accrual manipulation. Conversely, fiscal distress and fiscal capacity have a positive effect on accrual manipulation, indicating that high fiscal pressure and capacity encourage accounting flexibility to maintain the image and meet performance targets. Simultaneously, leverage, fiscal distress, and fiscal capacity contribute to the level of accrual manipulation by local governments during the COVID-19 pandemic.

**Conclusions:** This study concludes that fiscal distress and fiscal capacity significantly influence accrual manipulation among Indonesian provincial governments during the COVID-19 pandemic, whereas leverage has no effect. High fiscal pressure and capacity encourage accounting discretion to maintain the performance. Strengthening fiscal governance and audit oversight is essential for reducing the risk of manipulation in public financial reporting.

**Limitations:** The limitations of alternative indicators and objects to districts/cities.

**Contributions:** These findings have important implications for local governments in strengthening financial governance, auditors in increasing oversight of accrual items vulnerable to manipulation, and future researchers in expanding the variables and scope of research.

**Keywords:** *Accrual Manipulation, Covid-19 Pandemic Fiscal Capacity, Fiscal Distres, Leverage*

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## 1. Introduction

The COVID-19 pandemic has become a significant turning point in local government financial governance in Indonesia. The pandemic's negative impact has affected almost all aspects of life, particularly the economy (Algifari, Subiyakto, & Rohman, 2024). In line with this, a study by Putri, Abdullah, Adnan, and Yusmita (2023), showed that the COVID-19 pandemic significantly impacted public sector accounting practices, with increased costs and fiscal pressures requiring government entities to adjust their financial reporting strategies. The magnitude of this impact led to the declaration of a national disaster through Presidential Decree No. 12 of 2020, which encouraged central and

regional governments to implement rapid and flexible fiscal policy adjustments. The issuance of Law No. 2 of 2020 and Presidential Regulation No. 72 of 2020 provided significant flexibility for regions, including widening deficits, reallocating budgets without legislative approval, and utilizing the SiLPA (Low-Income Budget). While these policies are crucial for maintaining emergency health and economic responses, they also create opportunities for accrual manipulation in regional financial reports.

The accrual basis, as stipulated in Minister of Home Affairs Regulation No. 64 of 2013, is primarily intended to improve the transparency and quality of financial information. On this basis, local governments are expected to present more accurate financial information, reflecting rights and obligations, and facilitating performance analysis. However, the flexibility inherent in the accrual basis also creates opportunities for irregularities. Manipulation under the accrual basis is easier because it does not require physical cash evidence. Similarly, [Cohen, Bisogno, and Malkogianni \(2019\)](#) stated that accrual manipulation is a form of exploitation of accounting discretion to present a financial condition that differs from reality.

The phenomenon of accrual manipulation during the pandemic is a serious concern, not only because it impacts the quality of financial reports, but also because it threatens the principles of transparency and accountability. Financial reports must also be prepared in accordance with the company's actual circumstances to provide a clear picture of its operations. Information must be clearly organized and understandable, and the information must have predictive value, and be timely. It must also be reliable ([Ramdani & Prayitno, 2023](#)). If financial reports, which should form the basis for planning, evaluation, and decision-making, are distorted, the quality of public policy is affected negatively. In the context of public trust, this distortion of information has the potential to undermine the legitimacy of local governments in the eyes of the public.

Several factors can encourage local governments to manipulate accruals. First, leverage, or the level of dependence on long-term liabilities. High leverage places additional pressure on regions to maintain the appearance of fiscal health, making accrual manipulation an opportunistic choice for concealing a larger actual burden. Second, fiscal distress occurs when revenues cannot cover regional expenditures. Fiscal distress arises from structural imbalances between revenues and expenditures. In practice, this condition often encourages regions to manipulate reports to maintain favorable audit opinions or avoid political sanctions ([Tampubolon, Dewata, Indriasari, & Jauhari, 2023](#)). Third, fiscal capacity reflects a region's ability to raise revenue to finance public services ([Martinez-Vazquez & Jameson Boex, 2011](#)). Regions with low fiscal capacity tend to be more vulnerable to manipulation because of limited fiscal space ([Abdullah & Junita, 2020](#)).

The pandemic clarified how these three factors operate simultaneously. Many regions are experiencing fiscal pressure due to declining Regional Original Revenue, while spending needs have increased drastically. Conversely, several regions with relatively high fiscal capacity are still able to maintain transparent financial governance, demonstrating that manipulation is not an absolute consequence but rather depends on integrity, institutions, and oversight systems. This difference confirms the relevance and crucial nature of research on the influence of leverage, fiscal distress, and fiscal capacity on accrual-manipulation.

Furthermore, this research is important for understanding the factors causing manipulation and serves as a basis for formulating solutions and preventative strategies. By understanding the influencing variables, the central government can formulate stricter regulations for regional debt management, strengthen monitoring mechanisms for regions with high fiscal distress, and provide institutional support to regions with high fiscal capacity. low fiscal performance. From a long-term perspective, the results of this study can contribute to efforts to strengthen governance and improve the quality of fiscal accountability in the regions.

Based on this description, research on the effects of leverage, fiscal distress, and fiscal capacity on accrual manipulation in provincial governments in Indonesia during the COVID-19 pandemic is relevant. This study is expected to enrich the literature on public sector accounting practices in

Indonesia and provide practical recommendations for policymakers to strengthen fiscal oversight, prevent manipulation, and ultimately improve accountability in local government financial management.

## 2. Literature Review and Hypothesis Development

Accrual manipulation is the deliberate act of local governments exploiting the flexibility of accrual policies to alter financial reports to achieve specific targets (Cohen et al., 2019). Accrual manipulation stems from accrual-based accounting, which was officially adopted by Indonesia through Government Regulation 71 of 2010. While increasing accountability, the flexibility of the accrual basis opens up opportunities for financial report manipulation, such as concealing funding shortfalls (Ridhwan & Dwiati, 2022). Cohen et al. (2019) states that one crucial issue in the implementation of accrual accounting at the local government level is the increased risk of earnings management practices using accrual manipulation.

This is because manipulation can be carried out through discretionary accruals, which are a portion of accruals that fall within the scope of management discretion. This flexible component of accrual-based accounting is vulnerable to opportunistic exploitation by politicians and public administrators. Pressure from various stakeholders for local governments to be accountable for their management of public resources often encourages financial report preparers to adjust accrual accounting figures. Consequently, the information presented in financial reports may not fully reflect the actual situation but rather reflect efforts to maintain an image of fiscal accountability before the public.

Leverage is an important indicator of the extent to which local governments rely on external financing through debt or long-term liabilities. Under normal conditions, high leverage often creates incentives for management to manipulate accruals to maintain the image of financial performance and secure creditor and stakeholder support. The higher an agency's leverage, the greater the potential for tax aggressiveness, which can ultimately encourage accrual manipulation as a strategy to reduce the tax burden and manage reported profit (Gunawan & Mappadang, 2024). This aligns with the free cash flow theory proposed by Jensen (1986), which explains that leverage can act as a control mechanism but can also encourage opportunistic behavior by management.

This situation is increasingly relevant during the COVID-19 pandemic, when regional fiscal pressures have increased sharply due to a significant decline in local revenue and the increased need for public spending on healthcare and economic recovery. This situation of fiscal uncertainty makes it difficult for local governments to maintain the stability of their financial statements. To maintain a healthy fiscal capacity, local governments can use discretionary accruals as an instrument to smooth out performance fluctuations or disguise financial structural imbalances. In other words, high leverage during the pandemic can increase the opportunity for accrual manipulation because of the incentive to present a better financial condition than reality.

Empirical findings indicate a tendency to recognize more profit than loss. Local governments with lower or higher leverage are expected to use accounting policies to increase their revenue (Cohen et al., 2019). Therefore, it can be assumed that leverage influenced accrual manipulation during the COVID-19 pandemic.

*H<sub>1</sub>: Leverage influences accrual manipulation during the COVID-19 pandemic.*

Fiscal distress is a condition of significantly reduced fiscal capacity in local governments, indicated by increased reliance on transfer revenues, an increasing portion of administrative spending, increasing debt, and slow growth in local revenue (Trussel & Patrick, 2009). Maher, Oh, and Liao (2020) define fiscal distress as a situation in which a local government is unable to meet its financial obligations in both the short and long terms.

The COVID-19 pandemic has further exacerbated fiscal pressure. A sharp decline in local revenue (PAD) and increased spending on health care, social assistance, and other emergency needs have pushed many local governments into fiscal distress. In this situation, governments often seek ways to maintain

a stable financial condition, one of which is by manipulating accruals, for example, by accelerating revenue recognition or delaying expense recording, as well as manipulating depreciation. This aligns with statement [Kumar \(2024\)](#) that depreciation fraud is often carried out by entities facing financial pressure to maintain the image of financial health. Research results on the relationship between fiscal distress and accrual manipulation still show mixed results.

[Abdullah, Handayani, and Darwanis \(2022\)](#) found that fiscal distress negatively affected accrual manipulation. However, other studies, such as [Shafira and Abdullah \(2022\)](#), [Tampubolon et al. \(2023\)](#), [Uttunggadewi, Martini, and Aryani \(2024\)](#), have shown a positive effect. This finding suggests that local governments tend to manipulate accruals to maintain their financial image, avoid political pressure, and maintain public trust. [Uttunggadewi et al. \(2024\)](#) emphasized that these efforts also aim to gain support from the central government and fiscal incentives.

Within Indonesia's decentralization framework, fund transfers from the central government require high accountability for public service delivery. However, the pressure to meet stakeholder demands and obtain incentives can encourage the use of accounting discretion ([Makruf, 2024](#)). This aligns with the research findings of [Rohman, Daud, and Ubaidillah \(2018\)](#); [Shafira and Abdullah \(2022\)](#) showed that fiscal pressure can trigger accrual manipulation practices as a response to financial constraints and external demands. Based on this description, the hypothesis proposed in this study is as follows:

*H<sub>2</sub>: Fiscal Distress Influences Accrual Manipulation in Provincial Governments Throughout Indonesia During the COVID-19 Pandemic*

Fiscal capacity reflects a region's ability to generate revenue to finance the provision of public services ([Nazikha & Rahmawati, 2021](#)). According to [Martinez-Vazquez and Jameson Boex \(2011\)](#), fiscal capacity reflects a region's potential to meet operational needs, while [Baskaran and Bigsten \(2013\)](#) emphasize that fiscal capacity relates to the effectiveness of resource management for the benefit of the community. The size of a region's fiscal capacity can change annually, influenced by transfer policies from the central government and extraordinary circumstances such as the COVID-19 pandemic ([Putri et al., 2023](#)).

The COVID-19 pandemic has depressed the Regional Fiscal Capacity Index through a decrease in local revenue (PAD) and transfer funds, along with increasing regional spending that has become increasingly stringent due to central government policies. The implementation of lockdowns has also exacerbated the situation, including through the closure of the tourism sector, mobility restrictions, and rising unemployment. All of these factors have resulted in reduced regional revenue, which, in turn, weakens fiscal capacity. [Hardianto, Sari, and Leviany \(2023\)](#) suggest that dependence on central funds can lead to opportunistic behavior by local governments to maintain fund allocations.

However, empirical findings on the effect of fiscal capacity on accrual-manipulation practices remain inconsistent. [Abdullah et al. \(2022\)](#) found no significant effect, whereas [Putri et al. \(2023\)](#) showed a negative effect of fiscal capacity. These results align with [Mauro \(1998\)](#), who found that regions with stronger fiscal capacity and a strong transparency system tend to be able to suppress manipulation practices due to stricter oversight. Based on this description, the following research hypothesis was formulated:

*H<sub>3</sub>: Fiscal Capacity Influences Accrual Manipulation in Provincial Governments throughout Indonesia during the COVID-19 Pandemic*

Regional governments have both the authority and responsibility to manage and budget their finances, as stipulated in the Minister of Home Affairs Regulation Article 4, paragraph (1) of Law No. 13 of 2016, which requires financial management to be conducted in an orderly, lawful, effective, efficient, economical, transparent, and responsible manner, while still adhering to the principles of justice and benefit. However, in practice, regional financial management is not entirely free from manipulation. Since the implementation of accrual-based accounting in 2015, the scope for accrual discretion has become increasingly open, which, under certain circumstances, can be exploited to manipulate financial reports ([Rohman et al., 2018](#)).

Several characteristics of regional governments can encourage the emergence of accrual manipulation practices, including leverage, fiscal distress, and capacity. Leverage reflects the level of a regional government's dependence on debt financing compared to its assets or revenues. High leverage indicates pressure to meet financial obligations, creating an incentive for regional governments to embellish financial reports through accrual manipulation to maintain the appearance of fiscal stability in the short term. Fiscal distress occurs when a regional government faces an imbalance between revenue and expenditure, which leads to financial pressure. Under these conditions, regional governments have a greater motivation to improve their financial image through accrual-manipulation practices. accrual manipulation.

Fiscal capacity describes a region's ability to generate local revenue and effectively manage existing resources ([Baskaran & Bigsten, 2013](#); [Martinez-Vazquez & Jameson Boex, 2011](#)). Regions with low fiscal capacity tend to be more vulnerable to accrual manipulation to cover their financial limitations. This situation was exacerbated by the COVID-19 pandemic. The pandemic caused a significant decline in regional revenue, particularly from local revenue (PAD) and transfer funds, and increased spending on emergency needs, health care, and social assistance. Consequently, fiscal pressures in various regions have intensified, fiscal capacity has decreased, and the incentives to maintain the appearance of financial reports have increased sharply.

### 3. Research Methodology

This study uses a causality study, a type of research in the form of a causal relationship between two or more variables, to explain the influence of independent variables on dependent variables. This research was conducted using the official website of the Republic of Indonesia Audit Board (BPK RI), namely Bpk.ri.com. This research will be conducted from February to October 2025. In this study, the researcher determined the independent and dependent variables, which are explained as follows. The independent variables used in this study are leverage ( $X_1$ ), Fiscal Distress ( $X_2$ ), and Fiscal Capacity ( $X_3$ ). The dependent variable in this study is Accrual Manipulation in Regional Financial Reports ( $Y$ ). This Accrual Manipulation describes the extent to which local governments experience abnormal discretion to achieve a surplus/deficit close to zero. This variable is measured using the modified Jones model as follows:

Table 1. Operational variable

$$\text{Diskreksi Akruai (DAit)} = \text{Total Akruai (TAit)} - \text{Estimasi non Diskreksi (NDAit)}$$

Table 1 shows that the population in this study is all provinces in Indonesia, totaling 38 provinces whose financial reports were audited by the Indonesian Supreme Audit Agency (BPK RI) in 2020, 2021, and 2022. This study used a purposive sampling technique, which means determining the sample with certain criteria. The criteria for selecting the sample in this study were provinces that have been established and have financial reports from 2020. Therefore, the sample used in this study is the *Regional Government Financial Reports* of 34 provinces in Indonesia. The number of variables analyzed is 4 (four) variables, namely leverage, Fiscal Distress, Fiscal Capacity and Accrual Manipulation, and the period studied is three years, namely 2020, 2021, and 2022, so that the analysis unit totals 510 units. The sample that will be used in this study will be shown in table 3.2

Table 2. Research sample

No	Description	Total
1	The Provincial Government was formed in 2020-2022 and had a Regional Government Financial Reports in that year	38
2	The government that has not been formed in 2020 and does not have a Regional Government Financial Reports in that year	(4)
	Number of observation samples	34

Table 2 shows that the author used secondary data, which were obtained and collected indirectly by the author, but rather from intermediaries or other parties. This research data consists of Budget Realization Reports (LRA), Operational Reports (LO), Cash Flow Reports (LAK), and Provincial Balance Sheets throughout Indonesia for the 2020-2022 period, namely 34 provinces, obtained from the website of the Supreme Audit Agency of the Republic of Indonesia (BPK RI): <https://e-ppid.bpk.go.id/> In this study, the method used to collect data is documentation, namely by compiling Regional Government Financial Reports audited by the Supreme Audit Agency (BPK) for the period 2020 to 2022. These data were obtained from the official website of the Information and Documentation Management Officer (PPID) of the Republic of Indonesia BPK.

In addition to secondary data from financial reports, this research is also supported by other secondary sources in the form of previous research results, scientific articles, academic journals, and relevant books to strengthen the theoretical foundation and the analysis. In this study, multiple linear regression analysis was the appropriate technique to address the research objectives, particularly in terms of explaining the relationships between variables. This study used multiple linear regression analysis to examine the influence of independent and dependent variables. The multiple linear regression equation used in this study is as follows: Ordinary Least Squares (OLS):

$$MA = \alpha + \beta_1 LVx_1 + \beta_2 FDx_2 + \beta_3 FCx_3 + \varepsilon \quad (1)$$

Where:

- MA = Manipulation of Accrual (accrual manipulation)
- $\alpha$  = Constant
- LV = Leverage
- FD = Fiscal Distress
- FC = Fiscal Capacity
- $\varepsilon$  = error (Relevant variables that were not included in the observation)

#### 4. Results and Discussion

The statistical results of this study are discussed below. Partial tests were used to examine whether all independent variables individually or individually influenced the dependent variable in the regression model (Ghozali, 2018). The purpose of this study is to determine whether leverage, fiscal distress, and fiscal capacity have a significant partial effect on accrual manipulation. This test used a significance level of 0.05 and was one-sided. The hypotheses to be tested are as follows:

- $H_1$ : Leverage influences accrual manipulation in provincial government financial reports in Indonesia.
- $H_2$ : Fiscal Distress influences accrual manipulation in provincial government financial reports in Indonesia.
- $H_3$ : Fiscal Capacity has an effect on accrual manipulation in provincial government financial reports in Indonesia.

Table 3. Partial test results (T-test)

Dependent Variable: Y_MA				
Method: Panel EGLS (Cross-section random effects)				
Date: 08/22/25 Time: 21:17				
Sample: 2020 2022				
Periods included: 3				
Cross-sections included: 34				
Total panel (balanced) observations: 102				
Swamy and Arora estimator of component variances				
Variables	Coefficient	Std. Error	t-Statistic	Prob.
C	-3.297800	3.931165	-0.838886	0.4036
X1 LEVERAGE	0.022497	0.049272	0.456588	0.6490
X2 FD	9.100924	2.918108	3.118775	0.0024
X3 FC	0.740259	0.309177	2.394287	0.0186

Based on the t-test results in Table 3, the following tests can be performed:

1. The leverage coefficient test had no effect on accrual manipulation. This can be seen by determining the t-table, which can be found at a significance level of 0.025 in a two-sided test with degrees of freedom ( $df = n - k$  or  $102 - 3 = 99$ ) ( $n$  is the number of data points, and  $k$  is the number of variables). The t-table result was 1.98/-1.98. Based on the Eviews 12 output, the calculated t-test for the leverage variable was 0.0492. It can be seen that the calculated t-test is  $< t$ -table ( $0.0492 < 1.98$ ), and the significance value is  $0.649 > 0.05$ , thus rejecting  $H_1$ . Therefore, it can be concluded that leverage has no effect on accrual manipulations.

2. Testing the Fiscal Distress coefficient has a positive effect on Accrual Manipulation can be done by determining the t table at a significance of 0.05 tested two sides with degrees of freedom  $df = n - k$  or  $102 - 3 = 99$  ( $n$  is the number of data points, and  $k$  is the number of variables). The results obtained for the t-table are 1.98 / -1.98. Based on the output from Eviews 12, the results obtained show that the Fiscal Distress Variable t count is positive at 3.1187. It can be seen that  $t \text{ count} > t \text{ table}$  ( $3.1187 > 1.98$ ) and significance is obtained ( $0.002 < 0.05$ ), then  $H_2$  is accepted. Therefore, it can be concluded that fiscal distress has a positive and significant effect on accrual manipulation.

3. Testing the fiscal capacity coefficient for its positive effect on accrual manipulation can be done by determining the t-table, which can be found at a significance level of 0.025 in a two-sided test with degrees of freedom ( $df = n - k$  or  $102 - 3 = 99$ ) (where  $n$  is the number of data points and  $k$  is the number of variables). The result for the t-table is 1.98/-1.98. Based on the output from Eviews 12, the results show that the calculated t-value for the fiscal capacity variable is positive at 2.394. It can be seen that the calculated t-value is greater than the calculated t-value ( $2.394 > 1.98$ ) and the significance value is ( $0.0186 < 0.05$ ), thus  $H_3$  is rejected. Therefore, we conclude that fiscal capacity has a positive and significant effect on accrual manipulation.

The coefficient of determination was used to measure the extent to which the model could explain variations in the dependent variable. The coefficient of determination is between zero and one ( $0 < X < 1$ ). A small  $R^2$  value indicates that the independent variables' ability to explain the variation in the dependent variable is very limited, as other external factors influence the dependent variable in addition to the independent variable. A large value indicates that the independent variables have a sufficiently strong ability to predict variations in the dependent variable. The results of the coefficient of determination test ( $R^2$  test) are presented in Table 4.

Table 4. Results of the Determination Coefficient ( $R^2$ ) Test

<b>Weighted Statistics</b>			
Root MSE	6.553285	R-squared	0.145935
Mean dependent var	4.250891	Adjusted R-squared	0.119790
S.D. dependent var	7.126119	S.E. of regression	6.685688
Sum squared resid	4380.446	F-statistic	5.581798
Durbin-Watson stat	1.450566	Prob(F-statistic)	0.001411

Based on Table 4, the adjusted  $R^2$  value is 0.145. This result indicates the ability of the independent variables to explain the dependent variable. Leverage, Fiscal Distress, and Fiscal Capacity exert a 14% influence on accrual manipulation in provincial governments in Indonesia, while the remaining 86% is explained by other variables or factors that influence accrual manipulation in provincial governments in Indonesia. Hypothesis testing using the F distribution is a statistical test. Simultaneous testing (F-test) aims to determine whether all independent variables simultaneously or jointly influence the

dependent variable. Testing can be performed using the decision criteria of the F significance value at  $\alpha$  level. This study used an  $\alpha$  level of 0.05 (5 %). The hypothesis to be tested is as follows:  
 $H_5$ : Leverage, fiscal distress, and fiscal capacity simultaneously influence accrual manipulation in provincial governments in Indonesia.

The hypothesis-testing criteria are as follows:

1. If the F significance value is  $<0.05$  or the calculated F value is  $<F$  table, then  $H_5$  is accepted, meaning that all independent variables simultaneously influence the dependent variable.
2. If the F significance value is  $>0.05$  or the calculated F value is  $>F$  table, then  $H_5$  is rejected, meaning that not all independent variables simultaneously influence the dependent variable.

Table. 5 F Test Result

Weighted Statistics			
Root MSE	6.553285	R-squared	0.145935
Mean dependent var	4.250891	Adjusted R-squared	0.119790
S.D. dependent var	7.126119	S.E. of regression	6.685688
Sum squared resid	4380.446	F-statistic	5.581798
Durbin-Watson stat	1.450566	Prob (F-statistic)	0.001411

Based on Table 5, the calculated F-statistic test results are 5.5817. To determine the F-statistic, refer to the statistical table at a significance level of 0.05 with df (number of variables - 1) or  $df = (n - k - 1)$  or  $102 - 3 - 1 = 98$  (where n is the number of data points and k is the number of independent variables). The F-statistic is 2.697. Because the calculated F-statistic is greater than the F-statistic ( $5.5817 > 2.697$ ) and the significance level is 0.0014,  $H_5$  is accepted. Therefore, it can be concluded that leverage, Fiscal Distress, and Fiscal Capacity simultaneously influence Accrual Manipulation.

#### 4.1 The Effect of Leverage on Accrual Manipulation

Based on the partial test results (t-test) presented in Table 5 that the absence of a leverage variable on Accrual Manipulation can be determined by first determining the t-value. The t-table value was obtained at a significance level of 0.05 for a one-sided test with degrees of freedom (df) of n-k, namely  $102-3 = 99$ . Based on this calculation, the t-table value was  $\pm 1.98$ . Meanwhile, the output from Eviews 12 shows that the calculated t-value for the leverage variable is 0.0492. Because the absolute value of the calculated t-value is greater than the t-table ( $0.0492 < 1.98$ ) and the significance value of 0.649 is greater than 0.05, it can be concluded that  $H_1$  is rejected. This means that the leverage variable has no effect on accruals manipulation.

The results of this study are inconsistent with those of [Ishak \(2024\)](#) that local governments with lower or higher leverage are expected to use accounting policies to increase revenue. The level of leverage or debt in the Indonesian Regional Financial Report is not related to accrual manipulation because there is no tendency to recognize profits or revenue greater than losses in the Indonesian Regional Government's Financial Reports. Furthermore, there is no information asymmetry regarding profits and losses in Indonesian regional financial reports ([Gamayuni, 2022](#)). The leverage data between provinces showed significant fluctuations. Some regions experienced extreme spikes, such as Banten in 2020 at 122.67 and South Kalimantan at 91.06, while others remained relatively stable at low levels, such as the Yogyakarta Special Region and Papua. However, this variation is not related to the accrual manipulation patterns. This means that although leverage increased in some regions due to the fiscal pressures of the pandemic, this did not automatically trigger local governments to manipulate accruals in the financial reports.

According to [Jensen \(1986\)](#) free cash flow theory, leverage can function as a control mechanism by limiting managers' freedom to utilize cash flow while potentially preventing earnings management practices. However, research [Meisi and Syukriy \(2026\)](#) indicates an ambivalence: on the one hand,

leverage can suppress agency conflicts, but on the other, it can create new conflicts between shareholders and creditors. In the context of local governments in Indonesia, particularly during the COVID-19 pandemic, leverage did not significantly influence accrual manipulation because of the predominance of external factors.

The pandemic created uniform fiscal pressures across nearly all regions, with public spending sharply increasing for healthcare, social assistance, and economic recovery, while regional revenues declined drastically. However, this burden was largely covered by central government fiscal support, such as transfers to regions, regional incentive funds, and the National Economic Recovery Program. This support prevented the reliance on leverage from being the primary determinant of accrual decision-making.

Furthermore, increased public attention to COVID-19 budget transparency and strict oversight by the Supreme Audit Agency have limited the scope for local governments to manipulate accruals. Public accountability in the government sector is a key factor that can suppress the opportunistic behavior of officials, especially during times of crisis. Thus, leverage loses its relevance as a driving factor of accrual manipulation in the context of a pandemic. Overall, the results of this study strengthen the view that during a global health and economic crisis such as COVID-19, external factors in the form of regulations, central fiscal policies, and demands for public transparency have a greater influence on local government financial reporting practices than leverage conditions.

#### *4.2 The Effect of Fiscal Distress on Accrual Manipulation*

Based on the results of the partial t-test presented in Table 4, the calculated t-value for the Fiscal Distress variable ( $X_2$ ) was 2.854, with a significance level of 0.005. To determine the t-table, a significance level of 0.05 was used with a one-sided test and degrees of freedom (df) of  $n - k = 102 - 3 = 99$ , resulting in a t-table value of 1.98. Because the calculated t-value (3.1187) is greater than the t-table value (1.98) and the significance value is less than 0.05 ( $0.0024 < 0.05$ ), it can be concluded that  $H_2$  is accepted, indicating that Fiscal Distress has a significant positive effect on accrual manipulation.

This study indicates that the greater the fiscal pressure experienced by local governments, the greater the likelihood of accrual manipulation. These results are inconsistent with research by [Gamayuni \(2022\)](#); [Adnan, Abdullah, and Kamal \(2023\)](#), which concluded that fiscal distress negatively impacts accrual manipulation practices. Conversely, these findings support the findings of studies conducted by [Tampubolon et al. \(2023\)](#) and [Uttunggadewi et al. \(2024\)](#), which found that fiscal distress encourages opportunistic behavior in the form of manipulation of financial statement presentation.

An analysis of 34 provincial governments in Indonesia during the COVID-19 pandemic shows that fiscal distress positively affects accrual manipulation. This is evident in several provinces with high levels of fiscal distress, such as North Sulawesi in 2022 (1.84), Papua (1.46), and West Sumatra (0.99), which also exhibit significant absolute accrual manipulation. This phenomenon indicates that local governments engage in accounting maneuvers in response to fiscal constraints and budgetary pressures during pandemics. [Ferreira, Carvalho, and Pinho \(2013\)](#) noted that fiscal pressure drives the government to create a positive image through the manipulation of financial reports.

The relationship between fiscal distress and accrual manipulation can be explained by a combination of agency and legitimacy theories. From an agency theory perspective, [Meckling and Jensen \(1976\)](#) argue that fiscal pressure exacerbates conflicts of interest between local governments as agents and the public/central government as principals. In a fiscally constrained situation, agents have an incentive to present financial reports that do not fully reflect the actual conditions to cover deficits and maintain a performance image. Fiscal constraints also increase information asymmetry, which provides room for agents to manipulate accruals.

Public organizations seek to maintain social acceptance by adapting financial reporting practices to public expectations. When the COVID-19 pandemic created dual pressures in the form of declining

revenues and increasing regional spending, accrual manipulation emerged as a legitimacy strategy. By presenting seemingly healthy financial conditions, local governments seek to maintain legitimacy in the eyes of the public, central government, and regulatory agencies ([Goddard & Issa Mzenzi, 2015](#)). Thus, in the context of fiscal distress, accrual manipulation is motivated not only by conflicts of interest, as explained by agency theory, but also by the need to maintain public legitimacy, as explained by legitimacy theory.

These two theories complement each other in understanding the incentives of local governments to engage in opportunistic accounting practices amid fiscal pressures, particularly during the COVID-19 pandemic crisis. Furthermore, the COVID-19 pandemic has created dual pressures. On the one hand, regional revenues decline due to weakened economic activity and reduced fiscal transfers; on the other hand, regional spending increases drastically for healthcare, social assistance, and economic recovery. Under these conditions, accrual manipulation becomes an administrative strategy used by local governments to improve the appearance of their financial conditions.

This finding aligns with [Rohman et al. \(2018\)](#); [Shafira and Abdullah \(2022\)](#), who assert that fiscal constraints drive governments to engage in accrual manipulation as a response to budgetary pressures and external demands. Therefore, this study confirms that fiscal distress, particularly during crises such as the COVID-19 pandemic, has implications for increased accrual manipulation practices in local governments. This situation demonstrates the importance of strengthening oversight mechanisms and increasing the transparency of financial reporting to reduce the potential for accrual manipulation in the face of severe fiscal pressures.

#### *4.3 The Effect of Fiscal Capacity on Accrual Manipulation*

The partial regression test results presented in Table 5 indicate that the fiscal capacity variable has a t-statistic of 2.394, which is greater than the t-table value of 1.98 at the 0.25 significance level, and a significance value of 0.0186, which is less than 0.05. Therefore, we conclude that fiscal capacity has a positive effect on accrual manipulation, thus accepting  $H_3$ . The results show that fiscal capacity positively affects accrual manipulation. This means that local governments with high fiscal capacity are more likely to manipulate financial reporting.

This positive relationship indicates that the availability of substantial resources does not automatically suppress opportunistic practices but can be utilized to expand accounting flexibility. This situation is evident, for example, in the East Java Provincial Government, which recorded a fiscal capacity of IDR 11.63 trillion in 2022, with accrual manipulation reaching IDR 27.45 trillion, the highest at the national level. A similar situation occurred in West Java, which, despite consistently maintaining a fiscal capacity of over IDR 9 trillion during the 2020–2022 period, exhibited significant fluctuations in accrual manipulation figures, including extreme values in 2020 and 2021, indicating an aggressive accrual strategy.

This finding contrasts with previous studies that found a negative relationship between fiscal capacity and accrual manipulation, where strong fiscal capacity is believed to suppress manipulation practices due to its support for more stable and efficient financial management ([Putri et al., 2023](#)). This can be explained by agency theory. From an agency theory perspective, the positive relationship between fiscal capacity and accrual manipulation can be understood as a consequence of a conflict of interest between the principal (the public/central government) and agent (local government). High fiscal capacity provides local governments with greater flexibility in managing financial resources.

However, the availability of these resources also opens up opportunities for agents to act opportunistically by manipulating accruals to maintain a performance image, achieve budget targets or conceal management inefficiencies. During the COVID-19 pandemic, the crisis weakened the oversight and accountability mechanisms. In such situations, information asymmetry between principals and agents increases, making it easier for local governments to conceal manipulative practices in financial reports. This explains why high fiscal capacity encourages increased accrual manipulation, contradicting the previous view that strong fiscal capacity improves financial stability and governance.

Strong fiscal capacity leads to greater public expectations regarding the quality of regional financial governance and transparency. In this situation, local governments strive to maintain legitimacy by presenting financial reports that appear to be sound and meet stakeholder expectations. However, the pressure to meet these expectations can encourage agents to manipulate accruals, for example, by delaying expense recognition or accelerating revenue recognition, to appear to be managing fiscal capacity optimally. Thus, this study confirms that fiscal capacity, particularly during crises such as the COVID-19 pandemic, has implications for increased accrual manipulation practices in local governments. This highlights the importance of strengthening oversight mechanisms and increasing transparency in financial reporting to reduce the potential for accrual manipulation amidst severe fiscal pressures.

#### ***4.4 The Effect of Leverage, Fiscal Distress and Fiscal Capacity on Accrual Manipulation***

Based on the results of the simultaneous test, the effect of leverage, fiscal distress, and fiscal capacity on accrual manipulation can be seen in Table 4. The calculated F value was 8.875 with a significance value of  $0.0014 < 0.05$ . The F table value is 2.697, so the calculated F value is greater than the F table value ( $8.875 > 2.69$ ), thus  $H_5$  is accepted. This indicates that the studied variables, namely leverage, fiscal distress, and fiscal capacity, simultaneously influence accrual manipulation. This means that all independent variables simultaneously act as interdependent factors that influence accrual manipulation. Furthermore, the F-test results show a coefficient of determination or adjusted  $R^2$  value of 0.14, or 14%.

This indicates that the four independent variables explain 14% of the influence on the dependent variable, leverage, fiscal distress, and fiscal capacity, providing motivation and opportunity for stakeholders to engage in accrual manipulation to achieve specific goals. Meanwhile, the remaining 86% is explained by other variables due to other factors, such as incentives provided by the government to local government financial managers ([Gamayuni, 2022](#)). Pressure from external stakeholders and depreciation and impairment charges on fixed assets also encourage accrual-manipulation practices ([Arcas & Martí, 2016](#)).

## **5. Conclusions**

### ***5.1 Conclusion***

Leverage has been shown to have no significant effect on accrual-manipulation practices. Fiscal distress has a positive effect on accrual manipulation, meaning that the more severe the financial conditions faced by provincial governments, the greater their tendency to engage in accounting manipulation. In contrast, fiscal capacity positively affects accrual manipulation. This indicates that the greater the government's fiscal capacity, the greater the opportunity for accounting flexibility, which leads to manipulation practices to maintain its image and adjust financial targets. Simultaneously, leverage, fiscal distress, and fiscal capacity play a role in influence accrual manipulation in provincial governments in Indonesia. The combination of these three factors can collectively encourage or suppress local governments' tendency to engage in deviant accrual-based accounting practices.

### ***5.2 Research Limitations***

This study had several limitations. First, this study focuses solely on provincial governments in Indonesia, which limits the generalizability of the findings to districts, municipalities, or other public sector entities. Second, the study relies on specific proxies to measure accrual manipulation, fiscal distress, and fiscal capacity, which may not fully capture the complexity of the financial behavior of public institutions. Third, the observation period may not sufficiently reflect long-term fiscal trends or structural changes in the financial management of the government. These limitations suggest that the findings should be interpreted within the specific institutional and temporal contexts examined.

### ***5.3 Suggestions and Directions for Future Research***

Provincial governments are encouraged to strengthen financial governance mechanisms in planning, budgeting, and reporting processes to minimize accrual manipulation, particularly when under fiscal pressure. The central government, through the Ministry of Home Affairs and the Financial and Development Supervisory Agency, should enhance risk-based supervision in regions experiencing high

fiscal distress and possessing substantial fiscal capacities. Internal auditors and supervisory bodies can use these findings to identify vulnerable areas prone to accrual-based manipulations. Future research should incorporate additional explanatory variables, such as political factors, governance quality, audit opinions, and internal control effectiveness, to provide a more comprehensive analysis. Researchers are also encouraged to apply alternative measurement models for accrual manipulation and extend the research scope to districts and municipalities in Indonesia. Expanding the observation period and employing comparative or mixed-method approaches may provide deeper insights into fiscal behavior and financial reporting practices in decentralized public sector environments.

### Author Contributions

NY contributed to the conceptualization of the study, research design, and data collection. S was responsible for the data analysis and interpretation of the results. OS conceptualized the research framework, supervised the overall research process, conducted critical revisions and finalized the manuscript. SAR assisted with data processing, literature review development, and manuscript drafting. All authors reviewed, approved the final version of the manuscript, and agreed to be held accountable for all aspects of the work.

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