Principal Agents And Village's Fund Allocation: From Problems To Solution

Syofyan, Misri, Edi Sopian, Usman

Abstract: Principal agents issues is often discussed in the new institutional economy. In public institutions, principals and agents are the two parties that have authority due to the law. In public policy a person who acts as a principal in a particular institutional hierarchy is an agent on higher level fo institution. Therefore, discussing principal agents with interesting public policies to analyze is mainly related to policies issued by the government. In this study, principal agents are associated with village fund allocation as a development policy carried out by the government where the village head and village secretary are two parties who are bound in one principal and agent relationship. Principals and agents in this study are influenced by indicators determined by law. The same goes for village fund allocation. The relationship between them is influenced by the principal conflict of agents. This study aims to find out how the principal agent's relationship to the allocation of village funds, how principal agent conflicts affect's their relationship and seek solutions to overcome them.

Key-word: Principal Agent, Village Fund Allocation, Principal conflict Agent

1 INTRODUCTION

Eisenhardt (1989; 59) says that in agency theory, principals and agents are two parties with different goals and preferences where each individual has his own interests, limited rationality and avoiding risk. The organization where the principal agent relations is assumed to have a conflict of partial goals between principal and agent, efficiency as a criterion of effectiveness and information asymmetry. Principals and literature agents are also called positive flows, which focus on identifying situations where principal agents may face conflict of purpose in describing service mechanisms that limit agent behavior. The study was specifically carried out on the principal relations of agents on a large scale and public companies (Berle and Means, 1932); Down (1964), Jensen and Meckling (1976), Eisenhardt (1989; 59) and Olievera and Filho (2017: 599) define agency relations as contracts in which one part (agent) is tasked with carrying out certain activities in the name of another (principal). This theory emphasizes the search for contract models that best govern agreements between principals and agents. Both are considered to act in accordance with rational behavior, motivated by personal interests and the possibility to minimize contract costs. In the institutional economic literature, agency relationship is known as the principal relationship. Principal is also called the owner and agent is the manager. The difference in interests is caused by existence of hidden action and hidden knowledge factors. Agents have two advantages over principals namely hidden action and hidden knowledge (Lane, 2013: 85-89) and Schornet (2016: 22). Agency theory expresses the relationship between the actor (the company owner or the mandating party) and the agent (company manager or party receiving the mandate) based on the separation of ownership and control of the company, the risk of separation, decision making and control functions (Jensen and Meckling, 1976), Braun and Guston (2003: 303), Caers et al, (2006: 29), and Malmir et al, (2014: 4).

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There is a contract in the agency relationship, where one or more people (principals) instructs other people (agents) to perform services on behalf of the principal and authorized agents to make decisions or manage the best business for the principal. Optimizing agency problems requires new cost categories to significantly reduce the negative effects of agency costs. Agency costs can be minimized by using incentive compensation, monitoring, and signaling by agents (Chua et al. 2009: 359), Attila (2011: 709). Agency relations in the public sector are generally analyzed using public choice theory, namely by assuming that the State depends on democratically elected politicians, to make public policy, such as the service of the interests of civil society (Lemieux, 2015) Dixit (2002) says that people are actually stakeholders from the public sector, even though they are not directly involved in finance but they are directly involved through taxes. For this reason agents in the public sector will act in the interests of the community to respond their actions because they are chosen by the government and society (Sopta, Mikic and Boticki, 2017: 107). In his paper, Dixit (2002) says certain public sectors specifically influence the principal relations of agents and create an efficient incentive system. Specificity in the form of existence: Multiple Principals, Multiple Tasks, Lack of Competition, Motivated Agents. Basically, individual behavior regarding public decisions is not different from the behavior observed in business decisions. Individuals strive to maximize their own satisfaction and interests. In democratic governance, government policies will reflect the rationality of ordinary people (Buchanan and Tullock, 1962), Viscusi and Gayer (2015). In the concept of public choice, the state is not the dominant entity, but a product of political exchange, which exists to serve the community (Buchanan, 1975). This reasoning is basically the same as the concept of agency relations in Jensen and Meckling (1976), given that civil society can be seen as the principal and the State as an agent. Decisions made by bureaucrats consist of public choice, which deals with the definition of public goods to be produced and in what amounts (Silva, 1996). Sopta, Mikic, and Botikic (2017: 105) explain the public and private meanings in agency relations associated with the operations of public companies and public institutions. Public sector operational activities are different compared to the operations of private companies. The main reason lies in the issue of ownership. Private company ownership comes from private ownership, while in public companies the largest share is owned by the State. Thus, their business interests are significantly different. Similarly, the factors that influence private companies are not relevant to be applied to public companies. In principal agent relations there is information asymmetry and goal's conflict. Information asymmetry occurs when a company (stakeholder) has and or hides information to other parties (shareholders). Information Asymmetry is a condition where one party has more information than the other. This term is also called Information asymmetry gap. Attila (2011: 711) says in practice, the relationship between principals and agents is divided into two components, each of which is adverse selection and moral hazard. Adverse selection problems arise from asymmetric information before and / or after a contract, while moral hazard problems stem from unobservable managerial actions that occur after the contract (Sung 2005: 1021). Second, adverse selection and moral hazard comes from information asymmetry. If the cause can be controlled or even eliminated then the damaging effects of the existence of these two components will not appear with high intensity. Reducing this problem of principal-agent model can use incentive models in organizations (de la Rosa, 2011: 429). Furthermore, funding issued by principals to agents in the form of incentives aims to make agents act in accordance with the interests of principals (Van Horn, 2011: 14). Experts conclude that incentive allotment is the best solution. Incentives can be designed in various forms, but the main choices remain in the form of financial incentives. Macias (2012: 46) says that adverse selection is a condition where the principal cannot ascertain if the agent has the ability to carry out the burden of the task given to him. This problem occurs before the principal enters into the agency relationship with the agent. Adverse selection problem arises because the principal has no certainty about the agent's intensity and ability. The adverse selection model presents a situation where agents as decision makers have personal information and depend on that information. This information can negatively affect other parties. The principal makes a contract and offers it to the agent (Marinescu and Marin, 2011: 34). Macias, (2012: 45) states that moral hazard can occur every time whenever two parties make an agreement. Each party bound to a contract has the opportunity to benefit from actions that are different from the agreements agreed upon in the contract. Attila (2011: 709-710) says moral hazard is equivalent to rational economic behavior in an organization or individual. Moral hazard involves rational behavior, namely self-interest, which is characterized as opportunistic because it uses opportunities for personal gain, even if it harms others. Moral hazard arises when agents do not fulfill their duties properly and monitoring principals is imperfect and because of mistaken information that only agents have. (Barbagallo and Comuzzi, 2008: 8). When agent actions cannot be observed, parties design optimal contracts to maximize mutual benefits to reduce moral hazard (Pobletey and Spulber, 2011: 3). In public institutions, moral hazard can be observed after the contract. It is implemented and government cannot make a thorough observation. One effort that can be done to overcome is by contracting and making efficiency (Cox et al. 1996: 148). Oliveira and Filho (2017) said that moral hazard behavior will increase through the financial mechanism carried out by agents in the contractual relationships that are carried out. Allotment of the Ex-ante budget allows agents to act rationally and optimally. Furthermore, in addition to information asymmetry, the difference in interests between principal agents is also caused by a goal conflict Goal conflict is a situation where principal and agent are in a conflict situation, in terms of achieving goals and both are in different actions. The principal's aim is for agents to develop as much as possible the principal's business. Instead the agent is assumed to act for his own interests and will work at the minimum level accepted by the principal (Petersen, 1995), Macias (2012: 48). A destination conflict occurs because of the interests of agents who are different from the principal where the agent acts maximally or pursues his own utilities. Therefore, the principal must make a guarantee that the agent will act in accordance with the contract. Goal's conflict between principal agents can be resolved if there is an incentive mechanism that regulates the relationship (Milgrom and Robert, 1992), Macias, (2012: 48). Referring to Eisenhardt (1089: 59) then in this study, adverse selection, moral hazard and goal conflict are called as principal agent conflicts Allocation of village funds is a number of funds obtained by the village originating from the district / city financial balance funds and contained in the regional income and expenditure budget after being reduced by special fund allocations. Allocation of village funds is given to all villages. Since village fund policies have been implemented, many benefits and problems have arisen. In the initial stages problems arise from the side of village readiness in planning, implementation and results. As stated by Rahmawati et al (2015), the village has not been fully prepared because there are still obstacles in the implementation of the village law. The main factor that became the obstacle was the limited time in administrative preparation and understanding the contents of the law as the basis of the rules. Another factor is human resources are less supportive. Abidin (2015) also found the fact that the use of the Village Fund Allocation still encountered a number of problems in planning, implementation, reporting quality, and weak village institutions and coordination with the district / city government. Ruliyanti (2016) argues that organizational commitment and human resources have a significant positive relationship to the management of village fund budgets and the performance of village governments, the performance of village budget management but regulation and communication are not significant. From the macroeconomic aspects, Harahap (2018) found that village fund allocation provided economic growth and increased labor and human development indices. From the institutional aspect, Jamaluddin et al (2018) suggested the implementation of Law No. 6 year 2014 has benefits (ideal) and loss (reality):

Benefits (Ideal):

a) Village Funds as a resource to synergize the National-Provincial and regional Development programs.
b) Village Funds are motivated by the village community to return to or remain in the village to build villages through labor-intensive programs by

utilizing village potential and empowering the ability of citizens

c) Village fund policies contains economic and political values. Economically; with increasing infrastructure, it encourages the productivity of the community in managing their potential. Politically spurring public awareness of their rights to get involved in government and development.

Loss (Reality):

a) Villages find it difficult to account for the use of the fund in the format of the State's budget, income and expenditure report
b) The use of funds is not appropriate for the purpose.
c) Central actors are increasingly difficult to monitor budget using. Even if it is done through direct control, it has implications for increasing resources (human and budget) for monitoring and evaluation activities.Villages run programs according to their village mid-term program plans
d) Village mid-term program plans and pay little attention to regional development policies. Because the Village has the authority assigned by the Government based on the Village Law.
e) With that authority created a sectoral ego for each village, so that competition between villages occurs, and community productivity in managing their potential. Politically this spurred public awareness of their rights to be involved in government and development and there was no program synchronization to encourage the achievement of regional and regional development priorities.
f) Local Governments lack power to use Village Funds. Regions are only authorized to monitor and evaluate.

2 METHODOLOGY

The relationship of principal agents in this study is arranged in a structural equation model consisting of dependent and independent variables. The dependent variable is the principal agent relationship (PAR) and village fund allocation (VFA). Independent variables are prinsipal agent conflict (PAC). These conflict's indicators are adverse selection, moral hazard and goal conlict. This research adopts the principal agent concept into the principal form of public institutional agents. Operational definitions of variables and indicators are taken from Law No.6, year 2014 concerning villages and Minister of internal affair regulation's Republik of Indonesia, number 113, year 2014 concerning village financial management and agency theory in public institutions. Adverse selection, moral hazard and goal conflict in prinsipal agent conflict refers to eisenhard (1989: 59); (Milgrom dan Robert, 1992), Macias (2012: 46); Attila (2011: 709-710); Oliveira dan Filho (2017); the problems of village funds allocation refers to benefits (ideal) and loss (reality) in institution aspects of village funds allocation by Jamaluddin et al (2018). The purpose of studies is to identify problems of principal agent in village funds allocation refers on Jamaluddin et al (2018), influenced by principal agent conflict and propose solution.

Principals are village heads and agents are village secretaries in under developed and very under developed villages in Padang Lawas District, North Sumatra Province which amounts to 351. The number of respondents is 702 people. Data obtained from questionnaires. Data from research results are arranged in one table using the SPSS program. Data were analyzed descriptively and multivariate regression analysis. Data validity using confirm factor analysis (CFA). Analysis of data using the SPSS and Amos 22 Computer software program. This study quantitatively measures the effect of each variable in the principal relationship of public institutional agents formed by law.

3 RESULT AND DISCUSSION

The output Amos analysis of prinsipal agent relation (PAR) and village funds allocation (VFA) influenced by conflict principal agent (CPA) shown in table 1.1 below.

Table 1.1 *Correlation between variables*

Variable's		Variable's	Estimate
VFA	<-->	*PAR*	*.812*
VFA	<-->	*PAC*	*.529*
PAR	<-->	*PAC*	*.630*

Source: Output analysis by Amos, 2019

From table 1.1 we can see that the relationship between PAR and VFA has the highest correlation value compared to PAC with VFA and PAC with PAR. The correlation between PAR and VFA is very strong. The relationship between PAC and VFA and the relationship between PAC and PAR had moderate strength. Referring to Jamaluddin et al (2018) on the benefits of village funds, a very strong relationship between PAR and VFA proves that village fund allocation provides benefits as: (a) as a resource to synergize the National-Provincial and regional Development programs. (b) the motivation of the village community to return or remain in the village to build a village through labor-intensive programs by utilizing village potential and empowering the ability of citizens (c) to contain economic and political values. Economically; with increasing infrastructure, it encourages the productivity of the community in managing their potential. Politically spurring public awareness of their rights to get involved in government and developmentFurthermore, the influence of each indicator of the research variable can be seen from the regression values generated in the calculation. The regression value shows the effect of indicators on the research variable. This value is shown in table 1.2

Table 1.2 *regression's koefisien of indicator variables*

Description	*Ind.*		*Var*	*Est.*
Allocation of village funds is used for government administration	*y21*	*<---*	*VFA*	*0.482*
Allocation of village funds is used for the implementation of village development	*y22*	*<---*	*VFA*	*-0.562*
Allocation of village funds is used for village community development	*y23*	*<---*	*VFA*	*0.099*
Allocation of village funds is used to empower village communities	*y24*	*<---*	*VFA*	*0.229*
Allocation of village funds is used for under estimated expenditure	*y25*	*<---*	*VFA*	*-0.553*
Agents as technical executors, village financial management verify the evidence of receipt and expenditure of the village Revenue and expenditure budget	*y19*	*<---*	*PAR*	*0.431*
Agents compile reporting and accountability for the implementation of the village revenue and expenditure budget	*y18*	*<---*	*PAR*	*0.539*
Agents exercise control over the implementation of activities set out in the Village Revenue and Expenditure Budget	*y17*	*<---*	*PAR*	*0.497*
Agents draw up a draft village regulation on the Village Revenue and Expenditure Budget, changes to the Village Revenue and Expenditure Budget and accountability for the implementation of the Village Income and Expenditure Budget	*y16*	*<---*	*PAR*	*0.495*
The agent as a village financial management technical officer is tasked with preparing and implementing village management policies	*y15*	*<---*	*PAR*	*0.447*
Principals take actions that result in expenditures at the expense of the village Budget and expenditure budget	*y14*	*<---*	*PAR*	*0.414*
The Principal agrees to expenditures for activities specified in the village revenue and expenditure budget	*y13*	*<---*	*PAR*	*0.473*
The principal determines the officers who collect village revenue	*y12*	*<---*	*PAR*	*0.386*
The Principal determines the village financial management technical Implementation	*y11*	*<---*	*PAR*	*0.405*
The Principal establishes a policy regarding the implementation of the village budget and expenditure revenue	*y10*	*<---*	*PAR*	*0.682*
Planning decisions for village fund allocation programs are based on information, false facts so that the results are not in accordance with the actual objectives	*x41*	*<---*	*PAC*	*0.777*
The tendency to act that is not in accordance with the decision because of other factors that cannot be avoided so that the objectives of village fund allocation cannot be achieved properly	*x51*	*<---*	*PAC*	*0.822*
Differences in objectives and interests in allocating village funds, namely there are different objectives in determining village fund allocation planning	*x61*	*<---*	*PAC*	*0.847*

Resource: processed from Amos's output, 2019
Noot: Indi.= Indicator; Var.= Variable. Est.= estimation

From table 1.2 we found that (1) y21 more influential than the other indicators of VFA. (2) y22 and y25 have a negative effect on VFA (3) y23 and y24 are has smallest effect to VFA. (4) y10 for principal is more influential than other indicators of PAR. y18 for agent has stronger effect to VFA after y10 (4) All PAC indicator values have the highest influence compared to other indicators of all variables. (5) X61 is more influential than other indicators of PAC and has the strongest influence compared to all indicators of all variables. PAC is a mediator. From these data, referring to Jamaluddin et al (2018) regarding the loss of village funds in point a) the value of y18 indicates that the report has been implemented properly even though it must be improved. For loss point b) so that losses can be minimized all VFAs are used for only one or two goals, for example y21 or y22 only. For losses in point c) the central government is unable to carry out direct supervision because the regulation requires that, that in accordance with article 44 paragraph (1) and (2) chapter VI concerning guidance and supervision, the regulation of the internal affairs of minister of the Republic of Indonesia number 113 of 2014, those who provide guidance and supervision are the provincial government and district / city government. The effectiveness of guidance and supervision by the provincial government and district /city government as an extension of the central government needs to be improved. For point d) the correlation values are y15 and y16 indicating medium strength. The concrete form of Village mid-term program plans is the Village Budget. The formulation is carried out together with elements of the village community. There needs to be guidance and supervision from higher institutions in the formulation of Village mid-term program plans, so that village development does not contradict regional and national development even though village law has extensive autonomy. For point e) the sectoral ego is created because the law opens up this opportunity. From the value of the VFA indicator there are no factors that cause sectoral ego. The sectoral ego of each village can be minimized by strong coordination in the field of development planning by the institutions above it. For point f) the local government formally has no power over the allocation of village funds basically the same as the position of the central government. Based on the PAC, the values of adverse selection, moral hazard and goal conflict are very strong, proving that informally there are conflicts in decision making, tendencies to act that are not appropriate and differences in objectives and interests in village fund allocation. To overcome this problem, VFA is carried out by direct control of the central and regional governments. Need changes in technical regulations.

4 CONCLUSION

a) PAR and VFA have been carried out well and are a resource, the motivation of the village community in developing and containing economic and political values b)

VFA reporting has been carried out properly by the agent and needs to be improved c) the use of VFA is used only for one or two purposes d) need to increase coaching and supervision by local governments, by issuing new regulations e) Need guidance and supervision from higher agencies in the formulation of village RPJM, so that village development does not contradict regional and national development even though village law has extensive autonomy f) The sectoral ego of each village can be minimized by strong coordination in the field of development planning by the agency above it. g) VFA is carried out by direct control of the central and regional governments. Need changes in technical regulations.

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