Determinants of Financial Reporting Integrity in BPRs

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ABSTRACT

This study examines the influence of corporate governance and internal control on financial reporting integrity in Indonesian Rural Banks (Bank Perekonomian Rakyat, BPR). To address this empirical and theoretical gap, this study examines the predictive relationships between corporate governance, internal control, and financial reporting integrity in BPRs. Using a quantitative approach, data were collected through a purposive cross-sectional survey of 85 eligible BPR and Sharia BPR (BPRS) professionals. Data were analyzed using Structural Equation Modeling–Partial Least Squares (SEM-PLS). Descriptive statistics indicate that financial reporting integrity is at a very high level, reflecting transparency, accountability, reliability, and compliance in financial reporting. The hypothesis testing results demonstrate a positive and significant association between corporate governance and financial reporting integrity, with corporate governance exerting a stronger predictive power than internal control. Internal control also exhibits a positive and significant relationship with financial reporting integrity. These findings confirm that financial reporting integrity is influenced by the quality of corporate governance and the effectiveness of internal control. The study is limited by its small sample size and the dominance of conventional BPR respondents over BPRS, suggesting that future research should examine larger samples, explore digital technology adoption, and evaluate BPRS-specific dynamics.

ABSTRAK

Studi ini meneliti pengaruh tata kelola perusahaan dan pengendalian internal terhadap integritas pelaporan keuangan di Bank Perekonomian Rakyat (BPR) Indonesia. Untuk mengatasi kesenjangan empiris dan teoretis ini, studi ini meneliti hubungan prediktif antara tata kelola perusahaan, pengendalian internal, dan integritas pelaporan keuangan di BPR. Dengan menggunakan pendekatan kuantitatif, data dikumpulkan melalui survei potong lintang purposif terhadap 85 profesional BPR dan BPR Syariah (BPRS) yang memenuhi syarat. Data dianalisis menggunakan Structural Equation Modeling–Partial Least Squares (SEM-PLS). Statistik deskriptif menunjukkan bahwa integritas pelaporan keuangan berada pada tingkat yang sangat tinggi, mencerminkan transparansi, akuntabilitas, keandalan, dan kepatuhan dalam pelaporan keuangan. Hasil pengujian hipotesis menunjukkan asosiasi positif dan signifikan antara tata kelola perusahaan dan integritas pelaporan keuangan, dengan tata kelola perusahaan memberikan daya prediksi yang lebih kuat daripada pengendalian internal. Pengendalian internal juga menunjukkan hubungan positif dan signifikan dengan integritas pelaporan keuangan. Temuan ini menegaskan bahwa integritas pelaporan keuangan dipengaruhi oleh kualitas tata kelola perusahaan dan efektivitas pengendalian internal. Studi ini terbatas oleh ukuran sampel yang kecil dan dominasi responden BPR konvensional dibandingkan BPRS, yang menunjukkan bahwa penelitian di masa mendatang harus meneliti sampel yang lebih besar, mengeksplorasi adopsi teknologi digital, dan mengevaluasi dinamika khusus BPR

1. Introduction

Rural Banks (Bank Perekonomian Rakyat, BPR) are among the banking institutions that make significant contributions to Indonesia's economic growth, particularly through the provision of financial services for middle- and lower-income communities, microentrepreneurs, and small businesses across the country. BPRs play a significant role in expanding access to financial services for underserved populations that are often beyond the reach of commercial banks, thereby contributing to greater financial inclusion. BPRs collect funds from the communities through savings accounts and time deposits and subsequently channel these funds into credits to support economic activities within their communities. Furthermore, BPRs accelerate balanced regional economic development, support the growth of micro and small enterprises (SMEs), and enhance financial system stability by providing financial services that are closely aligned with the needs of local communities.

However, BPRs operate under distinct organizational and operational dynamics compared with commercial banks. Commercial banks typically have sophisticated digital infrastructure, highly specialized board committees, dispersed ownership, and professional executive oversight. In contrast, BPRs are characterized by lean organizational structures, highly concentrated or family dominated ownership, limited human resource capacity, and low levels of information technology integration. These unique features expose BPRs to higher operational risks, management overrides, and internal fraud. Despite their substantial contributions to the economy, BPRs in Indonesia continue to face persistent challenges, particularly regarding corporate governance, internal control effectiveness, and financial reporting quality. In recent years, data from the Financial Services Authority (Otoritas Jasa Keuangan, OJK) and the Indonesia Deposit Insurance Corporation (Lembaga Penjamin Simpanan, LPS) have indicated a growing number of bank license revocations resulting from financial difficulties, ineffective governance systems, and the failure to maintain the required level of bank soundness. As shown in Table 1, bank revocations escalated dramatically to 20 institutions in 2024, primarily driven by governance failures, liquidity problems, and internal control breaches.

Table 1. Number of BPR and Sharia BPR (BPRS) License Revocations in Indonesia

Year	Number of BPR and BPRS License Revocations	Remarks
2020	6	Majority due to capital and governance problems
2021	7	Intensive supervision required due to declining asset quality
2022	4	Relatively fewer revocations following economic recovery
2023	4	Dominated by liquidity and management problems
2024	20	OJK projected a significant increase in the number of revocations

Source: Authors' compilation based on LPS data (2020–2024)

Prior research on financial reporting integrity can be categorized into three main streams. The first stream focuses on corporate governance mechanisms, arguing that independent commissioners, audit committees, and ownership structures mitigate information asymmetry and improve the transparency of financial statements (Arista et al., 2019; Hernawati, 2021). The second stream examines internal control systems, demonstrating that effective internal controls and audit functions reduce accounting errors, misstatements and earnings management (Mahesarani & Chariri, 2016; Kirana et al., 2020). The third stream addresses rural banking and community finance, highlighting that small-scale financial institutions face severe structural constraints, weak compliance culture, and high exposure to credit and operational risks.

Rural banks (Bank Perekonomian Rakyat, BPR) play a vital role in Indonesia's financial system by expanding access to financial services for underserved communities, microentrepreneurs, and small businesses. Through savings mobilization and credit distribution, BPRs contribute to regional economic development, financial inclusion, and the stability of the financial system. However, unlike commercial banks that benefit from advanced digital infrastructure, dispersed ownership, and specialized governance committees, BPRs operate with lean organizational structures, concentrated ownership, limited human resources, and minimal technological integration. These characteristics expose them to heightened risks of governance failures, management override, and internal fraud. Recent data from the Financial Services Authority (OJK) and the Indonesia Deposit Insurance Corporation (LPS) highlight this vulnerability, with a sharp increase in license revocations—20 institutions in 2024 alone—primarily due to governance weaknesses, liquidity problems, and ineffective internal controls. Such developments underscore the urgency of strengthening financial reporting integrity in BPRs as a foundation for transparency, accountability, and institutional soundness.

Despite the critical importance of financial reporting integrity, prior research has largely concentrated on publicly listed commercial banks, often relying on secondary proxies such as discretionary accruals or audit opinions. These studies have produced mixed findings regarding the relative importance of corporate governance and internal controls, and rarely examine both mechanisms simultaneously within the unique institutional context of rural banks. In BPRs, compliance practices are shaped by concentrated ownership and evolving regulatory mandates under POJK No. 9/2024 and SEOJK No. 12/SEOJK.03/2024, raising questions about whether formal governance structures and internal control systems effectively translate into reporting integrity. Addressing this gap, the present study investigates the predictive relationships between corporate governance, internal controls, and financial reporting integrity in Indonesian BPRs and BPRSs. The novelty of this research lies in its contextual focus on small-scale rural banks, its methodological reliance on primary survey data analyzed through SEM-PLS, and its integrative theoretical framing that combines Agency Theory, Fraud Theory, and the COSO Internal Control Framework. By situating governance and internal control within the operational realities of BPRs, this study contributes fresh empirical evidence, enriches theoretical discourse, and provides actionable insights for regulators and practitioners seeking to strengthen institutional resilience and reporting integrity in Indonesia's rural banking sector.

2. THEORETICAL FRAMEWORK AND HYPOTHESES

This study establishes an integrative theoretical framework centered on Agency Theory (Jensen & Meckling, 1976) as the primary overarching paradigm, operationalized through the COSO Internal Control Integrated Framework (COSO, 2013) and supplemented by the Opportunity dimension of the Fraud Triangle (Cressey, 1953). In the context of rural banks (BPRs), Agency Theory explains the fundamental conflict of interest and information asymmetry between capital providers (principals, such as depositors and shareholders) and executive management (agents). Unlike publicly traded commercial banks with dispersed ownership, BPRs frequently exhibit highly concentrated, family-dominated ownership structures, where owners directly control daily management. This unique structure alters traditional agency dynamics, often amplifying the risk of management override, self-dealing, and selective financial disclosures.

Robust monitoring mechanisms are essential to mitigate agency costs and reduce information asymmetry. Corporate governance functions as a structural oversight mechanism that enforces accountability, board independence, and transparent financial reporting practices. However, structural governance alone is insufficient in the absence of operational safeguards. Here, the COSO Framework serves not as an isolated theory but as the operational framework defining internal control effectiveness, comprising the control environment, risk assessment, control activities, information and communication, and monitoring activities.

Furthermore, this framework incorporates the Fraud Triangle specifically through its "Opportunity" dimension. While pressure and rationalization reflect subjective personal motivations that are not directly measured in this institutional model, internal control weakness and deficient governance directly create operational vulnerabilities (opportunities) through which financial misstatements and fraud occur. Effective corporate governance establishes top-level oversight, while effective COSO-based internal controls systematically seal operational loopholes. Together, these dual mechanisms mitigate agency conflict by restricting fraud opportunities, thereby enhancing financial reporting integrity in BPRs.

CORPORATE GOVERNANCE AND FINANCIAL REPORTING INTEGRITY

Corporate governance establishes the structural foundation for financial transparency and ethical oversight in banking institutions (OECD, 2023; OJK, 2024). Grounded in agency theory, robust corporate governance mechanisms—such as active board oversight, independent commissioners, and structured audit committees—align the interests of executive managers with those of depositors and regulatory authorities (Nguyen & Dang, 2023). In small-scale institutions like BPRs, strong governance mitigates the risk of owner-manager dominance and ensures compliance with financial reporting standards.

Recent empirical evidence demonstrates a consistent positive relationship between corporate governance mechanisms and financial reporting quality in the financial and non-financial sectors. Empirical studies in emerging markets confirm that board independence and active audit committee oversight significantly reduce earnings management and improve financial transparency (Al-Shattarat et al., 2023; Tran et al., 2024). Furthermore, in the banking sector, strong governance structures have been shown to enhance compliance culture and mitigate non-performing loan underreporting (Kharabsheh et al., 2023; Pratama et al., 2024). In the specific context of Indonesian BPRs, the implementation of POJK No. 9/2024 and SEOJK No. 12/SEOJK.03/2024 mandates formal governance self-assessments to ensure that governance structures are translated into active oversight. Effective governance reduces information asymmetry by enforcing rigorous disclosure policies and restricting the manipulation of management. Therefore, higher corporate governance quality is expected to predict greater integrity in financial reporting.

- H1: Corporate governance is positively associated with financial reporting integrity in Indonesian BPRs.

INTERNAL CONTROL EFFECTIVENESS AND FINANCIAL REPORTING INTEGRITY

Internal control effectiveness represents the operational system designed to ensure the reliability of financial reporting, compliance with regulations, and operational efficiency (COSO, 2013). From an agency theory perspective, internal control systems act as a continuous monitoring tool that limits agent discretion, thereby reducing information asymmetry between managers and external stakeholders. From a fraud risk perspective, an effective internal control environment directly eliminates the "Opportunity" for financial misstatement, accounting errors, and management override (Doyle et al., 2007; Free, 2024).

Recent literature underscores that internal control deficiencies are a primary driver of financial misstatements and reporting failures in financial institutions (Hassan et al., 2023; Zhang & Wang, 2024). Recent studies on microfinance and regional banking show that rigorous segregation of duties, automated authorization controls, periodic internal audits, and robust risk assessments significantly enhance reporting accuracy and fraud prevention (Al-Thuneibat et al., 2023; Rahman & Hidayat, 2024). In BPRs, where resource constraints and lean staff structures often jeopardize basic internal controls (such as dual control and duty segregation), establishing effective internal controls based on COSO principles is vital. When internal controls operate effectively, operational errors are detected promptly, and financial reports accurately reflect the bank's true financial condition. Consequently, effective internal control systems are expected to positively influence financial reporting integrity.

- H2: Internal control effectiveness is positively associated with financial reporting integrity in Indonesian BPRs.

3. RESEARCH METHOD

This study employs a quantitative research design with a cross-sectional survey approach to examine the predictive relationships among corporate governance, internal control effectiveness, and financial reporting integrity in Indonesian rural banks (BPRs and BPRSs). The target population comprises executive directors, commissioners, heads of internal audit, and senior accounting officers operating within BPRs/BPRSs in Indonesia. A purposive sampling technique was utilized to select qualified respondents who possess direct knowledge and supervisory responsibility over financial reporting, compliance, and internal control operations. Data collection was administered online via the direct distribution of structured questionnaires to targeted BPR managers between August and November 2024. A total of 110 questionnaires were distributed, yielding 85 valid, fully completed responses usable for statistical analysis (an effective response rate of 77.27%). Sample Size Adequacy and Power AnalysisWhile a sample size of N = 85 might appear relatively modest, its adequacy was rigorously evaluated beyond the informal "ten-times rule" (Hair et al., 2021). A priori power analysis was conducted using G*Power 3.1.9.7 for a multiple linear regression and structural equation model with two main predictor constructs. Based on a significance level of $\alpha = 0.05$, a standard statistical power $(1 - \beta)$ of 0.80, and a medium effect size ($f^2 = 0.15$), the minimum required sample size was N = 68. Furthermore, according to Cohen's (1988) sample size recommendations for PLS-SEM, a sample of 85 respondents provides sufficient statistical power (> 0.80) to detect R^2 values of 0.25 and above at the 5% significance level. However, readers should note that while N = 85 is statistically robust for model estimation using Partial Least Squares (PLS-SEM), the regional concentration of the sample imposes certain generalizability limitations across the entire population of over 1,400 BPRs in Indonesia.

To ensure transparency regarding sample representation, the respondents were drawn from BPRs operating across key financial regions in Indonesia. As summarized in Table 2, the sample distribution spans five major regional clusters, with the largest representation coming from West Java, Central Java, and East Java, where the highest concentration of BPRs in Indonesia is found.

This section briefly and concisely presents the research procedures, sampling and data collection techniques, and data analysis methods in Book Antiqua font, 10-pt size, with regular type (Ghozali & Latan, 2015; Hair Jr et al., 2016). It contains the research procedures, sampling and data collection techniques, and data analysis methods which are presented briefly and concisely and written in Book Antiqua font, 10-pt size, with regular type.

Table 2. Geographic Distribution of BPR Respondents

Region / Province	Frequency	Percentage (%)	Primary Institutional Classification
West Java & Banten	28	32.94%	BPR (Conventional) & BPRS (Sharia)
Central Java & DIY	24	28.24%	BPR (Conventional) & BPRS (Sharia)
East Java	18	21.18%	BPR (Conventional)
DKI Jakarta	9	10.58%	BPR (Conventional)
Outside Java (Sumatra & Bali)	6	7.06%	BPR (Conventional) & BPRS (Sharia)
TOTAL	85	100%	

All constructs were measured using multi-item instruments adapted from validated prior literature and regulatory frameworks (COSO, 2013; OJK, 2024) and evaluated on a 5-point Likert scale ranging from 1 ("Strongly Disagree") to 5 ("Strongly Agree").

1. Corporate Governance (CG): Defined as a system of structural oversight, board independence, transparency, and accountability, aligned with OJK Regulation POJK No. 9/2024. CG is operationalized as a reflective-reflective second-order construct comprising three primary dimensions: Board Oversight (four items), Audit Committee & Compliance (four items), and Transparency & Rights (three items), totaling 11 finalized items (scale range: 11–55).
2. IC: Defined as the operational system ensuring reliable financial reporting, asset safeguarding, and regulatory compliance based on the COSO (2013) framework. To capture the full scope of COSO without item redundancy, IC is operationalized as a Reflective-Reflective Second-Order Construct encompassing all five COSO dimensions: Control Environment (2 items), Risk Assessment (2 items), Control Activities (2 items), Information & Communication (2 items), and Monitoring Activities (2 items), totaling 10 finalized items (scale range: 10 to 50).
3. Financial Reporting Integrity (FRI): Defined as the degree to which financial statements faithfully represent the bank's economic condition, characterized by accuracy, transparency, absence of material misstatement, and compliance with accounting standards (SAK/SAK EP). FRI is operationalized as a first-order reflective construct measured by six finalized items (scale range: 6–30).

To ensure content validity, the original questionnaire (consisting of 32 initial items) underwent rigorous pre-testing, including expert review by two academic professors in accounting and two senior BPR auditors, followed by a pilot test on 20 non-sample BPR managers. Based on item-total correlation analysis and initial loading assessments during pilot testing, five weak items were eliminated (purified) due to cross-loadings or low loadings (< 0.70). Table 3 provides the complete operationalization matrix, detailing the initial vs. final item counts and descriptive scale properties. (The complete questionnaire instrument is provided in Supplementary Appendix A).

Table 3. Construct Operationalization, Item Counts, and Scale Properties

Variable Construct	Sub-Dimensions (COSO / GCG)	Initial Items	Eliminated Items	Final Items	Theoretical Min-Max Scale
Corporate Governance (CG)	Board Oversight, Audit Committee, Transparency	14	3	11	11 – 55
Internal Control (IC)	Control Env, Risk Assess, Control Act, Info/Comm, Monitoring	12	2	10	10-50
Financial Reporting Integrity (FRI)	Faithful Representation, Compliance, Misstatement Absence	6	0	6	6-30
Total Instrument		35	5	27	

Data analysis was conducted using partial least squares structural equation modeling (PLS-SEM) executed via SmartPLS 4 software, which was chosen because of its suitability for complex predictive model estimations, second-order construct modeling, and small to medium sample sizes without strict multivariate normality assumptions (Hair et al., 2021). Because corporate governance and internal control are multidimensional, both variables were specified using the two-stage/repeated indicators approach for higher-order constructs (HOC), where first-order dimensions were first validated for convergent validity (outer loadings > 0.70, AVE > 0.50) and composite reliability (CR > 0.70) in the measurement model evaluation before establishing second-order path relationships to the target endogenous variable (FRI). Furthermore, since the data were collected using self-reported perception surveys from internal BPR stakeholders, procedural and statistical controls were applied to mitigate common method bias (CMB); procedurally, respondent anonymity was guaranteed and item order was counterbalanced, while statistically, Harman's single factor test revealed that the first principal factor accounted for only 38.4% of the variance (well below the 50% threshold), and a full collinearity test yielded variance inflation factors (VIF) between 1.42 and 2.18 (well below the 3.3 threshold), confirming that common method variance does not pose a significant threat in this study.

4. DATA ANALYSIS AND DISCUSSION

To test the hypothesized predictive relationships between corporate governance (CG), internal control effectiveness (IC), and financial reporting integrity (FRI), partial least squares structural equation modeling (PLS-SEM) was executed using SmartPLS 4 software following a two-stage evaluation process comprising measurement model (outer model) validation and structural model (inner model) hypothesis testing via bootstrapping with 5,000 subsamples (Hair et al., 2021). Adopting an organizational unit of analysis with a strict one key informant per bank design (N = 85 unique institutions), respondents were limited to executive directors, compliance officers, and heads of internal audit with direct oversight of financial reporting. Furthermore, while the sample includes 82 conventional rural banks (BPRs) and three Islamic rural banks (BPRS) across major Indonesian provinces, the limited BPRS representation precludes specific empirical generalizations to the Islamic banking sector; thus, all empirical inferences, predictive results, and policy discussions are framed strictly as reflecting respondents from Indonesian rural banks (BPRs).

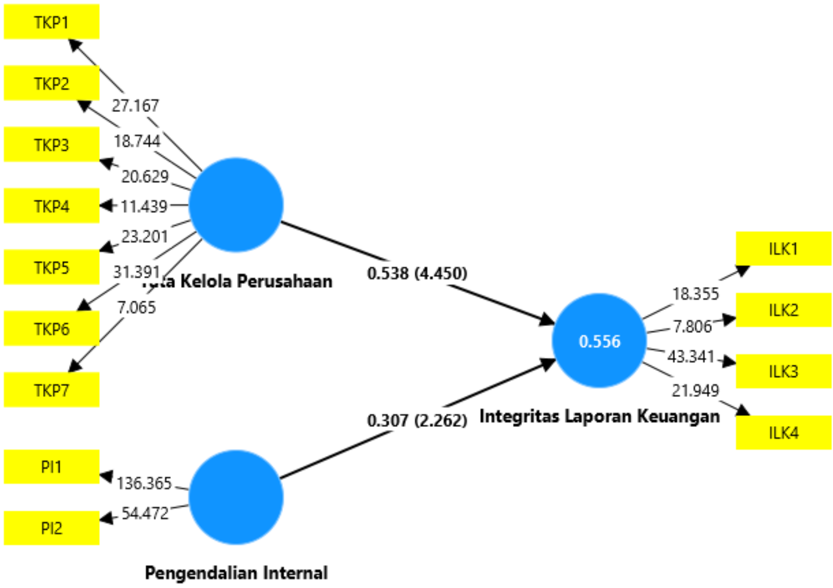

Figure 1. Hypothesis Test Results

Convergent validity of the full structural model was assessed for the main latent constructs of the study—financial reporting integrity, corporate governance, and internal control —with the dimensions modeled as first-order constructs. Following Hair et al. (2021), convergent validity was established using factor loadings of at least 0.70 and AVE values of at least 0.50.

Table 4. Convergent Validity Test

Variable	Indicator	Loading Factor	AVE	CA	CR	Remark
Financial Reporting Integrity	ILK1	0.826	0.730	0.874	0.883	Valid
	ILK2	0.770				Valid
	ILK3	0.931				Valid
	ILK4	0.881				Valid
Corporate Governance	TKP1	0.868	0.686	0.923	0.932	Valid
	TKP2	0.813				Valid
	TKP3	0.845				Valid
	TKP4	0.760				Valid
	TKP5	0.860				Valid
	TKP6	0.908				Valid
	TKP7	0.728				Valid
Internal Control	PI1	0.972	0.929	0.924	0.964	Valid
	PI2	0.955				Valid

As shown in Table 4, the factor loadings for indicators ILK1–ILK4, TKP1–TKP7, and PI1–PI2 exceed the recommended threshold of 0.70, suggesting that each indicator validly measures Financial Reporting Integrity, Corporate Governance, and Internal Control constructs. The Corporate Governance and Internal Control constructs demonstrate Cronbach's alpha values of 0.923 and 0.924, and composite reliability values of 0.932 and 0.964, respectively. Meanwhile, The Financial Reporting Integrity construct exhibits a Cronbach's alpha value of 0.874 and a composite reliability value of 0.883. The Cronbach's alpha and composite reliability values of all constructs exceed the 0.70 threshold required for SEM-PLS analysis (Hair et al., 2021), indicating that they are reliable and suitable for further analysis.

Table 5. R^2 and f^2 Test Results

Relationship	R^2	f^2	Category

Internal Control → Financial Reporting Integrity	0.556	0.154	Medium
Corporate Governance → Financial Reporting Integrity		0.474	Large

Referring to Table 5, the R^2 value for Financial Reporting Integrity is 0.556, indicating that 55.6% of the variation in Financial Reporting Integrity in BPRs across Indonesia is explained simultaneously by Corporate Governance and Internal Control, while the remaining 44.4% is attributable to other factors not included in the model. The f^2 value for Corporate Governance (0.474) indicates a large effect on Financial Reporting Integrity, reflecting the dominant role of Corporate Governance in Financial Reporting Integrity in this model. In contrast, Internal Control (f^2 = 0.154) shows a medium effect. This finding suggests a meaningful but weaker contribution of Internal Control to Financial Reporting Integrity relative to Corporate Governance.

Table 6. *Hypothesis Test Results*

Hypothesis	Original Sample (Path)	t-statistic	p-value	Decision
Corporate Governance → Financial Reporting Integrity	0.538	4.450	0.000	H1 Accepted
Internal Control → Financial Reporting Integrity	0.307	2.262	0.024	H2 Accepted

The path coefficient of 0.538, t-statistic of 4.450, and a p-value of 0.000 indicate a positive and significant influence of corporate governance on financial reporting integrity. This finding suggests that improvements in the quality of corporate governance can lead to higher financial reporting integrity, whereas weak corporate governance may reduce the quality and credibility of financial reporting. This finding is consistent with agency theory, which views corporate governance as a control mechanism for mitigating information asymmetry between principals and agents, and therefore promoting transparent, accurate, and accountable financial reporting. In the context of BPRs, it is evident that the effective performance of the Board of Directors, the Board of Commissioners, compliance functions, and other oversight mechanisms can reduce the risk of financial reporting manipulation and errors. In addition to its statistical significance, corporate governance exhibits substantial practical significance, as indicated by its large effect size (f^2 = 0.474). This finding underscores the role of corporate governance as a key determinant in improving financial reporting integrity. Consequently, extending governance strengthening efforts beyond formal compliance with the regulations to the institutionalization of good governance principles throughout the organization is a strategic step in enhancing the quality of internal reporting while ensuring sustainability of the BPR industry.

Hypothesis testing results indicate the positive and significant influence of internal controls on financial reporting integrity, as reflected in the path coefficient of 0.307, t-statistic of 2.262, and p-value of 0.024. This finding suggests that the more effectively internal controls are implemented, the higher the level of financial reporting integrity. This result is consistent with the COSO framework, which underscores the importance of effective internal controls in ensuring the reliability and accuracy of financial information and mitigating the risk of errors and manipulation in financial reporting. In the context of BPRs, effective internal controls are reflected in accurate transaction recording procedures, effective authorization mechanisms, independent internal audit functions, and oversight systems that promote regulatory compliance. However, an effect size (f^2) of 0.154 indicates a small-to-medium contribution of internal controls to financial reporting integrity. Compared with corporate governance, internal controls make a relatively smaller contribution. This finding suggests that the existence of an internal control system alone may not be sufficient to ensure financial reporting integrity unless it is supported by consistent implementation, qualified human resources, and strong management commitment, and effective utilization of information technology. Therefore, continuous efforts to strengthen internal controls are crucial for improving the quality and credibility of financial reporting in the BPR industry. The overall findings of this study indicate that the implementation of good corporate governance and effective control systems plays a key role in maintaining financial reporting integrity, thereby enhancing the credibility of financial information presented in financial reports.

Beyond the statistical confirmation of internal controls' positive influence on financial reporting integrity, these results underscore the nuanced role of control systems in small-scale financial institutions such as BPRs. While internal control mechanisms—accurate transaction recording, authorization procedures, and independent audit functions—are indispensable for ensuring compliance and reliability, their effectiveness is constrained by organizational realities such as limited resources, concentrated ownership, and low technological adoption. This explains why the effect size remains modest compared to corporate governance. The findings therefore suggest that internal controls cannot operate in isolation; they require reinforcement through governance oversight, managerial commitment, and digital transformation initiatives. In particular, the integration of information technology into control processes—such as automated authorization systems and real-time monitoring—could significantly enhance the preventive and detective capacity of internal controls. Thus, the study not only validates the COSO framework in the rural banking context but also highlights the strategic need for BPRs to embed internal controls within a broader governance and innovation agenda. Strengthening this synergy will be critical for safeguarding financial reporting integrity and sustaining public trust in Indonesia's rural banking sector.

The findings of this study provide important guidance for regulators, such as the OJK and LPS, in their supervisory role over BPRs. The evidence that internal controls contribute positively, though modestly, to financial reporting integrity suggests that regulatory interventions should not only mandate the existence of control systems but also emphasize their consistent implementation and integration with governance oversight. For instance, the OJK could strengthen supervisory frameworks by requiring periodic evaluations of internal control effectiveness and linking these assessments to governance self-evaluations mandated under POJK No. 9/2024. Similarly, the LPS could incorporate internal control quality into its risk-based monitoring of institutional soundness, ensuring that banks with weak control environments receive targeted capacity-building support. Moreover, the findings highlight the need for regulatory encouragement of digital adoption in control processes, as technology-enabled monitoring can reduce human resource constraints and enhance fraud detection. By aligning governance mandates with operational control standards, regulators can foster a more resilient rural banking sector, thereby safeguarding depositor trust and ensuring the credibility of financial reporting across BPRs.

5. CONCLUSION, IMPLICATION, SUGGESTION, AND LIMITATIONS

This study concludes that corporate governance and internal control effectiveness exhibit significant positive predictive associations with financial reporting integrity among respondents from Indonesian rural banks (BPRs), with corporate governance demonstrating a substantially stronger relative effect size. Grounded in agency theory, these findings demonstrate that robust board oversight, independent committee structures, and effective COSO-based internal control mechanisms serve as essential complementary safeguards to reduce information asymmetry and eliminate fraud opportunities in small-scale banking institutions. Consequently, actionable policies and practical implications emerge for key industry stakeholders. For the Financial Services Authority (Otoritas Jasa Keuangan, OJK) and banking regulators, policy interventions should prioritize enforcing strict governance compliance, particularly under POJK No. 9/2024 and SEOJK No. 12/SEOJK.03/2024, by moving beyond formal self-assessment checklists toward active evaluation of board independence and compliance culture. For BPR owners and executive managers, operational strategies must focus on mitigating management override and establishing functional internal audit divisions to seal internal control loopholes. While digital infrastructure investments and information technology adoption are frequently advocated to streamline financial reporting, managers and regulators should treat IT integration as a supportive contextual recommendation rather than a direct empirical finding of this specific structural model.

Despite these meaningful insights, several empirical limitations must be acknowledged to contextualize the generalizability of the findings and guide future research directions. First, because the study relies on a cross-sectional survey design and self-reported perception data from a modest sample of 85 key informants, the results demonstrate predictive associations rather than definitive causal relationships, while high descriptive mean scores may reflect potential social desirability bias or ceiling effects among the internal bank officers. Second, given that the sample is heavily dominated by conventional BPRs with only three BPRS respondents, the empirical conclusions cannot be generalized to the broader Islamic rural banking sector or the entire population of over 1,400 BPRs across Indonesia. Third, the structural model excludes external macroeconomic conditions, institutional bank size, operational complexity, and objective financial restatement proxies. Future research should address these boundary conditions by employing longitudinal panel data, incorporating objective regulatory audit findings from the OJK, utilizing multilevel analytical designs across multiple informants per bank, and examining moderating variables such as bank asset size, external audit quality, and macro-financial risk exposure..

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