

**ISLAMIC VILLAGE FINANCIAL
MANAGEMENT IN LOBUK VILLAGE,
EAST JAVA PROVINCE, INDONESIA**

ACHDIAR REDY SETIAWAN

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**ISLAMIC VILLAGE FINANCIAL MANAGEMENT
IN LOBUK VILLAGE, EAST JAVA PROVINCE,
INDONESIA**

by

ACHDIAR REDY SETIAWAN

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Achdiar Redy Setiawan
Centre for Islamic Development Management Studies (ISDEV)
Universiti Sains Malaysia.

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LIST OF ABBREVIATIONS

VFM	Village Financial Management
<i>BPD</i>	<i>Badan Permusyawaratan Desa</i> (Village Consultative Body)
<i>APBDesa</i>	<i>Anggaran Pendapatan & Belanja Desa</i> (Village Income & Revenue Budget)
<i>APBN</i>	<i>Anggaran Pendapatan & Belanja Negara</i> (State Income & Revenue Budget)
<i>RPJMDesa</i>	<i>Rencana Pembangunan Jangka Menengah Desa</i> (Village Medium Term Development Plan)
<i>RKPDesa</i>	<i>Rencana Kerja Pemerintah Desa</i> (Village Government Work Plan)
<i>PADesa</i>	<i>Pendapatan Asli Desa</i> (Original Village Income)
<i>BUMDes</i>	<i>Badan Usaha Milik Desa</i> (Village-Owned Enterprises)
<i>RW</i>	<i>Rukun Warga</i> (Group of Neighborhood Associations)
<i>RT</i>	<i>Rukun Tetangga</i> (Neighborhood Association)
GCG	Good Corporate Governance

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**PENGURUSAN KEWANGAN DESA ISLAM DI KAMPUNG LOBUK,
PROVINSI JAWA TIMUR, INDONESIA**

ABSTRAK

Undang-undang No. 6 Tahun 2014 tentang Desa merupakan tonggak penting bagi pemerintahan desa (kerajaan kampung) di Indonesia. Desa diberi kuasa besar untuk mengatur pembangunan kampung secara autonomi, disertai dengan mandat untuk melaksanakan Pengurusan Kewangan Desa (PKD). Bagaimanapun, jumlah dana yang besar yang diuruskan menimbulkan pelbagai masalah terutamanya penyalahgunaan kuasa yang berleluasa dalam melaksanakan PKD. Penyelidikan ini cuba mencari penyelesaian kepada pelbagai masalah berkaitan PKD di Indonesia dengan merumuskan tiga objektif. Pertama, mengenal pasti tadbir urus PKD Islam. Kedua, menganalisis pelaksanaan PKD Islam di sebuah kampung bernama Lobuk. Ketiga, untuk mengkonseptualisasikan kerangka asas PKD Islam untuk Indonesia berdasarkan hasil PKD Islam di Desa Lobuk. Kajian ini menggunakan pendekatan kualitatif untuk menjawab persoalan yang dikemukakan dalam kerangka antropologi Islam. Data kajian dikumpul melalui beberapa kaedah antaranya pemerhatian, temu bual dan dokumentasi. Analisis Tematik dan Analisis Etnometodologi digunakan sebagai kaedah analisis data dalam kajian ini. Hasil kajian terhadap pelaksanaan PKD di Kerajaan Kampung (Lobuk sebagai lokasi kajian) mendapati bahawa tiga prinsip dan tujuh elemen PKD Islam boleh menjadi nilai rujukan bagi semua kerajaan kampung di Indonesia dalam melaksanakan PKD yang baik. Kajian ini menyediakan model yang merujuk kepada imej masjid sebagai metafora. Bangunan masjid mempunyai tiga bahagian penting: a) asas, b) tiang penyangga, dan c) bumbung. Dalam konteks Perspektif PKD Islam di Indonesia, Prinsip Tauhid dan tiga elemennya (Kepercayaan, Kejujuran, dan Kebertanggungjawaban) merupakan asas yang

membentuk sokongan kuat terhadap bangunan tersebut. Selain itu, dua tonggak penting yang memastikan pembinaan masjid tegak ialah Prinsip Keadilan (dengan dua elemennya: Ketelusan dan Peraturan Jelas, Adil & "Sihat") dan Prinsip Syura (dengan dua elemennya: Penyertaan Substantif dan Amal Jama'i atau Kerjasama-Kebersamaan). Keseluruhan bangunan masjid memuncak atau mengalir ke satu matlamat tertinggi (dilambangkan dengan bumbung masjid), iaitu *Mardhatillah* atau keredhaan Allah SWT. Kesimpulan penyelidikan ini menyediakan asas saintifik yang mencukupi untuk menyusun semula tadbir urus PKD merujuk kepada nilai Islam, yang harus dicontohi untuk menangani masalah asas yang berterusan dalam konteks PKD di Indonesia.

**ISLAMIC VILLAGE FINANCIAL MANAGEMENT IN LOBUK VILLAGE,
EAST JAVA PROVINCE, INDONESIA**

ABSTRACT

Law No. 6 of 2014 concerning Villages is a substantial pillar for village government in Indonesia. Villages are granted significant autonomy to independently organize village development, accompanied by a mandate to implement Village Financial Management (VFM). However, the large amount of funds managed causes various problems, especially the widespread abuse of power in implementing VFM. This research attempts to find solutions to various problems related to VFM in Indonesia by formulating three objectives. First, to identify the Islamic VFM governance. Second, to analyze the implementation of Islamic VFM in a village called Lobuk. Third, to conceptualize a fundamental framework of Islamic VFM for Indonesia based on the results of Islamic VFM in Lobuk Village. This study employs a qualitative approach to address the questions raised within the framework of Islamic anthropology design. The research data was collected through several methods, including observation, interviews, and documentation. Thematic Analysis and Ethnomethodological Analysis are used as data and information analysis methods in this study. The study on the Islamic VFM implementation in Village Government (Lobuk as the study location) found that the three principles and seven elements of Islamic VFM can be a reference value for all village governments in Indonesia in implementing good VFM. This study presents a model that draws on the image of the mosque as a metaphor. The mosque building has three essential parts: a) the foundation, b) the supporting pillars, and c) the roof. In the context of the Islamic VFM in Indonesia, the Principle of Tawhid and its three elements (Trustworthiness, Honesty, and Accountability) are the foundations that form a strong support for the building. In

addition, two important pillars that keep the mosque building upright are the Principle of Justice (with its two elements: Transparency and Clear, Fair & "Healthy" Regulation) and the Principle of Shura (with its two elements: Substantive Participation and *Amal Jama'i* or Cooperation-Togetherness). The entire mosque building culminates in or flows into one highest goal (symbolized by the mosque's roof), namely *Mardhatillah*, or the pleasure of Allah SWT. The conclusions of this research provide a sufficient scientific basis for restructuring VFM governance based on Islamic values, which should be emulated to address the underlying problems that persist in the Indonesian VFM context.

CHAPTER 1

INTRODUCTION

1.1 Introduction

The general objective of this research is to gain an in-depth understanding of the implementation of village financial management (VFM) ¹, in Indonesia, grounded in Islamic Governance. The specific objective of the study is to identify and conceptualize the Islamic VFM governance for Indonesia. VFM is implemented as a consequence of the enactment of Law Number 6 of 2014 concerning Villages. The development process in Indonesia has undergone significant changes since the implementation of decentralization of government authority. It is no longer entirely centralized in the central government. Still, some are delegated to the level of government in the regions, starting from the province, city/regency (*kota/kabupaten*), sub-district (*kecamatan*), and village (*desa*) level.

This chapter also examines the historical context of the enactment of Law No. 6 of 2014 and its connection to the emergence of several cases of misuse or fraudulent financial management activities that accompanied the implementation of this regulation. This chapter outlines the background, problem statement, research objectives, research question, operational definition, scope and limitations of the research, as well as its research contribution and thesis organization. This initial discussion provides a comprehensive overview of related issues regarding VFM in Indonesia.

¹ Village Financial Management (VFM) in this study is defined as a mechanism, system, pattern and procedure for managing financial resources implemented by the Village Government. VFM must be implemented as a consequence of the implementation of several government authorities to the village government based on Law Number 6 of 2014 concerning Villages. All matters regarding VFM are specifically regulated in the Regulation of the Minister of Home Affairs Number 20 of 2018 concerning Village Financial Management and several other related regulations.

1.2 Background of the Research

This section consists of two significant parts. First, it begins with a discussion regarding the concepts of village development management at the global level. Next, the debate centered on VFM, one of the key components of village development management. In the second part, the topic will focus on the concept of village development in Indonesia. Then, it is followed by the implementation of VFM in Indonesia. This section provides a comprehensive explanation of the research position within the context of numerous studies conducted.

1.2.1 Village Development Management at The Global Level

Various countries are taking a serious approach to developing a village management system as an integral part of their respective countries' economic and social development. The Organisation for Economic Co-Operation and Development (OECD) (2006a) concluded that the rural development paradigm has undergone a significant shift. Each country of OECD members has developed village governance in line with the latest era. Table 1.1 indicates village development policies and governance as reported by the OECD:

Table 1. 1 Paradigm Shifting of Rural Development Governance and Policies

	Old Approach	New Approach
<u>Objectives</u>	farm competitiveness; farm income; equalization,	rural area's competitiveness; local assets' valorization; unused resources exploitation
<u>Key target sector</u>	agriculture	rural economic sectors (e.g., ICT industry, manufacturing, tourism, etc.)
<u>Primary tools</u>	subsidies	investments
<u>Key actors</u>	farmers, national governments	all government levels (local, regional, national & supra-national); all local stakeholders (NGOs, private & public NGOs)

Source: Organisation for Economic Cooperation and Development (OECD), (2006a)

Based on Table 1.1, it is evident that the current rural development paradigm is grounded in the reality of recent changes in the village. For instance, the agricultural sector, which has traditionally been the first to develop in rural areas, has diversified into other sectors, including rural tourism, Information and Communication Technology (ICT), and manufacturing. In line with this fact, from the evidence of his research site (Poland), da Silva, Figueiredo, Eusébio, & Carneiro (2016) justify that the rural area, although still often identified with agriculture, is no longer a productive agricultural unit. Agriculture seems increasingly portrayed as marginal or abandoned, being replaced (in the minds of most respondents) with other tourism and leisure activities.

This phenomenon has shifted farmers from being the sole principal agent driving the village's economy to being one of several interconnected stakeholders, alongside the public, private, and NGO (Non-Governmental Organizations). The dynamic changes in the villages also make the central government's control range too broad to address various village problems effectively. Issues in the village can only be solved through effective cooperation among all levels of government (supra-national, national, regional, and local). Therefore, rural development aims to enhance rural competitiveness, capitalize on local assets, and optimize the utilization of underutilized resources.

Furthermore, the Organisation for Economic Cooperation and Development (OECD) (2006b) explains some factors that characterize these new approaches. First, a development strategy that encompasses various factors, including infrastructure and the availability of a suitable workforce, impacts local entity performance. Second, there is a greater focus on local assets and knowledge and less investment in transfers outside the village area. Finally, there is a collective/negotiated governance approach

to such matters, involving national, regional, and local governments, as well as other stakeholders, in which the central government plays a less dominant role.

Additionally, the "new rural paradigm" necessitates considerable changes in how policies are conceived and implemented (Organisation for Economic Cooperation and Development (OECD), 2006b). Traditional hierarchical administrative structures are likely to be adjusted at both the central and local government levels. One of the substantial primary issues is reallocating resources to integrated rural policy among those hierarchical government structures (Organisation for Economic Cooperation and Development (OECD), 2006b).

Regarding rural development, China's experience is also essential to be seen as one of the countries with the most significant economic power in the world today. As the most populous country globally (and its population also resides primarily in rural areas), the Chinese government developed the concept of village development for poverty alleviation, which mainly accumulates in rural areas (Guo, Zhou, & Liu, 2019). Based on a case study of Fuping County, Guo et al (2019) found that poverty in Fuping has been significantly alleviated, and the goal of poverty elimination will be achieved as scheduled by combining poverty alleviation efforts with economic development initiatives by the government to stimulate the local economy. The targeted measures mainly involved industrial development, resettlement assistance, education security, health safeguards, land consolidation, and financial growth.

Li, Fan, & Liu (2019) revealed that the successful factor of transformational development of relatively successful villages in China is based on the integration and coordination of internal and external driving forces, the participation, negotiation, and Cooperation among key actors, and the formation and development of rural networks with these critical actors. The bearing model comprises actors, interactions, and

processes that can be theorized as a conceptual framework for rural development. The relationship between the government and the community, the government and markets, guidance and intervention, and authority and grassroots is needed. Li et al. (2019) finally stated that grassroots participation is the core concept and fundamental principle that should be adhered to during village development.

Moreover, Long, Tu, Ge, Li, & Liu (2016) analyzed current issues of allocating and managing critical resources (including human resources, land resources, and capital) in rural China since the turn of the new millennium. There is a need to restructure the rural development space, encompassing industry, social organizations, and management, to enhance resource utilization efficiency and fully understand the impacts of globalization on rural restructuring in China.

After outlining the concept and practice of village development management in various countries (such as China and OECD countries), the following subpart discusses one of the critical elements of village development: village financial management. Finally, experiences in different countries related to VFM will be exposed to provide an overview of applicable praxis.

1.2.2 Village Financial Management in Various Countries

One of the critical aspects of village development management is the allocation of financial resources. In this context, a significant challenge for the central government is providing a fair allocation of financial resources across village governments. At this point, the regulation of VFM is also related to determining financial resource allocation policies, which can be a driver of quality development in the village.

As discussed earlier, investment mechanisms are the primary tool for driving the village economy in the new paradigm (Organisation for Economic Cooperation

and Development (OECD), 2006b). Villages must be more independent in utilizing resources to finance all village development needs. Financial dependence on the central government through the subsidy mechanism has been deemed obsolete and is expected to be abandoned.

Even though it sounds ideal, in this context, it is a long journey for villages across the country to achieve financial independence in managing their own affairs. For instance, when considering investments in rural areas, it is essential to recognize that the nature and function of public goods that underpin economic activity and human welfare in rural areas often differ significantly from those in urban areas (Bryden, 2007). Additionally, the diverse nature and types of resources in villages pose a significant challenge to generating income to finance village development. Bryden (2007) also pointed out that, at the same time, another challenge lies in global changes in society impacting rural people and places, as well as structures of government and governance processes (central, provincial, and district/local government).

OECD member countries (most of which are categorized as developed countries²) have initiated the development of more independent villages based on existing resources and have tried to be more creative in managing their finances. OECD member countries (most of which are categorized as developed countries) (Organisation for Economic Cooperation and Development (OECD), 2006b). As a result, rural futures in many developed economies consist of decentralized bio-economy, colonial countryside, museum countryside, and rural business (Kuhmonen & Kuhmonen, 2015).

² Based on the latest information in www.oecd.org (accessed 20/03/2023), 36 OECD member countries span the globe, from North and South America to Europe and Asia-Pacific. Some are the USA, Kanada, Australia, UK, EU countries (Italy, France, Spain, Germany, Denmark, etc), Japan, Korea, and Turkey. The OECD also works closely with some of the world's largest economies: China, India, Indonesia, Brazil, and South Africa, who are OECD Key Partners.

Rural business is one of the most exciting topics studied by many researchers. One concept primarily driven in financial management is encouraging villages to become entrepreneurs, known as village social enterprises³. Many rural challenges and needs could be transformed into opportunities for social enterprise development (Steiner & Teasdale, 2019). Additionally, social enterprises can facilitate an integrated approach to addressing local issues at the village level, providing locally responsive services that align with the local context (Steiner & Teasdale, 2019).

Based on his case study on two rural areas in Poland and Austria, Richter (2019) reveals that rural social enterprises could connect rural communities with supra-regional networks and mobilize resources. At the same time, rural social enterprises are widely embedded in rural regions, allowing them to develop innovative solutions to communities' needs and find local support for implementing innovative solutions (Richter, 2019).

The rapid development of the ICT industry encourages villages to direct their economic movements toward digitalization. Lundgren & Johansson (2017) use the term "digital rurality" to redefine and promote Swedish rural areas in light of perceived threats, including budget cuts, unemployment, environmental damage, contested rural policy, and urban norms. Salemink, Strijker, & Bosworth (2017) highlight, through a systematic literature review, that digital connectivity and inclusion are becoming increasingly significant in the digital age, even as 'offline' social and economic developments continue to influence rural development.

The sustainability aspect of village development is also an essential subject closely related to the financial management of rural areas. Koopmans, Rogge,

³ Sarkar & Sinha (2015) use the term "village as a social entrepreneur," Deller, Kures, & Conroy (2019) use "rural entrepreneur," and Lang & Fink (2019) use "rural social entrepreneurship."

Mettepenningen, Knickel, & Šūmane (2018) revealed the development of new governance approaches that display the traits of increased vertical and horizontal coordination to support the shift towards multi-actor governance in rural areas (Bjärstig & Sandström, 2017). A Public-Private Partnership (PPP) is a promising mechanism for achieving sustainability. PPPs can be defined as 'collaborative arrangements in which actors from two or more spheres of society (state, market, and or civil) are involved in a non-hierarchical process, and through which these actors strive for a sustainability goal (Van Huijstee, Francken, & Leroy, 2007). In this context, partnerships between businesses, societal organizations, and/or governments are typically at the village level, particularly in support of independent and empowered villages.

The concept of rural development in developed countries, as applied in OECD member countries (which have entered a new paradigm), may differ from the experiences of developing countries. For example, the government subsidy mechanism remains the primary tool in financial management. For instance, Thailand's government released the Thailand Village and Urban Community Fund (VF) program. The purpose of this program is to provide a million baht (approximately RM 105,750 or USD 22,500) to 74,000 villages and over 4500 urban communities as working capital for locally run rotating credit associations (Boonperm, Haughton, & Khandker, 2013). The total fund reached 78 billion baht (approximately RM 8.25 billion or USD 1.75 billion) or 1.4% of 2002 GDP. The program experienced rapid improvements in a relatively short time. By the end of May 2005, the VF committees had lent or re-lent a total of 259 billion baht (approximately RM 30 billion or USD 6.4 billion) to 17.8 million borrowers, representing an average loan of USD 466 (Boonperm et al., 2013). The Village Fund had a significant impact on household incomes and spending.

Boonperm et al. (2013) found that the Village Fund had a moderate effect on household spending and (to a lesser extent) household income. The loan program's short-term nature makes it suitable for farmers, enabling them to obtain financing for inputs during the crop cycle and for consumer credit. However, this is not a sufficiently long-term (or perhaps significant) solution and is not very workable for most of the other remunerative activities that households might undertake.

1.2.3 Village Development Management in Indonesia

Law Number 6 of 2014 concerning Villages brings a new paradigmatic change in village development management in Indonesia, one of the developing countries in Asia. The law, often referred to as the Village Law, brings a new paradigm that positions the village as an empowered subject of development. Villages are no longer just objects of development; they are given greater authority to develop their regions according to their specific needs. Article 18 of the Village Law states that villages are granted greater authority in four categories: development implementation, governance, community development, and community empowerment, which are carried out based on original rights, village customs, and community initiatives.

A long history of legislation has been born to confirm the village's existence. During the more than 70 years of independence of the Indonesian Republic since the proclamation by Soekarno-Hatta in 1945, the history of constitutionality in Indonesia has noted ten amendments to the Law governing villages, either individually or as part of the regulations governing local government. These regulations brought a changing spirit to legal politics and even experienced paradigmatic changes. Based on the village rule changes from 1945 to 2013, only two rules governing the village were in effect: Law No. 19/1965 concerning Praja Village and Law No. 5/1979 concerning Village Government. Law No. 5 of 1979 positions the village as an organization under the sub-

district (*Kecamatan*). The village was limited to an administrative unit in the directorial order (Fadhly, 2018).

The presence of Law (*Undang-Undang*) No. 6 of 2014 concerning Village carried out with Government Regulation (*Peraturan Pemerintah/PP*) No. 43 of 2014 jo. *PP* No. 57 of 2015, as the implementing regulation, has brought new enthusiasm to implementing village governance, with several rules below. The Village Law and all derivative regulations governing VFM have successfully encouraged the realization of comprehensive village governance, encompassing governance, human resource development, optimization of public services, and broader community empowerment (Fadhly, 2018; Prasetyo & Muis, 2015).

The Village Law embodies the state's commitment to providing more expansive space for village communities to develop their regions more autonomously, thereby helping the state fulfill its constitutional responsibility to address social problems. The main points of regulation under this Law include the distribution of economic resources to villages originating from the State Budget and Expenditure or *Anggaran Pendapatan dan Belanja Negara (APBN)* (Letty, 2016; Briando, 2017). The law regulates the amount of funds distributed to villages. There is a financial budget distribution, known as "Village Funds" (*Dana Desa*⁴), from the central government to the village.

Additionally, the Law strengthens the village's democratization. The village decision-making process has to involve community representatives through a village discussion forum. There is also a body with a substantial role in control, budgeting,

⁴ Village Funds are funds originating from the state revenue and expenditure budget that are intended for villages that are transferred through the district/city regional income and expenditure budget and are used to finance government administration, development implementation, community development, and community empowerment (*Peraturan Pemerintah/Government Regulation* No. 43/2014 Article 1 paragraph 8).

and village legislation institution, namely the Village Consultative Body (*Badan Permusyawaratan Desa/BPD*). Structuring the village's development policy and independence, all development programs entering the village must adjust to the medium-term village development plan (*Rencana Pembangunan Jangka Menengah Desa/RPJMDesa*).

The Indonesian state's commitment to place villages as a significant part of national development is necessary. According to the World Development Indicators of 2013, it is estimated that 1.2 billion poor (living on USD 1.25 or less every day) live in rural areas, which is equivalent to 75% of the world's population⁵ (Rodríguez-Pose & Hardy, 2015). Therefore, it is not far from hyperbole to say that most countries in the world pay more attention to village development, particularly in low- and middle-income countries, including Indonesia.

1.2.4 Village Financial Management in Indonesia

As regulated in Law No. 6 of 2014 concerning Villages, Village Financial Management (VFM) is a consequence of village finances mandated to the village government. Article 71, paragraph 1 of the Village Law states that Village Finance encompasses all village rights and obligations that can be valued in money, as well as all related goods and services. Specifically, VFM that the village government must implement is regulated in more detail in the Regulation of the Minister of Home Affairs (*Permendagri*) Number 20 of 2018 concerning Village Financial Management (*lex specialist*). Article 1, number 6 of *Permendagri* Number 20 of 2018 explains that VFM carried out by the village government includes all structured programs and

⁵ Based on Sustainable Development Goal's Report 2019 (United Nation, 2019), around 79 percent of the global's poor (living on less than \$1.90 per day) live in rural areas.

activities, from planning and implementation to accounting & reporting, as well as financial accountability.

One of the most notable new VFM aspects is the Village Fund. As explained by *PP* No. 60 of 2014, jo. *PP* No. 22 of 2015 designates the Village Fund as a state budget fund for village development. The Village Fund mechanism is one of the key differentiators that sets the village as the subject of development. Before the Village Law was released, there was no mechanism for launching funds from the central government (State Budget/*APBN*) to village governments (Village Income and Expenditure Budget/*APBDesa*) for village development needs.

Village Funds mandated in Government Regulation (*PP*) No. 60 of 2014 concerning Village Funds sourced from the National/State Budget are also expected to support village development and a national development priority related to the village. On the other hand, government policies aimed at reducing the number of undeveloped villages have become national targets. *Rencana Pembangunan Jangka Menengah Nasional/RPJMN* (Medium-term National Development Plan) 2015-2019 states that the village development target is to reduce the number of undeveloped villages to at least 5,000. The amount of Village Funds is rising every year. Table 1.2 describes data on Village Fund distribution from 2015 to 2023.

The distribution of village funds to support community welfare, as observed from 2014 to 2023, has continued to increase. IDR 20,7 trillion was distributed to 74,093 villages (approximately IDR 279,400,000 or RM 93,797.9 or USD 19,957.1 per village) in 2015. In 2016, the Village Fund increased to around IDR 624,700,000 (RM 209,718.7 or USD 44,621.4 per village) with a total fund of IDR 46.7 trillion. Village Fund distribution to each village accelerated significantly in 2017, reaching approximately IDR 59.8 trillion (with each village receiving IDR 799,200,000,

equivalent to RM 267,965.80 or USD 57,014.30). The total then rose slightly in 2018 to IDR 59.9 trillion (approximately IDR 799,100,000 or RM 240,069.4 or USD 57,078.6 per village). The number of Village Funds increased again in 2019 and 2020, reaching IDR 69.8 trillion and IDR 71.1 trillion in total (approximately IDR 931,200,000 or RM 312,617.2 or USD 66,514.3 per village in 2019 and IDR 948,600,000 or RM 318,457.9 or USD 67,757.1 per village in 2020). The total Village Funds distributed by the central government increased again in 2021, amounting to a total of IDR 71.9 trillion, before decreasing gradually in 2022 and 2023 by 67.9 trillion (approximately IDR 905,800,000 or RM 304,090.1 or 64,700,1 USD per village) and 67.8 trillion (approximately IDR 905,500,000 or RM 303,986.6 or USD 64,678.6 per village).

Table 1. 2 Village Fund Distribution

Year	Amount (IDR)	Average Amount per Village (per year)		
		Indonesia Rupiah (IDR)	Malaysian Ringgit (MYR)	US Dollar (USD)
2015 (74,093 villages)	20.7 trillion	279,400,000	79,828.6	19,957.1
2016 (74,754 villages)	46.7 trillion	624,700,000	178,485.7	44,621.4
2017 (74,910 villages)	59.8 trillion	798,200,000	228,057.1	57,014.3
2018 (74,957 villages)	59.9 trillion	799,100,000	228,314.3	57,078.6
2019 (74,954 villages)	69.8 trillion	931,200,000	266,057.1	66,514.3
2020 (74,954 villages)	71.1 trillion	948,600,000	271,028.6	67,757.1
2021 (74,939 villages)	71.9 trillion	959,400,000	274,114.3	68,528.6
2022 (74,961 villages)	67.9 trillion	905,800,000	258,800,1	64,700,1
2023 (74,960 villages)	67.8 trillion	905,500,000	258,714.3	64,678.6

Source: Ministry of Village, Development of Underdeveloped Regional and Transmigration (2023).

Note: 1 US Dollar = ± IDR 14,000; 1 MR = IDR 3,500.

The various Village Development Programs have a positive impact on the village, including increasing the prosperity of village people and reducing poverty in the village. The results of using the Village Fund for social development can be seen on the Building Village Index (*Indeks Desa Membangun/IDM*). The number and proportion of villages are categorized as independent, developed, developing, undeveloped, and very undeveloped. This index comprises three composite dimensions (social security, economy, and ecology), comprising 22 variables and 52 indicators. Table 1.3 indicates the village status profile based on the Building Village Index of 2014 (the inauguration year of the Village Law) and 2023 (Ministry of Village, 2015; Ministry of Village, 2023):

Table 1. 3 Building Village Index (*Indeks Desa Membangun/IDM*) 2014 and 2023

IDM 2014 (73,709 villages)		IDM 2023 (74,960 villages)	
Category (Villages)	%	Category (Villages)	%
a) Very Underdeveloped Village (<i>Desa Sangat Tertinggal</i>) = 13453	18.25 %	a) Very Underdeveloped Village (<i>Desa Sangat Tertinggal</i>) = 4348	05.85%
b) Underdeveloped Village (<i>Desa Tertinggal</i>) = 33592	45.57 %	b) Underdeveloped Village (<i>Desa Tertinggal</i>) = 6762	09.10%
c) Developing Village (<i>Desa Berkembang</i>) = 22882	31.04 %	c) Developing Village (<i>Desa Berkembang</i>) = 28749	38.67%
d) Developed Village (<i>Desa Maju</i>) = 3608	4.89 %	d) Developed Village (<i>Desa Maju</i>) = 23028	30.98%
e) Independent Village (<i>Desa Mandiri</i>) = 174	0.24%	e) Independent Village (<i>Desa Mandiri</i>) = 11456	15.41%

Source: Ministry of Village, Underdeveloped Regional Development and Transmigration (2014 & 2023).

Table 1.3 shows an incontestable impact of the implementation of Law No. 6 of 2014 (including the distribution of the Village Fund inside) in terms of the village's development. Very underdeveloped and underdeveloped villages experienced a substantial decline in the first eight years following the enactment of Law No. 6 of 2014. Conversely, the number of developing, developed, and independent villages is on the rise.

Improvements to the Village Fund's governance continue to be optimized, with a focus on building infrastructure to enhance the quality of life and economy. Data from the Ministry of Village, Underdeveloped Regional Development and Transmigration (2023) show that the Village Fund brought community benefits within the first ten years, from 2014 to 2023. Some advantages could be seen from the increasing number of rural infrastructures that the Village Fund has built. A Ministry of Village Development, Undeveloped Regional, and Transmigration (2023) report states that the infrastructure sector includes 311,700,000 km of village roads and 1,602.2 km of village bridges. Besides, 12,300,000 village market units, 5,413 village water storage facilities (*embung*) units, and 40,600,000 integrated health center (*Posyandu*) units were constructed. Also, there are 1.28 million clean water facilities, 422,860 sanitary facilities (*Mandi Cuci Kakus/MCK*) units, 11,599 village childbirth facilities (*Polindes*) units, 64,400,000 kindergartens (*PAUD*) units, and 572.8 million drainage units.

This additional Village Fund budget presents a new paradigm in VFM. The Ministry of Home Affairs (*Kementerian Dalam Negeri*) has introduced a package of technical rules related to VFM, including the Minister of Home Affairs Regulation (*Permendagri*) No. 113 and 114 of 2014 regarding VFM (before being replaced by *Permendagri* No. 20 of 2018). Additionally, the Ministry of Village, Underdeveloped Regional Development and Transmigration (*Kementerian Desa PDTT*) has released a series of rules to oversee the implementation of Law No. 6 of 2014, including the priority of using the Village Fund every year. The presence of a series of rule-of-law packages indicates that the noble goal of empowering and prospering villages must be accompanied by additional responsibilities for all village governments regarding financial management.

Law No. 6 of 2014 concerning the Village is effectively entering its tenth year at the end of 2024. An in-depth investigation is required to comprehensively explore the implementation of the Village Law, particularly in the aspects of VFM. The research is essential to reveal, especially in evaluating the Village Fund's launch from the central government to the village government, which is worth hundreds of millions of rupiah each year. Due to the implementation of the Village Law, Village Governments are given greater authority to manage their finances autonomously. The influx of money that comes in and is managed by the Village Government has the potential for abuse. Therefore, a thoughtful and comprehensive evaluation and analysis of the implementation of VFM, which is nearly a decade old, is needed.

1.3 Problem Statement

As mentioned before, the issuance of the Village Law, along with various instruments (including Village Funds and the accompanying VFM obligations), has had a positive impact on the village, including increasing the prosperity of village people and reducing village poverty. However, the journey of effective VFM implementation began in the 2015 budget year, facing various problems that hindered the achievement of the noble objectives of the Village Law.

Based on the previous research studies, three issues of VFM emerge in general. First, the village's financial officers lack the ability to understand the internal control system and organizational culture to implement VFM. Human resources at the village government level mostly have a background of not too high educational levels (Eryana, 2018; Meutia & Liliana, 2017; Nurhakim & Yudianto, 2018; Rasmi, Salle, & Pangayow, 2018; Syaifullah, 2017; Umar, Usman, & Purba, 2018; Utamingtyas, 2019).

To facilitate and assist the implementation of VFM, the central government introduced an application-based information system, known as *Sistem Keuangan Desa* (*Siskeudes*). However, the limited capacity of human resources makes the utilization of the *Siskeudes* not optimal in assisting the implementation of VFM at the village level (Rahayu, Kurnia, & Dzulistina, 2019; Salisa, Aeni, & Chamid, 2019; Ubed, Ariutama, & Yudanto, 2017; Watulingas, Kalangi, & Suwerja, 2019; Wilma & Hapsari, 2019; Yulianti & Janie, 2017).

Second, the good governance values required for VFM implementation have not been fully implemented substantively. The Village Law mandates that VFM must be carried out with the principles of accountability, participatory, transparency, and in a disciplined way, but has not been substantively conducted (Basuki, Setyowati, & Wahyunengseh, 2019; Khusniyatun & Kiswanto, 2017; Kurrohman, 2015; Saputra, Anggiriawan, & Sutapa, 2018; Suhartono, Virana, Irmawati, & Putri, 2019).

Third, there are rampant cases of misuse or abuse of village finances, which often involve criminal acts of corruption. Figure 1.1 illustrates ICW monitoring results from 2015 to 2021 regarding fraud cases within the village territory. The chart illustrates the data related to the number of cases and the amount of state loss from village budget corruption in the first years of implementing Law No. 6 of 2014 concerning Village (2015-2021).

Figure 1.1 indicates that the number of village corruption cases tended to increase in the early years of VFM implementation in Indonesia (Indonesia Corruption Watch, 2022). In 2015, approximately 22 corruption cases were recorded, increasing to 48 cases in 2016. The number of corruption cases more than doubled in 2017 and 2018, reaching 98 and 96 cases, respectively. However, in 2019, the number declined to 48 cases. In 2020, the number of corruption cases in the village budget sector

increased significantly, reaching 129 cases. In 2021, cases of village financial corruption increased again, amounting to 154 cases. Thus, the total number of corruption cases that went to court exceeded 400 between 2015 and 2021.

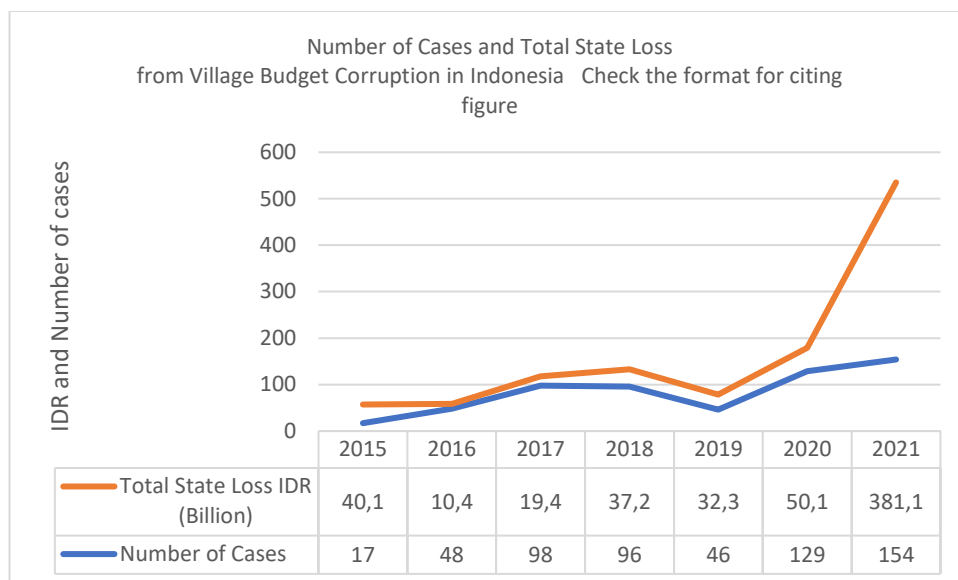


Figure 1. 1 Number of Cases and Total State Loss from Village Budget Corruption in Indonesia

Source: Indonesia Corruption Watch (2022).

Note: 1 US Dollar = ± IDR 14,000.

The fantastic number of village financial corruption cases that have been brought to court has resulted in significant material state losses. State losses due to village budget corruption in 2015 and 2016 were approximately IDR 40.1 billion (equivalent to approximately MYR 11.5 million or USD 2.9 million) and IDR 10.4 billion (equivalent to approximately MYR 2.9 million or USD 742,857). The amount of state losses went up significantly in 2017 and 2018, by IDR 19.4 billion (approximately MYR 5.5 million or USD 1.4 million) in 2017 and IDR 37.2 billion (approximately MYR 10.6 million or USD 2.7 million) in 2018. After decreasing slightly in 2019 (approximately IDR 32.3 billion or MYR 9.2 million / USD 2.3 million), state losses soared again in 2020, reaching IDR 50.1 billion (approximately MYR 14.3 million or USD 3.5 million). The figure for state losses continued to

increase significantly in 2021, reaching approximately IDR 381.1 billion (equivalent to around MYR 108.9 million or USD 27.2 million).

Furthermore, corruption cases related to the village government budget have occupied the highest number of corruption cases compared to other sectors in Indonesia over the last three years (Indonesia Corruption Watch, 2018, 2019, 2020, 2021). In 2018, corruption related to village finances was the highest case that went to court (96 cases), followed by corruption in the government and education sectors. In 2019, village budget corruption still reached its highest peak, surpassing that of the government and other sectors. Again, the number of corruption cases in the village government reached its highest levels in 2020 and 2021, with 129 cases and 154 cases, respectively. Table 1.4 illustrates the mapping of corruption cases by sector in Indonesia from 2018 to 2021.

Moreover, the Village Head (*Kepala Desa*) is the dominant actor who is caught in corruption. The total number of village heads caught in village budget abuse cases was around 300 from 2015 to 2021 (Indonesia Corruption Watch, 2022). This number continues to rise yearly, with 15 in 2015, 32 in 2016, 65 in 2017, and 102 village heads in 2018. In 2019, 45 village heads and 19 village officials were convicted of corruption in village finances. The number of village heads caught in corruption rose by 50 and 70 people in 2020 and 2021, respectively.

Indonesian Corruption Watch/ICW (2018) explains various factors that cause high cases of corruption in the village sector, including the lack of community involvement in the planning and monitoring process of the village budget, the lack of a supervisory function from village institutions such as the Village Consultative Body (*Badan Permusyawaratan Desa/BPD*), and the high political costs of village head

elections. All the presumed triggering factors make the opportunity for village financial abuse even more fantastic.

Table 1. 4 Mapping Corruption Cases by Sector 2018, 2019, 2020 & 2021.

Sector	Number of Cases			
	2018	2019	2020	2021
Village Budget	96	46	129	154
Government	57	30	40	50
Education	53	18	25	44
Transportation	32	31	29	40
Health	21	11	16	16
Water	21	11	15	23
Land	20	16	25	21
Social Communities	18	9	15	34
Banking	16	14	26	32
Licensing	14	0	0	0
Election	0	7	0	0
Labor	0	7	0	0
Sport	0	6	0	0
Energy & Electricity	0	6	0	0
Trading	0	6	0	13
Tax	0	0	16	0

Source: (Indonesia Corruption Watch, 2018b, 2019, 2020, 2021).

Additionally, the Indonesian Corruption Watch/ICW (2019) describes several modes of village fund corruption, including the first, fictitious project, i.e., entering a budget for work that never existed; second, double budget, which involves introducing funding for a project that has already been completed; and third, conducting debt by using Village Fund but never returning it.

Therefore, the high number of corruption cases in managing the village budget is due to the large budget (every village manages roughly IDR 1.5 to 2 billion, or USD 107,142.8, or RM 503,571.4, annually) that has been disbursed. The increasing number of corruption cases surrounding VFM during the initial implementation of Law No. 6

of 2014 is alarming. This fact signals potential abuse of the VFM budget (Indonesia Corruption Watch, 2017b).

This research focuses on addressing the primary challenge in VFM implementation: the issue of corruption. A large budget can cause problems with its implementation. The principles of transparency, participation, and accountability in village political, development and financial governance are still not working along with the good intentions of the village development philosophy (Artini, Atmadja, & Julianto, 2017; Mardika, Sulindawati, & Kurniawan, 2017; Mulyana, Dewi, & Sujana, 2018; Rusmianto, Maryani, & Makhsun, 2018; Agus & Pancawati, 2018; Arthana, 2019; Indah & Praptoyo, 2015; Santi & Sudrajat, 2017; Risyah & Nurodin, 2017; Yunianingrum & Kolopaking, 2018).

Some scholars have warned that the complexity of village autonomy contains the potential for abuse or misrepresentation (Hadiyati, Rosnidah, & Siswoyo, 2019; B. D. Lewis, 2015; Puspasari, 2015; Seputro, Wahyuningsih, & Sunrowiyati, 2017; Sumaryanto, Ngaisah, & W., 2019). This warning is similar to when regional autonomy (regency/city and provincial level), released in the reform order, has led to widespread misuse of state finances in the regions (Antlöv, 2003, 2004; Olken, 2007). Several instances of village financial abuse justify the negative opportunity or threat (Indonesia Corruption Watch, 2016a, 2016b, 2017b, 2018b, 2019; Komisi Pemberantasan Korupsi, 2016, 2017, 2018, 2019). The phenomenon of corruption over the past several years in villages is based on village strategic positions in the context of the electoral situation, the aspect of village head affiliation with specific political actor candidates, and the lack of knowledge and supervision of the village community (Satriajaya & Handajani, 2017; Briando, 2017).

Several previous studies expressed high concern about the increasing misuse of village finances. Several factors contributing to fraud have also been identified, including a lack of knowledge and confusion in implementing village finance, as well as opportunities to commit fraud (Yuhertiana, Widajatie, & Akbar, 2016). Insufficient internal control systems and a lack of community participation in monitoring are also contributing factors to fraud (Nurjaman, 2018). These widespread village finance abuses are not in line with Indonesian human values as a religious nation. Hence, efforts to prevent and return to transcendental religious and cultural values are also echoed by researchers as a solution to the high trend of village finance abuses (Latuconsina & Soleman, 2019; Nurjaman, 2018).

The reality of corruption cannot be separated from the context of society's cultural realm in understanding private and public ownership. Through bureaucratic reform, the transition to democracy has not fully changed the bureaucratic mentality or the community's understanding of public ownership (Santoso & Meyrasyawati, 2015). Quoting Lubis and Scott (1990), Baswir (2002) pointed out that corruption comprises two aspects: the abuse of power beyond the legal reasoning limit by officials or state apparatus, and the prioritization of personal or client interests over public interest by public officers. The higher the power (particularly in the financial aspect) delegated to the village, the higher the possibility of fraud, such as corruption, that may occur. Corruption never ends and always surfaces in various instances of power abuse. It is not excessive if every power in the country also has the potential to produce corruptors.

Corruption eventually developed as a cultural problem. From a sociological perspective, the village is defined as an area with a particular pattern. Indriati (2014) pointed out that culture is practiced in a way that is learned (culture is learned) and is

disseminated (culture is shared). The act of corruption is a learning process that originates from enculturation, a process of social interaction in which people learn from one another and develop habits. Local rules and relationships of people are growing within the community's structure and culture.

The high number of corruption cases reflects the fading implementation of norms and values of goodness in the social environment (Ganie-Rochman & Achwan, 2015; Indriati, 2014). The massive misuse of village finances reflects the increasingly permissive interpretation of the value of goodness in society, particularly in rural areas. The holders of the mandate to manage village finances do not show any shame when collecting illegal assets from corruption. The rampant cases of corruption at the village level require a solution in the form of creating social engineering that involves institutional mechanisms and systematic social structures. In the context of VFM management, which contains public resources, this social engineering is manifested in arrangements that contain principles, norms, and mechanisms (Ganie-Rochman & Achwan, 2015).

The set of norms and values regarding what is good and beneficial versus what is bad and destructive is a collective agreement that becomes a collective consciousness (Indriati, 2014). Norms and values of goodness should be practiced and become accustomed to as a guideline for life. It is substantial as a preventive measure so that reprehensible actions (such as corruption) do not become generally accepted habits. On the contrary, these evil actions must be fought and made the common enemy of all elements of society. The rampant cases of corruption in the implementation of VFM show that the values and norms of goodness have not become the primary concern for behavioral rules in village governance.

The ultimate value of goodness comes from religious values. A religious insight (in this case, Islam, as the religion most widely practiced by the Indonesian people) approach can be one of the places to return to solve management problems in the village. A cultural approach, which is heavily influenced by religious values, is also incorporated into the solution search. The Islamic religious agenda, including the objectives of Islamic law (*Maqasid al-Shariah*), guides the form of value principles that enable humans, both individually and in society (including the state), to lead a good life in pursuit of social justice and public welfare (Khan, 2022). Developing a civilized society requires creating a virtuous political, social, and economic reality based on spiritual values, involving two key elements: society and the state (Azra, 2010; Batchelor, 2014; Khan, 2022). Unfortunately, a consciousness of the importance of mainstreaming the internalization of good values from religion (and also religiously charged culture) has not received significant attention in several studies on VFM governance in Indonesia (Latuconsina & Soleman, 2019).

Various problems related to the village's financial abuses need to be resolved based on principles derived from religion (Islam). In this context, VFM in Indonesia must be implemented by all Village Governments and other related parties based on the principles of good governance derived from religious values. Implementing organizational operations based on the principles of good governance will not eradicate criminal activities. Still, it will narrow the actions that violate the law and morality, making it more difficult for an act of abuse to be carried out (OECD Committee, 2004). The principles of good governance that are formulated will later be followed by rules, regulations, and mechanisms created in line with the values contained in the principles of governance.