

**THE ROLE OF INTERNAL CONTROL SYSTEMS IN IMPROVING THE
QUALITY OF FINANCIAL REPORTS OF MICROFINANCE INSTITUTIONS
(CASE STUDY ON MICROFINANCE INSTITUTION MITRA SURYA
SEJAHTERA, PASANGKAYU REGENCY)**

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Abstract

This qualitative case study analyzes the role of internal control systems in improving financial report quality at Microfinance Institution (MFI) Mitra Surya Sejahtera, Pasangkayu Regency, using the COSO framework. Data were collected through in-depth interviews, observation, and documentation from management, finance department, and operational staff, with validity tested through triangulation. Results demonstrate that the internal control system significantly enhances financial report quality in terms of reliability, recording orderliness, and accountability. The control environment, supported by management's commitment to integrity and transparency, encourages employee work discipline. Control activities including transaction authorization, evidence completeness, and routine reconciliation effectively minimize recording errors. Regular financial communication and management monitoring further support the preparation of orderly and accountable reports. However, limitations were identified, including constrained human resources, suboptimal separation of functions, and a simple recording system. The study concludes that strengthening internal control systems is crucial for improving financial report quality and maintaining MFI operational sustainability. Findings contribute theoretically to micro-sector accounting literature and practically provide guidance for MFI managers in establishing transparent and accountable financial governance.

Keywords: Responsiveness, Empathy, Interpersonal Communication, Customer Satisfaction, Telecom Internal Control System, Financial Report Quality, Microfinance Institution, Case Study

INTRODUCTION

Microfinance Institutions (MFIs) have a strategic role in supporting financial inclusion and community economic empowerment, especially for micro-business actors who are not reached by conventional banking. As institutions that collect and distribute public funds, MFIs are required to present quality, transparent, and accountable financial reports. Quality financial reports serve as the main means of management accountability as well as the basis for decision-making by customers, regulators, and other stakeholders (Rahmah et al., 2023; Setiawan & Susanto, 2022).

The quality of financial reports is not only determined by compliance with accounting standards, but is also greatly influenced by the effectiveness of the internal control system implemented in the organization. Internal control systems function to provide reasonable assurance that operational activities run according to procedures, risks can be minimized, and financial information is presented reliably and in a timely manner (COSO, 2019; Chen, 2021). Without adequate internal controls, financial reports are at risk of containing material errors and losing their relevance to information users.

In practice, many MFIs face limitations in implementing internal control systems, such as weak separation of duties, inconsistent transaction documentation, and lack of internal oversight functions. This condition is exacerbated by limited human resources and the still dominant manual recording process. Research by Putri et al. (2022) shows that weaknesses in internal control are one of the main causes of low quality financial reports in microfinance institutions and credit unions.

An effective internal control system plays an important role in ensuring the reliability of financial reports through mechanisms for preventing and detecting errors and fraud. Dewi et al. (2021) affirm that strong internal controls are able to improve the accuracy of transaction recording and consistency in the application of accounting policies. Thus, internal control functions not only as a supervisory tool, but also as an instrument for improving the quality of financial information.

Empirical research in the last five years shows a positive relationship between the effectiveness of internal control systems and the quality of financial reports. Pratama et al. (2023) found that financial institutions with clear and structured internal control procedures tend to produce more reliable financial reports trusted by customers. Similar findings were also conveyed by Sari and Mulyani (2021), who stated that internal control encourages increased work discipline and compliance with accounting procedures. In addition to impacting the quality of financial reports, internal control systems also contribute to increasing public trust. Financial reports prepared based on good internal control systems reflect healthy and transparent institutional governance. Customer trust in MFIs is greatly influenced by perceptions of professionalism and accountability in fund management, one of which is reflected in the quality of financial reporting (Cahyani & Wiryawan, 2020; Rahmah et al., 2023).

In the regulatory context, internal control systems also function as a tool to ensure MFI compliance with accounting standards and regulations set by regulators. Setiawan and Susanto (2022) state that adequate internal control facilitates microfinance institutions in meeting supervisory demands and reducing the risk of sanctions due to reporting non-compliance. Thus, internal control becomes a key element in maintaining the operational sustainability of MFIs.

MFI Mitra Surya Sejahtera, located in Pasangkayu Regency, West Sulawesi, represents a typical rural microfinance institution serving smallholder farmers, fishermen, and micro-entrepreneurs in an area with limited access to formal banking services. As a non-bank financial institution operating at the grassroots level, this institution faces challenges commonly found in rural MFIs, including a small workforce with overlapping job functions, heavy reliance on manual bookkeeping systems, and the absence of a dedicated internal audit function. Preliminary observations conducted prior to this study identified inconsistencies in transaction recording and delays in periodic financial reporting, raising concerns about the reliability and transparency of its financial statements. These conditions position MFI Mitra Surya Sejahtera as a particularly relevant and important case for examining how internal control mechanisms operate in practice and how those conditions directly shape the quality of financial reports produced by the institution.

Although the importance of internal control systems has been widely discussed in the accounting literature, the majority of existing studies have adopted quantitative approaches, primarily focusing on measuring the statistical relationship between internal control variables and financial report quality through regression analysis or structural equation modeling. While these studies confirm the significance of the association, they provide limited understanding of how internal control is actually carried out in the daily financial recording and reporting activities of MFIs, including how control procedures are executed by individual staff members, how deviations from standard procedures are identified and addressed, and how organizational work culture shapes compliance with accounting policies. Qualitative case study research that explores these mechanisms in depth remains scarce, particularly in the context of rural microfinance institutions in Eastern Indonesia (Putri et al., 2022).

The qualitative approach is therefore particularly relevant to understanding this phenomenon more comprehensively, as it enables researchers to explore the perceptions, experiences, and actual practices of individuals directly involved in the financial recording and reporting process. Through in-depth interviews and direct observation, this study aims to reveal the role of internal control systems not only as a set of formal procedures, but also as an organizational work culture that shapes individual behavior and accountability (Sari & Mulyani, 2021).

Based on the foregoing, this study aims to analyze the role of internal control systems in improving the quality of financial reports in Microfinance Institutions, with a case study at MFI Mitra Surya Sejahtera, Pasangkayu Regency. This research is expected to provide theoretical contributions to the development of micro-sector accounting literature, as well as practical contributions for MFI managers seeking to strengthen internal control systems in order to produce reliable, transparent, and sustainable financial reports.

REVIEW OF LITERATURE

Previous Research

Table 1.
Previous Research

No.	Previous Research	Research Novelty
1.	Fauziah et al. (2025) examined the implementation of internal control systems to improve the	The present study differs in object, method context, and institutional setting. While Fauziah et al. focused on an Islamic rural bank (BPRS)

No.	Previous Research	Research Novelty
	quality of financial reports at BPRS Almasoem using a qualitative approach.	with relatively structured resources, this study examines a non-Islamic MFI operating in a remote area of Pasangkayu Regency, West Sulawesi, where resource limitations and manual recording practices create distinct internal control challenges not addressed in prior work.
2.	Nisa and Susilo (2025) analyzed the application of SAK EMKM and internal control on the quality of MSME financial reports in Jombang using a quantitative approach.	While Nisa and Susilo established a statistical association between internal control and financial report quality, the present study employs a qualitative case study approach to investigate the actual mechanisms through which internal control components are practiced in daily financial recording and reporting, revealing dimensions of behavior and organizational culture that quantitative measurement cannot capture.
3.	Ibrahim and Nurodin (2024) examined the effects of internal control and accounting information systems on the quality of financial reports at PDAM Sukabumi.	Ibrahim and Nurodin focused on a state-owned public utility with formal organizational structures and digital accounting systems. The present study focuses on a grassroots MFI characterized by direct community proximity, flexible organizational structures, and predominantly manual bookkeeping, representing a contextually distinct environment that has received limited scholarly attention.
4.	Bale et al. (2023) examined the influence of accounting information systems and internal control on the quality of local government financial reports.	Bale et al. examined public sector institutions governed by bureaucratic accountability frameworks. The present study extends the discourse to the private microfinance sector, where accountability is driven simultaneously by profit motives, social mission, and member trust, creating a qualitatively different internal control context that warrants separate investigation.
5.	Ningsih et al. (2024) analyzed the role of internal control systems in improving the quality of financial reports of Regional Government Agencies in Wonosobo Regency.	Unlike Ningsih et al., whose findings apply to government agencies with standardized reporting mandated by public sector accounting standards, this study investigates an MFI whose financial reporting obligations are shaped by member accountability, regulatory compliance, and community transparency, offering a perspective from a sector with fundamentally different governance dynamics.

Internal Control System

An internal control system is a process designed and implemented by management to provide reasonable assurance regarding the achievement of organizational objectives in three main categories: operational effectiveness and efficiency, reliability of financial reporting, and compliance with applicable laws and regulations (COSO, 2019). In the context of microfinance institutions (MFIs), internal control functions as a mechanism to ensure that all operational activities, including financial recording and reporting, run according to established standards and procedures (Ibrahim & Nurodin, 2024).

According to the COSO framework, internal control consists of five interrelated components: control environment, risk assessment, control activities, information and communication, and monitoring. Each of these components plays a distinct role in shaping the quality of financial reports, and their interaction creates a comprehensive system of accountability within the organization.

The control environment forms the foundation for all other control components. It involves the integrity, ethical values, and competence of organizational personnel, as well as management's philosophy and operating style (Fauziah et al., 2025). In MFI settings, a strong control environment establishes a culture of accountability that influences how staff approach financial recording responsibilities, thereby reducing the likelihood of unauthorized transactions or intentional misreporting.

Risk assessment is the process of identifying and analyzing risks that may hinder the achievement of organizational objectives, particularly in relation to the accuracy and reliability of financial reports (Dewi et al., 2021). For MFIs that rely heavily on manual bookkeeping and have limited staff, risk assessment enables management to identify vulnerabilities in the recording process, such as the risk of unverified transactions or misclassification of funds, before they result in material errors in financial statements.

Control activities include the specific policies and procedures implemented to ensure that management directives are carried out properly. These encompass authorization of transactions, reconciliation, verification, and separation of functions (Nisa & Susilo, 2025). In the context of financial report quality, control activities such as dual authorization and regular cash reconciliation directly support the reliability dimension of financial information by ensuring that every recorded transaction is legitimate, accurate, and traceable. Without such activities, financial reports are susceptible to errors that undermine their credibility and usefulness for decision-making.

The information and communication component ensures that relevant financial data is identified, recorded, and communicated in a timely and structured manner so that all parties can carry out their responsibilities properly (Raspati & Simanjuntak, 2024). This component has a direct bearing on the timeliness and transparency dimensions of financial report quality. When information flows effectively between field staff, bookkeepers, and management, monthly reports can be completed on schedule and made accessible to members and regulators, fulfilling the accountability expectations placed on MFIs.

Monitoring is the ongoing process of evaluating the quality of internal control performance over time, carried out through regular supervision or periodic independent evaluations (Raspati & Simanjuntak, 2024). Effective monitoring enables MFIs to detect deviations from established procedures, address inconsistencies in transaction documentation, and maintain the completeness of financial records, all of which are essential conditions for producing financial reports of consistent quality.

In the MFI context, internal control is critically important because these institutions manage public funds and are accountable to members, regulators, and the wider community. Effective internal control helps prevent misuse of funds, reduces operational risks, and increases stakeholder trust (Pratama et al., 2023). Several previous studies have confirmed that a strong internal control system has a significant positive impact on the quality of financial reports (Bale et al., 2023; Ningsih et al., 2024). Without adequate internal control, MFIs are at high risk of material errors, fraud, and reputational damage.

Quality of Financial Reports

The quality of financial reports refers to the extent to which the information presented in financial statements meets the qualitative characteristics required by accounting standards, namely relevance, reliability, comparability, and understandability (Fauziah et al., 2025). Quality financial reports not only comply with applicable accounting standards, but also genuinely provide useful information for decision-making by various parties, including management, members, regulators, and investors (Nisa & Susilo, 2025).

Relevance means that the information presented must be capable of influencing user decisions by helping them evaluate past, present, or future events. Reliability is the degree to which information is free from material errors, can be verified, and is presented fairly (Ibrahim & Nurodin, 2024). Comparability allows users to identify similarities and differences between two or more economic phenomena, while understandability relates to how easily users with reasonable business knowledge can interpret the information presented.

In the specific context of MFIs, however, the meaning of financial report quality extends beyond mere compliance with formal accounting standards. For small MFIs such as MFI Mitra Surya Sejahtera, financial report quality in practice encompasses the completeness of transaction evidence, including supporting documents such as receipts, loan disbursement records, and member savings ledgers; the accuracy and consistency of cash reconciliation conducted on a daily or weekly basis; the timeliness of monthly financial reports submitted to management and made available to members; transparency to members regarding the use and distribution of funds; and accountability to regulators through reports that comply with supervisory requirements. These dimensions reflect the operational reality of grassroots MFIs, where formal compliance criteria must be interpreted alongside practical standards of institutional accountability and community trust (Kwanbo et al., 2023; Olumoh et al., 2024).

Several factors affect the quality of financial reports in MFIs, including the competence of accounting personnel, the use of accounting information systems, compliance with accounting standards, and the effectiveness of internal control systems (Bale et al., 2023). A strong and structured internal control system has been demonstrated to improve the reliability of financial reports by reducing the risk of errors and fraud (Dewi et al., 2021; Ningsih et al., 2024). Furthermore, good governance and organizational commitment to transparency are important enabling factors in sustaining financial report quality over time (Raspati & Simanjuntak, 2024).

Quality financial reports carry strategic implications for MFIs, including increased stakeholder trust, improved access to external funding, and an enhanced institutional reputation (Pratama et al., 2023). Therefore, improving the quality of financial reports remains one of the central priorities in microfinance institution management, and the internal control system serves as the primary institutional mechanism through which this objective can be achieved and sustained.

RESEARCH METHOD

This study uses a qualitative approach with a case study method, which aims to explore in depth the role of internal control systems in improving the quality of financial reports at Microfinance Institution (MFI) Mitra Surya Sejahtera, Pasangkayu Regency. The case study method was chosen because it allows researchers to understand complex phenomena in a real and specific context, especially regarding how internal control mechanisms are implemented and perceived by actors directly involved in operational and financial processes (Fauziah et al., 2025).

Research Informants

Research informants were selected using the purposive sampling technique, which is the selection of informants based on criteria of relevance, direct involvement in financial recording and reporting activities, and a minimum of two years of work experience at MFI Mitra Surya Sejahtera. These criteria were applied to ensure that informants possess sufficient institutional knowledge and firsthand experience with the internal control practices under investigation.

A total of seven informants participated in this study, representing three hierarchical levels of the organization. The first category consisted of two informants from the institutional leadership level, namely the Director and the Operational Supervisor, both of whom are responsible for strategic policy formulation and overall organizational oversight. The second category comprised three informants from the finance department, including the Head of Finance, the Bookkeeper, and the Cashier, who are directly responsible for daily financial recording, preparation of financial reports, and implementation of internal control procedures. The third category included two operational staff members, namely a Field Credit Officer and a Member Service Officer, who carry out daily transactions and maintain direct contact with members. This selection ensured that data were obtained from multiple perspectives across different functional roles and hierarchical levels within the organization, thereby providing a comprehensive picture of how internal control is understood and practiced throughout the institution.

Data Collection

Data collection was carried out through three complementary techniques. First, in-depth interviews were conducted using a semi-structured format guided by an interview protocol developed based on the five components of the COSO internal control framework. A total of fourteen interview sessions were conducted, with each informant interviewed twice to allow for clarification and member checking of initial findings. Each interview session lasted approximately 45 to 75 minutes and was conducted at the MFI office during regular working hours. With the informed consent of all informants, interviews were recorded using a digital voice recorder to ensure completeness and accuracy of data capture. All recordings were subsequently transcribed verbatim into written form and reviewed by the researchers prior to analysis. Second, direct observation was conducted to examine operational activities at the MFI, focusing particularly on the processes of financial transaction recording, authorization procedures, cash reconciliation, and preparation of periodic financial reports. Observations were carried out over a period of three weeks and were documented in structured field notes. Third, documentation review was conducted to collect and analyze relevant institutional documents, including internal control policies, standard operating procedures (SOPs), transaction evidence such as receipts and disbursement records, member savings ledgers, and monthly as well as annual financial reports.

Data Analysis

Data analysis was performed using the Miles and Huberman interactive model, which consists of three concurrent and iterative stages: data reduction, data presentation, and conclusion drawing (Miles et al., 2014).

In the data reduction stage, all data obtained from interview transcripts, observation field notes, and documentation were systematically reviewed. Researchers applied an initial coding process to identify meaningful units of information relevant to the research questions. Open coding was first conducted to label raw data segments, followed by focused coding to group initial codes into broader categories. Since this study employs the COSO internal control framework as its analytical lens, the coding themes were organized according to the five COSO components, namely control environment, risk assessment, control activities, information and communication, and monitoring. In parallel, a second set of codes was developed to capture data related to the dimensions of financial report quality applicable to the MFI context, including reliability, timeliness, completeness of transaction evidence, consistency of cash reconciliation, transparency to members, and accountability to regulators. This dual coding structure enabled researchers to trace specific connections between each internal control component and its contribution to particular dimensions of financial report quality.

In the data presentation stage, coded data were organized into structured narrative descriptions and thematic matrices that mapped the relationship between COSO components and financial report quality indicators. This arrangement facilitated systematic pattern identification and supported cross-informant comparison across different hierarchical levels of the organization.

In the conclusion drawing stage, findings were interpreted within the COSO analytical framework to answer the central research question regarding the role of internal control systems in improving the quality of financial reports at MFI Mitra Surya Sejahtera. Interpretations were developed iteratively and revisited as new data patterns emerged during analysis.

Data Validity

The validity of research data was tested through two triangulation techniques. Source triangulation was conducted by comparing data obtained from informants across the three categories, namely institutional leadership, finance department, and operational staff, to identify consistencies and discrepancies in their accounts of internal control practices. Technique triangulation was conducted by cross-referencing data obtained through interviews, direct observation, and documentation review. Where discrepancies were found between informant accounts and documentary evidence, researchers returned to the relevant informants for clarification during the second interview session. These triangulation procedures strengthened the credibility of the findings and reduced the potential for subjective bias in the interpretation of results.

RESULTS AND DISCUSSION

Implementation of Internal Control System at MFI Mitra Surya Sejahtera

Based on research findings, MFI Mitra Surya Sejahtera has implemented an internal control system referring to the COSO framework, although the level of formality and complexity is adjusted to the scale of operations and available resources. The five

components of internal control have been implemented with varying degrees of effectiveness, as described below.

Control Environment

The control environment at MFI Mitra Surya Sejahtera is shaped by management's commitment to integrity, transparency, and accountability. This commitment is consistently communicated to staff through regular briefings and is embedded in daily operational practices. The institution has established a clear organizational structure with a defined division of tasks and responsibilities, although the separation of functions remains suboptimal due to the limited number of employees. The Director conveyed this clearly during the interview:

"We always remind staff that honesty is not negotiable in this institution. Every transaction must be recorded as it is, no matter how small. If staff are disciplined from the beginning, the reports will be clean."

This finding is consistent with Fauziah et al. (2025), who affirm that a strong control environment forms the foundation upon which all other internal control components function. The existence of a management-driven culture of accountability at MFI Mitra Surya Sejahtera, even in the absence of formal written codes of conduct, demonstrates that the control environment operates primarily through direct leadership influence, which is characteristic of small-scale MFIs where interpersonal supervision replaces formal institutional mechanisms.

Risk Assessment

The risk assessment process at MFI Mitra Surya Sejahtera is conducted informally through periodic coordination meetings between management and the finance department. The main risks identified include recording errors, loss of transaction documents, and non-performing loan risk. However, this study found that the institution does not maintain formal risk documentation, does not apply a systematic risk ranking procedure, and has not established written protocols for risk follow-up and preventive action. The Head of Finance acknowledged this limitation:

"We discuss risks in meetings, but we do not write them down formally. If there is a problem, we solve it directly. We have not yet made a structured risk register."

This absence of formal risk documentation represents a significant weakness. Without a written risk register and a structured follow-up procedure, risk identification depends entirely on individual memory and meeting attendance, which reduces institutional consistency and makes it difficult to track whether identified risks have been adequately addressed. Ibrahim and Nurodin (2024) emphasize that systematic risk identification is essential for preventing potential material errors in financial reporting. The current informal approach at MFI Mitra Surya Sejahtera, while practically functional, does not meet the standard of a robust risk assessment process and poses a vulnerability in the overall internal control system.

Control Activities

Control activities implemented at MFI Mitra Surya Sejahtera include transaction authorization, verification of transaction evidence, and routine reconciliation. Every financial transaction must be authorized by the designated officer before it is recorded in the accounting system. The finance department conducts daily cash reconciliation and monthly bank reconciliation to ensure the accuracy of financial records. Sequential numbering of

transaction documents is applied consistently to facilitate tracking and verification. A finance informant described the practice as follows:

"Every transaction must be checked by the person in charge before it is recorded, because we want to avoid differences between cash and the report. If the cash does not match the records at the end of the day, we look for the problem immediately."

These control activities have a direct and measurable effect on the reliability of financial reports. Daily cash reconciliation enables the detection of discrepancies before they accumulate into material errors, while authorization procedures ensure that no transaction enters the accounting records without prior review. Nisa and Susilo (2025) confirm that structured control activities contribute significantly to reducing recording errors and improving data accuracy. The practice observed at MFI Mitra Surya Sejahtera reflects a functional implementation of control activities that, despite the absence of sophisticated accounting software, succeeds in maintaining a reasonable level of recording accuracy through discipline and procedural consistency.

Information and Communication

The flow of information and communication at MFI Mitra Surya Sejahtera operates through regular coordination meetings and routine financial reporting cycles. Financial reports are prepared monthly and presented to management for evaluation and decision-making. Policy and procedure updates are communicated through direct briefings and written memorandums distributed to relevant staff. An operational staff member described how information reaches the field level:

"When there is a change in procedures, the supervisor tells us directly in the morning briefing. Sometimes there is also a written note posted in the office. We are expected to follow it from that day forward."

The timeliness and transparency of information flow at MFI Mitra Surya Sejahtera directly supports the quality of financial reports by ensuring that staff at all levels understand their recording responsibilities and are promptly informed of any procedural changes. Monthly report presentations to management create a structured accountability cycle that reinforces staff awareness of reporting standards. Raspati and Simanjuntak (2024) state that effective communication is a key component in ensuring that all organizational members understand their roles in the internal control process. The current communication practices at MFI Mitra Surya Sejahtera are adequate for the institution's scale, though the reliance on verbal briefings without systematic documentation of policy changes introduces a risk of inconsistent understanding among staff over time.

Monitoring

Monitoring at MFI Mitra Surya Sejahtera is carried out by management through direct supervision, surprise cash checks, and periodic evaluation of monthly financial reports. Transaction documents are regularly reviewed by the Operational Supervisor, and discrepancies are addressed directly with the relevant staff member. However, the institution does not have a dedicated internal audit function. The Director acknowledged this condition:

"We do the checking ourselves as management. There is no separate internal auditor yet because we are still small. The supervisor checks directly and reports to me."

While management-level supervision contributes to detecting procedural deviations, the absence of an independent internal audit function is a notable limitation that warrants critical attention. Monitoring conducted solely by management lacks the objectivity that an independent auditor would provide, since managers may be less inclined to report

weaknesses in systems they themselves designed or approved. This reduces the reliability of self-assessment and may allow persistent control gaps to go unaddressed. Putri et al. (2022) note that the absence of separate internal audit functions is common in small and medium-scale MFIs due to resource constraints, but caution that this condition increases institutional vulnerability to undetected errors and fraud. For MFI Mitra Surya Sejahtera, strengthening the monitoring component through periodic external review or the appointment of a part-time independent evaluator would significantly improve the objectivity and completeness of internal control assessment.

The Role of Internal Control System in Improving the Quality of Financial Reports

The findings of this study demonstrate that the internal control system at MFI Mitra Surya Sejahtera plays a meaningful role in improving financial report quality, particularly across three dimensions: reliability of financial information, recording orderliness and procedural compliance, and accountability and transparency.

Reliability of Financial Information

Transaction authorization and routine reconciliation procedures directly contribute to the accuracy and trustworthiness of financial information presented in reports. The finance department's practice of conducting daily cash reconciliation enables real-time detection and correction of discrepancies before reports are finalized. A bookkeeper informant explained:

"The reconciliation process is very helpful. Sometimes there is a difference of only a few thousand rupiah, but we still look for the source. If we let it pass, it will accumulate and the monthly report will not be clean."

This finding aligns with Bale et al. (2023), who confirm that structured internal control procedures improve the accuracy and reliability of financial information. The discipline with which reconciliation is conducted at MFI Mitra Surya Sejahtera, despite the manual recording environment, reflects a functional control activity that effectively supports the reliability dimension of financial report quality.

Recording Orderliness and Procedural Compliance

Internal control ensures that all transactions are recorded in a systematic and orderly manner consistent with established procedures. The requirement to use sequentially numbered transaction evidence enforces staff discipline in recording and creates an auditable trail for each transaction. The verification and authorization process adds an additional layer of assurance that transactions have been reviewed prior to entry. A field credit officer noted:

"Before a loan disbursement is recorded, it must be signed by the supervisor. We cannot just record it ourselves. This makes us more careful because we know it will be checked."

These findings support Dewi et al. (2021), who affirm that control activities such as verification and authorization are critical in maintaining consistency and compliance in financial recording. The authorization culture at MFI Mitra Surya Sejahtera effectively reduces the risk of unauthorized or incorrectly recorded transactions, contributing to the completeness and accuracy of financial reports.

Accountability and Transparency

Internal control strengthens the institution's accountability to members, management, and regulators. Monthly financial reports prepared on the basis of accurate and complete data allow stakeholders to evaluate institutional performance objectively. The Director described the institution's transparency commitment as follows:

"Every month we present the financial report to the supervisory board and the results are also communicated to members. We want members to trust that their funds are managed properly."

This practice reflects the accountability and transparency dimensions of financial report quality that are particularly significant in the MFI context, where member trust is central to institutional sustainability. Pratama et al. (2023) confirm that quality financial reports supported by strong internal control increase stakeholder trust in microfinance institutions. At MFI Mitra Surya Sejahtera, the integration of internal control with a culture of open reporting to members and regulators demonstrates that the internal control system functions not only as a technical mechanism but also as an institutional instrument for building and maintaining community trust.

Challenges, Limitations, and Recommendations

This study also identified several challenges in the implementation of internal control at MFI Mitra Surya Sejahtera. First, the limited number of employees results in suboptimal separation of functions, with some staff members handling multiple roles simultaneously, which increases the risk of both unintentional errors and potential fraud. Second, the predominantly manual recording system makes the reporting process more time-consuming and more susceptible to human error than a digital system would be. Third, the absence of a dedicated internal audit function means that monitoring relies entirely on management self-assessment, which limits the independence and objectivity of control evaluation.

These conditions are consistent with Putri et al. (2022), who note that small and medium-scale MFIs commonly face structural constraints in implementing ideal internal control due to limited human and financial resources.

To address these limitations within the operational scale of the institution, this study recommends several practical improvements. The institution should introduce a standardized transaction checklist to ensure that all required verification steps are completed before each transaction is recorded. Dual authorization should be applied for transactions above a specified monetary threshold to reduce the risk of unauthorized disbursements. Numbered receipt books with controlled issuance should be implemented to prevent document loss and duplication. Basic accounting software appropriate for small MFI operations should be adopted to reduce reliance on manual recording and minimize human error. A simple segregation of duties arrangement, such as separating the cashier and bookkeeper functions even within a small team, should be formalized. Finally, a periodic external review conducted by an independent party on a semi-annual basis would strengthen the objectivity of the monitoring function and compensate for the absence of an internal auditor.

CONCLUSION

This study concludes that the internal control system plays an important role in improving the quality of financial reports at MFI Mitra Surya Sejahtera. The five components of internal control, control environment, risk assessment, control activities, information and communication, and monitoring, have been implemented and contribute to the reliability, recording orderliness, and accountability of financial reports. The control environment formed through management's commitment to integrity and transparency encourages employee work discipline. Control activities such as transaction authorization, verification, and routine reconciliation help minimize recording errors and ensure data accuracy.

Information and communication that run routinely and monitoring by management support the preparation of financial reports that are more orderly and accountable.

However, this study also found several limitations in the implementation of internal control, including limited human resources, suboptimal separation of functions, and a recording system that is still simple. These limitations need to be addressed through efforts to strengthen human resource competencies, improve accounting systems, and add internal audit functions or external supervision. This research is expected to provide theoretical contributions in the development of micro-sector accounting literature, especially regarding the role of internal control in improving the quality of financial reports in microfinance institutions. Practically, the research findings can be input for MFI managers in strengthening internal control systems to produce reliable, transparent, and sustainable financial reports. For policymakers and regulators, this study can be a reference in formulating guidelines and assistance for microfinance institutions to improve the quality of financial governance.

For future research, it is recommended to conduct comparative studies between various types of microfinance institutions with different characteristics, as well as examine the role of technology and accounting information systems in supporting the implementation of internal control. In addition, quantitative research with a larger sample can be conducted to test the relationship between internal control effectiveness and the quality of financial reports more broadly. Efforts to strengthen internal control systems, through improvement of standard operating procedures, improvement of human resource competencies, and improvement of recording systems, become strategic steps to maintain stakeholder trust and support transparent and accountable financial governance.

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