

Effect of Weaknesses of the Internal Control Systems And Non-Compliance With Statutory Provisions on The Audit opinion of The Audit Board of The Republic of Indonesia

Hari Setiyawati

Faculty of Economics and Business Mercu Buana University – Indonesia

ABSTRACT

The purpose of this study was to see whether there is an influence of Weaknesses of the Internal Control System and Non-compliance With Statutory Provisions on the audit opinion of the audit board. The weakness of the internal control system measured by the audit findings Audit Board consisting of weaknesses of the accounting control system and reporting, and weaknesses of the budget implementation control system and weaknesses of the internal control structure. While non-compliance with statutory provisions are measured based on the audit findings Audit Board consisting of local loss, the potential loss of local , lack of receipt, administration, waste, inefficiency and ineffectiveness. This study is a survey of the region of the provincial government of DKI Jakarta and Banten for 2010 to 2014. Samples in this study were all the Local Government Unit that generate financial reports of local governments totaling nine units, so this study is census research, in the sense that the entire population sampled. Data analysis method used is the ordinal logistic regression because the dependent variable is the rank (category) and the data is not normal. From the results of the data analysis and discussion, it can be concluded that the weaknesses of the internal control system and non-compliance with statutory provisions affect the audit opinion of the audit board either jointly or partially.

Keywords: The Weakness of The Internal Control System , Non-compliance With Statutory Provisions and The Audit Opinion.

I. INTRODUCTION

One way of preventing the occurrence of corrupt practices is the development of a good accounting system by the government and control of the quality of the financial information of government agencies (SPKN, 2007). In Indonesia, the country's financial management reform was marked by the implementation of Law No. 17 of 2003 on State Finance, Law No. 1 of 2004 on State Treasury, and Law Number 15 Year 2004 concerning the Management and State Financial Accountability and its supporting regulations. Package legislation illustrates the seriousness of the ranks of the government and Parliament to improve the management, record keeping, accountability, and audit of government financial management both at central and local levels.

In connection with the audit of the management and financial responsibility of the state, in Article 9, paragraph (1) of Law No. 15 of 2004 states that in conducting audit of the management and financial responsibility of the state, the Audit Board can utilize the audit results of the Government Internal Control Apparatus (APIP). Although there is no obligation to implement the APIP reviews the financial statements before submission to the Audit Board to be audited, but until now, the implementation of Review is apparently still not fully able to improve the quality of government

financial reports. It is evident there are many government financial statements both at the ministerial level and at the local level are still getting disclaimers from Audit Board (Wahyudi, 2010). Poor local government financial reporting, as we said above is a phenomenon that occurs in Indonesia today.

Results of the Audit Board of the Republic of Indonesia on Local Government Finance Statement (LGFS) in 33 provinces in Indonesia are presented in three categories namely the opinion, the internal control system and compliance with statutory provisions. Currently the development of the quality of financial reporting and accountability for LGFS not as expected. This can be seen from the opinion LGFS given by the Audit Board of the Republic of Indonesia still have to get a disclaimer opinion . Government is obliged to exercise control over the implementation of the activities of government to achieve a state financial management effectively, efficiently, transparent and accountable. Internal control on local governments is designed based on the Government Regulation Number 60/2008 concerning the Government Internal Control System (GICS). Internal control is a process that is influenced by the leadership of the organization, management, and other personnel designed to provide reasonable assurance that organizational objectives will be achieved.

Rizal Yaya (2007), suggests that the low levels of accountability in financial management by local governments, which means the public can not fully trust the financial information presented by the local government in the financial statements. Furthermore, the Vice Chairman of the Audit Board Zainie Abdullah (2008), states that the local financial management and the local financial responsibility is still unsatisfactory because it is not transparent and accountable, and still many irregularities over use of public funds. These conditions illustrate that the quality of financial information, particularly those presented in LGFS not fully meet the qualitative characteristics of financial statements in accordance with Government Accounting Standards (GAS). This is not because of an opinion as a professional statement as examiner conclusions regarding the reasonableness of the level of information presented in the financial statements (Article 1 of Law No. 15 of 2004). In addition to the above opinion contains, each the Audit Board Audit result on LGFS also contains any suggestions for improvements based on the problems identified, either associated with the weakness of the internal control system and non-compliance with Statutory Provisions. With the Audit Board submitted improvement suggestions are expected to improve the quality of the presentation of information in LGFS which in turn will increase the acquisition LGFS opinion.

Based on the phenomenon that has been described above, the formulation of the problem in this study is: Does the weaknesses of the internal control system and non-compliance with Statutory Provisions affect the audit opinion of the Audit Board of the Republic of Indonesia? This study aims to identify and analyze the influence of the weaknesses of the internal control system and non-compliance with the statutory provisions on the Audit Board of the Republic of Indonesia. The usefulness of this study are:

1. Contributed to the development of science in order to support or supplemented the existing theories related to the accounting science and in particular public sector accounting and internal auditing.
2. For practitioners in the governmental accounting as the ideas contribution and references solving problems related to the implementation of accounting in local government.

II. LITERATURE, THEORITICAL FRAMEWORK AND HYPOTHESES

2.1. LITERATURE

2.1.1. The Internal Control System

Definition of Internal Control has undergone changes both in concept and components

in accordance with the development of increasingly complex business world. In the early development of internal control is defined as an internal check. Internal checks with the concept of similarity results through matching records from two or more parts. As revealed Certified American Institute of Public Accountants (AICPA) quoted Moener & Witt (1999; 81), the definition of internal control as follows: "Internal control comprises the plan of organization and an of the coordinate methods and measures adopted within a business to safeguard its assets, check the accuracy and reliability of its accounting data, promote operational efficiency, and encourage adherence to prescribed managerial policies"

Broader understanding of the internal controls put forward by Konrath (2002: 205), citing the AICPA Professional Standards, Internal Control defines as follows: "The process effected by an entity's board of directors, management, and other personnel designed to provide reasonable assurance regarding the achievement of objectives in the following categories: (a) operations control-relating to the effective and efficient use of the entity's resource; (b) financial reporting controls-relating to the preparation of reliable published financial statements; and (c) compliance controls-relating to the entity's compliance with applicable laws and regulations.

From the definition presented earlier, explained that internal control is a process that is run by a board of commissioners are intended to provide reasonable assurance about the achievement of the control objectives of effective and efficient operations, reliability of financial reporting, and compliance with applicable laws and regulations. Subsequent developments in 1992 the Committee of Sponsoring Organizations (COSO) of the Treadway Commission published a report entitled Internal Control-Integrated Framework. In the COSO are the representatives of the AICPA, the American Accounting Association, Institute of Internal Auditors, Institute of Management Accountants, and the Financial Executive Institute. Report consists of four volumes: (1) Executive Summary; (2) Framework; (3) Evaluations Tools; and (4) Reporting to external Parties.

COSO Report (1992, 912) also emphasizes that the fundamental concept is expressed in the following definition: a) Internal control is process. It is a means to an end, not an end itself. It consists of a series of actions that are pervasive and integrated with, not added onto, an entity's infrastructure. b) Internal control is effected by people It is not merely a policy manual and forms, but people at every level of an organization, including the board of directors, management, and other personnel c) Internal control can be expected to provide only reasonable assurance, not absolute assurance, to an entity's

management and board because of limitations inherent in an internal control systems and the need to consider the relative costs and benefits of establishing controls. d) Internal control is geared to the achievement of objectives in the overlapping categories of financial reporting, compliance, and operations.

Internal Control includes five basic components of management policies procedures designed to provide reasonable assurance that a certain company goals are met. Arens (2006; 273) argues that: Internal control includes five categories of controls that management design and implements to provide reasonable assurance that management's control objectives will be met. These are the five components of internal control and are: (1) Control Environment, (2) Risk Assessment, (3) Information and Communication, (4) Control Activities, (5) Monitoring.

2.1.2. Non-Compliance With The Statutory Provisions

In every organization, both public and private sectors, the management is responsible for every activity carried out goes according to / comply with applicable laws and regulations (Ganahadisurya). In general, public sector entities is subject to the legislation, laws and regulations than private sector organizations. Legislation, laws, regulations, and other authorities that applied to public organizations can be either the statute (/ regulation / law that created / compiled to run an organization) to the administrative requirements and detailed guidance. Structure of the legislation / laws / regulations are the basis for the legislature to control the sources and allocation of funds, as well as the use of state resources. A legislation / law may provide administrative and financial authority wide / over to the government, ministers, agencies, and companies to develop / establish rules that must be obeyed by the entity concerned. These regulations hierarchically under the legislation / the law and must be in accordance / compliance with the direction, conditions, and restrictions set by legislation / the law. In SPKN stated that the examiner should design the audit to provide reasonable assurance to detect material misstatements caused by non-compliance with statutory provisions that direct and material effect on the financial statements. Furthermore, to ensure that the examiner has conducted tests of compliance, SPKN requires that the audit result report on the financial statements should be disclosed that the examiner has conducted tests of compliance with statutory provisions that direct and material effect on the financial statements.

Laws and regulations affecting the Audit Board opinion is simply non compliance with

statutory that related with the financial statement presentation. Thus not all deviation from the statutory provisions into consideration in granting the audit board opinion.

2.1.3. The Opinion Of The Audit Board Of The Republic Of Indonesia

An opinion as the professional statements regarding the fairness of financial information presented in the financial statements based on the criteria of (i) compliance with governmental accounting standards, (ii) the adequacy of disclosure, (iii) compliance with statutory provision, and (iv) the effectiveness of internal control systems.

There are four (4) types of opinions to be given by the auditor, namely (i) an unqualified opinion, (ii) a qualified opinion, (iii) an adverse opinion, and (iv) a disclaimer. Explanation for any kind of opinion are as follows:

- a. Unqualified opinion states that the financial statements have been presented and disclosed appropriately and fairly, in all material respects. In other words, the financial information presented and disclosed in financial statements can be used by users of financial statements. This is the opinion expressed in the form of standard Audit Reports on Financial Statements.
- b. Qualified opinion states that the financial statements have been presented and disclosed appropriately and fairly, in all material respects, except for the effects of matters relating to the excluded. In other words, the financial information presented and disclosed in financial statements "are not excluded in the auditor's opinion" can be used by users of financial statements.
- c. Adverse opinion states that the financial statements are not fairly presented and disclosed and sufficient, in all material respects. In other words, the financial information presented and disclosed in financial statements can not be used by users of financial statements; and
- d. Disclaimer, rejecting an opinion stating that the financial statements can not be checked in accordance with auditing standards. In other words, the auditor can not provide assurance that the financial statements are free of material misstatement. Accordingly, the financial information presented and disclosed in financial statements can not be used by users of financial statements.

2.2. Theoretical Framework

In addition to the opinion contains LGFS, each the Audit Board Audit Result on LGFS also contains any suggestions for improvements based on the problems identified, either associated with the

weakness of the internal control system and non-compliance with statutory provision.

Hiro Tugiman, 2000) argue that the audit of the financial statements of local governments (LGFS) is intended to provide reasonable assurance that the financial statements comply with government accounting standards (SAP), laws and regulations, and internal control where the audit is done in order to create public accountability more transparent and accountable. Furthermore, he stated that the government accountability be seen from the given the Audit Board opinion on the financial statements were audited. Research conducted by Hottua and Siti Khairani (2013) showed that there was a decrease in the opinion given by the Audit Board on the Financial Statements of the Local Government Empat Lawang caused the weakness / material errors effectiveness of internal control systems, compliance to statutory provision and accordance to Financial statement presentation with Government Accounting Standards. The linkage between the weakness of the internal control system , non-compliance with statutory provisino and the opinion of the audit board of the Republic of Indonesia can be described as follows:

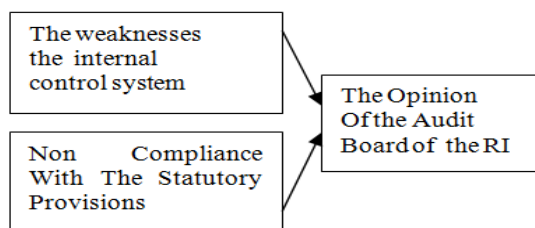


Figure 1 Theoretical Framework

2.3.Hypothesis

Based on the theoretical framework that has been stated previously, it can be compiled following research hypothesis:

H1: The weaknesses of the internal control system affect on the opinion of the Audit Board of the Republic of Indonesia

H2: Non-compliance with the statutory provisions affect on the opinion of the Audit Board of the Republic of Indonesia

III. METHODS

This research is exploratory study with the type of studies investigating causal (causal study) where the researchers want to find the cause of one or more problems (Uma Sekaran, 2007). This research tested the effect of the weaknesses of the internal control system and non-compliance with the statutory provisions on the opinion of the Audit Board of the Republic of Indonesia. The study population was all local governments in Indonesia, which consists of 33 provinces. Sampling was done by using purposive sampling is the local

government of Banten provincial and DKI Jakarta sampled. Researchers took samples in both provinces due DKI until 2014 had never obtain Unqualified Opinion whereas only Tangerang at the Banten province who obtained Unqualified Opinion (either city, district and South Tangerang). Observation period of the study was conducted from 2010-2014. Methods of data analysis used in this study is Ordinal Logistic Regression because of the dependent variable used in this study is the rating (category) and the data is not normal.

IV. DISCUSSION

The discussion is carried out referring to the hypothesis stated above. Based on the results of hypothesis testing using the parameter estimates, the X1 variables is the weakness of internal control system has a significance level of 0.028 or below 0.05 then it can be concluded that the weaknesses of internal control system affect on the opinion of the Audit Board of the Republic of Indonesia. This is consistent with the results of the Audit Board of the Republic of Indonesia on Local Government Finance Statement that one of the bases to provide an opinion is the effectiveness of the internal control system. In other words, the more effective internal control system on Local Government Unit then the better the Opinion of the Audit Board of the Republic of Indonesia. So the weaknesses of internal control system affect on the audit opinion of the Audit Board of the Republic of Indonesia. Therefore, the government has issued Government Regulation No. 60 / 2008 about of the Government Internal Control System which requires each reporting and accounting entities to conduct Internal Control System in accordance with the provisions of relevant laws and regulations.

The results of hypothesis testing using the parameter estimates for the X2 variable is non-compliance with the statutory provisions have 0.026 or below the level of significance of 0.05, it can be concluded that non-compliance with statutory provisions have an influence on the opinion of the Audit Board of the Republic of Indonesia. This is consistent with the results of the Audit Board of the Republic of Indonesia on Local Government Finance Statement that one of the bases to provide an opinion is the compliance with statutory provisions. Based on the IHPS the Audit Board of the Republic of Indonesia the second semester of 2013, the case for non-compliance with statutory provisions is increasing every year as stipulated in the background of this research. The impact of this case is the audit opinion of the Audit Board of the Republic of Indonesia on the Local Government Financial Statements throughout Indonesia just a little gain unqualified opinion or a 91% gain bad opinion.

V. FIGURES AND TABLES

6. Conclusion And Implications

6.1.CONCLUSION

Based on the analysis of the results and discussion presented above we can conclude the following things: 1.The Weaknesses of internal control systems on the reporting and accounting entity's in the local government influence on the Audit opinion of the Audit Board of the Republic of Indonesia. 2. Non-compliance with the statutory provisions on the reporting and accounting entity's in the local government influence on the Audit opinion of the Audit Board of the Republic of Indonesia.

6.2. Implications

The results of this study may have implications for government leaders that responsible for local government financial statements, in particular heads of agencies Local Government Unit in order to tighten the implementation of the internal control system in accordance with Regulation 60 / 2008 about of the Government Internal Control System. In addition, follow-up on audit findings of the Audit Board of the Republic of Indonesia related with cases of non-compliance with the statutory provisions. Follow-up of the audit findings Audit Board of the Republic of Indonesia findings should be done as quickly as possible.

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