

Internal Audit: Its Implications To Good Corporate Governance (GCG) In PT. Telekomunikasi Indonesia

Judith T. G. Sinaga¹ and Daniel Nicson Simanjuntak²

¹Universitas Katolik Parahyangan

²Universitas Kristen Maranatha

Abstract

The study aims to know the implications of audit internal to good corporate governance. It is known that audit internal plays a vital role in every entity or an organization. Audit internal helps achieve organizational objectives while good corporate governance emphasizes on how performance is monitored and optimized. This paper used descriptive method wherein data were gathered through questionnaires. Research questionnaires were distributed to 20 respondents who were working in Internal Audit Unit of PT. Telekomunikasi Indonesia. Internal audit as the independent variable has four (4) indicators, independence, professional competence, scope of work, and Implementation of audit activities. Good corporate governance as the dependent variable has four (4) indicator, these are, fairness, transparency, accountability, and responsibility. Data gathered were processed and concluded. Based on the result of the research, it is known that internal audit is related to good corporate governance with an $r = 0.661$, this means that the relationship of both variable is strong and positive. It is also known that audit internal affects good corporate governance with an $\alpha = 5\%$, it is known that it affects significantly. Also, the result shows that t_{value} of 3.574 is $>$ $t_{\text{table value}}$ of 1.734, which is means that H_0 is rejected.

Keywords: audit internal, good corporate governance, optimized, accountability

INTRODUCTION

At present, business world and economy is improving and developing so rapidly, and this includes Indonesia's government-owned business, or the so-called *Badan Usaha Milik Negara* (BUMN). BUMN (government-owned business) is a unit wherein the whole capital is subsidized by the government. Its purpose is to produce products or services for the people to live a prosperous life. Indonesia is expeting BUMN to boost the economy by increasing the revenue of the nation. Each BUMN is oblige to manage business applying the principles of Corporate Governance. Corporate governance and business has become the focus for the 21st century (Indermun and Bayat,2015).

Corporate governance is a way to control, evaluate, and monitor the performance of business. It guides the company to create value added and to take notice the stakeholders' interests. In the aftermath of corporate scandals and the global financial crisis, corporate governance has received significant attention from regulators and the public (Soh & Bennie,

2011). The governance structure shows how rights and responsibilities are shared among various stakeholders who are concerned with the operations of the organisation (Zvavahera & Ndoda, 2014). Corporate governance gives positif effect to the continuance of the business, whether it is governmentowned or privately owned companies. BUMN can achieve optimal performance if it is manage well, it it has a Good Corporate Governance. Well governed organisations perform better thus, emphasizing the need for good corporate governance (Miring'u and Mouria, 2011; Bebhuck et al, 2004). On the other hand, bad corporate governance has proven to lead to collapse of state enterprises (Kyerbaah and Biekpe, 2006). To avoid bad corporate governance, there is a need for internal audit to help management monitor the performance of every business. The presence of internal audit is critical to effective corporate governance (Elder, 2008), since the personnel doing the audit spend all of their time within one company and have much knowledge about the company's operations and internal controls.

Internal audit is very important to assist

management in their responsibilities through evaluating, analyzing, giving recommendation and comments that are objective. The importance of the internal audit function and its ability to contribute towards quality performance, through its oversight role, its improvements to the control and monitoring environment and its potential to mitigate fraud risk (Beasley et al, 2000; Coram et al, 2008).

The Board of Financial Accountability or *Badan Akuntabilitas Keuangan Negara* (BAKN), reported that in 2013 there are cases that shows financial deviation of government-owned companies. It indicated that BUMN were not able to manage well or can be considered as not implementing good corporate governance. There were 510 companies with cases on financial fraudulent reporting, of which, 234 cases involved the weak in internal control and the 276 cases pertained to noncompliance to government regulations.

In an effort to implement corporate governance, the role of internal audit is very important. Internal audit acts independently in controlling the company and ensure that the company had executed the principles of good corporate governance.

REVIEW OF RELATED LITERATURE

Internal Audit: Functioning Well or Not?

Most companies nowadays are relying on the work of the internal audit in evaluating effectiveness and efficiency of the operations, both financial and nonfinancial. According to Institute of Internal Auditors as cited by Boynton & Johnson (2006:985) "Internal audit is defined as an independent, objective assurance and consulting activity designed to add value and improve an organization's operations.". It is likely that internal audit helps management of a certain company to accomplish objectives or achieve goals. Internal audit, as emphasized by Pickett (2005:46) "should be professional, independent and resourced to perform to the professional standards enshrined in the new focus on risk management, control and governance; with a good balance of assurance and consulting effort." It is observed that internal audit adheres to the professional standards in order to produce reports that are reliable and credible. Internal monitoring is usually done by the internal audit.

It is one of the many functions of of internal audit.

Nevertheless, its primary function is to check the effectiveness and efficiency of business performance. Studies showed that CEOs in Malaysia were generally more positive in their perceptions of internal audit being an independent reviewer of the effectiveness and efficiency of firm's operations (Johl et al, 2013). Internal audit is also effective in fraud prevention. Salameh, et al (2011) shared that internal audit units are perceived effective in fraud prevention. Internal audit also detects fraud committed by the the top management. The study surprising result is that internal audit units may fear from retaliation when reporting fraud related to top management, however, this may result in weak independence and objectivity of internal auditors (Salameh et al, 2011). But then internal audit roles are changing as demonstrated by the recent studies by (Gramling et al, 2004; Carcello et al, 2005; Sarens and Da Beelde, 2006; Cohen et al, 2010) have reported significant changes in the role of internal audit function as a result of recent regulatory reforms in the USA, the UK and Australia. The result of the study suggests significant expansion and refocus of the roles of IA and perceptions of its effectiveness (Soh & Bennie, 2011). Elder et al (2008:836) mentioned that "internal auditing is expected to provide value to the organization through improved operational effectiveness, while also performing traditional responsibilities, such as reviewing the reliability and integrity of information, ensuring compliance with policies and regulations, and safeguarding assets." Internal auditors are guided by ethical principles and rules of conduct.

Corporate Governance: Good or Bad

Why business scandals happened? Major corporation collapsed because of mismanagement by the top executives. Businesses major motive is to operate the business and have profit. Stakeholders' aim is to establish a good corporate governance and in order to achieve it, good corporate governance must be practiced. Corporate governance refers

to the way organizations are regulated and governed (Zvavahera & Ndoda, 2014). Corporate governance can raise many strategic and policy issues which might need the intervention of management (Harvard Business Review, 2000). Corporate governance is about the way power is exercised over corporate entities ((Indermun and Bayat, 2015). Good corporate governance is about exhibiting ethical behaviour on all business dealings and also take good care of its employees' welfare by providing good working conditions and good salaries (Zvavahera & Ndoda, 2014).

A good government should run the government openly so that all interested parties in the government can actively participate, the state administration should be conducted in a transparent and implementation of the government must be accountable (Rahmawati, 2015). The study found that top management, and the Board were corrupt (Zvavahera & Ndoda, 2014). In a research that was carried in US companies by Kaplan (2012) it was found that CEOs were overpaid yet their organisations under performed. What was most disturbing was that top management was not penalised for the poor performance.

According to Indermun and Bayat (2015), "Corporate governance lies at the very heart of the way businesses are run. The extent to which business decisions reflect values and principles is a key to long term success."

There was lack of accountability and transparency in the way business was being done(Zvavahera & Ndoda, 2014). Weaknesses in governance mechanism cause losses to public enterprises so the culprits should not be spared (The Financial Express, 2015). Bad corporate governance leads to problems of mismanagement, pilferage, red tape, wastage, unreliable services and other operational inefficiencies (Zvavahera & Ndoda, 2014).

According to the OECD Principles on Corporate Governance (2004), responsibilities of the board are spelt as follows:

1. Operations of the organisation need to be above board.
2. The board needs to endorse the strategic vision of the organisation.
3. The growth and expansion of business needs approval of the board.

4. Salaries for senior management need to commensurate with experience and qualifications.

5. Human resources planning is critical for long-term survival of the organisation.

6. Top management salaries should be aligned to performance and long term objectives of the organisation.

7. The board has to be composed of people with relevant exposure and qualifications. 8.

Periodical financial reporting is critical.

9. Internal control systems are a pre-requisite.

10. Disclosure of financial and non-financial information to stakeholders are important.

11. The constitution of various committees to oversee operations of various business units is also desirable. Those are the guiding principles to make a governance good. Principles mentioned need to be properly executed in order for the organization attain such goal or objective.

The Effect of Internal Audit to Corporate Governance

The results of this study concluded that the existence of an internal audit encourage the achievement of implementation of good corporate governance (Rahmawati,2015). Internal audit function having an active role in corporate governance is significantly and positively associated with the use of riskbased audit plan, existence of quality assurance and improvement program, and audit committee input to the audit plan (Sarens et al, 2012). Internal audit can support Good Corporate Governance in local government (Rahmawati,2015). Regulatory responses have focused on increasing disclosure requirements relating to corporate governance and this has, in turn, driven increased awareness and demand for internal assurance on corporate governance processes, including internal control and risk management. Given its unique position within the organization, the internal audit function is well placed to provide this assurance and is an integral component of the corporate governance mosaic (Soh & Bennie, 2011). Internal audit is

in integral part to good corporate governance.

internal audit to corporate governance in PT. Telekomunikasi Indonesia.

Statement of the Problem

METHODOLOGY

The method used in this study is descriptive. Questionnaires were distributed to Internal Audit Unit, Finance Department, and top management of PT. Telekomunikasi Indonesia. Likert scale was used to measure each indicator of internal audit and corporate governance. Indicators for Internal Audit are independence, professionalism, scope of work, and audit activity implementation, while indicators for Corporate Governance

Hypothesis

Ha : Internal audit has an effect to corporate governance.

Ho : Internal audit has no effect to corporate governance.

RESEARCH RESULTS, INTERPRETATION, AND ANALYSIS

a. Internal Audit Function in PT. Telekomunikasi Indonesia

This study will answer the following questions:

1. Is internal audit functioning well in PT. Telekomunikasi Indonesia?
2. Is corporate governance well implemented in PT. Telekomunikasi Indonesia?
3. What is the effect of internal audit to corporate governance in PT. Telekomunikasi Indonesia?

Fairness, transparency, accountability, and responsibility. There were 20 respondents as the sample and these respondents represent individual who understand how internal audit and corporate governance are implemented. Data collected are being processed and analyzed. For statistical analysis, the researcher analyzed coefficient of correlation and t-test for hypothesis testing.

The role or the function of internal audit is indeed important to every entity. The internal audit of PT. Telekomunikasi Indonesia functions well as evidence by implementing standard operating procedures (SOP) and the result of each indicator (Independence, Professionalism, Scope of work, and Audit activity below: implementation) as shown in Table 1.

Purpose of the Study

The purpose of the study is to know the effect of

Table 1- Percentage of Respondents Answer –Internal Audit

No	Indicator	Score of Respondents' Answer					n (%)
		A (%)	O (%)	S (%)	AN (%)	N (%)	
1	Independence	(67,5 %)	(10%)	(22,5 %)	(0)	(0)	(100%)
2	Professionalism	(34%)	(40%)	(19%)	(7%)	(0)	(100%)
3	Scope of work				(0)		(100%)

		(44%)	(36%)	(20%)	(0)	(0)	(0)
4	Audit activity implementation	(25%)	(54%)	(21%)	(0)	(0)	(100%)

Always (A), Often (O), Sometimes (S), Almost Never (AN), N (Never)

Internal audit functions independently that this department is not influenced by any other decision maker. Internal audit do the job with full of responsibility, and objectivity. With a 67.5% result, this shows that Independence is always practice in the company. The second indicator, Professionalism shows 40% as the highest result, which means, it is often practice while executing the audit. Internal audit personnel possess knowledge and skills. Internal audit also assures the audit is being supervised, that internal audit abide with Internal Audit Standards, internal audit personnel are competent in terms of written and verbal communications, and participate in seminars, and training to improve technical competence. Scope of work indicates a 44%, the work given were always done properly by

the Internal audit; and Audit activity are implemented oftentimes, 54% falls on the category often. This means that internal audit oftentimes review the reliability and integrity of financial information, review the system regarding rules & regulations, policies and procedures, review the method to protect assets and to assess the result of work, operation or program if it is in accordance with the set plans.

b. Corporate Governance in PT. Telekomunikasi Indonesia

PT. Telekomunikasi Indonesia is stipulated in BoD Decree No.29/2007 and committed to implement good through the strengthened by the Guidance Group GCG policies on the implementation of GCG as No.602/2011.

Tabel 2- Percentage of Respondents Answer – Good Corporate Governance

No	Indicator	Score of Respondents Answer					n (%)
		A (%)	O (%)	S (%)	AN (%)	N (%)	
1	Fairness	(44%)	(43%)	(13%)	(0)	(0)	(100%)
2	Transparency	(72%)	(20%)	(8%)	(0)	(0)	(100%)
3	Accountability	(59%)	(37%)	(4%)	(0)	(0)	(100%)
4	Responsibility	(40%)	(60%)	(0)	(0)	(0)	(100%)

Table 2 represents the result of respondents' answer for Good Corporate Governance (GCG) with indicators Fairness, Transparency, Accountability, and Responsibility. PT.

Telekomunikasi Indonesia always practice Fairness as evidence by 44%. This indicates that the company proportionately shares dividend to the stockholders. The company operates in

accordance with the rules and regulation to protect the stockholders. The company offers equal opportunity to all stockholders, and the company follows the policies on compensation, compensating the performance of the employee according to their achievements. The result showed 72% for always, which means that the company is transparent in terms of preparing financial report, policies are well communicated, the company disclosed their vision, mission, objectives, and other important matters that influences the company. In addition to that, those who are financially interested with financial statements can obtain copy and read by themselves. For Accountability, it shows 59% for always. This indicates that every department is capable of

being accountable. Every employee is guided with job description and clear procedures. The function of internal audit boosts the Internal Audit Department. Employees are accountable towards objectives and authority given by the management. The company practice reward and punishment system. The last indicator, Responsibility shows 60% for oftentimes. This indicates that the company manages to care for what the community and its environment needs. Based on the statistical analysis, the correlation coefficient is 0.661, which means that the relationship of Internal Audit and Good Corporate Governance in PT. Telekomunikasi Indonesia is strong and positive as shown in Table 3 below.

The Effect of Internal Audit to Good Corporate Governance in PT. Telekomunikasi Indonesia

Table 3 – Result of Correlation Coefficient
Correlations

			Audit Internal	Good Corporate Governance
Spearman's rho	Audit Internal	Correlation Coefficient	1.000	.661**
		Sig. (2-tailed)	.	.001
		N	20	20
	Good Corporate Governance	Correlation Coefficient	.661**	1.000
		Sig. (2-tailed)	.001	.
		N	20	20

** . Correlation is significant at the 0.01 level (2-tailed).

Table 4 below proved that the Telekomunikasi Indonesia is significant at effect of Internal audit in PT. a significance level of 5%. This indicates that Ho is rejected and Ha is accepted having t_{value} of $3.574 > t_{table}$ 1.734.

Table 4 – Result of Significance Test

Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	42.035	7.210		5.830	.000
Audit Internal	.413	.115	.644	3.574	.002

a. Dependent Variable: Good Corporate Governance

CONCLUSION

From the data that have been gathered, processed, and analyzed, it is therefore concluded that internal audit in PT. Telekomunikasi Indonesia had followed the standard operating procedures (SOP) in doing the audit as represented by the indicators, independence, professionalism, scope of work, and audit activity implementation. Internal audit is functioning well and programs are well executed. PT. Telekomunikasi Indonesia is committed to implement good corporate governance. The indicators of good corporate governance are fairness, transparency, accountability, and responsibility. Internal audit plays a vital role to good corporate governance thus the internal audit has significant effect to good corporate governance at a significance level of 5%, or an $\alpha = .05$. The result showed that the company must involve internal audit in pursuant to good corporate governance.

REFERENCES

Beasley, M.S., Carcello, J.V., Hermanson, D.R., and Lapedes, P.D. (2000). "Fraudulent financial reporting: consideration of industry traits and corporate governance mechanisms". *Accounting Horizon*. Vol 14, No 4, pp.441-54.

Bebchuck, L., Cohen, A. and Ferrel, A. (2004). What matters in the corporate governance. *Working Paper*. Harvard Law School, Cambridge, MA.

Boynton, William C., Johnson, Raymond N.(2006), *Modern Auditing: Assurance*

Services and the Integrity of Financial Reporting.

John Wiley & Sons, Inc.

Carcello, J.V., Hermanson, D.R., and Raghunandan, K. (2005), "Changes In internal auditing during the time of the major US accounting scandals", *International Journal of Auditing*, Vol. 9 No. 2, pp. 117-27.

Cohen, J., Krishnamoorthy, G. And Wright, A. (2010), "Corporate governance in the post Sarbanes-Oxley era: auditor's experiences". *Contemporary Accounting Research*. Vol 27 No 3, pp 751-86.

Coram, P., Ferguson, C., and Moroney, R. (2008). "Internal Audit, alternative audit structures and the level of misappropriation of assets fraud". *Accounting and Finance*. Vol 48, No. 4, pp.1-17.

Gramling, A.A., Maletta, M.J., Schneider, A., and Church, B.K. (2004), "The Role of the internal audit function in corporate governance: a synthesis of the extant of internal auditing literature and directions for future research", *Journal of Accounting Literature*, Vol 23, pp.194-244.

Harvard Business Review, HBR (2000). *HBR on Corporate Governance*. Harvard Business School Press. ISBN1-57851-237-9.

Indermun and Bayat. (2015). A Focus on Corporate Governance and the relationship with Business , *Bus EcoJ*.6:1http://dx.doi.org/10.4172/2151-6219.1000137.

Johl, K. S., Kohl, K. S., Subaraiman, N., and

- Cooper, B.(2013). Internal audit function, board quality and financial reporting quality: evidence from Malaysia. *Managerial Auditing Journal* Vol. 28 No. 8 pp 780-814.
- Kaplan, S. N. (2012). Executive Compensation and Corporate Governance in the U.S.: Perceptions, Facts and Challenges University of Chicago - *Booth School of Business; National Bureau of Economic Research (NBER)*.
- Kyereboah-Coleman, A. and Biekpe, N. (2006). *Corporate governance* .Vol. 6. No. 5 Emerald Group Publishing Limited, South Africa.
- Miring'u, A.N. and Muoria, E.T. (2011). An analysis of the effect of Corporate governance on performance of commercial state Corporations in Kenya. *International Journal of Business and Public Management* Vol. 1 No.1 pp 36-41.
- OECD (2004) *Principles of Corporate Governance* Paris: OECD <http://businessdaily.co.zw/indexid-national-zk-32889.html#sthash.A9PHCPEp.dpuf>
- Pickett, K. H. S. (2005). *THE ESSENTIAL HANDBOOK OF INTERNAL AUDITING* Published in 2005 by John Wiley & Sons Ltd, The Atrium, Southern Gate, Chichester, West Sussex PO19 8SQ, England.
- Rafat Salameh, R., Al-Wesbah, G., Al-Nsour, M., Al-Hiyari,A.(2011). Alternative Internal Audit Structures and Perceived Effectiveness of Internal Audit in Fraud Prevention Evidence from Jordanian Banking Industry. *Canadian Social Science*, Vol.7, No.3, 2011, pp 40-50.
- Rahmawati, A. (2015). Effect of Performance Audit implementation of good corporate governance in Kab. Luwu (Case Study Inspectorate Kab. Luwu).*Journal of Economics and Behavioral Studies*, Vol.7, No. 1, pp.13-19. (ISSN:2220).
- Sarens,G., Abdolmohammadi, M.J., Lenz, R.(2012). Factors associated with The internal audit function's role in corporate governance. *Journal of Applied Accounting Research*, Vol. 13 Iss 2 pp.191-204.
- Sarens, G., De Beelde, I., and Everaert, P. (2009), "Internal audit: a comfort provider to the audit committee", *The British Accounting Review*, Vol. 41 No 2, pp.90-106.
- Soh, D.S.B, and Martinov-Bennie,N.(2011). The internal audit function: Perceptions of internal audit roles, effectiveness and evaluation. *Managerial Auditing Journal*, Vol. 26 Iss 7 pp. 605-622. *The Financial Express* [Dhaka] 06 June 2015. Corporate governance: Vital aspects and reality.
- Zvavahera, P. and Ndoda, G. R. (2014). Corporate governance and ethical behavior: The case of the Zimbabwe Broadcasting Corporation. *Journal of Academic and Business Ethics*, Vol 9. Pp.1-8.