

ANALYSIS OF EFFECTIVENESS OF INTERNAL MONITORING AND CONTROL INSTITUTION OF LPD IN BALI PROVINCE, INDONESIA

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Abstract

This research aims to study on the effectiveness of monitoring institution as LPD internal auditor and to study on the effectiveness of implementation of LPD internal control in Bali Province. The Monitoring Institution in LPD serves a great important role to monitor on the LPD operational activity and assess on the effectiveness of implementation of internal control. Population in this research is LPD in Bali province, by 1.468. Samples by 302 are LPD chairmen as the respondents. Data is collected by questionnaires based on likert scale. Data analysis technique is qualitative descriptive analysis. Results of the analysis, it is known that the effectiveness of LPD Monitoring Institution in Bali Province is namely by 4,61% in very effective criteria , 26,97% in effective criteria, 40,79% in quite effective criteria, 18,42% in less effective criteria and 9,21% in ineffective criteria, There is 7,89 % Effectiveness of internal control with very effective criteria, 44,74%, effectiveness with effective criteria, 32,89% effectiveness with quite effective criteria, 11,84% effectiveness with less effective criteria, and 2,63 % effectiveness with ineffective criteria.

Keywords: Effectiveness, internal monitoring, control institution, rural credit institution, LPD

INTRODUCTION

Rural credit institution (LPD) is a non-bank financial institution in Bali Province, Indonesia. As referred to by LPD in regulation of I level regional government of Bali number 2 of the year 1988 is a rural institution with operational unit has a function as a place for rural treasurers in the forms of money or other securities. LPD provides similar services to any services provided by other financial institutions such as saving and loan cooperative, rural credit bank and others.

There is a complexity on the LPD field of business, this leads to complicated and complex duties and responsibilities taken by LPD chairman. Towards the responsibility for achieving any plan, LPD chairman is necessary to conduct evaluation on any deviations from the determined plan. By the increasing LPD development activity, LPD chairman can no longer directly supervise on the company activities so that it must delegate some tasks, powers and responsibilities to other parties, namely the Monitoring Institution (internal auditor) as mandated in the Decree of the Governor of I Level Bali Province Number 491 of the year 1998.

A monitoring institution is a monitoring institution working on an LPD having its main task to determine whether any policies and procedures established by LPD have been complied with, whether the surveillance on LPD wealth is conducted duly and appropriately, and whether LPD can create reliability information. Concerning the duties given to the monitoring institution ultimately, it aims to enable LPD to produce reliable and accountable financial reports by the public.

LPD chairman not only pays attention on the service quality provided by the monitoring institution, it should also pay attention to the effectiveness of the implementation of internal controls to the LPD. Mulyadi (1992) stated that the applicable internal control structure in an entity is a determining factor on the quality of financial statements produced by the entity. Therefore, LPD chairman depends on the effectiveness of internal controls applied to LPD so that it can produce qualified accounting information. Although there is adequate preparation and implementation of internal control, it may be considered not fully effective because basically, there is no guarantee that the internal control can achieve organizational goals.

Quality of monitoring institution services and effectiveness of internal control will determine reliability of accounting information produced by LPD. To meet the quality of accounting information then the information should be understood by decision makers. Thus, the problem formulation is: how the effectiveness of monitoring institution on LPD in Bali Province is and how the effective of implementation of internal control on LPD in Bali Province is?

Research Goals

To study the effectiveness of monitoring institution as an internal auditor in LPD in Bali Province as well as to study on the effectiveness of implementation of internal control in LPD in Bali Province.

Research Benefits

- 1) For Knowledge Treasure. This research is an opportunity to improve understanding, expand knowledge and insight as well as apply theories in actual conditions, especially regarding the effectiveness of the Monitoring Institution functions, the effectiveness of internal controls and the reliability of accounting information in the LPD.
- 2) For Solving Operational and Policies. This research is expected to provide inputs on the importance of monitoring institution function and effectiveness of internal control in the LPD management.

LITERATURE STUDY

Definition of effectiveness

According to Handoko (1996), Effectiveness is an ability to choose appropriate goals or equipment to achieve predetermined goals, concerning how to do appropriate jobs. Yamit (2013) presented a definition on the effectiveness as a measure illustrating the extent to which targets can be achieved, both in quality and time, having orientation on the resulting outputs. The word of effective has connotation or related to the number of results achieved. Thus, effective or effectiveness can be interpreted as the level or degree of achievement on the expected results. Greater results achieved leads to more effective. Effective also means that any predetermined goals can be achieved maximally.

Monitoring Institution of LPD

According to Fitzsimmons and Mona (2001) a service quality can be described by comparing to the perceptions on the services provided to the expected services. An assessment on the quality of services is at the time the services are delivered. Hansen and Mowen (2005) operationally defined the quality of a product or service is something that meets or exceeds customer expectations. So, the quality means as customer satisfaction. Success in delivering qualified service quality is not a short-term effort, it is a continuous effort and as part of the management philosophy.

Internal auditor (monitoring institution) is an auditor working in a company having main tasks to; 1) supervise management and conduct internal audit on LPD, 2) provide guidance to

the board, 3) provide suggestions, consideration and solve problems, 4) socialize the existence of LPD, 5) provide regular organizer performance evaluation, and 6) arrange and submit supervisory results to Village officers. (Regulation of Governor of Bali No. 11 of the year 2013). Quality of monitoring institution services in the internal audit process is greatly determined by the ability of the monitoring institution to apply the internal audit norms when performing its duties.

Institute of Internal Auditors in Boynton and Kell (1996) stated that there are established five standards on the examination practice binding on its members, including issues of independence, professional expertise, scope of examination work, conducting monitoring work, and management of internal examination department. The Internal Audit norm is an indicator determining the quality of monitoring institution services in performing the examination practice. If it is related to the monitoring institution duty performing the examination on LPD activities, if the monitoring institution complies with more complete indicators, then the quality of examination results by the monitoring institution will be better.

Internal Control of LPD

Internal control is a process of organizational operational activity and an integral part of the management process, such as planning, execution, and control. According to IAI (2011), internal control is a process taken by boards of commissioners, management and other entity personnel designed to provide reasonable assurance on the achievement of three classes of objectives, namely (a) financial reporting reliability, (b) operational effectiveness and efficiency, and (c) compliance with applicable laws and regulations. Effective internal control of LPD will assist the board of management so that they can protect both physical and nonphysical assets from any abuse and fraud.

Then, according to COSO quoted by Boynton and Kell (1996) The internal control structure of business unit consists some components, namely (a) control environment, (b) risk assessment, (c) control activities, (d) information and communication, and (e) monitoring.

There is a satisfactory internal control when whole elements are applied appropriately. The appropriate internal control implementation in LPD will be able to produce qualified accounting information. The internal control structures within the company will result in or guarantee on the implementation of proper and reliable bookkeeping so that it can produce reliable financial reports (Kiryanto, 1999, Mulyadi, 1996). Effectiveness of good internal control is used to minimize any errors and misappropriation within reasonable limits. The effectiveness of internal controls is measured using indicators (a) control environment, (b) risk assessment, (c) control activities, (d) information and communications, and (e) monitoring.

RESEARCH METHOD

This research aims to; 1) study on the effectiveness of monitoring institution in the implementation of monitoring on the LPD, and 2) study on the effectiveness of internal control implementation on the LPD. Data collection is conducted by distributing questionnaires. Analysis technique is qualitative descriptive analysis technique and multiple regression analysis technique.

This research is conducted In Bali Province taking 9 regencies / cities. This study populations are all LPDs in Bali Province. Based on data from BPD bank in Bali, there are 1.468 LPD having their operation until the end of 2015. The number of samples is calculated based on Table Krejcie (Sugiyono, 2014). Based on the Krejcie Table, the number of samples for the population by 1,468 LPD is determined by 302 LPD. The number of sample required to support the variables in this study should be representative to be used as a basis for data testing. The research populations consisting of subpopulations such as regencies / cities, will provide two things, namely (1) more real homogeneity within each subpopulation or each stratum and (2) providing real-world inter-subpopulation heterogeneity. Therefore, the sampling technique used is Proportional Stratified Random Sampling.

The primary and secondary data obtained will then be analyzed by qualitative descriptive analysis method. The qualitative analysis is used to explain any opinions / responses taken from the respondents on the problems faced in performing the examination on the tasks and effectiveness of the implementation of internal controls on the LPD.

RESULTS AND DISCUSSION

Effectiveness of Monitoring Institution of LPD in Bali Province

This research is conducted in LPD in Bali Province. Based on the data obtained from Economy Guidance Bureau of Regional Secretary of Bali Province, there are 1.468 LPDs in Bali Province. In this research, the data collection is by distributing questionnaires to LPD Chairmen. Respondent determination is that the chairmen are considered to represent and most understand on the LPD Operational activity. The effectiveness indicators of Monitoring Institution functions in the implementation of examination are as follow:

- 1) Independence is the LPD Monitoring Institution should be independent and separate from any examined activities. Independent means as an ability to perform activities freely and objectively. Independence indicators include:
 - a. Monitoring Institution responsibilities to Pakraman village officers.
 - b. Whether having double positions of the Monitoring Institution as LPD board of management

- c. Whether having double positions of the Monitoring Institution as head of credit department
 - d. The Monitoring Institution does not participate in operational activities.
 - e. The relation of interest of the Monitoring Institution and the section to be examined is only limited to the responsibilities related to the examination duties.
 - f. The Monitoring Institution guarantees on the appropriateness of examination to the examination norms.
 - g. The implementation of the Monitoring Institution is applied by objective actions in accordance with authentic evidences obtained during the examination.
- 2) Professional Capability is the level of Professional Capability of the Monitoring Institution at LPD which is performed by professional expertise and thoroughness. Indicators of the professional ability are:
- a. The level of the Monitoring Institution ability / knowledge regarding banking industry, especially LPD in conducting the examination.
 - b. Development of the Monitoring Institution technical capacity by following development of audit techniques through seminars, courses or other advanced education in conducting banking / LPD audit.
 - c. The Monitoring Institution in performing its duties has been able to maintain good relations with the examined object.
 - d. The Monitoring Institution accuracy in the work and the application of professional proficiency optimally
- 3) The scope of work is the level of supervision and monitoring of the Monitoring Institution in the LPD to include testing and evaluation on adequacy and effectiveness of the Internal Control System by the organization and the quality of the responsibility implementation. The scope of work indicators are:
- a. The Monitoring Institution reviews and re-tests any data / facts / information obtained during the examination.
 - b. The monitoring level conducted by the Monitoring Institution on debtor development includes to non-performing credit classification to provide information to credit officers in order to be able to take further action.
 - c. The monitoring level conducted by the Monitoring Institution on credit provision is to find out whether the credit expenditure has been well-adjusted to LPD Credit Policy.
 - d. The monitoring is for all LPD officials related to the credit.

- e. The monitoring level conducted by the Monitoring Institution is to ensure that credit disbursement has been used in accordance with the credit purposes.
 - f. The monitoring level conducted by the Monitoring Institution on correction report is on any misuse of credit disbursement to credit purpose.
 - g. The monitoring level on implementation of document administration has been well-adjusted to any stipulated provisions.
 - h. The supervision level on the suitability of credit collectability to any applicable provisions.
 - i. The examination level of various tools or means used is to protect property of any types of losses such as theft, illegal activities and others.
4. Implementation of Examination Activity is the work performance level of the Monitoring Institution on LPD in conducting Examination Activity shall include examination planning, testing and evaluation of information, result notification and follow-up. Indicators of implementation of the examination activity are:
- a. The Monitoring Institution plans the examination in advance before conducting the examination.
 - b. The presence or absence of any collection, analysis, interpretation and verification on information validity to support examination results.
 - c. The presence or absence of the Monitoring Institution in conducting the examination so that it can make written report on the examination results in the form of documents.
 - d. Regularity of the Monitoring institution to create reports periodically (at least every three months).
 - e. Whether it submits or not any routine examination results report made by the Monitoring Institution to Pakraman Village officers in Paruman
5. Management of the Monitoring Institution is work performance level of the Monitoring Institution on LPD in managing the monitoring institution functions. The indicators of monitoring institution management are:
- a. The Chairman of the Monitoring Institution has express statements, objectives, powers and responsibilities.
 - b. The Chairman of the Monitoring Institution sets out any plans for the implementation of Monitoring Institution responsibilities.
 - c. The Chairman of the Monitoring Institution provides written policies and procedures used as staff guidance.

- d. The Chairman of the Monitoring Institution establishes and develops quality control or Quality assurance to evaluate various activities conducted by the Monitoring Institution.
- e. The Chairman of the Monitoring Institution coordinates internal audit with external auditor.

Respondents' responses on the effectiveness of the monitoring institution can be classified to the presentation in Table 1 as follow.

Table 1. Classification of effectiveness of the Monitoring Institution

No.	Range of Classification	Classification	Number of respondents	Value (%)
1	$135,2 \leq KSE \leq 145$	Very effective criteria (KSE)	7	04,61%
2	$125,4 \leq KSE < 135,2$	Effective criteria (KE)	41	26,97%
3	$115,6 \leq KSE < 125,4$	Quite effective criteria (KCE)	62	40,79%
4	$105,8 \leq KSE < 115,6$	Less effective criteria (KKE)	28	18,42%
5	$96 \leq KSE < 105,8$	Ineffective criteria (KTE)	14	09,21%

Based on Table 1, the respondents' responses on the assessment on the effectiveness of monitoring institution in a whole in LPD in Bali Province has been applied with very effective criteria by 4,61% or there are 7 respondents, with effective criteria by 26,97% or there are 41 respondents, with quite effective criteria by 40,79% or there are 62 respondents, with less effective criteria by 18,42%, and ineffective criteria by 9,21%. These show that the effectiveness of the monitoring institution on LPD in Bali province on the average has quite effective.

Effectiveness of LPD internal control in Bali Province

The elements of internal control include control environment, risk assessment, control activity, information and communication, as well as monitoring.

1. control environment is a basic for all other control elements and determining organizational condition and giving influence on control awareness by the managements and employees (James A. 2011). Basically, the control environment illustrates all behaviours, awareness and actions taken by the Monitoring institution, managements, employees, Pakraman village officers and other parties concerning the important role of control for LPD business unit. Effectiveness of information, communication and control activities greatly depends on the atmosphere created by the control environment.

The control environment indicators include:

- a. Pakraman villages and managers have adequate ethical and organizational standards.
- b. LPD managers communicate on ethical and behavioral standards in managing LPDs.
- c. Managers provide guidance and intervention in any situations and frequencies in accordance with the established controls.
- d. The recruitment practice of employee focuses on educational background, work experiences, as well as behavior and integrity.
- e. Employee promotion and rotation are based on periodic performance appraisals.
- f. LPDs provide training opportunities for the employees.
- g. Compensation method including bonuses is designed to motivate employees and to achieve the expected performance.

2. The risk estimation for the purpose of financial statement is identification, analysis and management on entity risk related to the preparation of financial statement so that it can be well-adjusted to the general accounting principles (PABU) in Indonesia (Mulyadi, 1996). The LPD risk estimation for the purpose of financial reporting is the risk estimation presenting certain assertion in the financial statement as well as design and implementation of control activity designed to decrease the risks in minimum level by considering on cost and benefits. The risk estimation indicators are:

- a. There is a special action taken against new employees so that they can understand their duties
- b. Managers have adequate consideration concerning performance of control activities on any employees moving their jobs or leaving the company
- c. Managers have access to the extent that new information and accounting systems will have influence on the internal control.
- d. Managers reconsider suitability of control activities when there are new information and accounting systems development and implementation.
- e. Employees obtain adequate trainings if there are any changes or replacements of information and accounting systems

3. The control activity is any policies and procedures to ensure than the management is applied (IAI, 2011). These policies and procedures provide certainty that any necessary actions are taken so that the risks are eliminated to achieve LPD goals. The control activity indicators are:

- a. There are effective operating budget and cash flow projection compared with the actual results.

- b. The Company has adequate safeguarded on accounting facilities and records from fire and restricted access to the places.
 - c. The employee performs a comparison of calculation result on the amount of physical assets with the controller's record
 - d. There is adequate duty and responsibility division on transaction, record authority and storage of company assets
 - e. Every transaction has been properly authorized.
4. Information system is the relevant information system to financial reporting purposes, including methods and records used to record, process, summarize, and report LPD transactions and to apply accountability on LPD assets, debts and equity. The information and communication indicators are:
- a. LPD managers obtain any necessary information in accordance with their responsibilities.
 - b. There is detailed and correct information availability according to the management level.
 - c. Information is always available on time.
 - d. There is significant accounting information based on functional line time.
 - e. Every transaction has been recorded correctly.
5. The monitoring is a process of determining internal control performance quality in all time (IAI, 2011). In this LPD monitoring, it includes determination of design and control operation in a punctual manner and taking any correction actions. The monitoring indicators are as stated:
- a. Investigation is conducted based on causes of customer complaints on the bills.
 - b. Managers provide quick response to any recommendations of the monitoring institution to improve internal control.
 - c. Managers reconcile periodically.
 - d. There is no follow-up from the external auditor suggestions.
 - e. The Monitoring Institution conducts *cash of name* periodically.

The respondents' responses on the effectiveness of internal control can be classified such as the presentation in Table 2 as follow.

Table 2. Classification of Internal Control Effectiveness

No.	Range of Classification	Classification	Number of respondents	Values (%)
1	$125,4 \leq KSE \leq 134$	Very effective criteria (KSE)	12	07,89%
2	$116,8 \leq KSE < 125,4$	Effective criteria (KE)	68	44,74%
3	$108,2 \leq KSE < 116,8$	Quite effective criteria (KCE)	50	32,89%
4	$99,6 \leq KSE < 108,2$	Less effective criteria (KKE)	18	11,84%
5	$91 \leq KSE < 99,6$	Ineffective criteria (KTE)	4	02,63%

Based on Table 2, the respondents' responses on the assessment on the effectiveness of internal control in LPD in Bali Province has been applied with very effective criteria by 7,89 % or there are 12 respondents, with effective criteria by 44,74 % or there are 68 respondents, with quite effective criteria by 32,89% or there are 50 respondents, with less effective criteria by 11,84%, and ineffective criteria by 2,63 %. These show that the effectiveness of the internal control on LPD in Bali province on the average has quite effective.

CONCLUSION

Based on the analysis results presented in the previous chapters, then it can be concluded as follow:

- 1) Effectiveness of Monitoring Institution in LPD in Bali Province in very effective criteria is 4,61%, in effective criteria is 26,97%, quite effective criteria is 40,79%, and less effective criteria is 18,42%, and ineffective criteria is 9,21%.
- 2) Effectiveness of internal control in very effective criteria is 7,89 %, in effective criteria is 44,74 %, in quite effective criteria is 32,89%, less effective criteria is 11,84 %, and ineffective criteria is 2,63%.

SUGGESTIONS

- 1) The Monitoring Institution should monitor the LPD management in running business activities so that it can be well-adjusted to their duties respectively.
- 2) The Monitoring Institution should continuously assess on the effectiveness of internal control implementation in each LPD activity.
- 3) The Monitoring Institution should develop technical capability in conducting the examination by following any audit technique development either through seminars, courses, training or sustainable education so that it can conduct the supervision on LPD activities.

LIMITATIONS

Limitation of this study is the respondents limited to the head of the LPD only, for future research suggestion is the respondents can be added from consumers who often used LPD services.

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