THE IMPLEMENTATION OF OPERATIONAL AUDIT

(A Case Study at Internal Control Unit of PT. TIMAH Tbk.)

A BACHELOR DEGREE THESIS

Presented as Partial Fulfillment of The Requirements
to Obtain The Bachelor Degree in Accounting Department



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ABSTRACT

Suryaekaningrum, Indri. (2004). **The Implementation of Operational Audit (A Study Case at Internal Control Unit of PT. Timah Tbk.)**. Yogyakarta: Accounting Department. Faculty of Economics. Islamic University of Indonesia

Nearly every business can effectively use operational audit as a part of comprehensive internal audit by integrating operational audit which can be used as an effective tool for examining the operating information and the mean used identify, measure and classify and report such information.

Operational audit objective is to review operational result of company for evaluating efficiency and efffectiveness and give constructive recommendation.

Constructive recommendation for improving operational of auditee usually will be given after all audit findings has been disclosed. Recommendation designedly for each activity that disclosed on audit audit findings, so that activity performance of auditee will be more efficient, economize and ableto achieve effective result.

This research took place at Internal Control Unit of PT. Timah, whereas Internal Control Unit is the only department that carrying out the internal audit within PT. Timah. Technique od data obtained based on observation and interview result from staff of Internal Control Unit

ABSTRAK

Suryaekaningrum, Indri. (2004). **The Implementation of Operational Audit (A Study Case at Internal Control Unit of PT. Timah Tbk.)**. Yogyakarta: Jurusan Akuntansi. Fakultas Ekonomi. Universitas Islam Indonesia.

Hampir setiap bisnis dapat melakukan audit operasional secara efektif sebagai bagian dari audit intern yang menyeluruh dengan memadukan audit operasional sebagai suatu alat yang efektif untuk memeriksa informasi tentang operasional dan juga mengidentifikasi, mengukur dan mengklasifikasi, dan pelaporan atas informasi

Tujuan utama operasional audit adalah untuk mengkaji ulang hasil operasional pada setiap perusahaan dengan tujuan untuk mengevaluasi atau menilai efisiensi dan efektifitas dan memberikan sara-saran perbaikan bagi obyek yang diaudit.

Saran-saran atau rekomendasi yang konstruktif untuk perbaikan operasional obyek yang diaudit biasanya disertakan setelah mengungkapkan setiap temuan hasil pemeriksaan. Saran-saran tersebut ditujukan agar kegiatan yang diungkap dalam temuan tersebut dapat dilaksanakan lebih efisien, lebih hemat dan dapat mencapai hasil yang efektif.

Penelitian ini dilakukan di Satuan Pengawasan Intern (SPI) PT. Timah Tbk. Dimana SPI merupakan satu-satunya unit/departemen yang melaksanakan fungsinya sebagai audit intern PT. Timah Tbk. dalam mengevaluasi semua kegiatan perusahaan. Teknik pengumpulan data dilakukan berdasarkan observasi dan wawancara terhadap staff SPI.

CHAPTER I

INTRODUCTION

1.1. Study Background

Today fast-passed business climate and soft economy call for creative strategies to manage change. Firms that choose not to respond to change effectively will not survive. As the environment changes, threats and opportunities are encountered. Some organizations react to the changing environment by implementing changes in their structure. These changes can affect the relationship between the firm and its environment, or the changes can relate to the internal operations of the firm. Changes relating to the relationship of a firm to its environment have more impacts on the organization effectiveness and changes involving the organizations internal operation have a greater effect on the efficiency of the firm.

Auditing plays a vital role in business, government, and our economy. Truthfully, auditing is an activity of comparing between real situation and situation as it ought to be. Auditing is a part of controlling. Controlling is evaluation of activity to organization designed for organization to implement its function properly and able to accomplish its ascertained objective. Internal auditing means free evaluation of unit or part within company toward activity presence on company, as services to company's Directors. Internal auditing is part of element from management controlling, whereas its function is to evaluate effectiveness of other elements of management controlling. Other elements of

management controlling are organization, policy, procedure, planning, personnel, recording, and reporting.

In many organizations, internal audit departments play many roles in seeking to strengthen control. As defined by The Institute of Internal Auditors (IIA), internal auditing is an independent appraisal activity within organization, established for the review of accounting, financial, and other operations as a basis for protective and constructive service to management. The competitive environment requires that the work being performed should be in an efficient, cost-effective way. Internal auditing does not only audit control activities, but also monitors company risk profile and plays a key role in identifying areas to improve risk management process. Understanding the business operations can make the auditors as a catalyst for change with a prominent position that is a key risk advisor. However, some internal auditing are known as operational auditing.

Operational auditing is free, selective, and analytical evaluation upon program, activity, or function designed for giving improvement recommendation to an audited object. Free evaluation means evaluation performed without any influence or pressure from any parties so that evaluation will be objective. Selective evaluation means audit operational conducted to a certain situation that needs special attention or improvement. Analytical evaluation means evaluation performed in details so that on each problem/finding disclosed has considered of existing facts. Principal objective of operational auditing is to disclose findings of audit result based on fact and certain criteria and gives recommendation for improvement to audited object. Findings of audit result should be based on

evidences/facts obtained by disclosing criteria, causes and effects of problem/deviation, opinion and comment from official of audited object. Constructive recommendation for improvement of operation of audited object is usually taken a part after disclosing each findings of audit result. Recommendation designed for activities being disclosed on that finding are aimed be more efficient, economical, and able to achieve effective result on its implementations. Besides recommendation also discloses several alternatives of problem solving from disclosure of problem.

Nearly every business can use effectively operational audit as a part of comprehensive internal audit by integrating operational audit which can be used as an effective tool for examining the operating information and means used to identify, measure and classify and report such information. Operational audit can also review the means for safeguarding the assets, ascertain if the results are consistent with the management's objectives and goals and if the operations are being carried out as planned, appraise the economy, efficiency, and effectively with which resources are employed and review established system to ensure compliance with policies, procedures, plans, laws and regulations. Having the operational audit conducted by an experience, objective third party helps insuring that the result will be accurate and unbiased. Based on audit results, implementing a process to insure the organization is properly utilizing its resources with maximum efficiency and effectiveness to achieve optimum results both at the present time and in the future. A successful operational audit helps managers making good decisions. Recommendations vary widely. Some recommendations

are process improvement to save money or time, some are suggestion for generating additional revenue, others may be suggestions for working collaboratively with other agencies, changing schedules, locations, purchasing equipment that helps automate steps, or they may be a programmatic changes, if allowed by law. Operational audits vary widely and are always collaborative endeavors.

Internal Control Unit (*SPI*) of PT.Timah Tbk. is the only department that carrying out the internal audit within PT.TIMAH. In conducting internal audit *SPI* PT.Timah Tbk. performed four type of internal audit, which are financial audit, routine/verification audit, operational audit, and special assignment audit. So, *SPI* PT.Timah Tbk. as the internal auditors of PT.Timah Tbk. has main task, which is to help Directors of company in performing function of controlling. Those functions of controlling are as follows:

1. Performing controlling toward practice of continual transaction in order to ascertain process of transaction in compliance with company policies.
2. Performing of studying/researching upon internal control system of operation system that holds for the entire company in order to evaluate efficiency and effectiveness of that system.
3. To give recommendations for improvement needed if there is practice or internal control system or less system of operation/ineffective or not going along smoothly.

Audit implementation starts when Internal Control Unit receives Instruction Letter of Audit, and then prepares audit programs. The audit program consists of

audit phases from beginning of audit until follow up upon findings. Those audit programs are scope of audit of Internal Control Unit *(SPI)*. Audit programs are as follows:

1. Yearly Audit Working Programs (*PKPT/Program Kerja Pemeriksaan Tahunan*)

   Is audit working programs in which every year audit program is prepared by Internal Control Unit. The audit program consists of operational and financial audit.

2. Non PKPT

   Is an incidental audit program and unprepared before or there is a special demand from directors in order to check certain matters.

3. Audit of Environmental Management System and Quality Management System (EMS/QMS)

   PT. Timah Tbk. operational activity had already got certificates of ISO 9001, 9002, and 14001 about quality and environment.

   a. Audit ISO 9000

      PT. Timah Tbk. has ISO 9001 and 9002 certificates about quality. Audit upon ISO 9000 is process of audit to working unit within process of production from input until output whether it has already complied with standard of ISO determined before about quality of working/production process. The object that being audited is Metallurgic Center (Pusat Metalurgi) Mentok (ISO 9002) and Workshop (Balai Karya /ISO 9001).

b. Audit ISO 14001

ISO 14001 is ISO that given to company that has applied environment management system effectively and efficiently. Whereas operational activity that performed by PT. Timah Tbk. has no negative impact to environment not even human..

SPI PT. Timah Tbk. considers operational audit as an integral part of internal auditing. Basically the audit work field are varied depends on what kind of organization activities, such as financial, production, marketing, personnel affair, etc included project activity or programs that perform by organization.

Regarding the statements and many considerations about the benefit and useful information from the observation, the researcher gives proposal a title: ***"THE IMPLEMENTATION OF OPERATIONAL AUDIT, CASE STUDY ON INTERNAL CONTROL UNIT (SPI) OF PT. TIMAH Tbk."***

1.2. Problem Identification

The purpose of this study is to explore the implementation of operational auditing by Internal Control Unit (SPI) of PT. Timah Tbk.

1.3. Problem Formulation

Based on the explanation of study background above, the main problem can be stated as:

1. Is the implementation of operational audit at PT. TIMAH successfully done (based on the practices, procedures, and standards as defined by Governmental Auditing Standard and Auditing Standard for SPI of BUMN/BUMD?
2. Does the implementation of operational audit have a positive impact to PT. TIMAH?
3. Is the implementation of operational audit able to improve the management performance of PT. TIMAH?

1.4. Problem Limitation

Due to time limitation, the researcher restricts this thesis on:

1. Research area is only limited to the implementation of audit operational.
2. Studying and discussing the implementation of audit operational based on policy and procedure determined by company.
3. This research will be conducted at Internal Control Unit (SPI) of PT. Timah Tbk., Pangkalpinang Bangka.

1.5. Research Objectives

These research objectives are:

1. To study the development and implementation of operational audit at PT. TIMAH.
2. To review the implementation of operational audit and build on the recommendation in conducting the operational audit.

1.6. Research Contribution

This research will give positive contributions to the following parties:

1. The researcher

   The researcher will be able to understand about operational audit implementation and to see real practice of operational audit mechanism at PT. Timah Tbk.

2. The company

   The result of the research can be used as input for PT. Timah Tbk. in understanding operational auditing.

3. The external users

   Other interested parties are able to use this research as their references and also able to enrich their knowledge about the related to the topic.

1.7. Definition of Term

The researcher gives the definition of term in order to make the reader understand about what they are going to read from the thesis title, the writer will explain each term of the title as follow:

1. Yearly Audit Working Program (*Program Kerja Pengawasan Tahunan/PKPT*) is:

   - Planning prepared by Internal Control Unit (SPI) for every year controlling working program based on government policy, company policy, evaluation of prior audit and input from Director by following guidance from *Badan Pengawas Keuangan dan Pembangunan (BPKP).*

- As one of management tool of controlling and also as a basis for external auditor to create integrated controlling within company.

2. Controlling is a whole process of activities within company in order for company to be able to perform its function properly and successfully accomplishing company's objectives.
3. Internal control is steps for getting certainty whether implementation has complied with company's objectives followed by steps of follow up if discrepancies happened.
4. Audit object is a working unit or a part of system within PT. Timah Tbk., which is possible to be targeting of audit conducted by authoritative audit.
5. Deskwork is early working audit preparations by collecting information/data before performing audit.
6. Audit Finding Sheet (*Lembar Temuan Audit /LTA*) is discourse prepared by audit team that consists of deviation/discrepancies with criteria, violation or other valuation that necessarily consider following up.
7. Audit team is audit team structure that consists of audit controllers that are responsible for audit, leader of audit team and team member that are assigned to perform audit to audited object mentioned on engagement letter signed by Chief of SPI.

1.8. Research Method

1.8.1. Type of Research Method

The research method applied here is a descriptive method within case study. Sekaran (1992) states that a descriptive method is undertaken in order to ascertain and to be able to describe the characteristics of variables in situation. Descriptive method is also undertaken to understand the characteristic of organizations that follow common practices. The goal of descriptive method is to describe relevant aspect of the phenomena of interest to the researcher from individual, organizational, industry or other perspective.

According to Consuelo (1999) the research with descriptive method is divided into several studies, such as case, survey, development research, follow up study, content analysis, and trend analysis and correlation analysis. A case study is a deep research about a certain object during certain period of time including the environment and past conditions and the researcher is trying to finds the relationship between one factor and the others.

1.8.2. Research Subject

The subject of this research is SPI PT. TIMAH.

1.8.3. Research Setting

This study takes place at PT. TIMAH located in Pangkalpinang, Bangka.

1.8.4. Data Sources

1.8.4.1. General Data

a. Company profile.

b. Organizational structure and job description.

c. Audit operational guideline.

1.8.4.2. Specific Data

a. Audit operational procedures.

b. Audit program.

c. Audit working papers.

d. Annual Report.

e. Corporate Governance.

1.8.5. Data Collection method

1.8.5.1. Library Research

Library research is a research that is done by reading literatures, books, journals, magazines, newspapers, company document and other data that have a correlation with research object and those collected data will be able to support the research construction.

1.8.5.2. Field Research

1.8.5.2.1. Observation

From the direct observation, researcher could collect the data by recording systematically the firm's activities in order to get direct description of a firm as a whole

1.8.5.2.2. Interview and Discussion

By doing interview (question and answer) and discussion, researcher expects to obtain information needed from the opinion, comment and suggested solution about the implementation of operational audit at PT. TIMAH.

1.8.6. Technique of Data Analysis

After all data are obtained, they will be analyzed. Steps that will be going to be conducted are:

1. Studying the implementation of operational audit at PT. TIMAH.
2. Studying audit operational phases.
3. Studying audit program.
4. Studying audit-working papers.
5. After the research complete, arranging and writing the report of the research and several inputs or suggestion to company

THESIS CONTENTS

CHAPTER I Introduction

This chapter will discuss about the study background, problem identification, problem formulation, research objective, and research benefit.

CHAPTER II Review of Related Literature

This chapter content is theoretical review and theoretical framework. The discussions are operational audit definition and concepts, operational audit objectives, operational audit phases, audit ISO, and corporate governance.

CHAPTER III Research Method

This chapter will discuss company background, company vision and mission, company organization structure and internal control (SPI) job description.

CHAPTER IV Research Findings, Discussion, and Implications

This chapter will discuss and analyze about how Internal Control Unit (SPI) of PT. Timah implementing operational auditing to all working unit within company.

CHAPTER V Conclusions and Recommendations

This chapter will conclude the result of the research and try to give recommendations to the competent parties, especially PT. TIMAH.

CHAPTER II

LITERATURE REVIEW

2.1. Theoretical Review

2.1.1. Audit Definition

According to Arens and Lobbecke (2000:9), auditing is the accumulation and evaluation of evidence about information to determine and report on the degree of correspondence between the information and established criteria. A competent, independent person should do auditing. The Report of Committee on Basic Auditing Concepts of The American Accounting Association (Accounting Review, vol. 47) defines auditing as a systematic process of objectively obtaining and evaluating evidence regarding assertion about the economic actions and events to ascertain the degree of correspondence between those assertion and established criteria and communicating the results to the interested users.

Several attributes of auditing contained on the definition above merit special comments:

1. A systematic process

   It connotes a logical, structured, and organized series of steps or procedures.

2. Objectively obtaining and evaluating evidence

   It means examining the basis for the assertions and judiciously evaluating the result without bias or prejudice either for or against the individual (or entity) making the assertions.

3. Assertions about the economic actions and events.

   Assertions about the economic actions and events are the representation made by the individual or entity. They comprise the subject matter of auditing. Assertions include information contained in financial statements, internal operating reports, and tax returns.

4. Degree of correspondence

   It refers to the closeness with which the assertions can be identified with established criteria.

5. Established criteria

   Established criteria are the standards against which assertions or representations are judged. Criteria may be a specific rules prescribed by a legislative body, budgets, and other measures of performance set by management, or generally accepted accounting principles (GAAP) established by the Financial Accounting Standards (FASB) and other authoritative bodies.

6. Communicating the results

   It is achieved through a written report that indicates the degree correspondence between the assertions and established criteria. Either

the communication of results enhances or weakens the credibility of the representations made by another party.

7. Interested users

Interested users are individuals who use (rely on) the auditor's findings. In business environment, they include stockholders, management, creditors, government agencies, and the public.

2.1.2. Types of Audits

Audits can be classified into categories. CPAs perform three types of audits, they are:

1. Financial Statement Audits

A financial statement audit is conducted to determine whether the overall financial statements (the information being verified) are stated in accordance with specified criteria. Normally the criteria are generally accepted accounting principles, although it is also common to conduct audits of financial statements prepared using cash basis or some other basis of accounting appropriate for the organization. Most financial statements included are the statements of financial position, income statement, and statement of cash flows, including accompanying footnotes.

2. Operational Audits

An operational audit is a review of any part of any organization's operating procedures and methods for the purposes of evaluating

efficiency and effectiveness. At the completion of an operational audit, management normally expects recommendations for improving operations. In operational auditing, the reviews are not limited to accounting. They can include the evaluation of organization structure, computer operations, production methods, marketing and any other areas in which the auditor is qualified.

3. Compliance Audits

   The purpose of compliance audits is to determine whether the audit follows specific procedures, rules, or regulations set by some higher authorities. Results of compliance audits would be typically reported to someone within the organizational unit being audited rather than to a broad spectrum.

2.1.3. Types of Auditors

The primary types of auditor are:

1. Independent Auditor

   Independent auditors are either individual practitioners or members of public accounting firms who render professional auditing services to clients.

2. Internal Auditors

   Internal auditors are employees of the companies they audit. This type of auditor is involved in an independent appraisal activity, called internal auditing, within an organization's activities. The objective of internal

auditing is to assist the management of the organization in the effective discharge of its responsibilities. The scope of internal audit functions extends to all phases of an organization's activities. Internal auditors are primarily involved with compliance and operational audits.

3. Government Auditors

   Government auditors' duty is to audit financial state upon government institution. In Indonesia, this audit performs by *Badan Pemeriksa Keuangan (BPK)* as an institution that not defer to government, hoped to be an independent institution. Result of audit will be reported to Legislative Representation as tool of control upon financial state.

2.2. Operational Auditing

Although operational auditing is a generally understood to deal with efficiency and effectiveness, there is a less agreement on the use of that term than one might expect. Many people prefer to use the term management auditing or performance auditing instead of operational auditing to describe the review of organizations for efficiency and effectiveness. Those people typically describe operational auditing broadly and include evaluating internal controls and even testing those controls for effectiveness (test of controls) as a part of operational auditing. Testing the effectiveness of internal controls by an internal auditor is therefore a part of operational auditing if the purpose is to help an organization operating its business more effectively and efficiently.

2.2.1. Operational Auditing Definition

Operational auditing definitions as follows:

1. According Boynton and Kell

   Operational auditing is a systematic process of evaluating and organization's effectiveness, efficiency and economy of operations under management's control and reporting to appropriate persons the results of the evaluation along with recommendations for improvement. (Boynton and Kell, 1996:846)

2. According to Strauser and Strauser

   Operational auditing is an organized search for ways of improving efficiency and effectiveness. It can be considered a firm constructive criticism. (Strauser and Strauser, 2001:20)

The essential parts of definitions above are:

1. Systematic process

   As in the case of financial statement audit, an operational audit involves a logical, structured, and organized series of steps or procedures.

2. Evaluating and organization's operations

   The evaluation of operations should be based on some established or agreed-upon criteria. In operational auditing, the criteria are often expressed in term of performance standards established by management. Operational auditing measures the degree of correspondence between actual performance and the criteria.

3. Effectiveness, efficiency, and economy of operations

   The primary purpose of operational auditing is to help management of the audited organizations to improve the effectiveness, efficiency, and economy of operations.

4. Reporting to appropriate persons

   The appropriate recipient of an operational audit report is management or the individual or agency that requests the audit.

5. Recommendations for improvements

   Unlike financial statement audits, an operational audit does not end with report on the findings. It extends to make recommendations for improvement.

2.2.2. The Objectives of Operational Auditing

1. To evaluate company's performance.
2. To provide owners and managers with an objective evaluation of there firm's strength and weaknesses.
3. To make recommendation about economic and efficient use of resource, effective achievement of business, objectives, and in compliance with company policies.

2.2.3. The Scope of Operational Auditing

1. The scope of operational auditing covered all management aspect that should be improved and increased its audit quality by management upon examination of activities/programs.
2. Management aspects that should get an attention in order to improve and to increase the quality of audit are organizations, company policies, planning procedures, recording, reporting, and personnel.

2.2.4. The Target of Operational Auditing

1. Operational auditing targets are programs/activities that suspect and need recommendations for operating improvements. Operational auditing should direct into certain target that has decided before, so that top management can use the result of SPI examination maximally.
2. Aspects that should be considered in deciding audit targets are as follows:
   a) The importance of audit target within the company.
   b) Problems, which can be, identify as having a possible economic, efficient, and effectively implementation or problems that related to safeguarded interest.
   c) Restrictions or enlargements outside the general practice in performing its functions.
   d) Characteristic and significant physical resource which takes a part in audit.

e) Prior experiences of internal auditors to programs/activities, either on audited object or others.

f) The report of SPI audit result and other institutions of audit.

g) There are new activities/programs/projects.

h) Big amount of revenues/expenses involved in activities/ programs/projects of audited object.

3. The scopes of operational auditing target are as follows:

a) Audit Economy

Economy concept related on how to minimize cost from the use of resources upon any activities by concerning a proper quality. It can also be said that economy related to the way of supplying resources.

b) Audit Efficiency

Efficient concept related to the relationship among outputs, which are, goods, services, or other output related to the resources being used.

c) Audit Effectiveness

Effectively concept related to the level of objective accomplishment.

4. Determination of audit target and audited object performed by President Director and Chief of SPI.

2.2.5. Types of Operational Auditing

Operational auditing can be implemented into certain parts of company operational, which are:

1. Functional

   Function is a means of categorizing the activities of a business. Functional audits deals with one or more functions in an organization. A functional audit has the advantage of permitting specialization by auditors. Certain auditors within an internal audit can develop considerable expertise in an area, such as production engineering. A disadvantage of functional auditing is the failure to evaluate interrelated functions.

2. Organizational

   An operational audit of an organization deals with the entire organization unit, such as department, branch, or subsidiary. An organizational audit emphasizes on how efficiently and effectively functions interact. The plans of organization and the methods to coordinate activities are especially important in this type of audit.

3. Special assignment

   In operational auditing, a special assignment arises at the request of management. There are wide varieties of such audits, for example determining the cause of an effective IT system.

2.2.6. Operational Auditing Approach

Operational auditing that performed Internal Control Unit of PT. TIMAH emphasizes on activities that needs improvement. There is a possibility that operational auditing on activities or certain parties' activities

will discontinue when those activities do not need longer improvement at that time. In determining audit objectives, operational auditing approaches of SPI PT. TIMAH are:

1. Selecting object of "activity"

   Objects of activity probably relate to several parts of activities in a whole. So that on the implementation of operational auditing, SPI audits teams will be connected with several parts of units, departments and others, for example personnel activity, fixed assets maintenance, etceteras.

2. Selecting the object of "any parts of any departments within the organization"

   SPI audit team limits certain activities of certain part of any departments within organization, such as the activity of fixed assets maintenance at Metallurgy Center (Pusmet).

3. Selecting the object of "activities of any department'

   SPI PT. TIMAH determines the audit object to all activities of any department. For example operational audit at Pusmet, covers all productions activity, personnel fixed assets maintenance and soon. By determining audit operational object, SPI PT. TIMAH audit teams are still necessary to confirm related parties, but the object of audit operational should be in compliance with setting down of audit object. Selecting or identifying activities needs an audit follow-up, they are as follows:

a. Arranging review to certain activities from beginning till end.

   With this step, auditors will be able to understand/obtain information as follows:

   1) How the implementation of program or actual activity is.
   2) Benefit of various phases on those activities.
   3) Result of activity in compliances with company objective, law regulation and rational considerations.
   4) The effectiveness of management controlling on activities.

b. By considering information obtained stated on (a), auditors will determine or select activities or part of activities that will be audited further, for example selected activity which its implementation was not in compliance with relevant procedures or selected sub of activity that its management controlling considered weak.

2.2.7. Phases of an Operational Audit

Length of time or duration of operational auditing from publish of mandatory letter up to finished report will be different from one assignment to another assignment. Those matters are caused by several factors, which are:

1. Scope of audit.
2. Size of activity that will be audited.
3. Complexity or difficulties of problem.
4. Auditors' ability and experience.

5. Amount of auditors.

Nevertheless, on a complete of operational auditing, SPI should pass a certain audit phase. To guarantee that audit will be effective, then each audit or findings on the report of audit result should perform audit follow-up.

1. Audit Preparation

   For audit preparation, audit program is developed for preparing arrangement of more detailed audit program. The purpose of audit preparation is to get general information about audited object as a basis for preliminary audit program arrangement. Activities covered on audit preparation are:

   a. Preliminary communication with auditee of audited object.
   b. Obtaining general information about audited object.
   c. The arrangement of summary of audit preparation result.

      To simplify preliminary audit program arrangement, audit preparation result should be included on summary that contains information obtained.

2. Preliminary Audit

   The purpose of preliminary audit is to identify weaknesses indication on management aspect that is still possible to be improved either its efficiency or economic in order to achieve company objective effectively and also to identify a good practice of management so that it can be used as an example by other parties. Discoveries obtained above from operational auditing called as findings.

Activities that will be performed at preliminary audit are:

1. Studying valid of relevant regulation applied.
2. Management controlling calibration.
   a. The essence management controlling is an action performed by management in order to direct or to run operation in compliance with standard or company objective. Thus management controlling includes organization system, procedure and practice within handling and accomplishing management task effectively.
   b. The purpose of management controlling calibration is to evaluate level of effectiveness and recognize the possibility of management controlling weaknesses of audited object.
3. The arrangement of preliminary audit findings result recapitulation.
   a. Based on preliminary audit activity, it has prepared the list of preliminary audit findings result recapitulation that will be added on audit program follow-up.
   b. Basically, preliminary audit findings result recapitulation should contain these elements below:
      1) Description concerning with the necessity of performing preliminary audit.
      2) Findings and temporary conclusions.
      3) Temporary recommendations.

4) Improvement measurement that has been performed by audited object and problems that have not being solved yet or cannot be done.
5) Points that need to be concerned from related parties outside audited object.
6) Auditors' recommendations to auditors of responsible concerning with the implementation of audit follow-up.

Basically findings obtained from preliminary audit are still necessary to be developed on audit follow-up. However, sometimes those findings can already be included on audit report.

3. Audit Follow-up

Audit follow-up is an audit or further assessment upon activities as far as needed for accomplishing audit objective. Audit follow-up activity contains of deepening and developing important and relevant findings that are useful for considering, supporting findings, conclusion and proposing recommendations. Standards that should be concerned on audit follow up are:

1) Studying company policies.
2) Findings development.

Finding development is obtaining and deepening of specific information related with audited object to be evaluated and analyzed because it will be useful for auditee of audited object.

3) Recommendations.

1) Basically findings end with recommendation given to auditee related with weaknesses correction or preventive actions upon weaknesses. Steps of improvement are auditee responsibility.

2) To give recommendations constructively, auditors should explain each of weakness completely. If auditors are not able to give better recommendations or various alternatives to take corrective actions, it's preferable for auditor to give recommendations based on auditors' opinions.

3) Auditors should also consider about cost of implementing recommendations and its benefit. To get corrective actions as soon as possible and determine it, then in certain case, to explain findings with verbally is an effective and efficient way. Though auditor has explained findings, conclusions, and recommendations verbally. The arrangement and audit report presentation are still needed in written form.

4) Discussion of audit follow-up results with audit supervisor and audit responsible.

The purposes of discussing audit follow-up results with audit supervisor and audit responsible are:

a) Operational auditing is more directed and controlled.

b) Findings and recommendations get better considerations.

c) Audit supervisor/audit responsible obtains wide comprehensive information as material discussion of findings with audited object.

5) Discussion of audit follow-up result with audited object.

The purposes of discussing audit follow-up result with audited object are:

a) To quicken the arrangement of concept of report.

b) To decrease the possibility of objection to audit report.

c) To be more complete and more accuracy concept of report.

d) Action for correction can be performed more quickly.

4. Audit Report

An audit report is media for explaining audit objective and scope of audit and also reports findings and audit conclusions and its recommendations for improvement.

Standards of report of audit result are as follows:

a. Internal auditor should report audit result in accordance with ascertained assignment.

b. Audit report should be:

1) Prepared in form of written.

2) Delivered to authoritative official on time in order to be useful.

c. Each of audit report should:

1) Accommodate scope of audit and audit objective.

2) Be prepared well.

3) Present reasonable information.

4) Statements that audit have been implemented in accordance with Norm of Auditing of SPI.

d. Each of audit report should:

1) Accommodate both findings and audit conclusion objectively and constructive recommendations.

2) Prioritize more on improvement or completion than critic does.

3) Disclose matters that are still unfinished problem until end of audit, if any.

4) Express confession upon prestige or action for improvement that have been implemented, especially if improvement applied on other part.

5) Express explanation of official of audited object about audit result.

5. Follow Up of Audit Result

Follow up audit result is each step of improvement/ completion/control/measurement performed by official/director/the responsible of part/working unit/program/project/activity in congruent with follow up recommendation upon audit result findings of SPI.

Audit result is findings/recommendations and it does not become end of objective, except for more important things is a step of improvement/ completion/control/measurement that performed by official/director/the

responsible of part/working unit/program/project/activity in congruent with follow up recommendation upon audit result findings of SPI.

Audit result findings without performing any follow up is time consuming, energy, and cost. Because of that, SPI should keep going on performed follow up to audit results by authoritative officials.

On category D of Auditing Norm of SPI BUMN/BUMD regulated about norms of follow up upon audit result, which internal auditor should participate on follow up upon audit findings that reported to ascertain correct action that has been taken and implemented.

Monitoring of audit follow up is performed by sending letter/memo once a month to authoritative official that performed follow up from audit result findings. The monitoring letter will be sent back as long as those audit findings has not finished yet to be followed up.

2.2.8. Audit ISO

PT. Timah has applied ISO 9000 and ISO 14001 since 1997. ISO 9001 and ISO 14001 have applied to the whole organization activities/operations. By using ISO standardization, PT. Timah hopes that they will be able to meet market requirements and societal forcers: rationality, practical applicability, environmental protection for sustainable development, safeguard for safety and health, and equal opportunity to engage in the world. Now days, all company should have ISO certificate in order to be more competitive in global market.

As internal auditor of organization, SPI PT. Timah should audit the implementation of ISO 9000 and ISO 14001. The purpose of audit ISO is to calibrate whether implementation of ISO 9000 and ISO 14001 has been applied effectively. SPI PT. Timah scheduling audit upon ISO minimally perform twice a week by appointed auditor and its activity refers to PT. Timah Standard Operating Procedure (SOP) that has been documented and implemented as report feedback for Directors of PT. Timah and process of continual improvement. Auditor that has followed audit training for ISO and appointed auditor should be independent at their area/working unit being audit should implement audit upon ISO. Action for correction that has been implemented by audited object in order to improve each of discrepancy that founded at the time of performing audit ISO. A preliminary audit performed for calibrating whether action for correction has implemented and effectively used by auditor/appointed official and prepared note for report or status from findings of discrepancy has closed out.

The ISO 9000 is primarily concerned with "quality management". The standards definition of quality refers to all those features of a product (or service), which are required by the customer. Quality management means what the organization does to ensure that its product or services satisfy the customer's quality requirements, and complies with any regulations applicable to those products or services. In the case of ISO 9000, the efficient and effective management of processes is, for example, going to

affect whether everything has been done to ensure that product satisfies the customer's quality requirements or not.

The ISO 14001 is primarily concerned with "environmental management". In plain language, this means what the organization does to minimize harmful effects on the environment caused by its activities. In the case of ISO 14001, the efficient and effective management of processes are going to affect whether everything has been done to ensure a product will have the least harmful impact on the environment, at any stage in its life, either by pollution, or depleting natural resources.

2.2.9. Corporate Governance

Forum for Corporate Governance in Indonesia (FGCI) defines Corporate Governance as a set of rules that defines the relationship between shareholders, managers, creditor, the government, employees and other internal and external stakeholders in respect to their rights and responsibilities, or the system by which companies are directed and controlled.

The objective of Corporate Governance is to create added value to stakeholders through:

- Increasing work of company performance.
- Decreasing risk.
- Increasing investor credibility.

Principles of GCG (by Decree of Ministry No. Kep-117/M-MBU/2002) are:

a. Transparency: decision-making and discloses company information.
b. Independent: managing professionally, free from conflict of interest and influence/pressure that not in compliance with laws.
c. Accountability: there is clearly of function, implementation, and responsibility of organization in order to have effectively management.
d. Responsibility. In compliance of management with valid of laws and corporate principles.
e. Fairness: justice and equality on fulfilling right of stakeholders in compliance with agreement and laws of regulation.

Good Corporate Governance urged management organization more democratically (because it is involving stakeholders), more accountable (because there is a system asking for responsibility upon every action), and more transparency. By applying Good Corporate Governance, important decisions are no longer determined by only one dominant party (for example Directors), but determined after getting input from and considering interest of stakeholders.

After facing financial difficulties on the early year of 1990, that was triggered by industry crisis of global tin that endanger business continual life of company, company restructuring its organization in order to recover competition capacity position that took 5 years and finally succeeded for doing privatization through offering public share. Besides that PT. Timah urged management to improve company performance continually.

PT. Timah commits to run exclusive restructuring. In accordance with business reorganization, company also restructured its finances that included quasi-reorganization, to rebuild system and accounting policy and renovation of Management Information System. Basically, quasi-reorganization restructured balances that obey Accounting Principle of Indonesia. Its strategies include deficit abolition on retained earning, assets revaluation, which is lower than its book value, and start from the beginning with zero retained earning, also reconstruction of capital structure. Real impact from quasi-reorganization toward company recapitulation was reducing of capital that deposited by government from Rp 300 billion to be Rp 120 billion, even though government distributed accompaniment of new capital to finance those restructuring. Success implementation of those strategies has avoided PT. Timah acclaimed for bankruptcy based on law.

By following guidance of Good Corporate Governance (GCG) principals, company tried to apply:

- Equality treatment to minority shareholders through establishment of independent commissioner's.
- Transparency disclosing of company performance information accurately and timely performed by Corporate Secretary.
- Management accountability through supervisor that actively performed by Internal Control Unit, Audit Committee, Independent Auditor, and General meeting of Shareholders.

- The responsibilities of company to obey the law and social responsibility to society around company operation area.

CHAPTER III

COMPANY BACKGROUND

3.1. Company Background

Geographically and geologically, Indonesia is a wealthy country. Across the inland and offshore tin reserves controlled by Timah, mineral deposits are some of the best in the world. The company holds tins exploration and mining right until 2025 of more than 10,000 square kilometers spread across several islands and offshore areas in the Java Sea. Timah has secured rights for gold exploration in North Sumatra, Kalimantan and Java. This right extends over 27,000 square kilometers. Even after a long history of tin mining, large portion of Timah's mining rights are as yet unexplored and untapped. The future holds vast potential. South East Asia's tin belt runs 3,000 kilometers from Myanmar to the southern part of Sumatra, averaging about 75 kilometers in width.

Historically, PT.TIMAH Tbk began about 18th century, 1709. Tin was discovered at Merawang and near Muara Alim at South of Bangka. At that time, these regions were under The Palembang Sultanate. On June 2, 1722 there was a monopoly agreement between Palembang Sultanate and VOC of buying tins at Bangka. By the transfer of government between VOC authorizations to Dutch government, there the activity of tin mining industry developed systematically, either by Dutch government or Dutch private entrepreneur.

PT. Timah Tbk. principal place of business is located in Pangkalpinang, Bangka Belitung. The history of company began from Dutch companies as follows:

1. At Belitung, tin mining industry organized by Dutch private enterprise, which was Gemeenscaapelijke Mijnbouwmaatschaapij Billiton (GMB).
2. At Bangka, tin mining industry organized by Dutch government, which was Bangka Tinwinningbedrijf (BTW).
3. At Singkep, tin mining Industry organized by Dutch private enterprise, which was NV Singkep Explotatie Tin Maatschappi (SITEM)

Following the Declaration of Independent of Indonesia in 1945, the tin mining industry gradually came under Indonesian controls as Dutch mining concessions ran out. This transfer of control culminated in 1961 with the Government Regulation No. 87 which established a State Tin Enterprise Coordinating Board and State Enterprise or three tin producing units on Bangka, Belitung, and Singkep Islands. In 1968, the four entities were brought under one single controlling state enterprise by the Government Regulation No. 21, 1968 dated on July 5, 1968, coordinating tin operations under State Company Tambang Timah which was given control of the known tin deposits in Indonesia.

The status of enterprise changed on January 24th, 1976 from PN Tambang Timah to be PT Tambang Timah (Persero), a limited liability corporation with Indonesian Government as the sole shareholder, based on the Government Regulation No. 3, 1976, whereas all rights and obligations, property and equipment of PN Tambang Timah at the time of liquidation moved to PT. Tambang Timah (Persero).

After consolidated as corporate body, based on notary deed of Imas Fatimah, SH No. 1 dated on August 2nd, 1976; PT. Tambang Timah Tbk (the company) was established, in Jakarta as the corporate head office, which was divided into four area of operation unit production based on geographical location. It covered Tin Mining Unit (TMU) Bangka, TMU Belitung, TMU Singkep, and Tin Melting Unit Mentok. The notary deed had been amended several times and the latest is notary deed of Imas Fatimah, SH No. 7 dated May 27th, 1998 JO Number 33, 1990.

On December 31st, 1990 PT. Tambang Timah simplified its organization structure through fusion and closure of several function. Units of production at Bangka, Belitung, Singkep changed into functional units of production. These unit productions are Tin Mining Unit MGM (Mesin Gali Mangkok) and Inland Mining Unit, and then Tin Mining Unit (TMU) Bangka, TMU Belitung and TMU Singkep Island were closed.

As a follow up of company restructuring, on August 2nd, 1991, corporate head office in Jakarta was relocated to Pangkalpinang, Bangka Island as a leading tin producers in Indonesia. Restructuring also included a program modernization and reconstruction of production facilities and concentration on core business activities.

Only in a short time, along with company restructuring program on February 17th, 1992 Tin Mining Unit MGM, Inland Mining Unit, and Tin melting Unit Mentok were closed and then those working units under coordination of PT. Tambang Timah (Persero). The purpose of this program was increasing the effectively of company operations and simplifier it's controlling.

On December 6th, 1994 the organization structure of PT. TIMAH changed, emphasized on an effort in shortening the gap between top management to low level of management and sharpened work-field.

On April 10th, 1995, The Minister of Finance of RI with a Decree No. S-189/MK.016/1995 dated on April 10th, 1995 through The Minister of Energy and Mineral Resources approved about PT. TIMAH capital rising through public offering of B Class shares at stock market.

The Minister of Justice had approved the latest amendment of these articles of association made by notary deed of Imas Fatimah, SH, No. 85 dated July 29th, 1995 and No.11 dated August 4th, 1995 concerning the simultaneous public offering of B Class shares and Global Depository Receipts (GDR) on domestic and international stock exchanges, by Decree No. C2-9985.H.T.01.04.Th.95 dated August 14th, 1995.

On October 19th, 1995 PT. TIMAH Tbk. was listed on Jakarta Stock Exchange (JSE), Surabaya Stock Exchange (SSE), and London Stock Exchange (LSE).

On August 9th, 1996 the name of the company changed to Perusahaan Peseroan (Persero) PT. Tambang Timah Tbk abbreviated to PT. Timah Tbk. and it had approved by The Minister of Justice.

The Minister of Justice had approved the latest amendment of the articles association made by notary deed of Imas Fatimah, SH, No. 7 dated May 7th, 1998, in accordance with the regulation of the Securities and Exchange Commission (*Badan Pengawas Pasar Modal/Bapepam*) No. 13/PM/1997 concerning with the restructuring of a company, by Decree No. C2-5421.H.T.01.04.Th.98 dated on May

27th, 1998. By such changes, the name of the Company changed from PT. Tambang Timah (persero) to Perusahaan perseroan (Persero) PT. Tambang Timah Tbk. abbreviated to PT. Tambang Timah Tbk.

PT. Tambang Timah Tbk. established its subsidiaries for business diversification in accordance with Extraordinary General Meeting of Shareholder on April 24th, 1998, which were: PT. Tambang Timah in accordance with notary deed of Imas Fatimah, SH, No. 73 dated on June 18th, 1998 and approved by the Minister of Justice by Decree No. C2-7752.H.T.01.01.Th.98 dated on June 25th, 1998., PT Timah Industri in accordance with notary deed of Imas Fatimah, SH, No. 74 dated on June 18th, 1998 and approved by the Minister of Justice by Decree No. C2-7751.H.T.01.01.Th.98 and PT. Timah Eksplomin in accordance with notary deed of Imas Fatimah, SH, No. 75 dated on June 18th, 1998 and approved by the Minister of Justice by Decree No. C2-7753.H.T.01.01.Th.98.

3.2. Vision and Mission

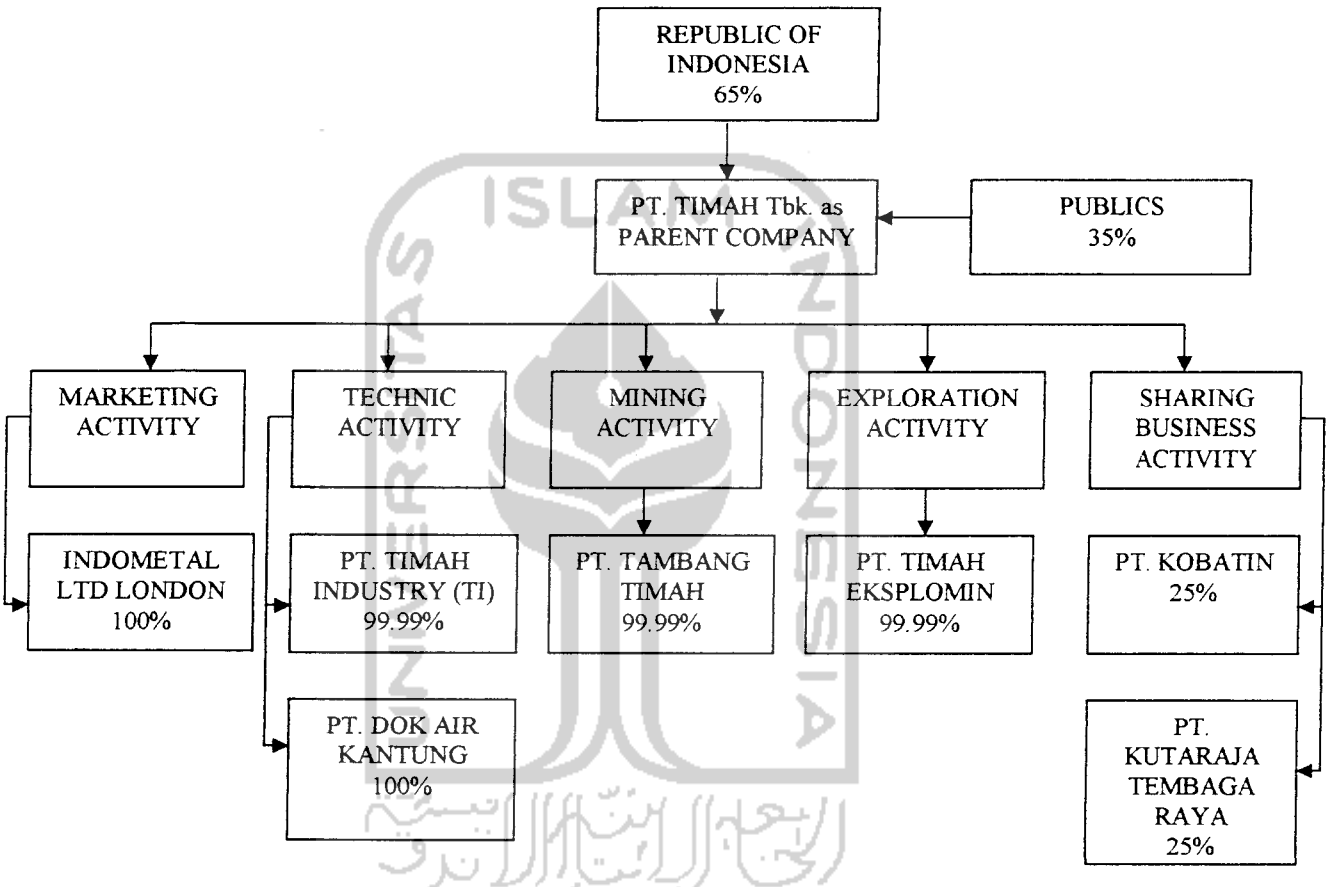
PT. Timah vision is to become a responsible world class company. PT. Timah mission is to provide value for its shareholders, employees and other stakeholders by focusing on the development of its human resource assets. In order to accomplish its mission, PT. Timah Tbk. will focus on:

1. Concentrating on current business and industry in a manner that is more effectively so as to improve the level efficiency.
2. Restructuring and streamlining its organization resources.

3. Using the expertise and competence that the company and its subsidiaries have acquired to develop and expand product and services to higher degree of quality so as add value.
4. Developing company and its subsidiaris new core competence to provide a string foundation for the company's non-tin business.

PT. TIMAH Tbk.

BUSINESS DIVERSIFICATION ORGANIZATION STRUCTURE



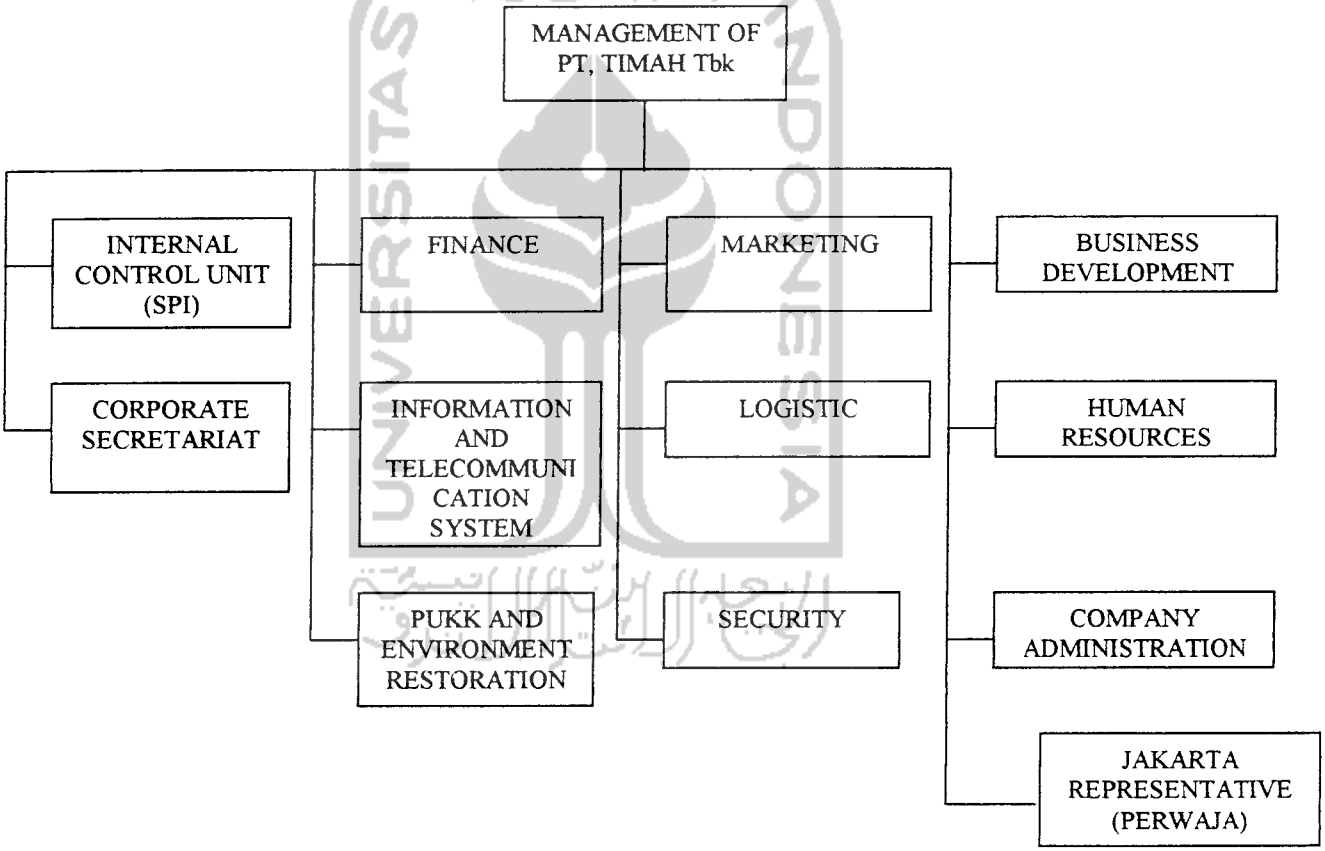
Picture 1: Business Diversification Structure of PT. Timah Tbk. (PT. Timah Tbk. as Parents Company) and each share percentage of shareholders.

3.3. Organization Structure of Business diversification of PT. Timah Tbk.

3.3.1. PT. Timah Tbk

PT. TIMAH Tbk

ORGANIZATION STRUCTURE



Picture 2: PT. Timah Tbk Organization Structure based on The Board of Directors decision of PT. Timah Tbk No.049/Tbk/SK-oooo/2003-B1 dated on April 3rd, 2003

PT. Timah Tbk organization structure based on the result of Annually General Meeting of Shareholder. The Board of Commissioners and PT. Timah Tbk Board of Directors are:

1. The Board of Commissioners of PT. Timah Tbk:
   - President Commissioner : DR. Wimpy S. Tjetjep
   - Commissioner : DR. R. Sukhyar
   - Independent Commissioner : Shanti L. Poesposoetjipto
2. The Board of Directors of PT. Timah Tbk:
   - President Director : Ir. Thobrani Alwi MSM
   - Production Director : Ir. Ari Fauzi, MBA
   - Finance Director : Ir. Wachid Usman, MM
   - HRM Directors : Surawardi MSc, MM

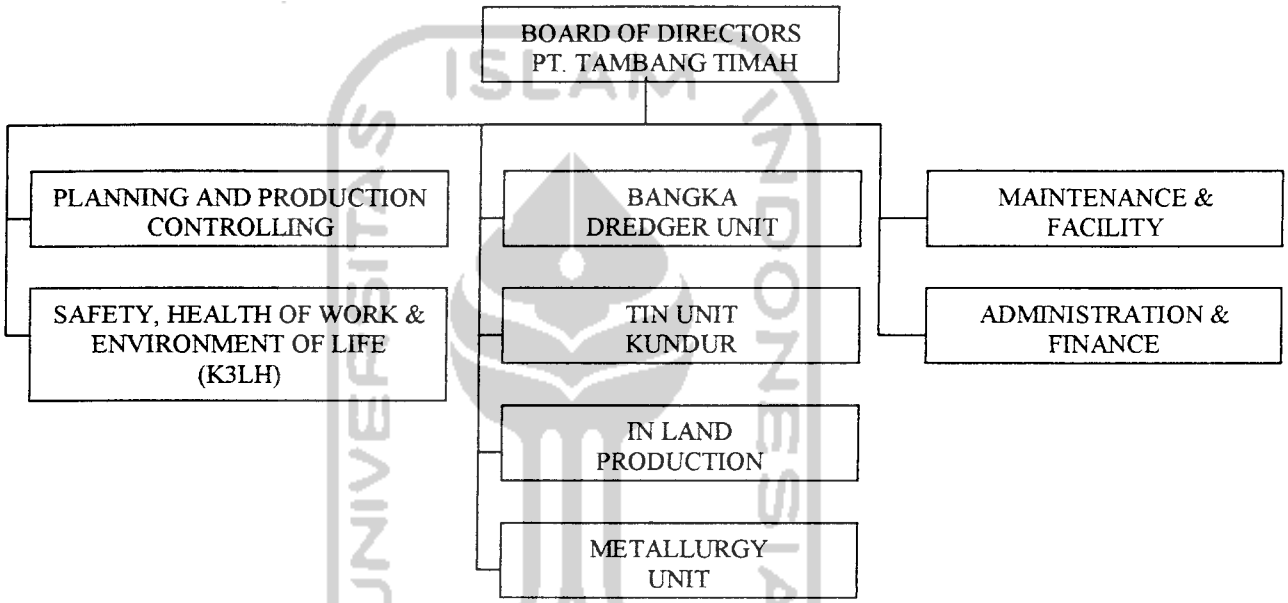
The board of Directors of PT. Timah Tbk, consists of at least three members, one of them appointed as President Director with helped by Production Director, Finance Director, and Human Resource Director. The board of director also helped by several staffs, such as Chief of Internal Control Department (SPI), Chief of Corporate Secretariat, Chief of Finance, Chief of Information and Telecommunication System, Chief of PUKK and Environment Restoration, Chief of Marketing, Chief of Logistic, Chief of Security, Chief of Business development, Chief of Human Resources, Chief of Company Administration and Chief of Jakarta Representative.

PT. Timah Tbk is Holding Company and does not have directly mining operational activity. PT. Timah Tbk forms a center of formulation and control of corporate strategy, and ensures that synergy exists between the operations of various subsidiary companies in the process of creating and adding value. PT.Timah Tbk determines the overall corporate structure of the Group, overall marketing strategies, budgets and allocation of fund, manages corporate finances and the financial affairs of its subsidiaries, sets the Group's values and norms, and determines the course of corporate development of its subsidiaries through alliances and/or acquisition. Government of Republic of Indonesia own 65% of PT. Timah Tbk shares and other shares owned by public of Indonesia either abroad.

3.3.2. PT. Tambang Timah

PT. TAMBANG TIMAH

ORGANIZATION STRUCTURE



Picture 3: PT. Tambang Timah Organization Structure based on Board of Directors of PT. Tambang Timah decision No. 101/TT/SK-1000/2003-B1 dated on May 5th, 2003.

PT. Tambang Timah is Subsidiaries Company and its operational activities are as follows:

a. Focusing on tin mining operational activities from perseroan. PT. Tambang Timah will take over whole tin mining operational activities, not including exploration. So that, assets and liabilities of perseroan that related to tin mining and production activities will be moved to PT. Tambang Timah as subsidiary company.

b. Besides focusing on tin mining operational, PT. Tambang Timah also focuses on mineral substance besides tin and ground material industry.

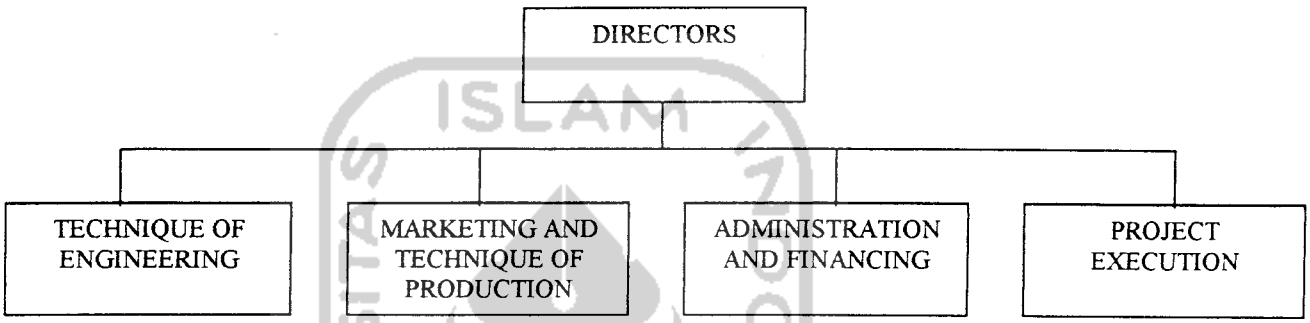
c. Its activities are in trading and services. Tambang Timah shareholders are:

   - 99.99% of shares owned by PT. Timah Tbk
   - 0.01% owned by PT. Timah Investasi Mineral.

3.3.3. PT. Timah Industri

PT. TIMAH INDUSTRI

ORGANIZATION STRUCTURE



Picture 4: PT. Timah Industri Organization Structure based on decision of PT. Timah Industri Directors No. 024/TI/SK-2000/2003-B1 dated on May 1st, 2003.

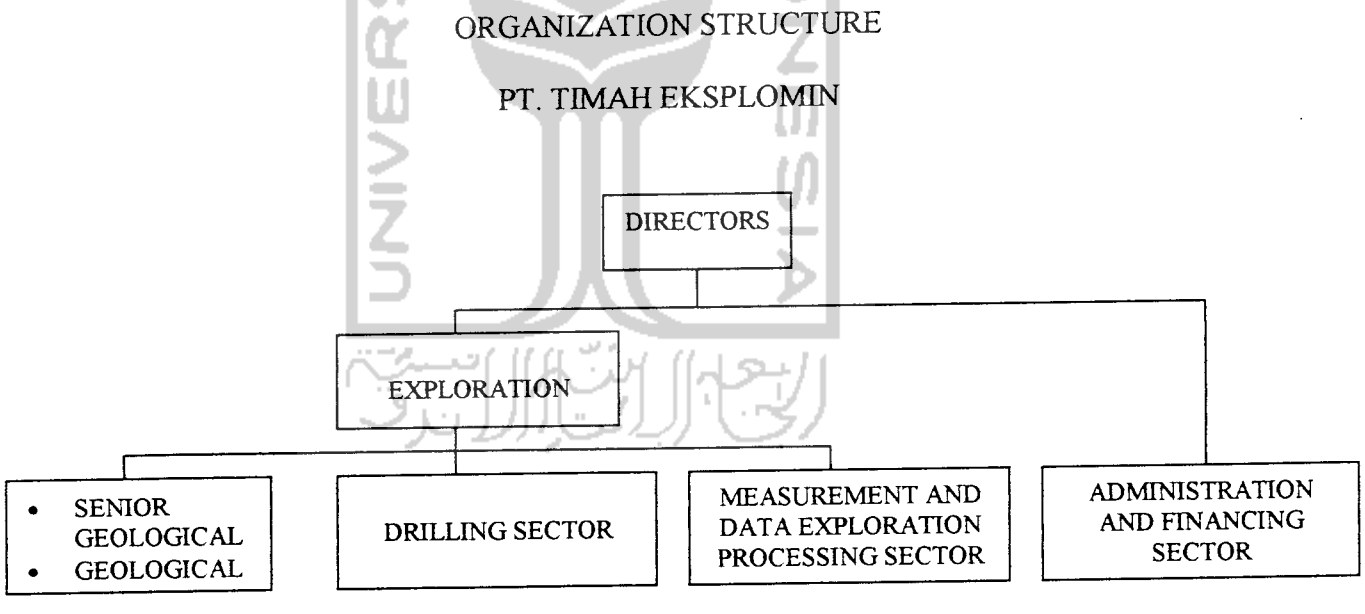
PT. Timah Industri is a new company subsidiary. PT. Timah Industri work-fields are trading, planning, technique, industry, and services. PT. Timah Industri focuses on operational technique activity, workshop and operational supporting. PT. Timah Industri will take over whole activities of techniques, workshop, and operational supporting activities from perseroan. PT.Timah Industri shareholders are:

- 99.99% of shares owned by PT. Timah Tbk.
- 0.01% owned by PT. Timah Investasi Mineral.

3.3.4. PT. Dok and Perkapalan Air kantung (DAK)

At beginning PT. Dok and Perkapalan Air kantung (DAK) is a ship dry dock, alliances between perseroan and PT. Dok and Perkapalan Kodja Bahari (persero). But now, its share 100% is owned by PT. Timah Tbk. PT. Dok and Perkapalan Air Kantung (DAK) gives ship dry dock services along with reparation and ship maintenance to PT. Tambang Timah or other companies.

3.3.5. PT. Timah Eksplomin



Picture 5: PT. Timah Eksplomin Organization Structure based on decision of PT. Timah Eksplomin Directors No. 011/TE/SK-3000/2003-B1 dated on April 9th, 2003.

PT. Timah Eksplomin work-fields are mining research, exploration, laboratory analysis of ground mineral example, the making of properness study pembuatan studi kelayakan, geology technique research, and geo-hydrology research. PT. Timah Eksplomin focuses its operational activities on exploration and services to tin and non-tin mining. PT. Timah Eksplomin accept transfer of tin mining exploration activities from perseroan. PT. Timah Eksplomin shareholders are:

- 99.99% of shares owned by perseroan
- 0.01% of shares owned by PT. Timah Investasi Mineral.

3.3.6. PT. Koba Tin

PT. Koba Tin is an alliance company between perseroan and Kajuara Mining Corporation from Australia, with 25% of shares owned by perseroan and 75% of shares owned by Kajuara Mining Corporation from Australia. PT. Koba Tin operation is based on contract of work with Indonesian Government. At this time Kajuara Mining Corporation had sold its shares to mining company from Malaysia.

3.3.7. PT. Kutaraja Tembaga Raya (KTR)

KTR is Alliances Company between perseroan and Phelps Dodge Australia Inc. perseroan owns its 25% of shares and Phelps Dodge Australia Inc owns 75% of shares. Based on its regulation, PT. Kutaraja Tembaga Raya (KTR) is allowed

running on its business on gold mining, gold marketing, and import of goods related to gold mining.

3.3.8. Indometal (London) Ltd

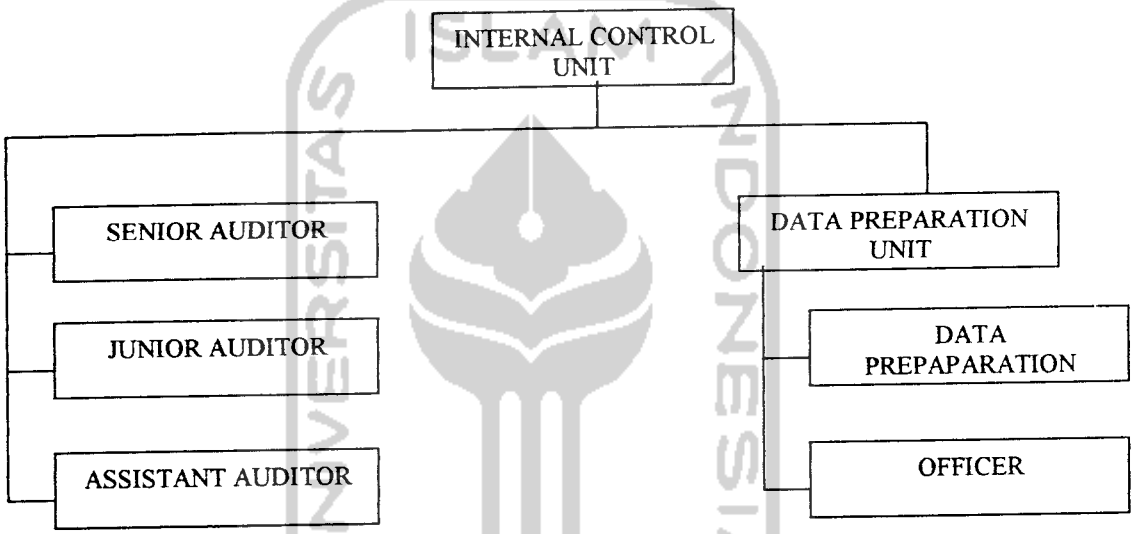
Indometal (london) Ltd is a subsidiary company of PT. Timah Tbk where 100% of shares is owned by PT. Timah Tbk. Indometal (London) Ltd established in London on January 22, 1988 with its purpose is supporting PT. Timah Tbk marketing activities on European.

3.4. Internal Control Department (SPI) of PT. Timah Tbk.

ORGANIZATION STRUCTURE

INTERNAL CONTROL DEPARTMENT

AT PT. TIMAH Tbk



Picture 6: Internal Control Department (SPI) Organization Structure of PT. Timah Tbk based on the Board of Directors decision of PT. Timah Tbk. No. 049/Tbk/SK-0000/2003-B1 dated on April 3rd, 2003

SPI Job Descriptions are as follow:

1. Chief of SPI

   Chief of SPI will be responsible for helping a president director in performing internal audit and evaluation of the effectively of whole operation activities of company internal control comprehensively. Besides that, Chief of SPI responsible

is for formulating and analyzing the performance of company policies at SPI department, and provides information upon data related to controlling and internal audit. Chief SPI is also responsible for being company counterpart in managing company external audit.

2. Senior Auditor

   Senior auditor is responsible for helping Chief of SPI in formulating company policies at SPI department and reporting the result of controlling, and managing the performance and analyzing the company policies. This is responsible as team leader of internal audit either on Annually Audit Working Controlling (PKPT), non Annually Audit Working Controlling (PKPT), or internal audit to ISO 9001, 9002, and 14001.

3. Junior Auditor

   Junior auditor is responsible as internal audit team leader and/or as an auditor staff in performing of internal audit, obtaining data, analyzing, collecting audit evidence, and researching data/information related to internal audit activities to PKPT, non-PKPT, and ISO.

4. Assistant Auditor

   Assistant auditor is responsible as auditor executor or as an internal control in performing internal audit, obtaining data, collecting audit evidences, and researching data/information related with internal audit activities.

5. Chief of Data Preparation

   Chief of Data Preparation is responsible in planning, coordinating, and controlling the performance activities to PKPT and Non-PKPT (The Board of Directions decision through Chief of SPI), evaluating follow-up of audit result (PKPT, Non-PKPT, ISP 9001/9002 and ISO 14001), company budget, preparing audit findings systematically and problems that are still in process or problem already finished to solve. Besides that, Chief of Data Preparation is also responsible in helping out the smooth performance of audit whether internal or external and coordinating SPI administration activities.

6. Data Preparation

   Data preparation is responsible for controlling and maintaining data/documents either hardware or software of performing PKPT and Non-PKPT activities (The Board of Directors decision through Chief of SPI), and evaluating audit follow-up (PKPT, Non-PKPT, ISO 9001, ISO 9002, and ISO 14001), systematically, either problems that are still in process or already being solved.

CHAPTER IV

RESEARCH FINDINGS, DISCUSSION AND IMPLICATIONS

4.1. Audit Planning

The establishment of Yearly Audit Working Program (*PKPT/Program Kerja Pengawasan Tahunan*) plans to be performed every July concerning to company activities in making Company Budgeting Working Planning (*Rencana Kerja Anggaran Perusahaan/RKAP*), whereas at that time each of working unit make their own working program.

Internal Control Unit establish Yearly Audit Working Program , by meaning all controlling activities will be able to achieve expected target and result, because of that the establishment of Yearly Audit Working Program should be finished before annual balancing of books in order to get cost estimation of implementation of Internal Control Unit activities for next year including budgeting of Yearly Audit Working Program.

Yearly Audit Working Program is one of tool of management controlling and used as a guidance for auditor to perform integrated controll to State Enterprises (BUMN) and other corporations.

In compliance with audit target of Internal Control Unit of State Enterprises and other corporations, PT. Timah Tbk. Internal Control Unit arranges Yearly Audit Working Programs for:

1. Activities report (such as financial report, production report, etc).
2. Smooth services of corporation to public.

3. Safeguarding State Wealth (for example possibility of leaking of secret, wastefulness, etc).
4. State Enterprise loyalty to the prevailing regulation.
5. The increasing of economic expending and increasing of efficiency and efffectivenes.

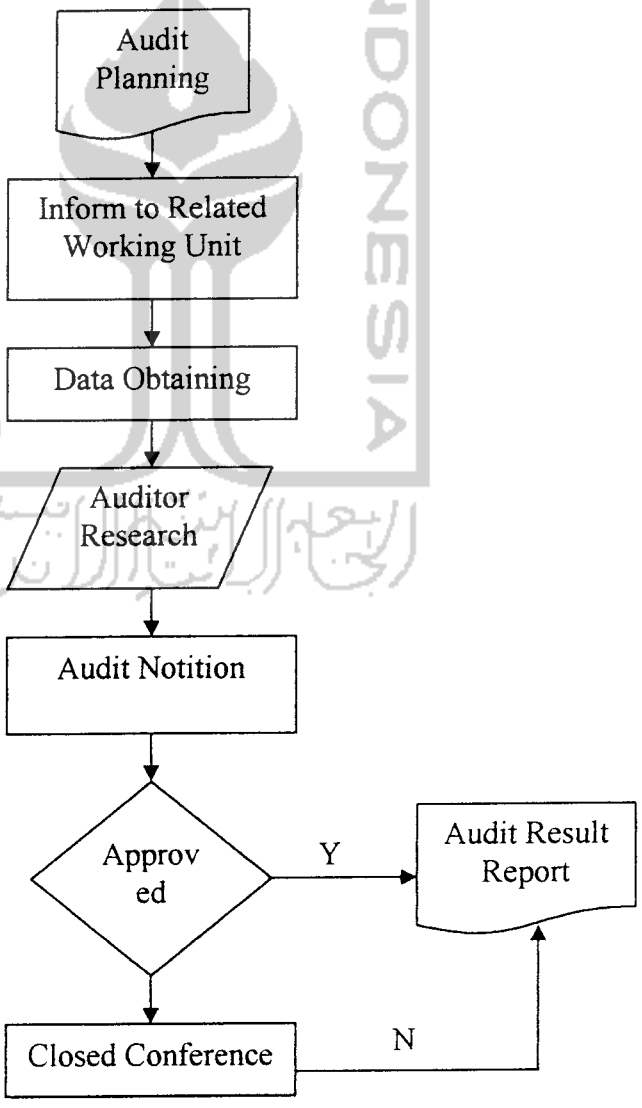
Audit target above is spelled out into group of audit target, as follows:

1. Financial Audit
    - Appraisal/evaluation of accounting and financial controlling system.
    - Audit of completeness and fairness of financial report.
    - Compliance audit to the prevailing regulation (including compliance to punctuality of financial report publishing).
    - Audit to state of wealth safeguarding.
    - Reexamined analysis of financial report.
2. Operational Audit
    - Smooth services of State Enterprises to public.
    - Audit compliance to prevailing regulation.
    - The increasing of economy expending and increasing of efficiency and effectiveness.

From the result of audit target analysis, then schedule of Yearly Audit Working of Internal Control Unit has been arranged. As a consequence of Yearly Audit Working Program, cost emerged will be accomodated into Company Budgeting Working Planning (*Rencana Kerja Anggaran Perusahaan/RKAP*).

In fact, during performing audit there are some parts of Yearly Audit Working Program Planning that cannot be conducted (for example appendix 2, which is realization of Yearly Audit Working Program of year 2002), it was caused by Directors instruction to perform audit of certain things that considered important to be audited, it was called as Audit non-Yearly Audit Working Program.

4.2. Audit Implementation



Audit is performed by Internal Control Unit based on established Yearly Audit Working Program. Internal Control Unit of PT Timah Tbk. Performing audit since instruction letter issued by Chief of Internal Control Unit as a base for audit team in performing audit.

Instruction letter accepted by audit team and its carboncopy will send to chief of related working unit as an announcement for them that their working unit will be audited.

Next step is audit program establishment by audit team. Audit program is a guidance for audit team that consists of audit procedure list to be followed during audit and also states the objectives of the audit. By having audit program, audit team will be able to accomplish audit objectives, because audit program will make their audit work more organized and focused and it has clear job sharing among other members of audit team so that none of all audit activity planning will be left behind during performing audit.

After establishing audit program, audit team obtain background information about activities to be audited by doing desk work, which is collecting information such as organization structures, job descriptions, prevailing regulations and procedures, etc. Internal Control Unit will take information from their own files because they always keep all information (information always up to date) on permanenet files and current files, so it will make their work more easier. Besides keeping files from their own sources, Internal Control Unit also lends other important files from other working units for supporting data. Besides performing desk work, audit team also performs field observation in order to see and to

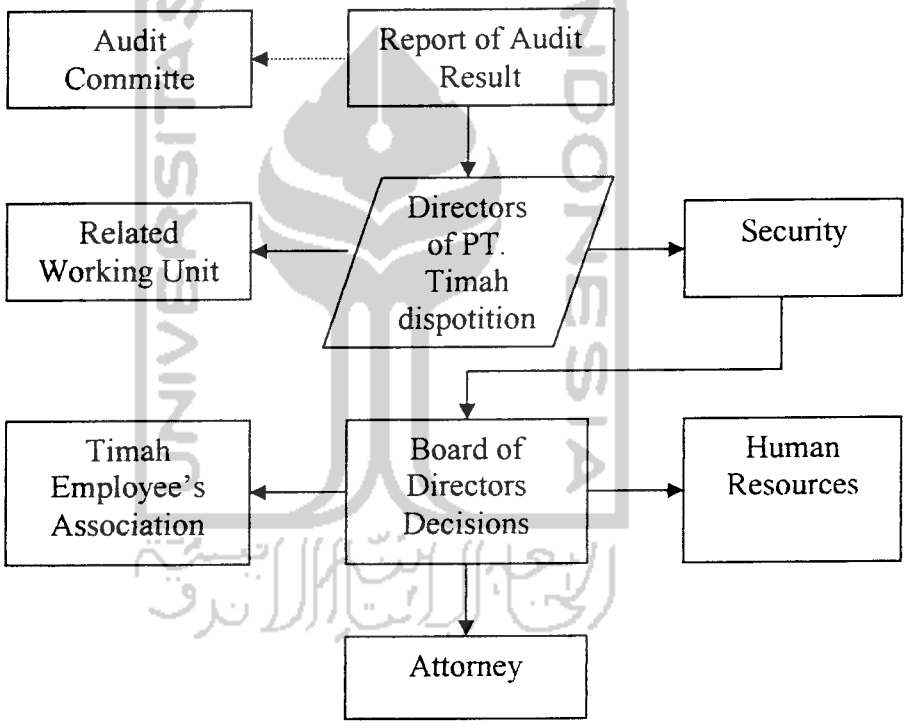
observe directly activity process of auditees. It is intended to see whether auditees have any indication of inefficiency and ineffectiveness and also will be able to increase auditor understanding about auditees problems. During field observation audit team interviews auditess in order to obtain deep information and confirmation of auditees activity.

After all audit working above has been performed, then audit team will analyze, interpret and prove reliability of information to support audit result. By doing this activity audit team will be able to find out whether all activity performed by auditees is in compliance with prevailing regulation, whether activities has been performed effectively, efficiency and economically and also able to find deviation (audit team suspect wrong doing) by auditees, such as possibility of fraud action by PT. Timah Tbk. official/employee

Based on the result of audit team work, audit team will issue interim report to related working unit which requires immediate attention (opinion). Interim reports may be written or spoken and may be transmitted formally or informally. If auditees agree with interim reports then report, of audit result can be establish directly. But to convince audit finding and recommendations on interim reports and if auditees do not accept interim report contents, then audit team will hold Closed Conference to discuss and review conclusions and recommendations. These discussion and reviews help to ensure that there has been no misunderstandings or misinterpretations of fact by providing opportunity for the auditee to clarify specific items and to express views of the findings, conclusions, and recommendations.

After contents of interim report accepted by auditees whether at the issuance of interim report or at closed conference, recommendations will be distributed to directors and chief of auditees for taking corrective action in order to improve weaknessess based on audit team recommendations.

4.3. Following Up Report of Audit Result



Report of audit result is published preferably in writting and delivered only to President Director of PT. Timah Tbk. Report of audit result includes scope of audit and audit objectives and it should be well arranged and clearly defined so that all parties who read report of audit result will understand its contents and

purpose of report of audit result. Report of audit result also provide proper information as an input for related parties, by providing report of audit result with findings and constructive recommendations for improvement. Report of audit result give its priority to improvement.

Each report of audit result is signed by Chief of Internal Control Unit and based on this report of audit result, President Director of PT. Timah Tbk. will make dispotition as basis for following up the audit and it will be forwaded to related working unit and security.

Dispotition from President Directors of PT. Timah Tbk. related working unit is constructive suggestion/recommendations for improvement of each problems finding on report of audit result. Based on its dispotition, Internal Control Unit will monitor related working unit activities to ascertain whether they have taken appropriate corrective action and achieved desired result or Internal Control Unit has assumed that they are not taking corrective action for improving their weaknesses.

Dispotition of President Director will be forwarded to security if any discipliner action/corruption indication are conducted by employees of PT. Timah Tbk. for performing intensive investigation. After investigation has finished , security will establish Official Report Investigation enclosed with reccommendations for punishment. This Official Report Investigation will be delivered to Board of Directors.

Based on Official Report Investigation, Board of Directors will make varied decision depend on its kind of violation/deviation conducted by employees of PT.

Timah Tbk. Board of Directors decision are warning either in spoken or writting and also suspension from their job).

For employee suspending, before making decision, Board of Directors should inform and asking for judgement/opininon from Timah Employee's Association whether that employee is proper to suspend or not (in compliance with cooperation agreement between employee of PT. Timah Tbk. and Timah Employee's Association. Then opinion from Timah Employee's Association is delivered to Board of Director as an input for the problems.

Meanwhile for high violation and can not be solved internally, for example law violation by employee of PT. Timah Tbk. and its violation has significant effect to company, then Board of Directors will remand that problem to outside party (attorney).

Besides delivered to Directors, report of audit result is also informed to audit committe as consequences of the appliance of Good Corporate Governance by PT. Timah Tbk.

4.4. Audit Operational of Dredger Kundur I Reconstruction

A. Basis of this audit operational of Dredger Kundur I Reconstruction are based on:

1. Directors Decision Letter no. 1512/SK-0000/94-B1 dated on December 29, 1994 about *Pedoman Pengawasan dan Pemeriksaan SPI di lingkungan PT. Tambang Timah (Persero).*
2. Yearly Audit Working Program (Program Kerja Pengawasan Tahunan/PKPT).
3. Instruction Letter from Chief of Internal Control Unit no. 009/Tbk/Print-0120/98-B1 dated on August 12, 1998.

B. Scope of Audit Operational

This audit objectives is to evaluate internal control structure, obediance to prevails regulation and also its efficiency, effectiveness, and economic of Dredger Kundur I Reconstruction.

Audit has performed by sampling to dismantling documents, transportation from Malaysia to Bangka Island, Indonesia and reconstruction/modification of Dredger, including physical examination.

C. Audit Result

From the audit operational performed by audit team to The Reconstruction of Dredger Kundur I, audit team concludes all audit result to audit notice. Audit notice are sent to related parties;they are Chief of Accounting of PT. Tambang Timah, Chief of Technique and Tool of PT. Timah Industri and Chief of Supplying and Warehousing of PT. Timah Industri.

1. Audit notice sent to Chief of Techique and Tools of PT. Timah Industri, among this audit findings are:

   a. 16 units of Inverter Welding Supply of ex Reconstruction of Dredger Kundur I which were valued for Rp. 180,571,752.50 and 21 units of Radio VHF Motorolla which were valued for Rp. 85,498,500,00 of ex Reconstruction od Dredger Kundur I not completed with suppotred documents (*Bukti Pemindahan Barang Inventaris/BPBI*).

   75 unit of Inverter Welding Supply has been bought (type 600 GMS and type 300 GMS) and they cost Rp. 724,704,409,000.00 for the need of Balai Karya Kundur, reconstructions of dredger Kundur I and dredger Menumbing. From 75 unit of Inverter Welding Supply, 43 of them were sent to Reconstruction of Deredger Kundur I location gradually and also completed with inventory number (barcode), but 16 unit of Inverter Welding Supply, which were 4 units of tpe 600 GMS @ Rp. 12,109,278.75 and 12 units of type 300 GMS @ Rp. 5,520,925.00 were not completed with supported document (*Bukti Pemindahan Barang Inventaris/BPBI*), so that the existence of assets could not be found.

   31 units of Radio VHF Motorolla were purchased through contract of ordering goods based on the list that made by Telkom on September 11, 1998. radio VHF at dredger were 10 units. The rest of (21 units) spreaded to various object but not completed with supported supported documents and its value was Rp. 85,498,500.00

Response from them upon audit notice from audit team, regarding to this problem was Project team of Reconstructions of Dredger of Kundur I would trace the existence of their assets as soon as possible and make BPBI for inventory/assetrs that do not have BPBI.

b. Material Ponton of Dredger Kundur used for the reconstruction of Deredger menumbing for Rp. 108,074,296 was not being corrected yet (its entry bookeeping)

Based on evidence of *Bon Sementara Pengeluaran Barang (Bon Pinjam)* and report of material used of Deredger Kundur I project made by material supervisors PT. Dok Air Kantung (DAK) and PT. Timah Tbk., the report was materials used/lent from Dredger Kundur I, they were profil and plate for the need of Dredger Menumbing Reconsructions on November-December 1996 along with preparation of Ponton Reconstruction of Dredger Kundur I.

Materials used for Dredger Menumbing were recorded on list/report of acceptance and uses of material of Plate and Profil of Dredger Kundur I until May, 1997 made by material supervisor of PT. DAK dated on June 1, 1997 and known by material supervisor of PT. Timah but only for PT. DAK it self.

And it was recorded again on report of acceptance/used of material of Dredger Kundur I until August 1997 that was made on August 26, 1997 and report of acceptance/uses of material of Dredger Kundur I until September 1997 that made on September 1997. These report only made for

the need of project team of Dredger Kundur I as data supporting of Working Realization Report, not confirmed to cost accounting so that entry bookeeping would never be done.

So that, cost capitalization of Ponton Reconstruction of Dredger Kundur I was Rp 108,074,296.

Response from them upon audit notice from audit team, regarding to this problem were:

- On November-December 1996, Plate and Profil has been lent/used for the need of Dredger 13 Menumbing reconstruction (according to list of material used recapitulazation that lend from Dredger 22 Kundur I dated February 12, 1997.
- Cost transfer to rescent capitalization of Dredger 13 Menumbing Reconstruction with memo no. 499/Ti/MO-2111/98-S7 on October 16, 1998 had been followed up.

2. Audit notices that sent to Chief of Supplying and Warehousing of PT. Timah Industri.

   a. Payment for the rest of contract for dismantling of Dredger Kuala Langat to Siew Seng Engineering Sdn. Bhd for MYR 389, 500.00 or Rp. 2,184,082,100.00 on August 1998 was late so PT. Timah Tbk. used higher rate of exchange.

   Paying of a debt for MYR 389,500.00 paid on August 1998 should be done on year 1997, when rate of exchange was still lower that was Rp370,002,064.00 (rate of exchange on November 1997 was Rp

3,300/USD and MYR 3,47/USD), so that PT. Timah could save budget for Rp. 2,184,082,100.00 – Rp. 370,002,064.00 = Rp. 1,814,080,036.00

Response for them was paying debt for temporary Retensi could not be paid at that time, considering bargaining price from Siew Seng Sdn. Bhd for reselling of old Ponton, Scarp Steel, Scrap Cable just got it on May 29, 1998, where it result cut from the rest of Retensi.

D. Recommendations

1. Recommendation for audit finding to Chief of Technique and Tool of PT. Timah Industri. are:

   a. 16 units of Inverter Welding Supply of ex Reconstruction of Dredger Kundur I valued for Rp. 180,571,752.50 and 21 units of Radio VHF Motorolla valued for Rp. 85,498,500,00 of ex Reconstruction od Dredger Kundur I not completed with suppotred documents (*Bukti Pemindahan Barang Inventaris/BPBI*).

   Recommendations were:

   - leader of project should trace the existence of assets as soon as possible. If last holder of assets did not prove the existence of its physical assets, then it would process further and get sanction in accordance with prevails law regulation of company.
   - Each Rescent made list of inventory and reported it to Cost Accounting for inventory/asset that did not have supported document, which BPBI would be made soon.

- To increase supervison for asset, barcode should put to each inventory that did not have barcode and also for new inventory that come out from warehouse.

b. Material Ponton of Dredger Kundur used for the reconstruction of Deredger menumbing for Rp. 108,074,296 was not being corrected yet (its entry bookeeping).

Recommendations were:

- Project team of Reconstruction of Dredger Kundur I (Technique and Tool) would soon report list of material used of Dredger Kundur I by Deredger 13 Menumbing to Cost Accounting.
- Chief of Accounting would transfer cost from rescent capitalization of supplying cost of Dredger Kundur I to rescent cost capitalization recondition of Dredger Kundur 13 Menumbing based on list of material used from Technique and Tool.
- On team, project should include personnel from accounting and PDI (Pengendalian Dana Investasi), so team project would have good cooperation on project implementation.

2. Recommendation for audit finding to Chief of Supplying and Warehousing of PT. Timah Industri were:

a. Payment for the rest of contract for dismantling of Dredger Kuala Langat to Siew Seng Engineering Sdn. Bhd for MYR 389, 500.00 or Rp. 2,184,082,100.00 on August 1998 was late so PT. Timah Tbk. used higher rate of exchange.

Recommendations are:

- Technique and Tool should cooperate each other better with Supllying, so that it would smooth supplying goods/services needed and its payment.
- Supplying increased their carefulness in studying contract and previous payment before making Payment Demand Notes (*Nota Permintaan Pembayaran/NPP)* for next payment, so that it would not be mistaken on payment.

CHAPTER V

CONCLUSIONS AND RECOMMENDATIONS

5.1. Conclusions

Based on the result of operational audit performed by Internal Control Unit as an internal auditor of PT. Timah Tbk. can be obtained conclusions as follows:

1. Basically internal audit performed at PT. Timah Tbk. was in accordance with regulation according to Auditing Standard of SPI BUMN/ BUMD and PT. Timah Standards and regulation about SPI.
2. Audit planning realized by established Yearly Audit Working Program (*Program Kerja Pengawasan Tahunan/PKPT*) clearly and in detailed, so that audit activity performed by Internal Control Unit would have clear direction, but in practice, it still found out that audit performance was not in accordance with audit time schedule. It was because during the time of PKPT implementation, director was in charge SPI with special instruction in order to perform audit of certain matters (audit non-PKPT). As consequences of Audit non-PKPT some of PKPT planning could not be implemented based on the schedule because of employee limitedness at Internal Control Unit that caused limitation of time to perform audit PKPT based on time scheduled. Nevertheless, some parts of audit PKPT that could not be implemented at that time will be implemented in the next year.

3. Audit activity performed by Internal Control Unit was based on PKPT schedule already decided before. Basically it was performed based on procedures (in accordance with flowchart) that had been set up by Chief of Internal Control Unit. But in practice, some of audit activity that performed by Internal Control Unit, audit team did not establish audit program though audit program was parts of audit procedures that should be followed by them when performed audit. It was all because of audit teams were experience and used to performed audit to related working unit so they already knew what producers that should be done during performing the audit.

5.2. Recommendations

From conclusion above, in order to improve Internal Control unit performance can be suggested that even though audit teams are experience and used to perform audit frequently to related working unit at PT. Timah Tbk., they should make audit program for each audit activity. The purpose of it, if there are other parties that want to see audit activity that have been performed by audit team. From audit program they can find out what procedures taken by audit team during performing audit. Besides that if staff of Internal Control Unit is transferred into other department, their result of audit will be able to find out without asking from transferred staff of SPI.

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