

III. Professional Infrastructure

This chapter describes Indonesia's professional accountancy infrastructure. Where appropriate, it compares Indonesian arrangements with relevant international standards and guidelines (see Appendix 4). The chapter is structured as follows:

- 1 – Introduction – describes the historical development of Indonesia's accountancy profession.
- 2 – Professional Organization and Regulation – discusses the assignment of professional functions and describes the legislation and organizations that regulate the profession and the professional bodies that represent accountants.
- 3 – Ministry of Finance (MOF) – describes the functions of the Directorate for Supervision of Accountants and Appraisers (*Direktorat Pembinaan Akuntan dan Jasa Penilai, DPAJP*).
- 4 – Indonesian Institute of Accountants (IAI) – examines the structure and activities of *Ikatan Akuntan Indonesia* (IAI), the national professional accountancy organization.
- 5 – Indonesian Accountancy Qualifications – describes and examines the four Indonesian accountancy qualifications.
- 6 – Other Professional Organizations – discusses the activities of related professional associations, such as the Indonesian Chapter of the Institute of Internal Auditors (IIA).
- 7 – The Appraisal (Valuation) Profession – describes the Indonesian appraisal profession and the challenges it faces.
- 8 – Globalization and Liberalization Challenges – describes the challenges posed by liberalization and how the profession is responding to these.
- 9 – Professional Quality Control and Assurance – describes and examines the arrangements and mechanisms that are intended to support professional quality control. These include legislative sanctions against negligent auditors and provisions for civil actions.
- 10 – The Draft Public Accountant (PA) Law – describes development of the draft PA Law.
- 11 – Issue Synopsis: Professional Infrastructure – summarizes the issues identified in this chapter.

1. Introduction⁵⁵

76. There was no domestic accountancy profession until the 1950s—almost all Indonesian accountants were Dutch-trained and professionally qualified. The enactment of the *Accountant Title Law (No. 34) 1954 (Undang-undang Tentang Pemakaian Gelar “Akuntan”)* provided the foundation for training Indonesian accounting graduates, restricted use of the Accountant title, required accountants to register with the Ministry of Finance (MOF) and authorized the Finance Minister to regulate the profession.

77. In 1957, the first group of accounting students graduated from the University of Indonesia. However, local Dutch auditing firms did not recognize their qualifications. Later that year, together with senior Indonesian Dutch-trained accountants, these graduates established the Indonesian Institute of Accountants (*Ikatan Akuntan Indonesia, IAI*) in 1957. Its objectives, among other things, are to promote the status of the accounting profession, support national development and upgrade the skills and competence of accountants.

Table 13. Development of the Indonesian Accountancy Profession

1954	Enactment of <i>Accountant Title Law (No. 34) 1954</i> provides the foundation for training Indonesian accounting graduates, restricts use of the Accountant title, requires accountants to register with the MOF and authorizes the Finance Minister to regulate the profession.
1957	First accounting graduates emerge from the University of Indonesia and, together with senior Dutch-trained accountants, establish the Indonesian Institute of Accountants (IAI).
1960s	Decrease in financial activity reduces demand for accountancy services and impedes the profession's development.

⁵⁵ Primary Sources:

- Bachtiar, Emil. 2001 August. The Professionalization of Accounting in Indonesia. Paper presented to the Second International Accounting History Conference, Osaka, August 2001.
- Diga, Joselito and Hadori Yunus. 1997. “Accounting in Indonesia” in *Accounting in the Asia-Pacific Region*, edited by Nabil Baydoun, Akira Nishimura and Roger Willet. John Wiley: Singapore. pp. 286-287.
- Foo, See Liang. 1997. “Indonesia” in *Financial Reporting in the Pacific Asia Region*, edited by Ronald Ma. Singapore: World Scientific Publishing. pp. 347-364.
- Siddik, A. F. and H. L. Jensen. 1984. *The Evolution of Accounting in Indonesia*. The Academy of Accounting Historians.
- Yunus, H. 1990. History of Accounting in Developing Nations: The Case of Indonesia. *Tim Koordinasi Pengembangan Akuntansi*, Jakarta.

PROFESSIONAL INFRASTRUCTURE

- 1967 In permitting the first partnership between a local KAP and an international KAP, government requires the international KAP to support accountant training and development of the profession.
- 1971 Although MOF Decree No. 76/1971 restricts the terms and conditions of partnerships, six major international KAPs establish correspondent firms with Indonesian KAPs between 1971 and 1975.⁵⁶
- 1974 Indonesian Accountancy Development Foundation (YPIAI) formed to support the profession's development.
- 1985 Coordinating Agency for Accountancy Development (TKPA) supersedes YPIAI. Its mission is to develop accounting education, the accounting profession, a set of professional standards and a code of ethics. It eventually closes in 1994
Association of Internal Auditors of State-Owned Enterprises and Local Government SOEs (FKSPI BUMN/BUMD) formed to improve internal auditing practices.
- 1986 Finance Minister Decree stipulates requirements for establishing a KAP and legitimizes KAP correspondence relationships with foreign firms (KAPAs).⁵⁷
- 1988 World Bank-supported *Accountancy Development Project* begins—it operates until 1994.
- 1994 IAI Public Accountants Professional Standards Committee (KSPAP) issues Professional Standards for Public Accountants (SPAPs).
- 1995 Second World Bank-supported *Accountancy Development Project* commences—it closes in 2000.
Capital Markets Law (No. 8) 1995 with associated regulations, introduces controls over PAs and KAPs engaged in capital market activities.
ASEAN member countries agree to liberalize trade in services and to mutually recognize each other's service suppliers, including accountants.
- 1997 International-standard Public Accountant Certification Examination (USAP) introduced.
Finance Minister Decree on Public Accountant Services (No. 43/KMK.017/1997) tightens licensure procedures, strengthens oversight and (ostensibly) introduces penalties for erring PAs. PAs must now gain a license to practice, but citizenship requirement is removed.
Asian Financial Crisis hits Indonesia hard. Many companies and banks, whose financial statements had been given clean audit opinions, collapse in its wake.
- 1998 ADB-supported FGRSDP requires legislation and regulations making: (i) auditors liable for negligence in performing audits; and (ii) directors liable for false information in annual reports and other public information.
- 1999 Finance Minister Decree amendment reiterates government-licensing requirement.

⁵⁶ Diga, Joselito and Hadori Yunus. 1997. "Accounting in Indonesia" in *Accounting in the Asia-Pacific Region*, edited by Nabil Baydoun, Akira Nishimura and Roger Willet. John Wiley: Singapore. pp. 286.

⁵⁷ Finance Minister Decree No. 763/KMK.011/1986 on Public Accountants.

2000	IAI approves revised Rules of Conduct for Public Accountants.
2001	MOF-BPKP review finds that ten KAPs violated professional standards in relation to their audits of 38 liquidated banks. Unable to impose sanctions, government issues warning letters. MOF Academic Paper proposes basis for a new Public Accountant Law. MOF assumes responsibility for quality assurance over PAs and KAPs from BPKP.
2002	IAI considers breaches by ten KAPs. Three are acquitted on all charges, three are ordered to undergo retraining and four are given a strong warning and temporarily barred from auditing banks.

78. During the 1960s, the decrease in financial activity reduced demand for accountancy services and impeded the profession's development. Changed conditions towards the end of the decade provided renewed impetus for growth. In particular, a Finance Minister Decree made IAI membership compulsory for licensed accountants. In 1973, IAI established the Accountant Examination Norm Committee (*Komite Norma Pemeriksan Akuntan, KNPA*) to support improvements in examinations. The Indonesian Accountancy Development Foundation (*Yayasan Pengembangan Ilmu Akuntansi Indonesia, YPIAI*) was formed in 1974 to support the profession's development through training programs and research activities. The Coordinating Agency for Accountancy Development (*Tim Koordinasi Pengembangan Akuntansi, TKPA*) superseded YPIAI in 1985. IAI and the World Bank supported TKPA's activities until its closure in 1993. Its mission was to develop accounting education, the accounting profession, a set of professional standards and a code of ethics.⁵⁸

79. Further progress was made in the 1990s under the World Bank-sponsored *Accountancy Development Projects*.⁵⁹ Accounting and auditing standards were developed, professional standards were strengthened and the Public Accountant Certification Examination (*Ujian Sertifikasi*

⁵⁸ Deloitte Touche Tohmatsu Emerging Markets Ltd. 2000 May. Indonesian Accounting Standards (PSAK): Recommended Changes in Selected PSAKs for Improving Conformity with the International Accounting Standards. Report Prepared for the Financial Governance Reforms Support Project: Capital Markets Component ADB TA No. 1620-INO. pp. 2-3.

⁵⁹ Accountancy Development Projects:

- World Bank Loan 3801-IND: *Accountancy Development Project II* (1995–2000), for \$25 million approved on 22 September 1994.
- World Bank *Accountancy Development Project I* (1988–1994), for \$113 million, approved on 17 May 1988.

Akuntan Publik, USAP) was introduced. The international-standard USAP has been mandatory for practicing PAs since 1997 (accountants who were already in public practice in 1997 were not required to sit the USAP). The USAP's introduction was supported by a decree that also tightened licensure procedures, strengthened oversight and (ostensibly) introduced penalties for erring PAs.⁶⁰ There are four levels of Indonesian accountants: (i) MOF-registered Accountants; (ii) IAI PA Certificate (*Bersertifikasi Akuntan Publik, BAP*) holders; (iii) MOF PA Certificate holders; and (iv) holders of MOF PA Practicing Licenses.

80. Forty-five years after its foundation, IAI has developed into a nationally respected professional institute. Its 6,000 members—of whom more than 65 percent reside in Jakarta—comprise practicing accountants, management accountants, government accountants and accounting academics.

81. Significant numbers of Indonesian companies and banks—with apparently sound financial positions—collapsed in the 1997-98 Asian financial crisis's wake. Most had received unqualified audit opinions. Subsequent events questioned the legitimacy of these opinions. In June 1998, ADB approved the Financial Governance Reforms Sector Development Program (FGRSDP) to support government efforts to promote and strengthen the governance of the financial and public sectors.⁶¹ Government-agreed FGRSDP policy conditions included enacting legislation and regulations making: (i) auditors liable for negligence in performing audits; and (ii) directors liable for false information in annual reports and other public information.

82. In 2001, the MOF released an *Academic Paper*⁶² that examined issues to be covered by a new Public Accountants (PA) Law. It identified the PA Law's objectives as: (i) protecting the public trust provided to PAs; (ii) providing a better legal framework for the public accountancy profession; and (iii) supporting national economic development and preparing for the liberalization of public accounting services. In

⁶⁰ Finance Minister Decree on Public Accountant Services (No. 43/KMK.017/1997) as amended by Finance Minister Decree No. 470/KMK.017/1999.

⁶¹ The FGRSDP was approved on 25 June 1998 and comprised a program loan for \$1,400 million (Loan No. 1618-INO); a \$3 million equity investment; a \$47 million investment loan (Loan 1619-INO); a \$50 million technical assistance loan to support commercial bank restructuring, governance improvements and institutional strengthening of various government agencies (TA Loan No. 1620-INO).

⁶² Ministry of Finance (MOF). 2001. *Academic Draft: Draft of Public Accountant Law*. MOF: Jakarta.

particular, the *Academic Paper* contended that existing arrangements provided weak support for criminal and civil sanctions against PAs and Public Accounting Firms (*Kantor Akuntan Publik, KAPs*).⁶³ The Government intends to submit the draft PA Law to the state secretariat in 2003.⁶⁴

83. Whatever the case, shortcomings in existing laws and regulations meant that government oversight bodies were unable to sanction seemingly errant auditors. In particular, there is growing consensus that IAI disciplinary arrangements are flawed and need urgent revision. A strong accountancy profession, with regional representation, is essential to Indonesia's development.

84. First, investors and lenders realize that good accounting and auditing standards are worthless when poorly implemented.⁶⁵ It is essential that investors perceive that effective mechanisms exist to ensure that audits are conducted in accordance with auditing standards and ethical rules.

85. Second, decentralization has devolved financial responsibilities to local governments, but there is a shortage of suitably experienced and qualified accountants outside Jakarta.

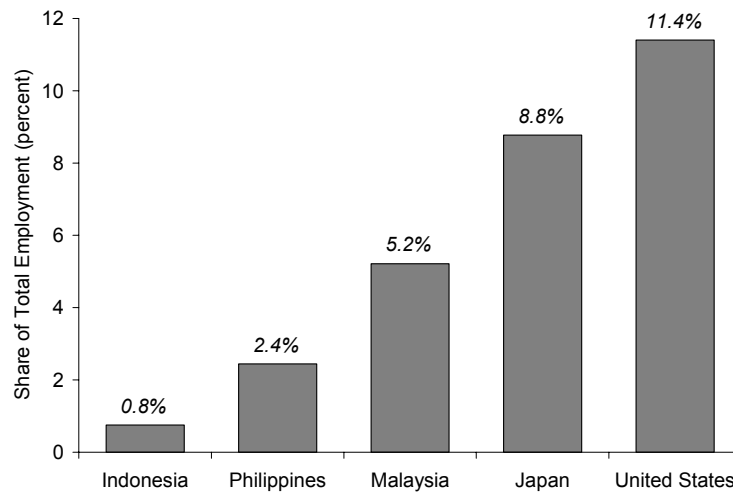
⁶³ *Ibid*, p. 17.

⁶⁴ Although the PA Law had not been enacted, ADB reviewed the FGRSDP policy conditions and, in July 2002, agreed to release the third and final program tranche of \$350 million.

⁶⁵ McKinsey & Company. 2002 July. *Global Investor Opinion Survey: Key Findings*.

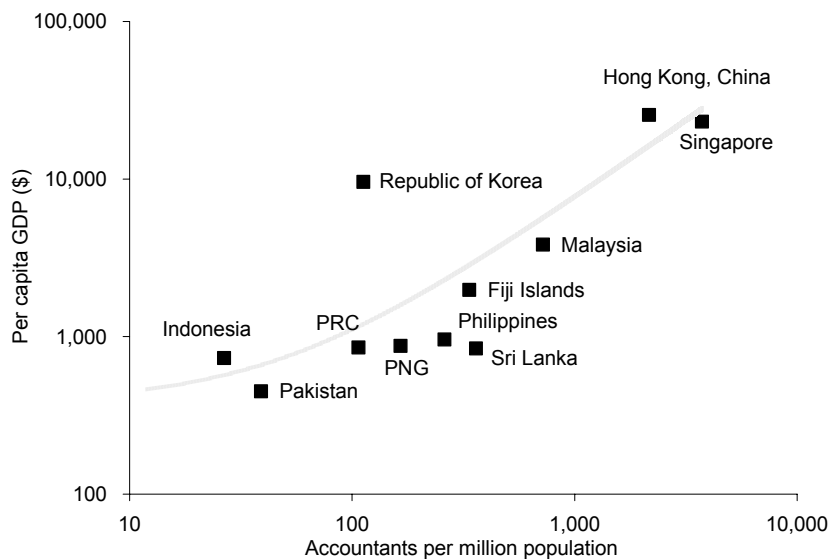
Figure 4. Indonesian Financial Sector Professionals

(a) Indonesia has a relative scarcity of financial sector professionals in general (1997) ...



Employment in Finance, Insurance, Real Estate, and Business Services as a Percentage of Total Employment by Country (1997)⁶⁶

... and (b) comparatively few accountants in particular (2001-02).



Various sources including: ADB. 2001. *Key Indicators of Developing Asian and Pacific Countries. Volume XXXII*. ADB Diagnostic Studies of Accounting and Auditing. Manila: ADB.

⁶⁶ United Nations (UN). 1997. *Statistical Yearbook 1997*. UN: New York. Cited in: Pomerleano, Michael (Lead Financial Specialist, World Bank). 2002 April. Back to the Basics: Critical Financial Sector Professions Required in the Aftermath of an Asset Bubble. *The Appraisal Journal*. pp. 173-181.

86. Third, evidence suggests that the availability of financial sector skills affects the buildup, duration and severity of equity and property bubbles (and restructuring in their aftermath). Countries that have capable professionals—such as accountants, appraisers, analysts and insolvency experts—recognize and respond more swiftly to asset bubbles than countries with limited financial sector skills.^{67, 68} However, Indonesia has a comparative dearth of financial sector professionals, including accountants (see Figure 4).

“Essentially, financial markets with depth and breadth are able to manage crisis better than markets without them. Development of non-bank financial institutions, such as insurance schemes and collective investment instruments, requires a high level of professional expertise. The strong correlation among the base of skills, the growth of non-bank financial intermediation, and the stability of the financial system suggests that poor prevention and weak responses to financial crises are linked to inadequate skills and human capital in the financial services sector.”⁶⁹

2. Professional Organization and Regulation

Introduction

87. Indonesia is reviewing professional arrangements in preparation for the new PA Law (p. 88). This section examines professional organization in general and then describes Indonesian arrangements.

Assignment of Professional and Regulatory Functions

88. Country institutional structures reflect historical and cultural influences. But, given the pace of change in developing and transitional countries, there is seldom time for institutions to develop organically. Therefore, other countries' structures are borrowed.⁷⁰

89. Transitional and developing countries usually assign professional responsibilities to government organizations (such as the Finance

⁶⁷ Allen, Franklin and Douglas Gale. 2000 January. Bubbles and Crises. *Economic Journal*. 110. pp. 236-55.

⁶⁸ Pomerleano, Michael (Lead Financial Specialist, World Bank). 2002 April. Back to the Basics: Critical Financial Sector Professions Required in the Aftermath of an Asset Bubble. *The Appraisal Journal*. pp. 173-181.

⁶⁹ *Ibid.* p. 175.

⁷⁰ Narayan, Francis B., Ted Godden, Barry Reid and Ma. Rosa P. Ortega. 2000. *Financial Management and Governance Issues in Selected Developing Member Countries: A Study of Cambodia, People's Republic of China, Mongolia, Pakistan, Papua New Guinea, Uzbekistan, and Viet Nam*. ADB: Manila.

Ministry). Along with historical reasons, they argue that government action plugs a hole until private sector capacity is developed. But, evidence suggests that this approach impedes the accountancy profession's development.⁷¹

90. Some economies have better professional infrastructures than others because of their legal traditions. Common law countries have independent judges and juries and legal principles supplemented by precedent-setting case law to respond to evolving circumstances (e.g., Malaysia and the U.S.). Civil law countries rely on legal codes containing specific rules (e.g., Indonesia and the Republic of Korea). Consequently, civil law countries are less adept at responding to changing economic and environmental circumstances. Legal traditions affect the development of professions to a remarkable degree.⁷² Indeed researchers have found a robust correlation between the civil law tradition and lack of professions, on one hand, and a supporting and beneficial impact of professions on the rule of law, on the other.⁷³

91. Historical accounting influences also affect professional arrangements, particularly the degree of government involvement (see Table 14).

Table 14. Accounting Practices Classified by Country Grouping

Accounting System	Accounting Model	Features	Countries
Standards Based Accounting	British Commonwealth	<ul style="list-style-type: none"> • Commercially driven • Overriding rule is that financial statements show a 'fair' picture. • Accounting practices reflect, and develop with, business practices • Professional regulation dominates. 	Australia, Bahamas, Ireland, Fiji Islands, India, Jamaica, Kenya, Malaysia, Netherlands, New Zealand, Pakistan, Papua New Guinea, Zimbabwe, Singapore, South Africa, Sri Lanka, Trinidad & Tobago, United Kingdom.

⁷¹ See, for instance, Armstrong, Mikael and Katerina Hellström. 1998 April. *A Case Study of the Czech Republic*. Stockholm School of Economics: Paper presented at 21st EAA Congress: Accounting in Times of Transition. Antwerp.

⁷² Pomerleano, Michael (Lead Financial Specialist, World Bank). 2002 April. Back to the Basics: Critical Financial Sector Professions Required in the Aftermath of an Asset Bubble. *The Appraisal Journal*. pp. 173-181.

⁷³ La Porta, Rafael, Florencio López-de-Silanes, Andrei Shleifer and Robert W. Vishny. 1998. Law and Finance. *Journal of Political Economy*. Vol. 106(6). pp. 1113-1155.

ACCOUNTING AND AUDITING PRACTICES IN INDONESIA

Accounting System	Accounting Model	Features	Countries
	United States	<ul style="list-style-type: none"> • Same as British Commonwealth Model except that professional regulation coexists with government regulation. 	Canada, Indonesia , Japan, Republic of the Marshall Islands, Mexico, Panama, Philippines, United States.
Uniform Accounting Plans	Soviet Union	<ul style="list-style-type: none"> • Government driven • Dominated by statistics and taxation requirements • Accounting practices are statute-based • Accountancy profession not required 	Azerbaijan, People's Republic of China, Mongolia, Russia, Uzbekistan.
	Continental European	<ul style="list-style-type: none"> • Government driven • Dominated by taxation requirements • Accounting practices are statute-based 	Belgium, Cambodia, France, Germany, Italy, Spain, Sweden, Switzerland, Viet Nam, Venezuela.
	Latin American	<ul style="list-style-type: none"> • "Castilian model" • Very similar to continental European model. 	Argentina, Bolivia, Chile, Colombia, Ethiopia, Paraguay, Peru, Uruguay.

Source: Modified from, Nobes, Christopher and Robert Parker. 1995. *Comparative International Accounting*: Fourth Edition: Prentice Hall. p. 67.

92. Table 15 considers professional and regulatory assignments. It compares full government regulation with full professional delegation. In practice most countries have, or are moving towards, a mixed approach with regulated semiautonomous bodies coexisting with independent professional associations.

Table 15. Assignment of Professional and Regulatory Activities

Activity	Objectives and Issues	Comparison of Arrangements	
		Government	Professional Body
Accountant Certification	Involves setting certification criteria, preparing examinations, conducting examinations, grading examinations, evaluating practical experience and approving qualifications. Institutional arrangements should support high certification standards. The process offers rent-seeking opportunities.	<ul style="list-style-type: none"> ▪ May lack capability ▪ Rent-seeking activities may undermine quality 	<ul style="list-style-type: none"> ▪ Has powerful incentives to support high certification standards ▪ Being closer to the market, is more likely to be responsive to employer needs
Auditor Licensing	For countries that license auditors, the process involves: setting criteria, examining applications and approving applications. The process offers rent-seeking opportunities. Arrangements should support high standards.	<ul style="list-style-type: none"> ▪ Has legislative power ▪ May lack capability ▪ Rent-seeking activities may undermine quality 	<ul style="list-style-type: none"> ▪ Has powerful incentives to support high licensing standards ▪ Larger firms may dominate process

ACCOUNTING AND AUDITING PRACTICES IN INDONESIA

Activity	Objectives and Issues	Comparison of Arrangements	
		Government	Professional Body
Professional Standard Setting	Professional standards generally comprise an Ethical Code and Professional Rules of Conduct. Although these standards are largely internationally harmonized, individual countries may tighten rules or incorporate legal references. Conversely, other countries may dilute standards to reduce auditor exposure to sanctions and liability.	<ul style="list-style-type: none"> ▪ Has legislative power ▪ May lack capability ▪ May be less responsive to international changes 	<ul style="list-style-type: none"> ▪ Has capability and understanding ▪ Internal lobby groups may dilute provisions
Enforcement and Sanctions: Public Accountant Negligence ⁷⁴	Accounting and auditing standards and disclosure requirements have little value when they are not backed by appropriate compliance sanctions. Possible sanctions include warnings, public reprimands, license suspension, license revocation, administrative penalties, criminal penalties or civil litigation. But in developing or transition economies, judicial inadequacies often render the civil liability deterrent ineffective.	<ul style="list-style-type: none"> ▪ Has legislative power ▪ May lack capability ▪ Rent-seeking activities may undermine effectiveness 	<ul style="list-style-type: none"> ▪ May lack legislative support ▪ Professional bodies tend to be reticent to punish public accountant firms
Quality Control over Public Accounting Firms	Involves adopting or developing quality control standards and relevant guidance that require firms of practicing accountants to establish the quality control policies and procedures necessary to provide reasonable assurance of conforming with professional standards in performing services.	<ul style="list-style-type: none"> ▪ Has legislative power ▪ May lack capability ▪ Rent-seeking activities may undermine effectiveness 	<ul style="list-style-type: none"> ▪ Has capability and understanding ▪ May lack a power basis for discharging function

⁷⁴ Most countries assign other disciplinary enforcement (e.g., advertising breaches) to professional bodies.

PROFESSIONAL INFRASTRUCTURE

Activity	Objectives and Issues	Comparison of Arrangements	
		Government	Professional Body
Accounting Standard Setting	The standard-setting process should be transparent, orderly and inclusive. Most importantly, financial statement users should be well represented. The adoption of IASs lessens the process's complexity.	<ul style="list-style-type: none"> ▪ Has legislative power ▪ May lack capability 	<ul style="list-style-type: none"> ▪ Has capability ▪ May lack power ▪ May be biased towards financial statement preparers and auditors
Auditing Standard Setting	The standard-setting process should be transparent, orderly and inclusive. The standards should provide a sound basis for civil or administrative sanctions—auditors have powerful incentives to support weak auditing standards, thereby reducing potential liabilities. ⁷⁵ The direct adoption of ISAs lessens these risks.	<ul style="list-style-type: none"> ▪ Has legislative power ▪ May lack capability 	<ul style="list-style-type: none"> ▪ Has capability ▪ Auditors have powerful incentives to support weak auditing standards, thereby reducing potential liabilities

Indonesian Professional Organization and Regulation

93. The Indonesian accountancy profession is largely self-regulated. IAI undertakes certification, standard setting, quality assurance and disciplinary activities. Table 16 summarizes the regulation and organization of the accountancy profession. Importantly, on 30 September 2002, the Finance Minister signed a new decree on public accountant services.⁷⁶ The following sections provide further information on governing legislation, and the mandate and activities of the MOF and IAI.

⁷⁵ During the 2000 US election cycle (in the period to 30 June 2000) the US accountancy profession gave \$10.4 million in campaign contributions to House, Senate and Presidential candidates. Major contributors included AICPA (\$0.7 million), Andersen Worldwide (\$1.5 million), Deloitte & Touche (\$1.4 million), Ernst & Young (\$2.2 million), KPMG (\$1.0 million) and PricewaterhouseCoopers (\$1.4 million). Source: BusinessWeek. 2000 September 25. Accounting Wars: Powerful Auditor-Consultants are the Targets of Arthur Levitt's Crusade. Magazine Article.

⁷⁶ Finance Minister Decree No. 423/KMK.06/2002. 30 September 2002.

Table 16. Regulation and Organization of the Accountancy Profession

Governing Laws and Regulations	<ul style="list-style-type: none"> ▪ The <i>Accountant Title Law (No. 34) 1954</i> restricts use of the Accountant title and provides for the Finance Minister to regulate the profession. ▪ The <i>Capital Markets Law (No. 8) 1995</i> regulates the activities of PAs that support the capital markets. It is supported by several implementing regulations, in particular, the <i>Rules for the Registration of Public Accountants 1996</i>. ▪ The <i>Finance Minister Decree on Public Accountant Services No. 43/KMK.017/1997</i>⁷⁷ details licensing requirements and organizational structures. ▪ Several laws require financial statements to be audited by PAs. These include the <i>Law on Limited Liability Companies (No.1) 1995</i> (PT Law 1995), <i>Banking Law (No. 7) 1992</i>, <i>Law on Pension Funds (No. 11) 1992</i>, and the <i>Capital Markets Law (No. 8) 1995</i>.
Regulatory Bodies	<ul style="list-style-type: none"> ▪ DPAJP (MOF) supervises PAs and KAPs (About 31,000 Accountants were registered with DPAJP at July 2002). This involves licensing the profession, ensuring adequate professional standards are in place, policing the standards and developing the profession. DPAJP also supervises the appraisal (valuation) profession. ▪ <i>Bapepam</i> registers and supervises PAs and KAPs engaged in capital market activities (As of August 2001, 137 KAPs were registered with <i>Bapepam</i>, allowing them to provide services to capital market participants, see page 41). However, the Financial Services Authority (<i>Otorita Jasa Keuangan, OJK</i>) will assume these functions (once operational). ▪ Bank Indonesia (BI) registers KAPs for financial sector audits and supervises their activities. However, OJK will assume these functions (once operational). ▪ The National Accreditation Agency (<i>Badan Akreditasi Nasional, BAN</i>) accredits accountancy programs at state universities.
Professional Associations	<ul style="list-style-type: none"> ▪ IAI is Indonesia's primary professional accountancy body. Its 6,000 members comprise public sector accountants (35 percent), public accountants (25 percent), management accountants (20 percent), academic accountants (5 percent) and other accountants (15 percent). ▪ IAI is involved in accounting and auditing standard setting, certification, ethics and discipline, and Continuing Professional Education (CPE).

⁷⁷ As revised by the *Finance Minister Decree No. 470/KMK.017/1999 Concerning Changes in Finance Minister Decree 43/KMK.017/1997*.

- Other related professional bodies exist. Of these, the internal auditors' institutes and the Indonesian Society of Appraisers (*Masyarakat Profesi Penilai Indonesia, MAPPI*) are particularly important.
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Governing Laws and Regulations

94. This subsection describes the key legislation that governs the accountancy profession. Most of the substance is contained in lowly-ranking ministerial decrees.⁷⁸ However a new Public Accountant (PA) Law is being drafted (see page 88).

95. The Accountant Title Law (No. 34) 1954 allows only those who have accepted qualifications to call themselves accountants (see Appendix 13).⁷⁹ Furthermore the law:

- Establishes the Expert Committee (*Panitia Ahli*) whose organizational structure and procedures are determined by the Education and Finance Ministers. The Finance Minister may assign other tasks to the Committee relating to the regulation, management or development of accountancy. The Committee comprises accounting academics from the Universities of Indonesia and Gajah Mada.
- Requires accountants to either: (i) complete an accepted academic degree at a government-recognized university; or (ii) complete other Committee-approved examinations.
- Stipulates that accountants' details must be recorded in the MOF State Register of Accountants (*Register Negara*).
- Requires that KAP heads hold the Accountant title—violations are punishable by two months imprisonment or a maximum fine of Rp 10,000 (\$1.15).
- Implicitly bars accountants from practicing as limited liability companies.

96. The Capital Markets Law (No. 8) 1995 regulates the activities of PAs that support the capital markets (see Appendix 14). In particular, this law:

⁷⁸ The legal hierarchy is: (i) 1945 Constitution; (ii) laws; (iii) government regulation in place of law (*Perpu*); (iv) government regulation (PP); (v) presidential decrees; and (vi) ministerial decrees.

⁷⁹ However, employees of the State Accounting Office and the Directorate General of Taxation are exempted from the law (due to conflicts with rules and regulations governing wages and salaries, which designates their positions as tax accountants, assistant accountants, etc).

- Identifies PAs and KAPs as capital market-supporting professionals who must register with *Bapepam* before engaging in capital market activities (Article 64).
- Requires that PAs have a valid professional license (Article 64) and comply with their professional association's ethical code and professional standards, as long as those standards do not conflict with the law or its implementing regulations (Article 66).
- Allows *Bapepam* to impose administrative sanctions against *Bapepam*-registered PAs for violations of the law or its implementing regulations (Chapter XIV).
- Allows criminal penalties to be imposed on unregistered PAs—up to five years imprisonment and maximum fines of Rp 5 billion (\$620,000)(Article 103).
- Stipulates that persons who suffer losses arising from violations may sue responsible PAs and KAPs for compensation (Article 111).

97. *Bapepam Implementing Regulations* apply to *Bapepam*-registered PAs engaged in capital market activities. These regulations were issued in accordance with the *Capital Markets Law (No. 8) 1995* and include the *Rules for the Registration of Public Accountants (Kep-37/PM/1996)* require PAs to: (i) undertake Continuing Professional Education (CPE); and (ii) comply with the PA *Professional Standards (SPAPs)* and *Code of Ethics*. This rule also prescribes KAP structures and requires that they be subject to IAI external quality control reviews (see Appendix 15).

98. Before 1997, licensed PAs were automatically entitled to run KAPs. In keeping with new *Bapepam* regulations, in January 1997, the *Finance Minister Decree on Public Accountant Services (No. 43/KMK.017/1997)* required PAs to obtain a license to run a KAP. Moreover, the Decree tightened licensing criteria by requiring PAs to: (i) be domiciled in Indonesia; (ii) pass the IAI certification exam; (iii) be an IAI member; and (iv) have at least three years relevant practical experience. Furthermore, the Decree required that KAPs must be headed by licensed PAs and employ at least three auditors.⁸⁰ The 1999 amendment of this Decree was minor in that it reiterated the government-licensing requirement.⁸¹

⁸⁰ Bachtiar, Emil. 2001 August. The Professionalization of Accounting in Indonesia. Paper presented to the Second International Accounting History Conference, Osaka, August 2001.

⁸¹ *Finance Minister Decree No. 470/KMK.017/1999 Concerning Changes in Finance Minister Decree 43/KMK.017/1997.*

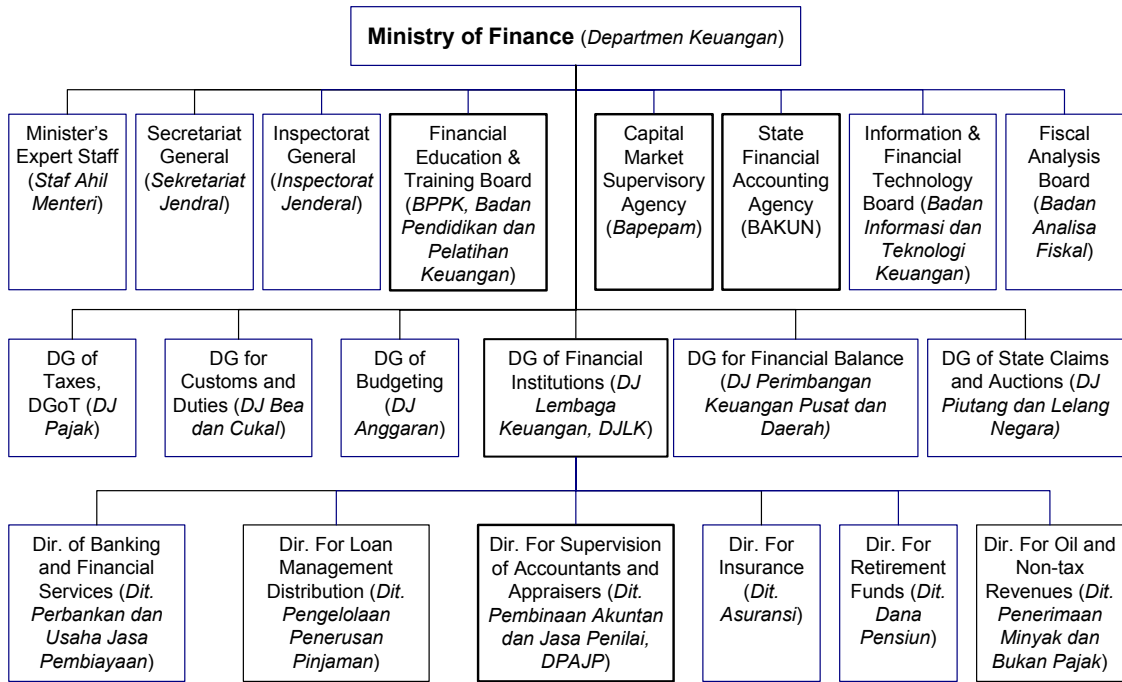
99. On 30 September 2002, the Indonesian Finance Minister signed a Decree on Public Accountant Services. Among other things, the new decree reflects international trends and: (i) tightens public accountant licensing requirements and procedures; (ii) mandates audit partner rotation (three years) and auditing firm rotation (five years); (iii) requires periodical quality reviews of local public accountant firms that have signed cooperation agreements with foreign firms; (iv) specifies supervision and inspection arrangements; and (v) specifies sanctions for infringements. The Decree is presented in Appendix 22.

3. Ministry of Finance (MOF)

100. The MOF comprises *Bapepam*, DGoT and the Directorate General for Financial Institutions (*Direktorat Jenderal Lembaga Keuangan, DJLK*) (see Figure 5). DJLK administers applicable legislation⁸² and formulates and implements policies based on laws, implementing regulations and Finance Minister policies. It also develops standards, norms, guidelines, criteria and procedures in relation to its responsibilities. Furthermore, DJLK develops technical guidance for, and conducts evaluations of, organizations and professions under its oversight.

⁸² Accountant Title Law (No. 34) 1954 and Finance Minister Decree on Public Accountant Services No. 43/KMK.017/1997.

Figure 5. MOF Organizational Structure



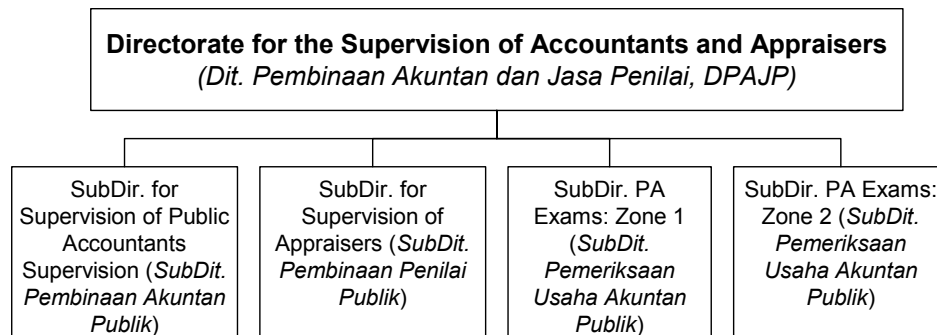
Sources: MOF, Gold Group Asia-Pacific Ltd. 2002. *Indonesian Governments Guide* 2002. pp. 134-140.

101. The Directorate for Supervision of Accountants and Appraisers (*Direktorat Pembinaan Akuntan dan Jasa Penilai, DPAJP*) within DJLK supervises PAs and KAPs (see Figure 6). This involves licensing the profession, ensuring adequate professional standards are in place, policing the standards and developing the profession. DPAJP is also responsible for the appraisal (valuation) profession (see page 79).

102. On 1 January 2001, DPAJP assumed responsibility for reviewing KAPs (from BPKP). It is developing its capacity and procedures (e.g., human resources and standard operating procedures) to undertake this important responsibility.⁸³ At July 2002, 31,000 accountants were registered with MOF (*Register Negara*).

⁸³ AusAID is supporting these activities through the Technical Assistance Management Facility II (TAMF II) Project.

Figure 6. DPAJP Organizational Structure



Sources: MOF, Gold Group Asia-Pacific Ltd. 2002. *Indonesian Governments Guide* 2002. pp. 134-140.

4. Indonesian Institute of Accountants (IAI)

Introduction

103. Before 1957, accountants were without local professional representation. In 1957, in accordance with the *Accountant Title Law* (No. 34) 1954), the first group of accounting students graduated from the University of Indonesia. But Dutch professional organizations did not recognize their qualifications and they could not sign audit reports for Dutch auditing firms.⁸⁴ Together with senior Indonesian Dutch-trained accountants, these graduates established IAI in 1957. Professor Soemardjo Tjitrosidojo, a Dutch-trained academic, was the Institute's first Chair.⁸⁵

104. IAI's professionalization efforts gathered pace following its first convention in 1969. In particular, a Finance Minister Decree made membership compulsory for licensed accountants and, in 1973, the Institute established the Accountant Examination Norm Committee (*Komite Norma Pemeriksmen Akuntan, KNPA*).⁸⁶ The Institute's objectives, among other things, are to promote the status of the accounting profession, support national development and upgrade the skills and competence of accountants.

⁸⁴ Akuntansi. 1989 January. *Lambat tapi Pasti* (Slowly but Surely): An Interview with Drs. Hendra Darmawan. Magazine Article.

⁸⁵ Yunus, H. 1990. *History of Accounting in Developing Nations: The Case of Indonesia*. Tim Koordinasi Pengembangan Akuntansi, Jakarta.

⁸⁶ Bachtiar, Emil. 2001 August. *The Professionalization of Accounting in Indonesia*. Paper presented to the Second International Accounting History Conference, Osaka, August 2001.

105. Forty-five years after its foundation, IAI has developed into a nationally-respected professional institute, with 6,000 members in 20 branches nationwide.⁸⁷ Its membership comprises public accountants, management accountants, government accountants and academics.

IAI Organizational Structure⁸⁸

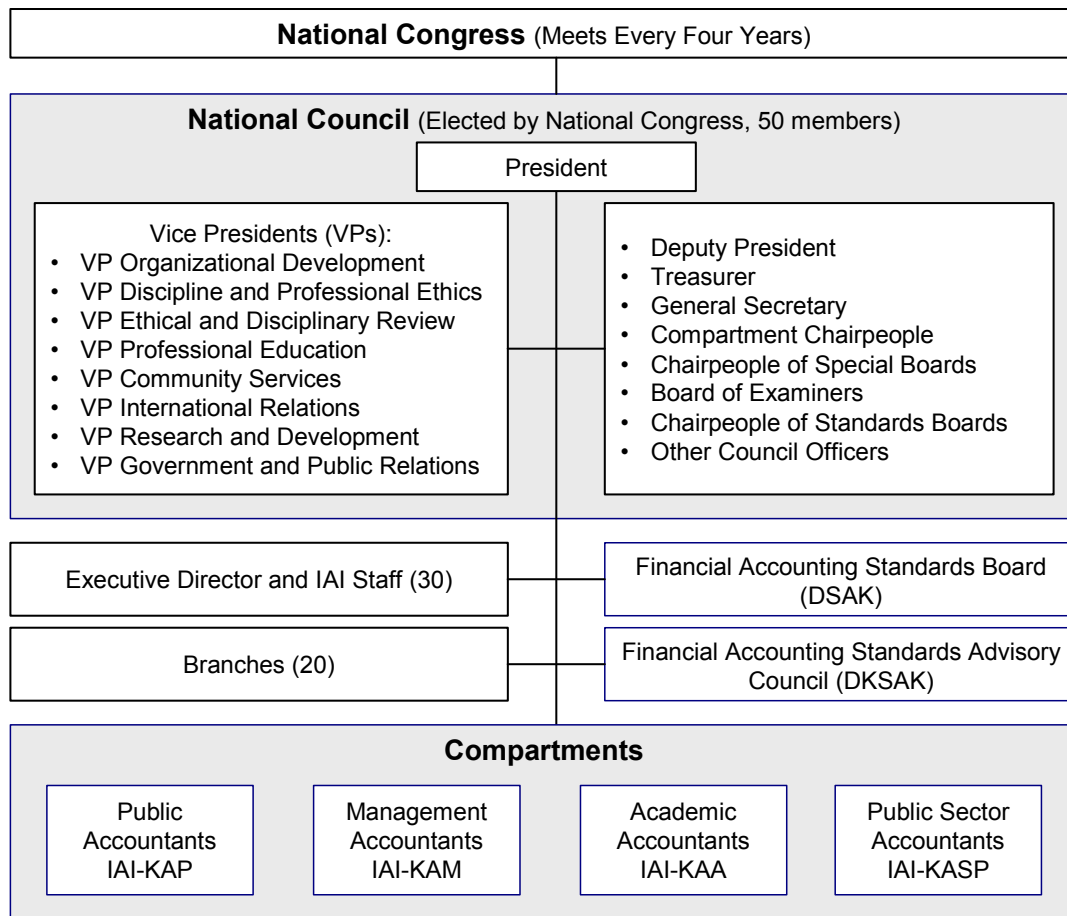
106. The IAI Congress convenes every four years. It elects the National Council, which comprises about 150 members and is led by the Institute President. The Institute has four compartments and two boards (see Figure 7). An Executive Director heads the Institute's fulltime staff of about 30 people. The four compartments are:

- Academic Accountants Compartment (IAI-KAA) The IAI-KAA (*IAI Kompartemen Akuntan Akademikita*) advises on improvements to academic curricula. It also prepares the curricula for the USAP exam and CPE requirements.
- Management Accountants Compartment (IAI-KAM) IAI-KAM (*Kompartemen Akuntan Manajemen*) prepares and implements proposals regarding management accountant standards of competency. IAI-KAM is also considering developing qualifications for management and commercial accountants.
- Public Accountants Compartment (IAI-KAP) IAI-KAP (*Kompartemen Akuntan Publik*) regulates KAP licensing, sets professional standards, reviews disciplinary breaches and imposes sanctions.
- Public Sector Accountants Compartment (IAI-KASP) IAI-KASP (*IAI Kompartemen Akuntan Sektor Publik*) promulgates EDs for public sector accounting standards and financial reporting requirements.

⁸⁷ www.akuntan-iai.or.id

⁸⁸ Primary source: www.akuntan-iai.or.id

Figure 7. IAI Structure



Source: Modified from IAI materials (2002).

IAI Activities⁸⁹

107. The Institute undertakes the following activities:

- (i) **Standard Setting.** IAI is committed to international harmonization. It develops and promulgates accounting standards, auditing standards, attestation standards, accounting and review services standards, quality control standards and consulting services standards.
- (ii) **Training.** Practicing PAs must undertake a minimum of 30 Continuing Professional Education (CPE) hours per annum and 120 CPE hours over every three-year period. IAI conducts two to

⁸⁹ Primary source: www.akuntan-iai.or.id

- three CPE courses each week, comprising seminars and workshops. These events are open to the public.
- (iii) Public Accountant Certification Exam (USAP). IAI administers the Public Accountant Certification exam twice annually, in Jakarta and Surabaya.
 - (iv) Publication. IAI publishes *Media Akuntansi* (the journal for the accounting profession), and technical journals including: *Jurnal Riset Akuntansi Indonesia* (Accounting Research Journal); and *Jurnal Riset Akuntansi Sektor Publik* (Public Sector Accounting Research Journal).
 - (v) Training and Consulting Services. IAI provides training and consulting services to small businesses.
 - (vi) Political Lobbying. From time to time, IAI lobbies government on matters of interest to the profession and the public.

IAI Membership Composition

108. IAI bylaws classify members into three types: (i) *Regular Members* are those who hold the MOF Accountant title; (ii) *Non-regular Members* are those who have completed their *Sarjana Strata Satu* (S1) economics degree with an accounting major. Organizations or individuals that use the accounting profession's services may also qualify as non-regular members; and (iii) *Honorary memberships* may be granted to Indonesian citizens that have made significant contributions to the accounting profession's development.

109. Most IAI members reside in major cities (more than 65 percent live in Jakarta). IAI's 6,000 members comprise public sector accountants (35 percent), public accountants (25 percent), management accountants (20 percent), academic accountants (5 percent) and other accountants (15 percent).

Affiliations

110. IAI is a member of the ASEAN Federation of Accountants (AFA), IASC and IFAC. It has memorandums of understanding with the Institute of Chartered Accountants in Australia (ICAA) and CPA Australia. IAI withdrew from the Confederation of Asian and Pacific Accountants (CAPA) in 1999 due to financial constraints.⁹⁰

⁹⁰ Narayan, Francis B. 2000 May 15. Back-to-Office Report of Mission to Laos, Viet Nam, Cambodia and Indonesia. ADB: Manila.

Resources and Financing

III. Table 17 summarizes IAI's financial performance for the past two years and reveals that the Institute relies heavily on income from commercial activities (e.g., training and publications) rather than membership fees. IAI faces three significant challenges in relation to membership fees. First, IAI's decentralization of billing responsibilities to branch offices has hampered billing procedures (i.e., some members are not billed). Second, IAI members are not good at paying their dues. Third, less than one-fifth of registered accountants are IAI members. Nevertheless, Table 17 reveals reasonably healthy financial performance.

Table 17. IAI Revenues and Expenses

Item	Year Ended 30 June 2001				
	Revenues		Expenses		Surplus/ (Deficit)
Indonesian Rupiah	(Rp 000)	%	(Rp 000)	%	(Rp 000)
<i>Non-Restricted Fund:</i>					
Membership Fees	647,270	15.9	457,199	14.8	190,071
CPE Training Courses	1,201,052	29.5	527,141	17.1	673,911
IAI Special Events	106,321	2.6	221,156	7.2	(114,835)
Other	592,766	14.6	..	..	592,766
Professional Training	..	..	4,742	0.2	(4,742)
Administration	..	..	882,198	28.5	(882,198)
Jakarta Initiative	105,752	2.6	11,741	0.4	94,011
<i>Restricted Fund:</i>					
USAP Fees	410,588	10.1	373,628	12.1	36,960
Publication Sales	947,923	23.3	524,085	17.0	423,838
SME Clinics	8,450	0.2	57,966	1.9	(49,516)
Donations	45,006	1.1	30,160	1.0	14,846
	4,065,128	100.0	3,090,016	100.0	975,112
U.S. Dollars	U.S.\$	%	U.S.\$	%	U.S.\$
<i>Non-Restricted Fund:</i>					
Membership Fees	72,727	15.9	51,371	14.8	21,356
CPE Training Courses	134,950	29.5	59,229	17.1	75,721
IAI Special Events	11,946	2.6	24,849	7.2	(12,903)
Other	66,603	14.6	..	..	66,603
Professional Training	..	..	533	0.2	(533)
Administration	..	..	99,123	28.5	(99,123)
Jakarta Initiative	11,882	2.6	1,319	0.4	10,563
<i>Restricted Fund:</i>					
USAP Fees	46,133	10.1	41,981	12.1	4,152
Publication Sales	106,508	23.3	58,886	17.0	47,622
SME Clinics	949	0.2	6,513	1.9	(5,564)
Donations	5,057	1.1	3,389	1.0	1,668
	456,755	100.0	347,193	100.0	109,562

Note: IRP-USD conversion at 8,900.

Source: IAI. 2001. *IAI Financial Statements for the Year Ended 30 June 2001*. Jakarta.

Issues and Challenges

112. IAI faces significant challenges. First, less than 20 percent of the 31,000 registered accountants are IAI members. Second, the Institute's disciplinary procedures are being criticized as inappropriate and ineffective (see Box 2, p. 84). Third, IAI membership is highly concentrated in Jakarta. Although there are 20 branches nationwide, most are inactive. Fourth, although members are required to pay annual dues, they seldom do.⁹¹ Fifth, the proposed PA Law will potentially lead to significant professional restructuring. Sixth, liberalization commitments require efforts to strike mutual recognition agreements (MRAs) that in turn require maintenance of professional standards (see page 81). Seventh, IAI wishes to further strengthen certification requirements (i.e., curriculum, examination and practical experience requirements).

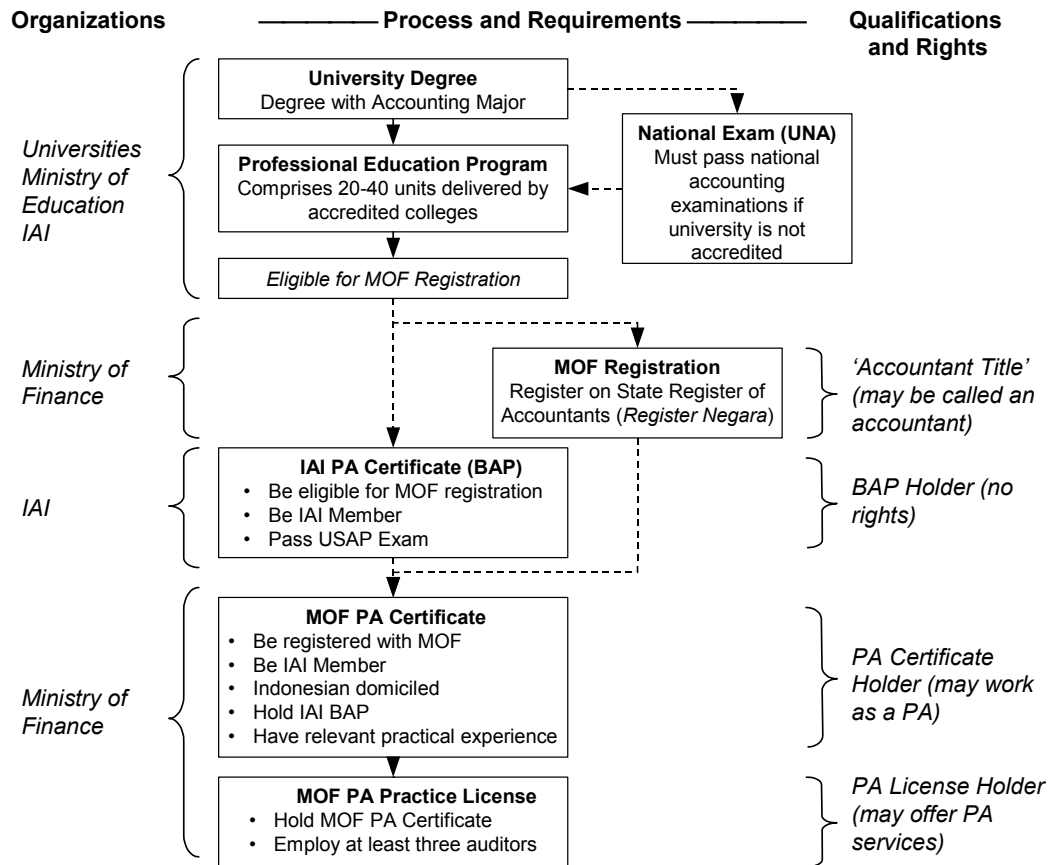
5. Indonesian Accountancy Qualifications

Introduction

113. Before the *Accountant Title Law (No. 34) 1954*, there were no restrictions on using the Accountant title. Figure 8 describes Indonesian accountancy qualifications. This section examines these qualifications and compares them to international norms.

⁹¹ Narayan, Francis B. 2000 May 15. Back-to-Office Report of Mission to Laos, Viet Nam, Cambodia and Indonesia. ADB: Manila.

Figure 8. Indonesian Accountancy Qualifications



University Accountancy Qualification

114. In accordance with the *Accountant Title Law (No. 34) 1954*, accountants must first complete an accredited economics degree (*Sarjana Strata Satu, S1*) majoring in accounting. Seventeen universities are currently accredited to offer these degrees.

115. The Directorate General of Higher Education (*Direktorat Jenderal Pendidikan Tinggi, DIKTI*), within the Ministry of National Education (*Departemen Pendidikan Nasional, DPN*), is responsible for higher education, including quality assurance. In 1995, DPN established the National Accreditation Agency (*Badan Akreditasi Nasional, BAN*) to act as an accreditation board and a quality assurance agency to maintain high

teaching and research standards.⁹² BAN accredits study programs into four categories: A (excellent), B (good), C (average) and D (poor).

116. IAI must first recommend universities to offer accountancy programs before BAN considers accrediting them. Graduates from unaccredited universities must pass the national accounting examinations (*Ujian Nasional Akuntansi, UNA 1 dan 2*). These were developed under the World Bank-supported Accountancy Development Project II.

Professional Education Program

117. A 1999 decision to implement professional accountancy education aims to improve accountancy education standards and the accreditation program.⁹³ ADB is supporting its implementation through the *Technological and Professional Skills Development Sector Project (2000–2006)*.⁹⁴

118. Accounting graduates who have completed 144 credit units must complete the Professional Education Program, before they can register with DPAJP and use the Accountant title. Accredited colleges deliver the Professional Education Program, which comprises 20-40 credit units.

MOF Registration

119. Accountant title users must: (i) have either completed an accredited *S1* accountancy degree, or passed the national accounting examinations (UNA 1 and 2); (ii) have completed the Professional Education Program; and (iii) be registered with DPAJP (*Register Negara*). At July 2002, 31,000 Accountants were registered with DPAJP.

IAI PA Certificate (BAP)

120. IAI may issue the Public Accountant Certificate (*Bersertifikasi Akuntan Publik, BAP*) to people who: (i) are IAI members; (ii) are eligible to hold the Accountant title; and (iii) have passed the Public Accountant Certification Examination (USAP).

121. The USAP was introduced in 1997. Accountants who were already in public practice before then did not have to sit the USAP. It was

⁹² Assisted under ADB Loan 1253-INO: *Higher Education Project*, for \$140.0 million, approved on 21 September 1993 and completed in March 2000.

⁹³ *Ministry of Education and Culture (MOEC) Decision Letter No. 56, On the Regulation of Professional Education for Accountants, dated 31 March 1999.*

⁹⁴ Loan 1792-INO: *Technological and Professional Skills Development Sector*, for \$180 million, approved on 29 November 2000.

developed with World Bank assistance in line with IFAC guidance and international norms (USAP is based on the Australian, Canadian and U.S. CPA exams).⁹⁵

122. IAI administers the USAP twice annually (in March and November) in two examination centers (Jakarta and Surabaya). It comprises five subjects: accounting theory and practice, auditing and other professional services, management accounting and financial management, taxation and commercial laws, and accounting information systems. The exam is very competitive; fewer than 10% of candidates pass all five subjects in one sitting.⁹⁶ In contrast to most other countries, no examination exemptions (cross-credits) are allowed.

123. USAP candidates must be: (i) IAI members; and (ii) eligible for the accountant title. This study revealed no indications of 'leakage' (for instance, DPAJP has received no complaints in this regard). Although, the BAP gives no special rights, larger KAPs generally require staff to complete the USAP.

124. To retain the BAP, holders must undertake a minimum of 30 CPE credit units per annum and 120 CPE credit units over each three-year period. IAI conducts CPE seminars, workshops and training sessions.

MOF PA Certificate⁹⁷

125. DPAJP may issue a PA Certificate to people who: (i) are on the State Register of Accountants; (ii) are domiciled in Indonesia; (iii) hold the IAI-issued BAP; (iv) are IAI members; and (v) have at least 3,000 hours relevant practical experience.

126. In addition to general audit experience with a KAP or state audit agency, the practical experience must include at least one year supervising general audit assignments. The certificate is valid for life.

MOF PA Practice License⁹⁸

127. MOF PA Certificate holders may not offer PA services without first obtaining the DPAJP-issued PA Practice License. DPAJP may issue a PA Practice License to those who: (i) hold the MOF PA Certificate; and (ii)

⁹⁵ World Bank Loan 3801-IND: *Accountancy Development Project II* (1995–2000), for \$25 million approved on 22 September 1994.

⁹⁶ Source: www.akuntan-iai.or.id

⁹⁷ *Finance Minister Decree on Public Accountant Services* (No. 43/KMK.017/1997) as amended by *Finance Minister Decree No. 470/KMK.017/1999*.

⁹⁸ *Ibid.*

employ at least three MOF PA Certificate holders. The license is valid for life and is free of charge.

International Comparison

128. IFAC-issued International Education Standards (IESs) and International Education Guidelines (IEGs) address pre-qualification education of professional accountants and continuing professional development. Appendix 4 describes the international guidelines for accountancy qualifications. Moreover, IFAC recently released new IES and IEG exposure drafts (EDs) for public comment (see Appendix 5).

129. Table 18 shows that the Indonesian MOF PA Certificate meets international guidelines and compares favorably with the qualifications of selected countries.

Table 18. Comparison of Public Accountant Qualifications

Requirement	International	Indonesia	California (U.S.)	Philippines
Education	Recognized education program (IFAC: IEG 9, Para 26).	✓ Accredited accounting degree supplemented by a university-based professional education program (pp. 72-73).	✓ Core course comprising 45 semester units of accounting, auditing or business-related subjects (a variety of other qualifications are accepted).	✓ A revised curriculum for the Bachelor of Science in Accountancy, which reflects IEG 9 requirements, is being introduced.
Examination	Yes, a significant portion of responses must be written (IFAC: IEG 9, Para 44).	✓ Yes. Developed in line with IFAC Guidelines (p. 73).	✓ Yes.	✓ / ✗ Multiple-choice questions (to reduce leakage).
Experience	Minimum of three years practical experience in an appropriate, supervised environment (IFAC: IEG 9, Para 49).	✓ Minimum of 3,000 hours prescribed practical experience (p. 74).	✓ / ✗ Two, three, or four years prescribed experience; depending on education level.	✗ None, a CPA with no practical experience can conduct audits and issue audit opinions (the introduction of practical experience is being considered).

Requirement	International	Indonesia	California (U.S.)	Philippines
Continuing professional education	Annual minimum of 30 hours, or 90 hours over each three-year period, of structured learning activities (IFAC, ISAR).	✔ 120 hours over three years with a minimum of 30 hours per year (p. 73).	✔ 80 hours for each two-year license renewal period (following first license renewal).	✘ None, Senate suspended the CPE requirement in 1999 on the basis that it infringed constitutional rights (the introduction of compulsory CPE is proposed).

Source: Table adapted from: Favere-Marchesi, Michael. 2000. Audit Quality in ASEAN. *The International Journal of Accounting*. Vol. 35(1). pp. 121-149. Californian data from ADB. 2002. *Accounting and Auditing Practices in the Republic of the Marshall Islands*. Manila. Philippines data from ADB. 2002. *Accounting and Auditing Practices in the Philippines*. Manila.

6. Other Professional Organizations

Introduction

130. This section describes the composition and activities of other relevant professional organizations.⁹⁹ The Indonesian Society of Appraisers (*Masyarakat Profesi Penilai Indonesia, MAPPI*) is discussed separately (p. 79).

Forum for Corporate Governance in Indonesia (FCGI)

131. Established in February 2000, the aim of the Forum for Corporate Governance in Indonesia (FCGI) is to support improved corporate governance practices in Indonesia. FCGI's activities complement those of the National Committee on Good Corporate Governance (NCCG), which is responsible for drafting the *Code of Conduct of Good Corporate Governance* and developing strategies to implement the *Code*.

132. FCGI's activities have included: (i) publishing booklets on Good Corporate Governance; (ii) developing a self-assessment questionnaire that enables companies to assess their corporate governance arrangements; (iii) publishing information on good corporate governance; and (iv) broadcasting a television program that promotes

⁹⁹ Much of this section's content is sourced from www.fcgi.or.in

good corporate governance practices. FCGI's membership comprises business and professional associations.¹⁰⁰

Institute of Internal Auditors (IIA)—Indonesia Chapter

133. The U.S.-based Institute of Internal Auditors (IIA) is an international professional association that supports the promotion and development of internal auditing. The IIA Indonesia Chapter was established in 1989. Members can sit for the Certified Internal Auditor (CIA) exam, which comprises four parts; internal audit process, internal audit skills, management control and information technology, and the audit environment.

134. The IIA Indonesia Chapter has around 200 members and publishes an internal auditing magazine every two months. It has four strategic priorities: (i) raising awareness of internal auditing in Indonesia with both private and public sector organizations; (ii) increasing membership; (iii) increasing the number of CIA-qualified auditors; and (iv) providing training and education. The IIA provides internal auditing practitioners, executive management, boards of directors and audit committees with standards, guidance and information on internal auditing.

Association of State-owned Enterprise (SOE) Internal Auditors (FKSPI BUMN/BUMD)

135. Established in 1985, the Association of Internal Auditors of State-Owned Enterprises and Local Government SOEs (*Forum Komunikasi Satuan Pengendalian Intern BUMN/BUMD, FKSPI BUMN/BUMD*) supports improvements in internal auditing practices and represents members' interests. Its membership comprises about 1,000 internal auditors from around 190 SOEs. Membership numbers are expected to increase significantly as internal auditors from local government SOEs join.

¹⁰⁰ FCGI's membership comprises: (i) Institute of Internal Auditors (IIA) – Indonesia Chapter; (ii) Association of State-owned Enterprise Internal Auditors (FKSPI BUMN/BUMD); (iii) Internal Auditor Education Foundation (YPIA); (iv) Association of Publicly Listed Companies (AEI); (v) Indonesian Financial Executives Association (IFEA); (vi) Indonesian Society for Transparency (MTI) ; (vii) Association of Indonesian Securities Companies (APEI) ; (viii) Indonesian Society of Appraisers (MAPPI); (ix) IAI - Management Accountants Compartment (IAI-KAM); and (x) The Indonesian Netherlands Association (INA). Although not a member, the Jakarta Initiative Task Force (JITF) is actively involved in FCGI.

Internal Auditor Education Foundation (YPIA)

136. FKSPI BUMN/BUMD supported the 1995 establishment of the Internal Auditor Education Foundation (*Yayasan Pendidikan Internal Auditor, YPIA*). YPIA's main activities are organizing training and education for internal auditors, particularly SOE internal auditors. It also provides internal auditing consulting services and supports research and development activities.

Association of Publicly Listed Companies (AEI)

137. Established in 1988, the Association of Publicly Listed Companies' (*Asosiasi Emiten Indonesia, AEI*) membership has grown from 24 to 314 publicly-listed companies. AEI is involved in the development of Indonesia's capital markets and is often relied upon by *Bapepam* to provide input into the formulation of capital market regulations.

Indonesian Financial Executives Association (IFEA)

138. The Indonesian Financial Executives Association (IFEA)¹⁰¹ was founded in 1975. Initially a consultative association, a major IFEA activity is now negotiating with government on financial market policy. IFEA has about 200 members and is a member of the International Association of Financial Executives Institute (IAFEI).

Indonesian Society for Transparency (MTI)

139. The Indonesian Society for Transparency (*Masyarakat Transparansi Indonesia, MTI*) was established to encourage and support good governance and to minimize KKN.

Association of Indonesian Securities Companies (APEI)

140. Established in 1995, the Association of Indonesian Securities Companies (*Asosiasi Perusahaan Efek Indonesia, APEI*) provides training courses for underwriters, brokers and investment managers. Its membership comprises about 185 securities companies.

¹⁰¹ IFEA was originally known as the Indonesia Financial Executives Institute (IFEI).

7. The Appraisal (Valuation) Profession

Introduction

141. Appraisers value property, including commercial property, Industrial property (manufacturing plants and warehouses), residential property, machinery and personal property. Rooted in economics, asset valuation principles and techniques were initially established in the 1930s. Appraisers reduce the risk involved in property transactions by assigning credible values to property based on a standard method. Financial statement preparers and external auditors rely heavily upon the professional work and opinions of the appraisal profession. Appraisal opinions are also an integral part of insolvency procedures and financing activities.

142. In many countries, the regulation and development of the profession usually have followed a crisis of some sort: the savings and loan crisis in the U.S., the property crisis in the 1980s in Europe, the reform of the centrally planned economies in Eastern Europe, and the 1997-98 financial crisis in Asia.

143. Countries establishing mortgage-lending markets and introducing mortgage-based instruments in their capital markets need to improve valuation standards. Clearly, appraisal standards should be correctly applied and regulated. This can be accomplished by establishing professional standards of valuation, educational requirements, methodology, ethics and oversight in developing real estate markets.

Indonesian Arrangements

144. In January 2001, DPAJP became responsible for supervising the appraisal profession. This involves licensing the profession, ensuring adequate professional standards are in place, policing the standards and developing the profession. In comparison to other countries, Indonesia has few appraisers (see Table 19). DPAJP issues licenses to appraisers and firms.

145. Two professional appraisal bodies exist. The Indonesian Society of Appraisers (*Masyarakat Profesi Penilai Indonesia, MAPPI*) is the oldest body. The Indonesian Association of Appraisal Firms (*Gabungan Perusahaan Penilai Indonesia, GAPPI*) was formed more recently.

146. MAPPI recognizes three appraiser levels: (i) registered appraisers; (ii) certified appraisers; and (iii) public appraisers. Indonesian appraisal services include: (i) valuating tangible and intangible assets; (ii) share and business valuations; (iii) property management; (iv) project

feasibility studies; (v) project management; and (vi) investment intermediation.

Table 19. Appraisal, Actuarial and Insolvency Professionals by Country

Country	—Appraisers—		– Insolvency Experts –		— Actuaries —	
	Number per Million		Number per Million		Number per Million	
	Number	Population	Number	Population	Number	Population
PRC	13,420	10.6	8	0.01	8	0.01
Germany	8,000	97.4	81	0.99	1,661	20.22
Hong Kong, China	1,084	159.5	..	..	199	29.27
India	350	0.3	33	0.03	111	0.11
Indonesia	1,400	6.7	4	0.02	7	0.03
Japan	5,700	45.0	5	0.04	853	6.73
Korea, Republic of	1,724	36.5	1	0.02	11	0.23
Malaysia	500	21.5	26	1.12	..	..
Singapore	519	129.2	11	2.74	82	20.41
Sweden	500	56.4	14	1.58	246	27.74
Thailand	..	..	8	0.13	13	0.21
United Kingdom	20,000	334.8	1,614	27.02	4,764	79.75
United States	80,000	284.1	1,841	6.54	14,968	53.16

Source: Michael Pomerleano (Lead Financial Specialist, World Bank). 2002 April. Back to the Basics: Critical Financial Sector Professions Required in the Aftermath of an Asset Bubble. *The Appraisal Journal*. pp. 173-181.

Indonesian Society of Appraisers (MAPPI)

147. Established in 1980, the Indonesian Society of Appraisers (*Masyarakat Profesi Penilai Indonesia, MAPPI*) represents appraisers. MAPPI is a member of the International Valuation Standards Committee (IVSC).

148. Its 1,400 members include individuals and companies engaged in appraisal activities (e.g., appraisal firms, banks and financial institutions, capital market firms, the Directorate of Land and Building Taxation, insurance agencies, auction houses and property companies). Jakarta-based MAPPI has branches in Medan, Surabaya and Semarang.¹⁰²

¹⁰² www.fcgi.or.in

Valuation Standards

149. Founded in 1981, IVSC formulates and promulgate IVSs and associated procedural guidance. Subsidiary IVSC goals include: (i) encouraging IVS recognition by IASB and other accounting standard-setting bodies; and (ii) encouraging professional recognition of valuers by other disciplines. IVSC has 52 participating country bodies. It coordinates its activities with these country bodies, IAASB, IASB, IFAC, IOSCO, OECD and the World Bank.¹⁰³

150. MAPPI and GAPPI have together formed the Indonesian Valuation Standards Committee (*Komite Penyusun Standar Penilaian Indonesia, KPSPI*). In 2002, KPSPI promulgated a set of Indonesian Valuation Standards (*Standar Penilaian Indonesia, SPIs*).¹⁰⁴ SPIs are directly based on IVSs.

8. Globalization and Liberalization Challenges

151. When the Uruguay Round of trade negotiations was agreed in 1994, measures to liberalize trade in services were included for the first time through the adoption of the General Agreement on Trade in Services (GATS). The WTO created a Working Party on Professional Services (WPPS), which was instructed to give priority to reviewing the international operation of services in the accountancy sector and in determining how a more liberal regime might be introduced.

152. IFAC appointed a special GATS task force to monitor the WPPS's work, comment on proposals and make implementation suggestions. The WPPS's work program is addressing three areas: (i) international standards; (ii) mutual recognition of qualifications as a means of promoting mobility among qualified accountants; and (iii) rules regarding domestic professional regulation (usually the greatest barrier to the free provision of services—although domestic regulations are needed to protect the public, there is a danger that they can become protectionist).

153. Indonesia is involved in the GATS negotiations. It is also a party to, and has corresponding obligations under, several other international memberships and agreements that are relevant to the Indonesian accountancy profession including IFAC, APEC and ASEAN.

154. In December 1995, ASEAN members entered into an agreement to promote preferential trade in services, including business services.

¹⁰³ Source: www.ivsc.org

¹⁰⁴ KPSPI. 2002. March. Indonesian Valuation Standards (*Standar Penilaian Indonesia, SPI*). KPSPI: Jakarta.

Under the accord, ASEAN member countries agreed to liberalize trade in services by substantially eliminating all existing discriminatory measures and market access limitations among members and prohibiting the enactment of new restrictions or limitations. Members also agreed to mutual recognition of each other's licensing or certification requirements for service suppliers.

155. Table 20 presents the findings of a 2000 survey that compared restrictions on accountancy services across economies. The domestic index reflects restrictions on the establishment and ongoing operations of domestic service providers. The foreign index reflects restrictions facing foreign service providers when establishing and conducting operations in the local market. Of the 34 economies surveyed, Indonesia had the third most restricted environment for foreigners.¹⁰⁵

Table 20. Restrictions on Accountancy Services

Index	Low	Medium	High
Foreign Index:	Finland, Netherlands, United Kingdom	Argentina, Australia, Belgium, Brazil, Canada, Chile, Denmark, France, Germany, Greece, Hong Kong (China), India, Italy, Japan, Luxembourg, Mexico, New Zealand, Portugal, Singapore, South Africa, Spain, Sweden, Switzerland, Turkey, United States	Austria, Indonesia, Republic of Korea, Malaysia, Philippines, Thailand
Domestic Index:	Chile, Finland, Indonesia, Malaysia, South Africa, Switzerland, Turkey	Argentina, Australia, Greece, Italy, Luxembourg, Mexico, Netherlands, Singapore, Sweden, Thailand, United Kingdom	Austria, Belgium, Brazil, Canada, Denmark, France, Germany, Hong Kong (China), India, Japan, Republic of Korea, New Zealand, Philippines, Portugal, Spain, United States

Source: Nguyen-Hong, Duc. 2000 August. *Restrictions on Trade in Professional Services*. Staff Research Paper. Australian Productivity Commission: Commonwealth of Australia. pp. 19-23.

156. There are currently no automatic recognition or mutual recognition agreements (MRAs) between IAI and its counterparts in other countries

¹⁰⁵ Nguyen-Hong, Duc. 2000 August. *Restrictions on Trade in Professional Services*. Staff Research Paper. Australian Productivity Commission: Commonwealth of Australia. p. 32.

(Appendix 4 describes WTO-GATS guidelines for MRAs). Furthermore, the domestic profession is largely closed to direct foreign participation—international firms are able to establish correspondent relationships with local firms, but are barred from direct investment.

157. However, in May 2002, the Seventy-fourth AFA Council Meeting agreed that representatives from Indonesia, Malaysia, Philippines, Singapore and Thailand would meet in Jakarta, later in 2002, to identify actions to liberalize the ASEAN accountancy profession.¹⁰⁶

158. A recent paper examined efforts to protect Indonesia's domestic accountancy profession over the past 50 years, and the current liberalization trend.¹⁰⁷ In particular, a 1986 Finance Minister Decree legitimized correspondent relationships with foreign accountancy firms.¹⁰⁸ A 1997 Decree further relaxed restrictions on foreign accountants by removing citizenship requirements.¹⁰⁹ The development of the draft Public Accountant (PA) Law continues this liberalization trend (p. 88).

9. Professional Quality Control and Assurance

Introduction

159. Significant numbers of Indonesian companies and banks—with apparently sound financial positions—collapsed in the wake of the Asian financial crisis. Most had received unqualified audit opinions. Subsequent events indicated that these opinions were incorrect.

160. Legislative weaknesses meant that oversight bodies could not sanction erring auditors and relied on IAI to take disciplinary action. But IAI's response was considered weak. Some commentators contend that IAI disciplinary arrangements need urgent revision (see Box 2). This section describes the mechanisms and processes that support professional quality.

¹⁰⁶ ASEAN Federation of Accountants (AFA). 2002 May 5. Minutes of 74th AFA Council Meeting. www.mia.org.my

¹⁰⁷ Bachtiar, Emil. 2001 August. *The Professionalization of Accounting in Indonesia*. Paper presented to the Second International Accounting History Conference, Osaka, August 2001.

¹⁰⁸ *Finance Minister Decree on Public Accountants (No. 763/KMK.011/1986)*.

¹⁰⁹ *Finance Minister Decree on Public Accountant Services (No. 43/KMK.017/1997)*.

Box 2. Accountants' Accountability

... Indonesia has seen many accounting frauds even though the chicanery [did] not set off the fierce public attacks on auditors as those in the U.S..

Part of the problem is caused by lax law enforcement against auditors as public accounting firms are virtually outside the government legal arm, overseen only by [IAI]. Accounting firms accused of violating major auditing rules are tried by a judiciary board whose panel of judges are also representatives of accounting firms who are appointed by and answer to [IAI].

One can easily question the independence of this peer oversight process. For example, ten public accountants who were found guilty of accounting fraud in connection with their audited reports on banks, which went bankrupt in 1998 and 1999, were given only very lenient punishments. Three of them were acquitted of all charges, three were ordered to undergo retraining and four were given a strong warning and barred for some time from auditing banks.

Moreover, regulations on auditing principles virtually close almost all avenues for liability lawsuits against auditors because their reports always start with a statement that the financial accounts are the responsibility of the management since outside auditors are legally required only to give an opinion and not judgment, in accordance with Indonesian [GAAP].

... A thorough review of the rules determining how companies draw up their accounts, and how these accounts should be independently audited, is now most imperative.

Independent auditors now seem to depend too much on the internal audit system and the presumption that the management is honest. Instead of digging too deeply into the accounts, they usually only do sample audits to check the internal control system. No wonder audited accounts appear to be designed mainly to avoid liability suits and not to inform the public on the process of calculations that lead into the numbers in the accounts.

The Finance Ministry may consider adopting the recent order by the U.S. [SEC] that requires the management and chief financial officers at major publicly-traded companies to swear under oath in writing that the numbers in their financial statements are correct. This threat of civil and criminal penalties would go a long way in preventing management fraud.

Given the vital role of auditors in maintaining the integrity of the financial market, the supervision of the accounting profession also needs to be strengthened with an independent oversight committee and an independent judiciary board, unlike the current one which acts simultaneously as the prosecutor and the judge and is run entirely by the accounting community themselves ...

– Editorial, The Jakarta Post, 16 July 2002¹¹⁰

¹¹⁰ The Jakarta Post. 2002 July 16. *Accountants' Accountability*. Newspaper Editorial. p. 6.

Professional Ethics and Standards

161. The Public Accountants Professional Standards Board (*Dewan Standar Profesional Akuntan Publik, DSPAP*) promulgates SPAPs. DSPAP comprises auditing practitioners, from small and large firms, and is part of the IAI Public Accountants Compartment (IAI-KAP). SPAPs comprise auditing standards, attestation standards, accounting and review standards, consulting services standards, quality control standards and the code of professional conduct.

162. In May 2000, DSPAP approved revised *Rules of Conduct for Public Accountants* (see Table 21) The *Rules* are directly based upon the AICPA *Rules of Conduct*.ⁱⁱⁱ Appendix 4 describes international guidelines and norms for professional quality control and assurance (see page 162), which are comparable to the AICPA *Rules of Conduct*.

Table 21. Effective Indonesian SPAPs as at 30 June 2002

Number	Title	Effective Date
	<i>Standards for Consulting Services</i>	
100	Definition and Standards for Consulting Services	1 January 1998
	<i>Quality Control Standards</i>	
100	Quality Control Systems for Public Accounting Firms (KAPs)	1 January 1998
200	Formulation of Quality Control Policies and Procedures	1 January 1998
300	Standards for Conducting and Reporting Quality Reviews	1 January 1998
	<i>IAI-KAP Rules of Conduct for Public Accountants</i>	
100	Independence, Integrity and Objectivity	} 5 May 2000
200	General Standards and Accounting Principles	
300	Responsibilities to Clients	
400	Responsibilities to Colleagues	
500	Other Responsibilities and Practices	

Source: IAI. 2001. *Professional Standards for Public Accountants*. Jakarta.

IAI Disciplinary Arrangements

163. Within IAI-KAP, the Judiciary Body for Public Accountants (*Badan Peradilan Profesi Akuntan Publik, BP2AP*) considers public complaints regarding the application of professional standards and ethical issues. When complaints are filed, BP2AP follows due-process procedures

ⁱⁱⁱ www.akuntan-iai.or.id

involving: (i) evidence gathering; (ii) hearings; (iii) determination; and (iv) sanctions. As with other countries, this process may take up to a year (although BP2AP Guidelines suggest a maximum timeframe of three months).

164. In the past, BP2AP has sanctioned PAs for misconduct including: (i) insufficient communication with other auditors; (ii) failure to maintain adequate audit working papers; (iii) failure to maintain independence and objectivity; (iv) soliciting and inappropriate advertising; and (v) failure to observe ethics. PAs may appeal BP2AP findings to the IAI Honorary Council (also within the IAI-KAP). The Honorary Council comprises senior government officials, industry representatives and public accountants.¹¹²

Regulatory Mechanisms for Quality Control and Enforcement

165. At first glance, Indonesian regulatory mechanisms for sanctioning negligent PAs and KAPs appear sound. However, Bank Indonesia's powers only became effective in May 1999. Moreover, *Bapepam* and MOF sanctions must be applied in a consecutive manner—warnings are the usual result of disciplinary action. Furthermore, although injured parties may take civil action against negligent auditors, Indonesia's dysfunctional judicial system blunts this mechanism.

All PAs and KAPs

166. MOF may impose administrative sanctions on negligent PAs and KAPs, including: (i) warnings; (ii) license suspension, for a maximum 24 months; and (iii) license revocation. However, these sanctions must be imposed in a consecutive manner.¹¹³

167. Before 2001, BPKP conducted quality reviews of KAPs (both domestic and foreign). The reviews were based on SPAPs. On 1 January 2001, DPAJP assumed responsibility for reviewing KAPs from BPKP. It is currently developing its capacity and procedures (e.g., human resources and standard operating procedures) to undertake this responsibility.¹¹⁴

¹¹² Kurniawan, Dudi M. and Nur Indriantoro. 2000. *Corporate Governance in Indonesia*. Paper Presented to the Second Asian Roundtable on Corporate Governance. Hong Kong, China. 31 May – 2 June 2000. pp. 22-23.

¹¹³ *Finance Minister Decree on Public Accountant Services (No. 43/KMK.017/1997)* as amended by *Finance Minister Decree No. 470/KMK.017/1999*.

¹¹⁴ AusAID is supporting these activities through the Technical Assistance Management Facility II (TAMF II) Project.

Capital Markets

168. *Bapepam* may impose administrative sanctions for violations of the *Capital Markets Law (No. 8) 1995* or its implementing regulations, including: (i) written reprimands; (ii) fines; (iii) restrictions on business activity; (iv) suspensions of business activity; (v) revocations of business licenses; (vi) cancellations of approvals; and (vii) cancellations of registrations.¹¹⁵ However, these sanctions must be applied in a consecutive manner.

169. *Bapepam* is authorized to investigate and evaluate PAs and KAPs that provide services in the capital markets.¹¹⁶ To this end, it regularly issues warning letters to PAs and KAPs, but has not imposed other sanctions.

Financial Sector

170. Bank Indonesia (BI) is responsible for banking supervision. In relation to this, BI contracts KAPs to undertake audits.¹¹⁷ BI's initial intention was to only appoint the very largest international KAPs as bank auditors however, in the face of professional lobbying, this policy was relaxed and second-tier firms are now approved.

171. An independent financial services supervisory board is being established.¹¹⁸ The Financial Services Authority (*Otorita Jasa Keuangan, OJK*) will assume banking supervision responsibilities from BI. Meanwhile, BI will supervise banks until OJK is established (no later than 31 December 2002).¹¹⁹

172. BI may impose administrative sanctions on negligent PAs and KAPs, including: (i) fines; (ii) warnings; (iii) revocation or annulment of business licenses by the competent institution if the violation is conducted by an entity; (iv) imposition of disciplinary sanctions if the violation is conducted by a business entity.¹²⁰

173. BI has revoked some KAP appointments but has not imposed any other sanctions. Moreover, BI has only had this authority since May 1999 with enactment of the *Bank Indonesia Law (No. 23) 1999*. Consequently, it was unable to sanction the auditors in relation to the 1997-98 bank audits.

¹¹⁵ Chapter XIV, *Capital Markets Law (No. 8) 1995*.

¹¹⁶ Article 65, *Capital Markets Law (No. 8) 1995*.

¹¹⁷ In accordance with Article 30, *Bank Indonesia Law (No. 23) 1999*.

¹¹⁸ In accordance with Article 34, *Bank Indonesia Law (No. 23) 1999*.

¹¹⁹ Article 35, *Bank Indonesia Law (No. 23) 1999*.

¹²⁰ In accordance with Article 72, *Bank Indonesia Law (No. 23) 1999*.

Civil Actions Against Negligent Auditors

174. Under provisions of the *Civil Code*—and in conjunction with various company, capital market, and banking laws and regulations—parties that suffer losses due to audit failures may sue auditors (see Box 3). Nevertheless, as of July 2002, investors or shareholders had never filed a class action lawsuit against PAs or KAPs.¹²¹

Box 3. Provision for Civil Action Against Negligent Auditors

“Any person who suffers losses arising from violations of this Law and or its implementing regulations can sue for compensation, either jointly or severally with other Persons with similar claims, against the person or persons responsible for such violations.”

– Article III, *Capital Markets Law (No. 8) 1995*.

10. The Draft Public Accountant (PA) Law

Introduction

175. The Asian financial crisis revealed weaknesses in Indonesian financial governance arrangements. In June 1998, ADB approved the FGRSDP to support government efforts to improve resource allocation efficiency, and promote and strengthen the governance of the financial and public sectors.¹²² To achieve this objective, the FGRSDP promoted: (i) the adoption of best-practice financial governance arrangements; (ii) improved disclosure and transparency of financial accounting, auditing and reporting; and (iii) the strengthening of the legal and regulatory framework to support effective implementation of financial and public sector reforms. In relation to auditing, the existing legal framework for

¹²¹ The Jakarta Post. 2002 July 22. *Class Action Suit Against Crooked Accountants Urged*. Newspaper Article. p. 1.

¹²² ADB 1998. *Report and Recommendation of the President to the Board of Directors on the Proposed Loans to the Republic of Indonesia for Financial Governance Reforms: Sector Development Program (FGRSDP) and a Proposed Equity Investment in a Secondary Mortgage Facility*. Manila.

The FGRSDP was approved on 25 June 1998 and comprised a program loan for \$1,400 million (Loan No. 1618-INO); a \$3 million equity investment; a \$47 million investment loan (Loan 1619-INO); a \$50 million technical assistance loan to support commercial bank restructuring, governance improvements and institutional strengthening of various government agencies (TA Loan No. 1620-INO).

public accountants does not explicitly make PAs liable for audit negligence.¹²³ Government-agreed policy conditions included enacting legislation and regulations making: (i) auditors liable for negligence in performing audits; and (ii) directors liable for false information in annual reports and other public information.¹²⁴

176. A draft PA Law was prepared in 2000, but was limited in scope and subsequently abandoned. In 2001, a special team was established to draft a PA Law.¹²⁵ Later that year, in accordance with Indonesian procedures for preparing bills¹²⁶, government released an *Academic Paper* proposing the approach to be taken by the new law.¹²⁷ Drafting activities recommenced following its release. The draft law remains under review and, since November 2001, AusAID has been assisting the preparatory process.¹²⁸ Although the PA Law had not been enacted, ADB reviewed the FGRSDP policy conditions and, in July 2002, agreed to release the third and final program tranche of \$350 million. Meanwhile, government remains committed to the draft PA Law, which it plans to submit to the State Secretariat in 2003 (see Box 4).

¹²³ However, under provisions of the Civil Code – and in conjunction with various company, capital market, and banking laws and regulations – parties that suffer losses due to audit failures may sue auditors.

¹²⁴ ADB. 2002 June. Progress Report on the Release of Third Tranche: Financial Governance Reforms Sector Development Program (Loan 1618-INO) to Indonesia. Board Paper: Manila.

¹²⁵ Finance Minister Decree No. 186/KMK.06/2001. 16 April 2001.

¹²⁶ Presidential Decree No. 188/1998, dated 29 October 1998, *Procedures for the Preparation of a Bill*.

¹²⁷ MOF. 2001. *Academic Draft: Draft of Public Accountant Law*. Jakarta.

¹²⁸ Through the AusAID Technical Assistance Management Facility II (TAMF II) Project.

Box 4. Government Drafts New Bill on Accountancy Profession

The government is drafting a new bill on the accountancy profession in a bid to help prevent misstatements and misrepresentations in audited financial reports. Mirza Mochtar, Director of Public Accounting and Appraisal Services at the Ministry of Finance, said the new bill would provide better legal protection for both clients and accountants.

"The bill aims to provide a stronger legal foundation for both clients and accountants, including protecting clients from being defrauded by their accountants," Mirza told The Jakarta Post on Wednesday.

In the wake of the Enron and WorldCom scandals involving Arthur Andersen, one of the world's big five accounting firms, public accountants worldwide have been under fire for allegedly cooking their clients' books. However, Mirza claimed that the bill did not have anything to do with the latest financial scandals. "The current law on the accountancy profession was out-of-date even when it was put on the statute books in 1954. It is no longer appropriate for current conditions. That's why we need to draft a new one," he said.

According to Mirza, his directorate had set up a team to draft the bill. After the draft was finished, the next step would be to form an inter-ministerial team to discuss the draft. The inter-ministerial team would consist of officials from the Ministry of Justice, the Ministry of Finance and the State Secretariat.

Mirza said that according to the bill, any public accountants found violating professional ethics and standards would have their licenses revoked by the government without prior notice. He added that the bill would also open the possibility for criminal charges to be laid against accountants or accounting firms who deliberately made misstatements or misrepresentations in financial reports.

"It is difficult to bring accountants before the criminal courts as the current ministerial decree does not authorize the filing of criminal prosecutions," he explained.

The new bill also provides that a company may only retain the services of an accounting firm for a maximum of four years. Under the current law, there is no such limitation. Mirza added that the new bill would also force accounting firms to give up their consulting services to avoid conflicts of interest.

Another crucial change under the bill, Mirza said, was that the government would conduct a regular review of accounting firms. The reviews would be held annually to assess the performance of the firms and to see if they had carried out their work in accordance with the set standards and rules.

– The Jakarta Post, 5 July 2002¹²⁹

The 2001 Academic Paper

177. In 2001, the MOF released an *Academic Paper*¹³⁰ that examined issues to be covered by the new PA Law. The *Academic Paper* identified the PA

¹²⁹ The Jakarta Post. 2002 July 5. *Government Drafts New Bill on Accountancy Profession*. Interview with Mirza Mochtar, Director of Public Accounting and Appraisal Services at the Ministry of Finance. Newspaper Article.

¹³⁰ MOF. 2001. *Academic Draft: Draft of Public Accountant Law*. Jakarta.

Law's objectives as: (i) protecting the public trust provided to PAs; (ii) providing a better legal framework for the public accountancy profession; and (iii) supporting national economic development and preparing for the liberalization of public accounting services.¹³¹ In particular, the *Academic Paper* contended that existing arrangements provided weak support for criminal and civil sanctions against PAs and KAPs.¹³² It reviewed existing arrangements and made proposals for the new PA Law—comparator countries included Japan, the Republic of Korea (ROK), Singapore and the U.S.

178. Appendix 6 summarizes the description, analysis and proposals that the *Academic Paper* presents. The following key changes are proposed. First, professional arrangements would be restructured. Second, PA and KAP obligations, responsibilities and prohibitions would be clearly stated, providing a basis for enhanced quality control and greater legal responsibility—KAPs would be required to hold professional indemnity insurance. Third, the law would stipulate administrative, civil and criminal sanctions. These would not apply in a step-by-step manner (as previously) and KAP partners would be jointly and fully accountable. Fourth, the PA Law would be consistent with liberalization commitments (on a reciprocal basis).

Support for the New Public Accountant Law

179. The Government has stated that it will strengthen financial governance arrangements. Until July 2002, this commitment was supported by FGRSDP policy conditionalities including enactment of the PA Law. However, Parliament's legislative agenda is extremely busy (about 200 bills are either with Parliament, or are being developed.¹³³). At the same time, very few laws are being passed due to "political bickering" and resource constraints.^{134, 135} Nevertheless, two factors provide domestic pressure for public accounting reform in this difficult legislative environment.

180. First, because of recent U.S. failures, accounting and auditing arrangements are currently receiving heightened attention internation-

¹³¹ *Ibid*, pp. 8-9.

¹³² *Ibid*, p. 17.

¹³³ MOF Estimate.

¹³⁴ The Jakarta Post. 2002 July 17. *House Leaders Ask for More Funds for Passage of Bills*. Newspaper Article. p. 1.

¹³⁵ The January–March 2002 House Session endorsed three out of a planned 24 bills. The May–July 2002 House Session endorsed two out of a planned 22 bills.

ally. In response, many countries are strengthening their accounting and auditing arrangements to retain investor confidence. Meanwhile, FDI approvals in Indonesia during the first five months of 2002 declined by almost 60 percent, when compared to the same period in 2002.¹³⁶ Not surprisingly, legislators are interested in the draft PA Law (see Box 5).

Box 5. 'Strong Sanctions Against Bad Accountants a Must'

A senior legislator supported the Government's move to draft a new bill on the accounting profession, saying that the ruling could help ensure good corporate governance in Indonesia.

Learning from the current accounting scandals in the U.S., the bill should impose stiffer sanctions for delinquent accountants to deter them from fraud in the future, said Faisal Baasir, Deputy Head of the House of Representatives Commission IX on Financial Affairs.

... Faisal acknowledged that the new bill had yet to reach the hands of the legislators, as it was still being drafted by the government. "The sooner the better," said Faisal, who pledged that legislators would push for imposing strong punishments, including jail terms for bad accountants.

- The Jakarta Post, 13 July 2002¹³⁷

181. Second, parallels have been drawn between the U.S. failures and certain Indonesian failures. Some commentators contend that Indonesia's self-regulating regime is ineffective (see Box 6). However, some PAs strongly contest this assertion. They argue that too much time has passed since the failures, and the government investigations lacked rigor.¹³⁸

¹³⁶ The Jakarta Post. 2002 July 13. *Japanese Investors Urge RI to Improve Business Climate*. Newspaper Article.

¹³⁷ The Jakarta Post. 2002 July 13. *Strong Sanctions Against Bad Accountants a Must*. Newspaper Article.

¹³⁸ Study interview notes.

Box 6. Indonesia is No Stranger to Accounting Scams: Expert

“Scams have already occurred in Indonesia, and it should serve as a wake-up call for the Indonesian public and accounting community,” [Professor Wahyudi Prakarsa, University of Indonesia] said, while pointing at the latest financial fraud case involving ten public accountant firms here.

The ten firms had audited 37 banks before the 1997 financial crisis, and the audit results revealed that the ... banks were sound. However, as the financial crisis struck the country, the banks collapsed due to poor financial performance. It was revealed later by a government investigation that the firms had been involved in accounting scams.

The government has reprimanded the firms, but no sanctions were given, as the government has no right to impose any sanctions. The only body that has the right to sentence accounting firms is a non-governmental agency formed by the [IAI] called the Judiciary Body for Public Accountants (BP2AP). The agency investigated the case and handed down the punishment. But, the sanctions were considered too lenient, as the agency only prohibited three firms from auditing banking clients, while the remaining seven walked free.

Wahyudi believed that the case is only the tip of the iceberg [and that there are] many other similar accounting scams here. ... Therefore, the most important step, he asserted, was for the government, which is currently drafting an accounting bill, to create tight regulations to prevent possible fraud.

– The Jakarta Post, 11 July 2002¹³⁹

11. Issue Synopsis: Professional Infrastructure

182. This chapter concludes that—although some professional arrangements meet international norms—others compare very badly. Fortunately, some improvements are straightforward, inexpensive and easy to implement. These include making the PA Law changes and disallowing correspondent relationships in favor of direct foreign firm presence. Others will take time and involve easing professional access, strengthening qualifications (below BAP level) and raising the profession’s status.

183. Chapter VIII—*Issues and Recommendations*—identifies and describes constraints and proposes corrective actions. These include the following issues regarding Indonesia’s professional accountancy infrastructure:

- The draft PA Law presents a unique opportunity to strengthen the profession, raise the credibility of financial reporting and support economic development. This study supports the general thrust of the draft PA Law. However:

¹³⁹ The Jakarta Post. 2002 July 11. *Indonesia is No Stranger to Accounting Scams: Expert*. Interview with Professor Wahyudi Prakarsa from the University of Indonesia. Newspaper Article. p. 13.

- The assignment of certain functions should be carefully considered (i.e., training and accreditation). This study strongly supports IAI retention of the certification function and cautions against direct DAI provision of training.
- The efficacy of the proposed arrangements depends on DAI composition, appointment, dismissal and funding arrangements.
- The draft PA Law focuses solely on public accountants and ignores other accounting professionals.
- The proposed arrangements must be implemented in a practical and realistic manner.
- Quality control rigor depends on how exposed international parents are to domestic operations. But international firms have little or no liability for their Indonesian activities, so the most powerful mechanism for ensuring quality audits is ineffective.
- There is only one internationally-comparable accountancy qualification (BAP). However, IAI-KAP is undertaking preliminary work on establishing management accountant qualifications and IAI has long considered introducing an Accountant Technician qualification.