

IV. Accounting and Auditing Standards

This chapter describes the accounting and auditing standards that govern the preparation of external financial reports and the audit of those reports. It is structured as follows:

Part One: Accounting Standards

- 1 – Introduction – reviews the historical development of Indonesian accounting standards.
- 2 – Financial Accounting Standards Board (DSAK) – outlines the role and composition of DSAK, the primary accounting standard-setting body.
- 3 – Accounting Standard-Setting Process – describes the accounting standard-setting process.
- 4 – Indonesian Financial Accounting Standards (PSAKs) – describes Indonesian financial accounting standards.
- 5 – Conformity with International Accounting Standards (IAS) – compares PSAKs and IASs.
- 6 – Legal Status of PSAKs – describes the legal status of PSAKs for financial reporting.
- 7 – Taxation Reporting Requirements – reviews the relationship between PSAKs and taxation reporting practices.
- 8 – Public Sector Accounting Standards – describes the standards that govern public sector reporting.

Part Two: Auditing Standards

- 9 – Introduction – describes the historical development of Indonesian auditing standards.
- 10 – Auditing Standard Setting – discusses audit standard-setting arrangements.
- 11 – Indonesian Auditing Standards (SPAPs) – describes Indonesian auditing standards.
- 12 – Comparison with International Standards on Auditing (ISAs) – examines differences between Indonesian auditing standards and ISAs.
- 13 – Public Sector Auditing Standards – describes government auditing standards.
- 14 – Issue Synopsis: Accounting and Auditing Standards – summarizes the issues identified in this chapter.

Part One. Accounting Standards

1. Introduction¹⁴⁰

184. Over the past three decades, the basis for Indonesian financial reporting has evolved substantially—it is now broadly consistent with International Accounting Standards (IAS).¹⁴¹ IAI can take credit for this achievement—although much was accomplished with external support, IAI members contributed countless days of voluntary time to develop standards. Table 22 traces the evolution of Indonesian Financial Accounting Standards.

¹⁴⁰ Primary Sources:

- 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.
- 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.
- 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.
- Rosser, Andrew. 1999 July. The Political Economy of Accounting Reform in Developing Countries: The Case of Indonesia. Murdoch University: Working Paper No. 93.
- Saudagaran, Shahrokh M. and Joselito G. Diga. 2000. The Institutional Environment of Financial Reporting in ASEAN. *International Journal of Accounting*. Vol 35(1). pp. 1-26.

¹⁴¹ In 2001, the International Accounting Standards Board (IASB) assumed responsibility from the International Accounting Standards Committee (IASC) for promulgating IASs. In future, IASB-issued standards will be called International Financial Reporting Standards (IFRSs). Although the IASB now expects its standards to be called IFRSs, this report uses the term IASs (in the interests of continuity).

Table 22. Evolution of Indonesian Financial Accounting Standards

Until 1973	<i>Early Dutch Accounting</i>	Dutch-based legislation and accounting requirements.
1973–1984	<i>Early U.S. GAAP</i>	In 1973, IAI adopts Indonesian accounting principles (PAIs), which are directly based on U.S. GAAP (as it existed in 1965).
1984–1994	<i>Updated U.S. GAAP</i>	In 1984, PAIs are significantly revised to expand their coverage and reflect developments in U.S. GAAP.
1994 to date	<i>International Accounting Standards (IAS)</i>	At its September 1994 Congress, IAI endorses the use of IAS as a basis for domestic financial reporting. IAS-based Financial Accounting Standards (PSAKs) are subsequently issued. Since 1994, IAI has worked to harmonize PSAKs with IASs.

185. Before 1973, financial reporting requirements were based upon the prescriptions of Dutch-based company law that simply required “adequate accounts to be kept”. Two factors led to the 1973 adoption of U.S.-based generally accepted accounting principles (GAAP). First, Indonesian academics were increasingly influenced by U.S. accounting thought and practices. In particular, an important 1962 academic study¹⁴² contended that U.S. arrangements were most appropriate for the Indonesian environment and strongly advocated their adoption. Second, after a substantial fall in activity—following the 1960 suspension of trading in the shares of Dutch companies—the capital market eventually closed in 1968. However, government officials recognized that properly functioning capital markets were necessary to increase FDI levels. In response, officials established three bodies and made them responsible for reactivating the capital markets.¹⁴³ Their functions included working with IAI to prepare and promulgate Indonesian accounting standards.

186. In 1973, IAI formed an *ad hoc* committee to develop Indonesian GAAP. The committee based its work directly upon U.S. GAAP (as it

¹⁴² Hadibroto, Suhadji. 1962. A Comparative Study of American and Dutch Accountancy and their Impact on the Profession in Indonesia. Unpublished PhD Dissertation, Lembaga Pencrbit Fakultas Ekonomi, Universitas Indonesia, Jakarta.

¹⁴³ In 1968, the *Money and Capital Markets Preparation Team* was created to recommend policy actions to BI, on the development of Indonesian money and capital markets. Two other BI-led bodies were established in 1970 and 1972 to implement these policy actions, reactivate the capital market and to supervise its activities.

existed in 1965¹⁴⁴). In December 1973, IAI adopted the Committee's recommendations in the form of Indonesian accounting principles (*Prinsip Akuntansi Indonesia, PAI*), which comprised basic accounting principles, practices, methods and techniques. IAI coordinated its efforts with the MOF Directorate General of Taxation (*Direktorat Jenderal Pajak, DJP*) and *Bapepam* thereby ensuring that PAIs gained official endorsement (e.g., as an acceptable basis for tax assessments). IAI subsequently established the Indonesian Accounting Principles Committee (*Komite Prinsip Akuntansi Indonesia, KPAI*) in 1974 to set accounting standards on an ongoing basis.

187. In response to economic reforms and market deregulation, KPAI issued significantly revised PAIs in 1984. However, despite substantial improvements, the revised PAIs still did not address industry-specific accounting practices (e.g., banking, insurance or mining) and had a narrow coverage (for instance, they largely ignored consolidation and provisioning). The limited coverage of PAIs, combined with an absence of legal backing, meant that companies still had enormous latitude in their financial reporting choices.

188. By the early 1990s, more than 200 companies were listed in Indonesia—a tenfold increase in just a decade. Demands from investors, creditors and lenders for comprehensive and high quality accounting standards accompanied this rapid growth. Consequently, in 1994, the IASC-issued *Framework for the Preparation and Presentation of Financial Statements* was adopted. At the same time, IAS-compatible Financial Accounting Standards (*Pernyataan Standar Akuntansi Keuangan, PSAKs*) were developed. In September 1994, the Seventh IAI National Congress endorsed the use of IAS as the basis for domestic financial reporting and approved the new PSAKs. Since 1994, IAS-harmonization activities have continued.¹⁴⁵

¹⁴⁴ Grady, Paul. 1965. Inventory of Generally Accepted Accounting Principles for Business Enterprises, *Accounting Research Study No. 7*. American Institute of Public Accountants.

¹⁴⁵ These efforts were part of the 1988-2000, World Bank-sponsored, 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.

2. Financial Accounting Standards Board (DSAK)

189. In 1994, KPAI was reconstituted as the Financial Accounting Standards Committee (*Komite Standar Akuntansi Keuangan, KSAK*). In 1998, KSAK's structure and processes were altered to strengthen standard-setting arrangements. First, the more independent Financial Accounting Standards Board (*Dewan Standar Akuntansi Keuangan, DSAK*) superseded KSAK. Second, three fulltime staff were appointed to support DSAK's activities. Third, DSAK's procedures were revised to improve standard setting. For instance, criteria for selecting issues for consideration were developed and implemented. Moreover, formal standard-setting processes were developed. DSAK's composition (see Table 23) and processes are determined by formal rules.

Table 23. Financial Accounting Standards Board (DSAK) Composition

Sector	1994	July 2002
<i>Private Sector:</i>		
Practicing accountants	5	5
Management accountants	2	4
Academics	5	2
<i>Public Sector:</i>		
<i>Bapepam</i>	1	1
Directorate General of Taxation (DGoT)	1	1
Supreme Audit Board (BKP)	1	..
Ministry of Finance (DPAJP)	1	..
Bank Indonesia (BI)	1	1

190. Established in 1998, the Financial Accounting Standards Advisory Council (*Dewan Konsultatif Standar Akuntansi Keuangan, DKSAK*) advises DSAK on issues to be addressed by accounting standards and raises funds to support standard-setting activities. DKSAK represents a wider constituency that includes regulators, public accounting firms, business entities and state owned enterprises.

191. In 2001, the MOF Directorate General for Financial Institutions (*Direktorat Jenderal Lembaga Keuangan, DJLK*) released an *Academic Paper* proposing the approach and contents of a new Public Accountants (PA) Law.¹⁴⁶ It envisages an independent accounting standard-setting board. Government plans to submit the draft PA Law to the State Secretariat in 2003.

¹⁴⁶ Ministry of Finance (MOF). 2001. *Academic Draft: Draft of Public Accountant Law*. MOF: Jakarta.

192. The issue of whether accounting standard setting should be a government or private-sector function is a common one faced by many countries and is influenced by a range of factors.¹⁴⁷ However, this proposal aligns with international trends for semiautonomous, representative bodies to set accounting standards (for instance the 2001 reconfiguration of international accounting standard-setting arrangements).

3. Accounting Standard-Setting Process

193. A sound accounting standard-setting process has five phases: (i) **design**—a particular aspect of accounting is identified and researched and an exposure draft prepared; (ii) **approval**—the draft is subjected to review and, if it survives, it is approved as a standard; (iii) **education**—financial statement users and preparers are educated in the impacts and implementation of the new standard; (iv) **implementation**—the requirements of the new standard are implemented by financial statement preparers; and (v) **enforcement**.¹⁴⁸

194. The Indonesian standard-setting process meets international norms regarding the first three phases. It is prescribed in DSAK rules and has eight broad stages:

- (i) *Issue Identification*: The IAI National Congress, which meets every four years, issues resolutions on DSAK's strategic work program. In addition, DSAK monitors and considers pronouncements made by IASB and other standard setters, and reviews direct submissions by other parties.
- (ii) *Preliminary Consideration*: DSAK discusses the identified issues and, where necessary, commissions and conducts studies of issues before they are included in the DSAK work program.
- (iii) *Preparation of Accounting Discussion Paper*: For each accepted topic, a DSAK project committee is established to prepare a Topic Outline and an Accounting Discussion Paper, which describes and critically examines the topic.

¹⁴⁷ Zeff, Stephen. 1987. Setting Accounting Standards: Some Lessons from the US Experience. *Accountant's Magazine*. December. p. 27.

¹⁴⁸ For further discussion, see: Narayan, Francis B., Ted Godden, Barry Reid, and Maria Rosa 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*. Asian Development Bank. pp. 24-26.

- (iv) *Preparation of Exposure Draft (ED)*: Following consideration of the Accounting Discussion Paper, DSAK develops a preliminary Exposure Draft (ED) on the topic. The ED must be entirely consistent with the IAS Framework. The preliminary ED is circulated to interested parties (including practitioners, academics, industry associations and other interested parties) for their comments. DSAK considers comments and refines the ED.
- (v) *Publication of ED*: The ED is published in *Media Akuntansi* (the IAI journal) and distributed to relevant parties at least one month before public hearings begin.
- (vi) *Public Hearings*: Public hearings are held at which interested parties can express their views and opinions on the ED. In considering these views and opinions, DSAK consults further with government agencies, other relevant organizations and individuals before finalizing the PSAK.
- (vii) *PSAK Preparation*: Where necessary, DSAK amends the ED to reflect consultations.
- (viii) *Approval and Promulgation*: DSAK approves the PSAK for promulgation. The approved PSAK is published in *Media Akuntansi* and on the IAI website.

4. Indonesian Financial Accounting Standards (PSAKs)

195. Appendix 7 lists the 57 existing PSAKs at 30 June 2002. PSAKs were developed and refined under the World Bank-sponsored *Accountancy Development Projects*.¹⁴⁹ ADB has also supported PSAK improvements.¹⁵⁰ In 1994, IAI agreed that PSAKs should be IAS-compliant. To this end, DSAK contends that every PSAK is consistent with the IAS Framework.

¹⁴⁹ 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.

¹⁵⁰ See for instance, Deloitte Touche Tohmatsu. 2000 May. Indonesian Accounting Standards (PSAKs): 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.

196. PSAKs are principle-based rather than the U.S. rule-based alternative.¹⁵¹ Moreover, some PSAKs are more advanced than either IAS or U.S. GAAP. For instance, PSAK 53 *Accounting for Stock-based Compensation* is compulsory, whereas its U.S. counterpart (SFAS 123) is optional (due to lobbying pressure). IASB is only now addressing this contentious issue.

197. In many countries, small and medium scale-enterprises (SMEs) are required to comply with IAS-based accounting standards. In Indonesia's case, all limited liability (PT) companies must prepare their financial statements in accordance with IAS-based PSAKs.¹⁵² Some exemptions are given, for instance only publicly-listed companies must apply PSAK 56 *Earnings per Share*.

198. However, like U.S. GAAP, IAS is intended for financial reporting by publicly listed companies. Some IAS accounting and disclosure requirements may be inappropriate for SMEs—which may lack the capacity to correctly apply the provisions of certain standards—hence compliance costs may outweigh benefits. Although international initiatives are underway to address this issue, this is likely to take some years to resolve.¹⁵³ In the meantime, a number of countries including Canada, Fiji Islands, New Zealand, United Kingdom and the U.S. have formalized full or partial exemptions from accounting standards for certain entities, usually smaller or closely-held entities (*differential reporting*).¹⁵⁴

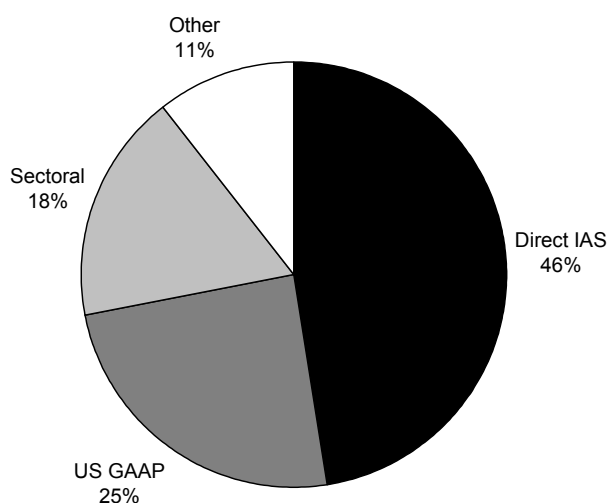
¹⁵¹ In the principle-based system, standards provide general principles. In contrast, rules-based standards attempt to cover every business situation. Rules substitute for professional judgment – a criticism of the rules-based approach is that legal form is emphasized over economic substance (see p. 119 for further discussion).

¹⁵² *Law on Limited Liability Companies (No.1) 1995* (PT Law).

¹⁵³ For a detailed discussion, see, Narayan, Francis B., S. Lakshman Athukorala, Barry Reid and Ma. Rosa Ortega. 2002. *Accounting and Auditing Practices in Selected Developing Member Countries: A Study of Azerbaijan, Fiji Islands, Marshall Islands, Philippines and Sri Lanka*. ADB: Manila.

¹⁵⁴ Refer FASB Statement No. 126 *Exemption from Certain Required Disclosures about Financial Instruments for Certain Nonpublic Entities*; United Kingdom Accounting Standards Board *Financial Reporting Standard for Smaller Entities (FRSSE)*; Institute of Chartered Accountants of New Zealand *Framework for Differential Reporting*; and Canadian Accounting Standards Board Exposure Draft (July 2001), *Differential Reporting*.

Figure 9. PSAK Analysis



An analysis of the 57 PSAKs reveals that: 27 have direct IAS parents. For instance, PSAK 2 *Cash Flow Statements* is IAS 7. 14 come directly from U.S. GAAP. For instance, PSAK 3 *Interim Financial Statements* is APB Opinion No. 28 (1973). 10 give specific sectoral guidance. For instance, PSAK 29 *Accounting for the Oil and Gas Industry* provides sectoral financial reporting rules—it is based on U.S. SFAS 19, 25 and 69, together with Indonesian Oil and Gas Regulations. 6 have been developed for other purposes. For instance, PSAK 47 *Accounting for Land* reflects Indonesian Land Regulations. All PSAKs were developed to be consistent with the IAS Framework.

Source: Information provided by an analysis of extant Indonesian PSAKs at 31 June 2002.

5. Conformity with International Accounting Standards (IAS)

Introduction

199. In the past decade, significant government, World Bank and ADB resources have been committed to ensuring that PSAKs are IAS-compliant. Millions of dollars have been spent. To this end, all PSAKs are developed with reference to the IAS Framework. Nevertheless a recent study contends that “[Indonesian] accounting standards are not yet up to international norms and are enforced weakly.”¹⁵⁵

200. Chapter II reviews weak disclosure enforcement mechanisms and proposes corrective improvements. However, the contention that PSAKs do not meet international norms is overstated. The following subsections describe the development of PSAKs and examine differences between IASs and PSAKs.

¹⁵⁵ Department of Foreign Affairs and Trade (DFAT). 2002. *Changing Corporate Asia, What Business Needs to Know: Volume I. Main Report*. Economic Analytical Unit (EAU), DFAT, Australia. pp. xxxi-xxxii.

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201. In 1994, IAI decided to move away from U.S. GAAP and adopt IAS. Several factors drove this decision. First, U.S. GAAP is fragmented and complex. It comprises several accounting research bulletins, 31 APB opinions, over 140 FASB statements, and scores of interpretations and technical bulletins, statements of position, and accounting guides issued by AICPA, as well as other relevant professional literature. Among other things, translating and keeping abreast of this material is challenging. Second, U.S. GAAP is inextricably intertwined with U.S. laws and legal precedents—factors not easily transferred to another country. Third, U.S. GAAP is rules-based rather than principle-based (see page 102). Fourth, IAS has been developed in a consistent manner and is less complex to apply (see Box 7). In July 2002, 34 IASs were supplemented by 31 SIC (Standing Interpretations Committee) Interpretations (see Appendix 8 and Appendix 9).

Box 7. Detailed Standards¹⁵⁶

The International Accounting Standards Committee (IASC) has stated that it has no intention of trying to duplicate [U.S. GAAP], and indeed, subscribes to a philosophy of providing general guidance rather than detailed standards addressing every nuance of business practice. There are many who believe that the troubles experienced by accountants in recent years, particularly the explosion of litigation against them, can be traced to the attempt (doomed to fail, some would argue) to establish specific guidance for a vast array of transactions and events.

202. In 2002, more than half of the OECD member countries have either directly adopted, or are in the process of directly adopting, IAS. The G8, IOSCO and the BIS now endorse it. With a few exceptions, most countries are in the process of making their accounting standards IAS-compliant.

203. Things were very different in the early 1990s—IAS coverage was narrow and few countries accepted its usage—some considered IAS an endangered species. It was in this environment that PSAKs were initially developed.

204. Government's 1994-2000 accountancy development strategy emphasized using IAS as the primary reference for Indonesian

¹⁵⁶ Epstein, Barry J. and Abbas Ali Mirza. 2001. *IAS 2001: Interpretation and Application*. John Wiley & Sons: New York.

accounting standards.¹⁵⁷ TA from the *Accountancy Development Project II* was designed to: (i) formulate 40 accounting and 16 auditing standards; (ii) process them through draft exposure, public hearing, adoption by the IAI's professional committees and final production; (iii) support MOF's efforts to train key personnel to eventually lead the IAI; and (iv) develop and begin executing a CPE program for IAI members.¹⁵⁸

205. Accordingly, the IAS Framework provided the PSAK foundation. First, existing IASs were translated and directly adopted (e.g., IAS 24 *Related Party Disclosures*, 1984). IASs that were irrelevant to Indonesian conditions were not adopted (e.g., IAS 29 *Financial Reporting in Hyper-inflationary Economies*, 1989). Second, IAS was compared with U.S. GAAP and, where significant gaps were identified, U.S. standards were directly adopted. For instance, there was no IAS on intangible assets—this gap was plugged by APB Opinion No. 17 (1970) *Intangible Assets* (In 2002, DSAK replaced the U.S. standard with IAS 38 *Intangible Assets*, 1997). Third, Uniform Accounting Plans influenced standards development; PSAKs were developed for specific sectors.¹⁵⁹ In some cases, these PSAKs were based on U.S. GAAP. In all cases, they were developed in line with the IAS Framework (e.g., PSAK 37 *Accounting for Toll Roads*, 1997). Fourth, standards were developed to reflect the accounting requirements of Indonesian legislation (e.g., PSAK 40 *Accounting for Changes in the Equity of Subsidiaries or Associates*, 1997, reflects Indonesian Corporation Regulations).

206. In summary, PSAKs are an amalgam of three accounting systems: IAS, U.S. GAAP and Uniform Accounting Plans. They represent an attempt to combine the best aspects of each system, within an overarching IAS Framework.

IAS-PSAK Differences

207. In addition to the earlier-mentioned report (see page 103), three recent studies have examined IAS-PSAK differences (see Table 24). Most differences are due to PSAKs being out-of-step with IAS issuances. Some are due to regulatory conflicts, for instance, tax regulations drive occasional revaluations. This study identifies necessary changes to fully realign IAS-based PSAKs with their IAS counterparts (see Appendix 12).

¹⁵⁷ World Bank. 1994 July 29. *Indonesia Second Accountancy Development Project*. Staff Appraisal Report No. 12883-IND. World Bank: Washington D.C. p. 3.

¹⁵⁸ *Ibid.* p. 8.

¹⁵⁹ Table 14 describes Uniform Accounting Plans (see page 55).

208. Despite these differences, it would be difficult to conclude that Indonesian accounting standards are not yet up to international norms. Indeed Indonesian accounting standards compare well with those of most other countries in the region.

Table 24. Comparative Studies of IAS and PSAKs

<p>Deloitte Touche Tohmatsu (May 2000)¹⁶⁰</p>	<p>This ADB-commissioned study identified four sources of IAS-PSAK difference: (i) local standards cover certain topics that IAS does not; (ii) some IASs are irrelevant to Indonesia, for instance IAS 29; (iii) IASs have been revised but their PSAK comparators have not; and (iv) Indonesian regulations may restrict IAS usage in some areas (e.g., leasing). The report recommended changes to eight PSAKs. In response:</p> <ul style="list-style-type: none"> ▪ Some of the standards have been revised (PSAK 19 <i>Intangible Assets</i> and PSAK 31 <i>Accounting for Banking</i>) ▪ Others are currently being revised (PSAK 16 <i>Fixed Assets and Other Assets</i> and PSAK 30 <i>Accounting for Leases</i>); and ▪ Some recommendations have not been implemented (PSAK 7 <i>Related Party Disclosures</i>, PSAK 8 <i>Contingencies and Events Occurring after the Balance Sheet Date</i>, PSAK 10 <i>Transactions in Foreign Currencies</i> and PSAK 13 <i>Accounting for Investments</i>).
<p>Nobes (October 2001)¹⁶¹</p>	<p>This study identifies differences between country accounting standards and IAS. Twenty IAS-PSAK differences are identified. Of these differences:</p> <ul style="list-style-type: none"> ▪ Three have already been addressed through PSAK revisions ▪ Two are due to practical Indonesian problems (e.g., there are no specific rules regarding the fair values of financial assets and liabilities, as these rules would be difficult to apply given Indonesian interest rate fluctuations) ▪ Two are due to regulation-standard conflicts (revaluations and leases) ▪ Two are minor (inventory valuation) ▪ Nine are caused by timing delays in PSAK issuances, and ▪ Two are due to differences between ISAKs and SICs.

¹⁶⁰ Deloitte Touche Tohmatsu. 2000 May. *Indonesian Accounting Standards (PSAKs): 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.

PricewaterhouseCoopers (August 2001) ¹⁶²	This comprehensive study compares Indonesian GAAP with IAS, U.S. GAAP and UK GAAP. It identifies a number of differences, most notably: (i) regulation-driven revaluations; (ii) lease classification approaches; and (iii) employee benefit treatments. ¹⁶³
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The Danger of Being Different: PSAK Structure Problems

209. When the PSAK structure was designed, few countries had adopted IAS. The situation is very different today. First, IAS has become a true international standard. Second, investors strongly support international harmonization.¹⁶⁴ However, although PSAKs provide a robust set of accounting standards, they are not directly comparable to IAS. This potentially causes misunderstandings, thereby reducing investor confidence.

210. Moreover, the PSAK structure, comprising IAS, U.S. GAAP and sector-specific standards, is maintenance intensive. Consequently, there will be a tendency for PSAKs to remain out-of-step with IAS. Finally, even countries with strong accounting academia, well-resourced standard-setting bodies and an active constituency of financial statement users have opted for direct IAS adoption—the complex structural design of PSAKs may not be suited to Indonesian conditions.

¹⁶¹ Nobes, Christopher W. (Ed.). 2001 October. *GAAP 2001: A Survey of National Accounting Rules Benchmarked against International Accounting Standards*: Jointly published by Andersen, BDO, Deloitte Touche Tohmatsu, Ernst & Young, Grant Thornton, KPMG, PricewaterhouseCoopers.

¹⁶² PricewaterhouseCoopers. 2001 August. *Indonesian GAAP: Similarities and Differences Among IAS, Indonesian GAAP, US GAAP and UK GAAP*. Assurance & Business Advisory Services.

¹⁶³ IAS 17 classifies a lease as a finance lease if it meets the following criteria: (i) ownership is transferred at the end of the lease; (ii) the lease contains a bargain purchase option; (iii) the lease is for a major part of the asset's useful life; and (iv) the present value of the minimum lease payments is greater than or substantially equal to the asset's fair value. Conversely, PSAK 30 lists the following as preconditions for a lease to be classified as a finance lease: (i) the lease has a purchase option at a price that has been agreed by the lessor and lessee prior to the lease commencement; (ii) the present value of minimum lease payments is greater than or equal to fair value of the asset; and (iii) the lease term is for a minimum of two years. (Source: Foo, See Liang. 1997. "Indonesia" in *Financial Reporting in the Pacific Asia Region*, edited by Ronald Ma. Singapore: World Scientific Publishing. p. 355).

¹⁶⁴ McKinsey & Company. 2002 July. *Global Investor Opinion Survey: Key Findings*.

6. Legal Status of PSAKs

211. DSAK has no legal status as a standard-setting body. However, *Bapepam* requires listed companies to comply with PSAKs and the *Law on Limited Companies (No. 1) 1995* requires limited companies to prepare their financial statements in accordance with PSAKs. The Directorate General of Taxation (DGoT) and BI also require that companies under their jurisdiction use PSAKs.

7. Taxation Reporting Requirements

212. The DGoT administers Indonesian income tax laws, excepting those that apply to the oil and gas industry. Tax regulations require Indonesian businesses to maintain and preserve detailed accounting records for at least ten years.

213. IAI has made ongoing efforts to ensure that the DGoT is involved in the development of PSAKs. Moreover, government supported these efforts with the release of a 1979 taxation policy that gave tax incentives to companies that submitted audited financial reports.¹⁶⁵

214. Indonesian tax regulations limit accounting policy choices (for taxation purposes)—they specify doubtful debts treatments, depreciation rates and leasing approaches. Nevertheless, few additional accounting requirements are imposed by taxation requirements.¹⁶⁶

8. Public Sector Accounting Standards

215. The MOF State Financial Accounting Agency (*Badan Akuntansi Keuangan Negara, BAKUN*) is responsible for government accounting arrangements. Indonesia has not yet established a set of public sector accounting standards. Public sector report preparation is largely based on the *Indische Comptabiliteitswet 1925* (a treasury law enacted by the Dutch colonial authorities) and PSAKs, some of which may not be suitable for public sector reporting.

216. Work is currently underway to implement the IMF system of Government Finance Statistics (GFS) in central government. GFS mandates accounting bases and budgeting and reporting classifications. In an effort to provide legislative support for public sector financial

¹⁶⁵ Bachtiar, Emil. 2001 August. The Professionalization of Accounting in Indonesia. Paper presented to the Second International Accounting History Conference, Osaka, August 2001.

¹⁶⁶ Tearney, Michael G. 2001. An Evaluation of Disclosure of Financial Information by Public Companies in Indonesia. Unpublished Paper. Von Allmen School of Accountancy, Gatton College of Business and Economics, University of Kentucky.

management reforms, the Government submitted three bills to parliament in September 2000 (covering state finances, state treasury, and state audit). The draft state treasury law effectively assigns accounting-standard setting authority to the Minister of Finance (Article 2(2)).

217. Furthermore, in April 2001, the MOF established the Financial Management Reform Committee (KPMK) to guide the financial management reform process and to coordinate with Parliament on the three bills being considered. Part of this work will involve the development of public sector accounting standards—BAKUN has indicated an intention to move government organizations to a modified accrual basis of accounting in 2003. ADB is supporting the process of accounting standard development and implementation.¹⁶⁷ IAI plans to establish a Board to develop public sector accounting standards.

Part Two. Auditing Standards

9. Introduction

218. Indonesian generally accepted auditing standards (*Standar Profesi Akuntan Publik, SPAPs*) form part of the *Professional Standards for Public Accountants*.¹⁶⁸ The Professional Standards comprise auditing standards, attestation standards, accounting and review standards, consulting services standards, quality control standards and the code of professional conduct.

219. Since 1994, IAI has been committed to raising professional standards to international levels. Most are based upon the U.S. AICPA-issued Statements on Auditing Standards (SASs). The decision to adopt SASs was based upon considerations of the quality of the SASs and their coverage of most areas of professional practice. However, IAI refers to International Standards on Auditing (ISAs) in areas where SASs have not been issued. Together with the revised accounting standards, SPAPs were issued on 1 August 1994.

¹⁶⁷ ADB TA 3764-INO: *Supporting Country Financial Accountability*, for \$300,000, approved on 12 November 2001.

¹⁶⁸ Indonesian Institute of Accountants (IAI). 2001. *Professional Standards for Public Accountants*. IAI: Jakarta.

220. In 2000, IAI prepared a report on Indonesian Corporate Governance.¹⁶⁹ Although concluding that the Indonesian accounting profession was satisfied with its professional standards, the report identified three SPAP-related challenges. First, in spite of mandatory CPE, there were indications that practitioners had not kept abreast with new pronouncements. The report suggested that IAI could improve CPE programs and develop more learning tools. Second, the report found that academic curricula sometimes did not reflect SPAP developments. Moreover, since U.S. auditing texts are used heavily, some lecturers and students are more familiar with U.S. auditing standards. Third, the report concluded that practitioners sometimes face difficulties implementing certain standards.

10. Auditing Standard Setting

221. Table 25 traces the evolution of Indonesian audit standard-setting bodies. The Public Accountants Professional Standards Board (*Dewan Standar Profesional Akuntan Publik, DSPAP*) promulgates SPAPs. It comprises seven auditing practitioners and is part of the Public Accountants' Compartment (IAI-KAP).¹⁷⁰

Table 25. Evolution of Audit Standard Setting Bodies

1973–1994	Accountant Examination Norm Committee (<i>Komite Norma Pemeriksman Akuntan, KNPA</i>).
1994–1999	Public Accountants Professional Standards Committee (<i>Komite Standar Profesional Akuntan Publik, KSPAP</i>).
1999 to date	Public Accountants Professional Standards Board (DSPAP).
1999 to date	Public Accountants Professional Standards Advisory Council (DKSPAP).

222. The Public Accountants Professional Standards Advisory Council (*Dewan Konsultatif Standar Profesional Akuntan Publik, DKSPAP*) was established to advise DSPAP on issues to be addressed by professional standards and to raise funds to support standard-setting activities.

223. In accordance with IAI-KAP rules,¹⁷¹ DSPAP follows a formalized 'due process' procedure to identify, develop and revise SPAPs. First,

¹⁶⁹ 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.

¹⁷⁰ *Ibid.* p. 20.

¹⁷¹ IAI-KAP Rule No. 01/TK/IAI-KAP/XI/2001 *DSPAP Due Process for SPAP Standard Setting* (21 November 2001).

DKSPAP and DSPAP identify topics that might require professional standards. A risk analysis is undertaken of these topics. A Task Force, comprising DSPAP members and other competent people, is established to analyze chosen topics, identify potential issues and develop an ED. Once DSPAP is satisfied with the ED, it is mailed to regulatory bodies (e.g., BI, *Bapepam* and DJLK), state audit agencies (BPK and BPKP), academics, practitioners and other interested parties. The ED is also published in *Media Akuntansi*, announced in the media and posted on the IAI website. A minimum period of 60 days is allowed for written comments. Having analyzed these comments, DSPAP organizes public hearings. Following DSPAP's review and consideration of received comments, the ED is approved and promulgated as an SPAP.

224. The 2001 *Academic Paper*¹⁷² envisages an independent professional standard-setting board. This proposal aligns with international trends, for instance, the recent establishment of the International Auditing and Assurance Standards Board (IAASB) in place of the IFAC International Auditing Practices Committee (IAPC).

11. Indonesian Auditing Standards (SPAPs)

225. Appendix 10 lists the SPAPs that were effective at 30 June 2002—SPAPs were last revised and reissued in 2001. IAI publishes SPAPs in *Professional Standards for Public Accountants*.¹⁷³

226. SPAPs comprise a mixture of U.S. generally accepted auditing standards (GAAS) and International Standards on Auditing (ISAs).

12. Comparison with International Standards on Auditing (ISAs)

227. In 2002, the IAASB replaced the IAPC. IAASB is an independent standard-setting body under IFAC auspices. Its key pronouncements are ISAs and International Auditing Practice Statements (IAPs)(see Appendix 11). ISAs and IAPs are designed for adoption as national auditing standards.

228. Although no in-depth comparison has been made between Indonesian SPAPs and either AICPA or IAASB pronouncements, it seems reasonable to assume that SPAPs are broadly comparable to these

¹⁷² Ministry of Finance (MOF). 2001. *Academic Draft: Draft of Public Accountant Law*. MOF: Jakarta.

¹⁷³ Indonesian Institute of Accountants (IAI). 2001. *Professional Standards for Public Accountants*. IAI: Jakarta.

pronouncements, given their parentage (IAASB pronouncements were initially based upon U.S. GAAS). Certainly, no evidence suggested otherwise.

“The quality of international auditing standards is very close to U.S. GAAS ... but gaps do exist (e.g., in the addressing of claims arising out of litigation. U.S. GAAS has a whole statement on the topic, whereas international standards have just a paragraph or two). ... In some areas, such as illegal acts, international standards are more rigorous than GAAS.”¹⁷⁴

13. Public Sector Auditing Standards

229. The Supreme Audit Board (*Badan Pemeriksa Keuangan, BPK*) promulgates government auditing standards and requires their usage by external and internal government auditors. These auditing standards were last updated and distributed in 1995, based upon the Government Auditing Standards (1994) of the U.S. Government Accounting Office (GAO).

230. A draft law on state audit has been submitted to parliament (see page 108). Although Article 3(5) of the draft law requires that audits be performed based on generally accepted auditing standards, these are not defined. However, government has requested that ADB consider providing technical assistance to facilitate improvements in state auditing, including procedures, standards and their legal basis.

14. Issue Synopsis: Accounting and Auditing Standards

231. This part of the study concludes that—although Indonesian private sector¹⁷⁵ accounting and auditing standards generally meet international benchmarks—accounting standards could be improved to: (i) raise the overall credibility of Indonesian financial disclosure; (ii) reduce business compliance costs, particularly for SMEs; (iii) reduce standard-setting resource requirements; and (iv) improve access to guidance and training materials.

232. However, these potential efforts should be considered in light of more important priorities; such as improving compliance with these accounting and auditing standards by strengthening auditing practices and professional arrangements.

¹⁷⁴ Craig, James L. Jr., Douglas R. Carmichael and Dan M. Guy. 2000 June. Are International Auditing Standards Ready to Replace U.S. GAAS? *The CPA Journal*.

¹⁷⁵ Authors' Note: In contrast to other country DSAs, this study is limited to the private sector. Public sector arrangements and challenges are described for completeness.

233. The proposed restructuring of accounting and auditing standard-setting bodies (the new PA Law) is in line with international trends, would improve independence and would give stronger legal support to accounting and auditing standards. Nevertheless, Chapter VIII—*Issues and Recommendations*—identifies and describes constraints and proposes corrective actions. These include the following issues regarding accounting and auditing standards:

- The PSAK structure reflects a variety of influences under an IAS umbrella. But, this structure potentially undermines investor confidence and may not suit Indonesian conditions. Moreover, it reduces access to high-quality training and guidance materials.
- The financial statements of most SMEs must comply with PSAKs, as Indonesia does not have a differential reporting regime. This imposes unnecessary compliance costs and potentially undermines the quality of SME financial statements.
- As with PSAKs, SPAPs comprise a mixture of U.S. and international pronouncements. Although there are potential ways to strengthen SPAPs, such as by directly adopting IAASB pronouncements, any such changes should be low priority.
- A recent IAI report identified concerns regarding practitioner and academic familiarity with SPAPs (see page 109). It suggests that practitioners and academics be educated on SPAPs and ongoing developments, through continuing education and other initiatives.