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THE ROLE OF INTERNAL AUDIT EFFECTIVENESS OF RAW MATERIALS INVENTORY INTERNAL CONTROL IN PT.NUSANTARA BETA FARMA PADANG

SKRIPSI



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ABSTRACT

The aim of this research is to evaluate the role of internal audit in the effectiveness of raw materials inventory internal control in PT. Nusantara Beta Farma, Padang. This study is descriptive research in form of case study and research source is the result of interview. The output of this research is the information related with the role of internal audit and effectiveness of raw materials inventory internal control. This research shows result that is in PT. Nusantara Beta Farma, internal audit is said to be good in view of the initial procedure by having a close look at the schedule and the audit programs developed previously that include financial auditing and operational auditing. The role of internal audit in the effectiveness of raw material inventory internal control is still poor. It is because the effectiveness is only assessed pursuant to estimates or forecasts and not accompanied by the measuring to assess the effectiveness of internal control of raw material inventory. Raw material inventory internal control in PT. Nusantara Beta Farma has yet to run properly.

Keyword: Internal Audit, Effectiveness of Raw Materials Inventory Internal Control.



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CHAPTER I

INTRODUCTION

1.1 Background

An increasingly dynamic competition in the industry will lead the company to make the right decision to allow survival and growth of business enterprises. In making decisions in the operation of an industry should be targeted to improve its product quality and competitive advantage both in the domestic market and foreign markets. To improve the quality of production in accordance with specific quality standards it is necessary to continuously control efforts, so that product damage can be reduced as low as possible that ultimately wasteful costs can be reduced.

Internal audit is an activity involved in an organization that provides the best input to achieve organizational goals. Internal audit includes the utilization of a systematic methodology for analyzing business processes or organizational problems and provide an alternative solutions to these problems. Internal audit activities includes ensuring the operational run effectively and efficiently, prevent and investigate fraud, security of assets, and compliance with laws, regulations, policies, and procedures applicable in the organization.

Internal control in a company can significantly improve the way of company operation. When a company implements an effective internal control in

operational run effectively and efficiently, internal control is needed to control the process in using raw material and the process when the raw material come to inventory. Management is responsible establishing and managing those controls, and internal auditors both assess their effectiveness and make recommendations as appropriate.

PT Nusantara Beta Farma which is a company engaged in the pharmaceutical industry also had difficulty in decision making caused by the problems faced by its company. Many problems currently being experienced by PT. Nusantara Beta Farma. The most prominent is the delay of raw material available (the effectiveness of supply of raw materials), so it causes the process of production be hung up that give impact to consumer who feels aggrieved due to unavailability of goods (drugs) on time. A result from these problem, PT. Nusantara Beta Farma feels very aggrieved because this problem constantly happened. Then, PT Nusantara Beta Farma adopted a policy to conduct a control that called internal controls.

In order to achieve the purpose, the company needs to increase the effectiveness current production process. Internal control is one of the most important and fundamental concepts that business professionals at all levels and both external and internal auditors must understand. According to Muller (2009), internal controls are processes, implemented by management, that are designed to provide reasonable assurance for:

- Reliable financial and operational information
- Compliance with policies and procedures plans, laws, rules, and regulations

- Safeguarding of assets
- Operational efficiency
- Achievement of an established mission, objectives and goals for enterprise operations and programs
- Integrity and ethical values

Based on the above descriptions, the writer interested in conducting research in the preparation of thesis with the title: “The Role of Internal Audit in Effective Internal Control of Raw Materials Inventory in PT. Nusantara Beta Farma, Padang”

1.2 Problem Identification

Based on the background states above, the problem the writer would like to discuss in this research is: How is the role of internal audit in the effectiveness of raw materials inventory internal control at PT. Nusantara Beta Farma, Padang?

1.3 Objectives and Benefit of the Research:

The purposes that the writer wants to reach by doing this research are:

1. To understand the implementation of internal audit of supply of raw material that is applied in PT. Nusantara Beta Farma, Padang.
2. To understand the degree of the effectiveness of control of raw materials in PT. Nusantara Beta Farma, Padang.

3. To understand the role of internal audit in the effectiveness of raw materials inventory internal control in PT. Nusantara Beta Farma, Padang.

This research hopefully will give some contributions and benefits to the following parties:

1. Researcher expects to enrich current knowledge on accounting issues of (student, lecturer, and others) especially the role of internal audit toward the effectiveness of raw materials inventory internal control that good and efficient.
2. The company may take the results of this study as input material, information, and use the data for the development of the company.
3. The reader can get the ideas and information in internal audit topic.

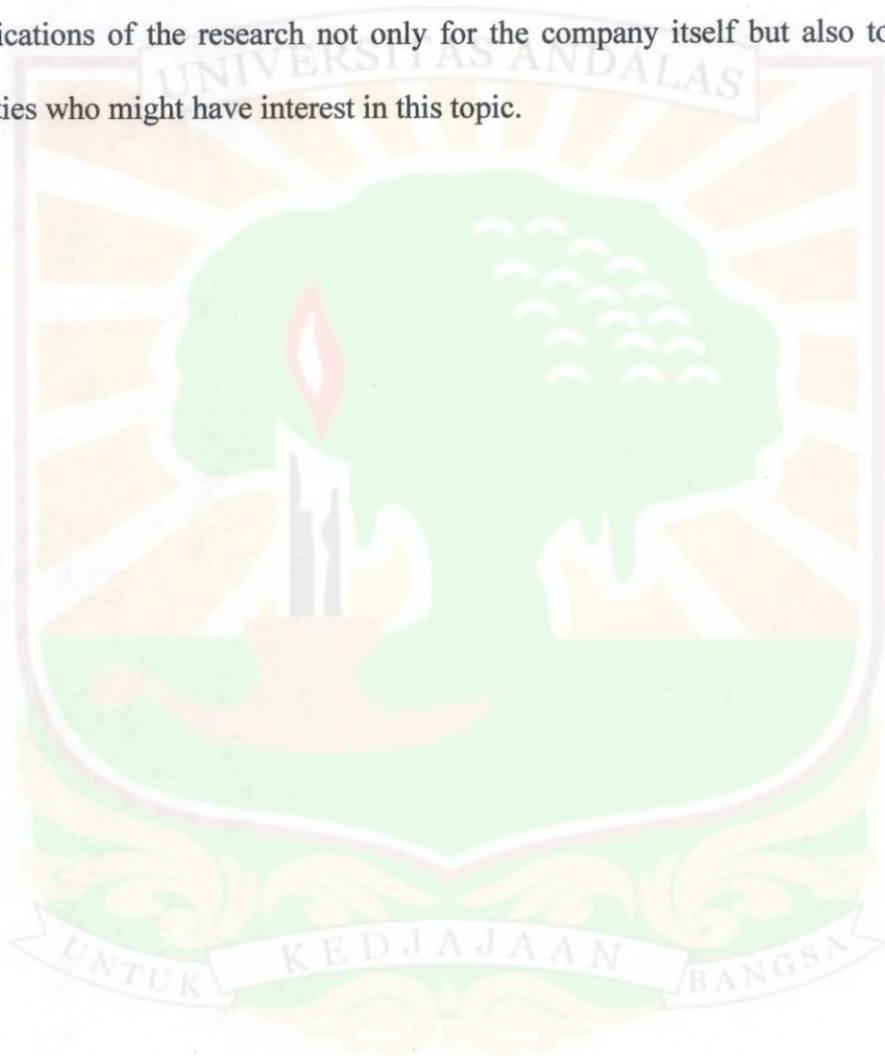
1.4 Writing Systematic

This research is divided into five chapters. Chapter one explains the overview of the background of the introduction, problem identification, purpose and benefit of the research and writing systematic. Chapter two includes the literature surveys of any related theories and opinions of the experts gathered from different sources, such as text books, the result from previous research, journals, and internet based content and information.

Chapter three discusses the research methodology used in preparation of these types of research, types and sources of data, any information needed for the thesis. Chapter four is divided into two parts, first part is about the

company profile of case study in this research. The second part is the analysis the role of internal audit in the effectiveness of raw materials inventory internal control in PT. Nusantara Beta Farma.

Chapter five consists the research conclusions from previous chapters. This chapter will also explain the research limitations as well as suggestions and implications of the research not only for the company itself but also to other parties who might have interest in this topic.



CHAPTER II

THEORETICAL FRAMEWORK

In this chapter, author will explain about theoretical framework and review of previous research. In part, it will show references that related to the problem that will be studied in this research. It will become a base for this research. For previous research, the author will review related problem conducted by previous research. The review concerns about research object, research mechanisms, and the barrier of the research.

2.1 Internal Audit

Internal auditing appeared first in the business world after an audit of public accountants. The main factor is the need for expansion of internal audit controls facing the range of the company that employs thousands of employees and manage the activities in various places scattered. Various deviations and irregularities in the conduct of the company's books is a real problem that must be faced.

To detect and prevent various problems existing in the company's internal audit required conduct surveillance in a way to test and evaluate the activities of the company.

2.1.1 Definition of internal audit

In general, internal auditing is an appraisal function in an organization to examine and evaluate organization activity. Its appraisal follow all activities in an

organization include appraisal in organization structures, planning, policy, employees reward, and adherence to procedures.

"Internal audit is an auditing conducted by an organization's internal audit division on both the financial statements and accounting records of the organization as well as adherence to top management's specified policies and compliance with government regulations and the applicable provisions of the Professional Association." (Agoes, 2004)

"Internal Audit is capable of making observations and affecting the implementation of the program and budget plan." (Mulyadi 2001)

According to Tugiman (2006) explain the internal auditing; *"Internal auditing is an independence appraisal function in an organization to examine and evaluate organization activities."*

Then refer to Moeller (2009), *"internal auditing is an independence appraisal function established in an organization to examine and evaluate organization activities as a service for organization."*

According to IIA (2008) stated that definition of internal auditing is;

"Internal auditing is independence, objective assurances, and consulting activity designed to add value and improve organization operations. Its help an organization accomplish its objective by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance process".

According to all definition above, it can be explained that internal auditing characteristic include (Moeller, 2009) the followings:

1. Internal auditing is an independence appraisal activity in an organization. It means the person who appraised the employees in an organization.
2. In measurement conducted by internal auditor, independence and objectivity should be maintained.
3. In a measurement, internal auditors are responsible to management.
4. Internal auditors examine and evaluate financial and non financial activities.
5. Internal auditors determine whether policies and procedures is running well to achieve the goal.
6. Internal auditor is an activity to give assurance, confidence, and consultation.
7. Internal auditors give a systematic approach to evaluate and improve management risk, control and governance process.

Internal auditor will achieve their professionals when professional's standard of internal auditor is fulfilled. The purpose of the *Standards for the Professional Practice of Internal Auditing* (the Standards) is to provide auditors with specific professional guidance related to the responsibilities of internal auditor. After that the internal auditor will work well in order to finish their work.

According to IIA (2008) states the standards for the professional practice of internal auditing as follows:

Attribute Standard

1. Purpose, authority and responsibility
2. Independence and objectivity
3. Proficiency and due professional care
4. Quality assurance and improvement program

Performance Standard

5. Managing the internal audit activity
6. Nature of work
7. Engagement planning
8. Performing the engagement
9. Communicating result
10. Monitoring Progress
11. Resolution of senior management acceptance risk.

The entire standard above needed by internal auditor to bring out their professionalism and their role in the organization in order to achieve the goal.

2.1.2 Independence and objectivity

Independence is really needed by internal audit. Internal auditor needs it to fulfil their responsibility as an auditor. Independence in internal auditor is also used by for the member of auditor in public service. It is because the internal auditor should use their professionalism or unbiased attitude to fulfil their responsibility.

According to Elder, Beasley, & Arens (2008) stated that;

“Independence of auditor is divided in two types. There are independence in fact and independence in appearances. Independence in fact exists when the auditor is actually able to maintain an unbiased attitude throughout the audit, whereas independence in appearance is the result of others interpretations of this independence.”

Based on the previous analysis, independence of auditor is necessary for auditor to fulfil their responsibility and apply their professional ethic. Then independence is applied in a condition when an entity need to get fair decision is appear.

2.1.3 The Role and Responsibility Internal Audit

Internal auditor has the role and responsibility to provide information about the effectiveness of internal control and quality of organizations. It performance will help the organization to achieve their objectives.

According to the IIA (2008) stated that:

“Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps

an organization to accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes."

IIA also stated the major roles and responsibilities of internal audit function, that are summarized as below:

1. evaluates and provides reasonable assurance that risk management, control, and governance systems are functioning as intended and will enable the organization's objectives and goals to be met
2. reports risk management issues and internal controls deficiencies identified directly to the audit committee and provides recommendations for improving the organization's operations, in terms of both efficient and effective performance
3. evaluates information security and associated risk exposures
4. evaluates regulatory compliance program with consultation from legal counsel
5. evaluates the organization's readiness in case of business interruption
6. maintains open communication with management and the audit committee
7. teams with other internal and external resources as appropriate
8. engages in continuous education and staff development
9. Provides support to the company's anti-fraud programs.

Based on the explanation from IIA above about the role and responsibility of internal auditor, it can be concluded that the role and responsibility of internal auditor gives a good impact to the company in order to accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the

effectiveness of risk management, control, and governance processes and then improve an organization's operations. It will support the company in fraud prevention by good internal control and other related as well.

2.1.4 Proficiency and Due Professional Care

Internal auditors in carrying out their work should perform the best skill and performance. Internal auditor not only performs their audit skill but also other skill and knowledge to carry out their responsibility given. Internal auditor should apply the care and expected skill in performing their work. Internal auditors need to continue and improve their skill, performance, and knowledge to face new world.

Proficiency and due professional care described also in IIA professional standard of internal auditor revised 2008, as follows:

Proficiency

Internal auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities.

Interpretation:

Knowledge, skills, and other competencies is a collective term that refers to the professional proficiency required of internal auditors to effectively carry out their professional responsibilities. Internal auditors are encouraged to demonstrate their proficiency by obtaining appropriate professional certifications and qualifications, such as the Certified Internal Auditor designation and other designations offered

by The Institute of Internal Auditors and other appropriate professional organizations.

1. The chief audit executive must obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

2. Internal auditors must have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization, but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.

3. Internal auditors must have sufficient knowledge of information technology risks and controls and available technology-based audit techniques to perform their assigned work. However, not all internal auditors are expected to have the expertise of an internal auditor whose primary responsibility is information technology auditing.

4. The chief audit executive must decline the consulting engagement or obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

Due Professional Care

Internal auditors must apply the care and skill expected of a reasonably prudent and competent internal auditor. Due professional care does not imply infallibility.

1. Internal auditors must exercise due professional care by considering the:

Extent of work needed to achieve the engagement's objectives;

a. Relative complexity, materiality, or significance of matters to which

assurance procedures are applied;

- b. Adequacy and effectiveness of governance, risk management, and control processes;
- c. Probability of significant errors, fraud, or non-compliance; and Cost of assurance in relation to potential benefits.

2. In exercising due professional care internal auditors must consider the use of Technology-based audit and other data analysis techniques.

3. Internal auditors must be alert to the significant risks that might affect objectives, operations, or resources. However, assurance procedures alone, even when performed with due professional care, do not guarantee that all significant risks will be identified.

4. Internal auditors must exercise due professional care during a consulting engagement by considering the:

1. Needs and expectations of clients, including the nature, timing, and communication of engagement results;
2. Relative complexity and extent of work needed to achieve the engagement's objectives;
3. Cost of the consulting engagement in relation to potential benefits.

Continuing Professional Development

Internal auditors must enhance their knowledge, skills, and other competencies through continuing professional development.

Based on explanation above, IIA completely explain about proficiency and due professional care. IIA stated that knowledge, skills, and other competencies is a collective term that refers to the professional proficiency required of internal

auditors to effectively carry out their professional responsibilities. Internal auditors are encouraged to demonstrate their proficiency by obtaining appropriate professional certifications and qualifications. It means internal auditor should perform well to carry out their professional responsibilities.

2.1.5 Quality Assurance and Improvement programs.

Internal auditor has many activities include in conducting internal auditing. In those activities, internal auditor should be controlled and evaluated their activities in order to make sure that they are working accordance with the code of ethic and standard. The chief audit executive is the one that hold the responsibility. Quality assurance and improvement programs are designed to cover all aspect of internal audit activities. It's appropriate with professional standard of internal auditor, as follows:

“A quality assurance and improvement program is designed to enable an evaluation of the internal audit activity’s conformance with the Definition of Internal Auditing and the Standards and an evaluation of whether internal auditors apply the Code of Ethics. The program also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement.”

In IIA it also states about the requirement of quality assurance and improvement programs, as follows:

1. Internal Assessments

Internal assessments must include:

- Ongoing monitoring of the performance of the internal audit activity; and

- Periodic reviews performed through self-assessment or by other persons within the organization with sufficient knowledge of internal audit practices.

2. External Assessments

External assessments must be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organization. The chief audit executive must discuss with the board:

- a. The need for more frequent external assessments; and
- b. The qualifications and independence of the external reviewer or review team, including any potential conflict of interest.

Based on the requirement above, the quality assurance and improvement programs should include the item as proper evaluation of internal audit activity's conformance with the Definition of Internal Auditing and the Standards and an evaluation of whether internal auditors apply the Code of Ethics and also an assessment of efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement.

2.1.6 Managing of the Internal Audit Activities

Internal auditors should carry out audit activities to obtain the information that supports the activities of the audit. In the internal audit activities, internal auditor should be able to identify, analyze, evaluate, and document the appropriate information to ensure achievement of objectives, ensuring quality, and increased staff capacity (Tugiman, 2006).

The chief audit executive must effectively manage the internal audit

activity to ensure it adds value to the organization. Internal audit activity must effectively manage so that internal audit activity achieve the purpose and conform to standard. In IIA it's stated that internal audit activities are as follows:

1. Planning

The chief audit executive must establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organization's goals.

2. Communication and Approval

The chief audit executive must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The chief audit executive must also communicate the impact of resource limitations.

3. Resource Management

The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.

4. Policies and Procedures

The chief audit executive must establish policies and procedures to guide the internal audit activity.

5. Coordination

The chief audit executive should share information and coordinate activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimize duplication of efforts.

6. Reporting to Senior Management and the Board

The chief audit executive must report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility, and

performance relative to its plan. Reporting must also include significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by senior management and the board.

According to explanation above, can conclude that internal auditor in doing the internal audit activity should be effectively managed and the activities are conducted by chief audit executives. And then the internal audit activity is effectively manage when the results of the internal audit activity's work achieve the purpose and responsibility included in the internal audit charter, the internal audit activity conforms with the definition of internal auditing and the standards and the individuals who are part of the internal audit activity demonstrate conformance with the code of ethics and the standards.

2.1.7 Nature of Work

Internal auditor has some responsibility in organization to help achieving the goal. Internal auditors verify the effectiveness of their organization's internal controls and check for mismanagement, waste, or fraud. They examine and evaluate their firms' financial and information systems, management procedures, and internal controls to ensure that records are accurate and controls are adequate. They also review company operations, evaluating their efficiency, effectiveness, and compliance with corporate policies and government regulations. They may recommend and review controls for their organization's computer systems, to ensure their reliability and integrity of the data (IIA, 2008).

Nature of work of internal control described in IIA revised 2008 professional standard of internal auditor, as follows:

Nature of Work

The internal audit activity must evaluate and contribute to the improvement of governance, risk management, and control processes using a systematic and disciplined approach.

1. Governance

The internal audit activity must assess and make appropriate recommendations for improving the governance process in its attempt to accomplish of the following objectives:

- Promoting appropriate ethics and values within the organization;
- Ensuring effective organizational performance management and accountability;
- Communicating risk and control information to appropriate areas of the organization; and
- Coordinating the activities of and communicating information among the board, external and internal auditors, and management.

2. Risk Management

Determining whether risk management processes are effective based on the judgment resulting from the internal auditor's assessment which:

- Organizational objectives support and align with the organization's mission;
- Significant risks are identified and assessed;
- Appropriate risk responses are selected that align risks with the organization's risk appetite; and
- Relevant risk information is captured and communicated in a timely

manner across the organization, enabling staff, management, and the board to carry out their responsibilities.

3. Control

The internal audit activity must assist the organization in maintaining effective controls by evaluating their effectiveness and efficiency and by promoting continuous improvement.

Referring to IIA explanation, there are three classification of work nature of internal auditor, which is governance, risk management, and control. All of that works should be improved by using a systematic and discipline approach. After that it will help the company in achieving their goal.

2.1.8 Engagement Planning

Based on IIA professional standard revised in 2008 internal auditor must develop and document a plan for each engagement, including the engagement's objectives, scope, timing, and resource allocations. In each of that activity the internal auditors to do the best in order to achieve the goal and nature of work of internal auditing.

In order to understand more, the IIA explain about engagement's objectives, scope, timing and resource allocations, as follows:

Planning Considerations

In planning the engagement, internal auditors must consider:

- a. The objectives of the activity being reviewed and the means by which the activity controls its performance;
- b. The significant risks to the activity, its objectives, resources, and

operations and the means by which the potential impact of risk is kept to an acceptable level;

- c. The adequacy and effectiveness of the activity's risk management and control processes compared to a relevant control framework or model;
- d. The opportunities for making significant improvements to the activity's risk management and control processes.

Engagement Objectives

Objectives must be established for each engagement.

- a. Internal auditors must conduct a preliminary assessment of the risks relevant to the activity under review. Engagement objectives must reflect the results of this assessment.
- b. Internal auditors must consider the probability of significant errors, fraud, noncompliance, and other exposures when developing the engagement objectives.
- c. Adequate criteria are needed to evaluate controls. Internal auditors must ascertain the extent to which management has established adequate criteria to determine whether objectives and goals have been accomplished. If adequate, internal auditors must use such criteria in their evaluation. If inadequate, internal auditors must work with management to develop appropriate evaluation criteria.
- d. Consulting engagement objectives must address governance, risk management, and control processes to the extent agreed upon with the client.

Engagement Scope

- a. The established scope must be sufficient to satisfy the objectives of the engagement.
- b. The scope of the engagement must include consideration of relevant systems, records, personnel, and physical properties, including those under the control of third parties.
- c. If significant consulting opportunities arise during an assurance engagement, a specific written understanding as to the objectives, scope, respective responsibilities, and other expectations should be reached and the results of the consulting engagement communicated in accordance with consulting standards.
- d. In performing consulting engagements, internal auditors must ensure that the scope of the engagement is sufficient to address the agreed-upon objectives. If internal auditors develop reservations about the scope during the engagement, these reservations must be discussed with the client to determine whether to continue with the engagement.

Engagement Resource Allocation

Internal auditors must determine appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources.

Engagement Work Program

Internal auditors must develop and document work programs that achieve the engagement objectives.

- a. Work programs must include the procedures for identifying, analyzing,

evaluating, and documenting information during the engagement. The work program must be approved prior to its implementation, and any adjustments approved promptly.

- b. Work programs for consulting engagements may vary in form and content depending upon the nature of the engagement.

Based on the IIA explanation above, engagement planning is made accurately, internal auditor should consider about consideration of planning and then establish the objective of engagement, after that internal auditor make the scope of the engagement and then Internal auditors must determine appropriate and sufficient resources to achieve engagement objectives, and develop and document work programs that achieve the engagement objectives.

2.1.9 Performing the Engagement

Continue the engagement planning; in the performing stage plan internal auditor perform all that was planned in engagement planning. Internal auditor identifies, evaluates, documents and analyses proper information to achieve the objective in engagement planning. It's appropriate with statements IIA professional standard (2008) that:

“In the performing engagement, internal auditors must identify, analyze, evaluate, and document sufficient information to achieve the engagement’s objectives.”

IIA also described what internal auditor should do in identifying, analyzing, evaluating, and documenting proper information to achieve the

engagement objectives and also supervision engagement, as follows:

Identifying Information

Internal auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement's objectives.

Analysis and Evaluation

Internal auditors must base conclusions and engagement results on appropriate analyses and evaluations.

Documenting Information

Internal auditors must document relevant information to support the conclusions and engagement results

Engagement Supervision

Engagements must be properly supervised to ensure objectives are achieved, quality is assured, and staffs are developed.

Those steps are used by internal auditor in performing the engagement. It can create the ensuring to the internal auditor that the engagement will be achieved and staffs are developed.

2.1.10 Communicating Result

Engagement planning, planning consideration, engagement objective, engagement scope, engagement resource allocation, engagement work program, and then performing engagement are the process of internal auditor in engagement to achieve the engagement objective or the result all of that process. Internal auditor must communicate the engagement result.

According to IIA professional standard (2008) the communicating result of

result engagement and related information about communicating result are as follows:

Criteria for Communicating

- Communications must include the engagement's objectives and scope as well as applicable conclusions, recommendations, and action plans.
- Final communication of engagement results must, where appropriate, contain internal auditors' overall opinion and/or conclusions.
- Internal auditors are encouraged to acknowledge satisfactory performance in engagement communications.
- When releasing engagement results to parties outside the organization, the communication must include limitations on distribution and use of the results.
- Communication of the progress and results of consulting engagements will vary in form and content depending upon the nature of the engagement and the needs of the client.

Quality of Communications

Communications must be accurate, objective, clear, concise, constructive, complete, and timely.

Errors and Omissions

If a final communication contains a significant error or omission, the chief audit executive must communicate corrected information to all parties who received the original communication.

Use of "Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing"

Internal auditors may report that their engagements are “conducted in conformance with the International Standards for the Professional Practice of Internal Auditing”, only if the results of the quality assurance and improvement program support the statement.

Engagement Disclosure of Non-conformance

When non-conformance with the Definition of Internal Auditing, the Code of Ethics or the Standards impacts a specific engagement, communication of the results must disclose the:

- Principle or rule of conduct of the Code of Ethics or Standard(s) with which full conformance was not achieved;
- Reason(s) for non-conformance; and
- Impact of non-conformance on the engagement and the communicated engagement results

Disseminating Results

The chief audit executive or designee reviews and approves the final engagement communication before issuance and decides to whom and how it will be disseminated.

From explanation above it can be conclude that communicating result of engagement result has a purpose to communicate the result of engagement in a right condition, situation, criteria and requirement with accurate, objective, clear, concise, constructive, complete, and timely result that achieve the objective of engagement.

2.1.11 Monitoring Progress and Resolution of Senior Management's Acceptance Risk

Monitoring progress and resolution of senior management acceptance risk is the last professional standard of internal auditing especially performance standard. All those standards needed to monitor and communicate result to management. IIA in standard professional (2008) described about that, as follows:

Monitoring Progress

The chief audit executive must establish and maintain a system to monitor the disposition of results communicated to management.

- The chief audit executive must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action.
- The internal audit activity must monitor the disposition of results of consulting engagements to the extent agreed upon with the client.

Resolution of Senior Management's Acceptance of Risks

When the chief audit executive believes that senior management has accepted a level of residual risk that may be unacceptable to the organization, the chief audit executive must discuss the matter with senior management. If the decision regarding residual risk is not resolved, the chief audit executive must report the matter to the board for resolution.

Based on IIA explanation above, the last standard of professional standard of internal auditor is the standard for internal auditor. For monitoring progress that the standard make sure to communicate result to management by monitoring the disposition result. The resolution of senior management acceptance risk is the

continuity from monitoring result. The standard is used to make decision about residual risk of the result that not resolved and it must report it to the board for resolution.

2.2 Definition of Internal control

Internal control is the process run by board of management commissioner and other personnel designed to give adequate confidence to achieve three classes of purposes (Mulyadi, 2001). These classes are as follows:

- (1) Reliability of financial statements;
- (2) Compliance with laws and regulations;
- (3) Effectiveness and efficiency of operation.

According to Sunarto (2003), *“Internal control is organization planning and method that used to keep and protect the assets, result the information actually and can be trusted, improve efficiency and encourage compliance with management policies.”*

2.2.1 The purpose of internal control

Effective internal control has four main objectives (Mulyadi, 2001):

1. Keeping the organization's assets and records
2. Checking the accuracy and accounting data
3. Encourage accounting efficiency
4. Encourage to compliance management policies.

According to Tampubolon (2005), there are five elements of company's internal control:

1. Control environment

2. Risk assessment
3. Information and communication
4. Control activities
5. Monitoring

According to Sunarto (2003), internal control limits are as follows:

1. Error in consideration
2. Congestion
3. Collusion
4. Violations by management
5. Cost versus benefit.

2.3 Inventory

According to Chases, Aquilano, & Jacobs (2001), *“Inventory is the stock of any item or resource used in an organization. An inventory system is the set of policies and controls that monitor level should be maintained. When stock should be replenished, and how large orders should be.”*

2.3.1 Types of inventory

1. Raw material inventory: the total cost of all component parts currently in stock that have not yet been used in work-in-process or finished goods production.
2. Work in process inventory: That part of a manufacturer's inventory that is in the production process and has not yet been completed and transferred to the finished goods inventory.

3. Finished goods inventory: Amount of manufactured product on hand that awaits sale to customers. (Charter, 2004)

2.3.2 Inventory record

There are two methods of inventory record:

1. Perpetual inventory method

In this method all output and input of inventory is booked in inventory from the related goods. Nevertheless, estimation of amount inventory available will always updated perpetually. That is will help the company to know about the amount of the inventory available without doing physical examination of stock directly.

2. Physical inventory method

According to this method all input and output of inventory is not recorded at the time when inventory used. Inventory input is recorded at the sales estimation. So, the amount of inventory shows the ending available from related goods only. That is why if a company wants to know about the amount of updated inventory has to do physical examination to the warehouse.

2.4 Effectiveness

“Effectiveness means doing the right things to create the most value for the company.” (Chases et al., 2004)

According to Arens & Loebbecke (2003), *“Effectiveness refers to the*

accomplishment of objectives, where as efficiency refers resource used to achieve those objectives.”

2.4.1 Effectiveness measurement

In measuring effectiveness Oakland (2003), says: “*Effectiveness then looks at the output outside of the process and it is about the implementation of the objectives.*” Effectiveness measures should reflect whether the organization, group process owner are achieving the desired result, accomplishing the right things. Measures that may include:

1. Quality
2. Quantity
3. Timelines
4. Cost/price

According to Stevenson (2005), the factors that affect the effectiveness are:

1. Facilities
2. Product and service factors
3. Process factors
4. Human factors
5. Operational factors
6. Supply chain factors
7. External factors

In measuring effectiveness, adding effectiveness may be defined as the percentage actual over the expected output. (Oakland, 2003).

$$\text{Effectiveness} = \text{actual output/expected output}$$

If: effectiveness ≥ 1 , it means effective, effectiveness > 1 , it means not effective.

2.5 Review Previous Research

To support this research, the author also uses the information from other researcher. The first review is the research conducted by Elisabeth (2007), which is closely related to the subject discuss in this thesis. The title of her thesis is “the Role of Internal Auditor of Effectiveness of Internal Control of Raw Material Inventory in PT. Mutiara Mukti Farma Industri Farmasi, Medan“. There are several important point to be concluded here:

The things that examined in the study:

1. How is the role of internal auditor of the effectiveness of internal control of raw material inventory in PT Mutiara Mukti Farma Industri Farmasi, Medan.
2. Does the implementation of internal audit can play a role in effectiveness of of internal control of raw material inventory in PT Mutiara Mukti Farma Industri Farmasi, Medan.

The study yielded the following conclusions:

1. The examination that has been done by internal auditor in PT MUTIFA is good enough, through the preliminary procedure by looking schedule, and audit program that has been made including financial auditing, and operational auditing, then auditor watches, learns, observes every procedures in the place that will be audited and compare with Standard Operational Procedure (SOP) in department in PT. Mutiara Mukti Farma

Industri Farmasi, Medan.

2. The role of internal audit in effective internal control of raw material inventory is defined not good enough because the effectiveness is only define based on estimation not include with measurement that examines effectiveness from internal control of raw material inventory.
3. Internal control of raw material inventory in PT. MUTIFA not well done namely: time schedules standard, the record that has been used only perpetual inventory method that only based on estimation.

This research is a guidance for the author to understand what is author needs in the research and help the author to analyze role of internal audit of effectiveness of internal control of raw material inventory.

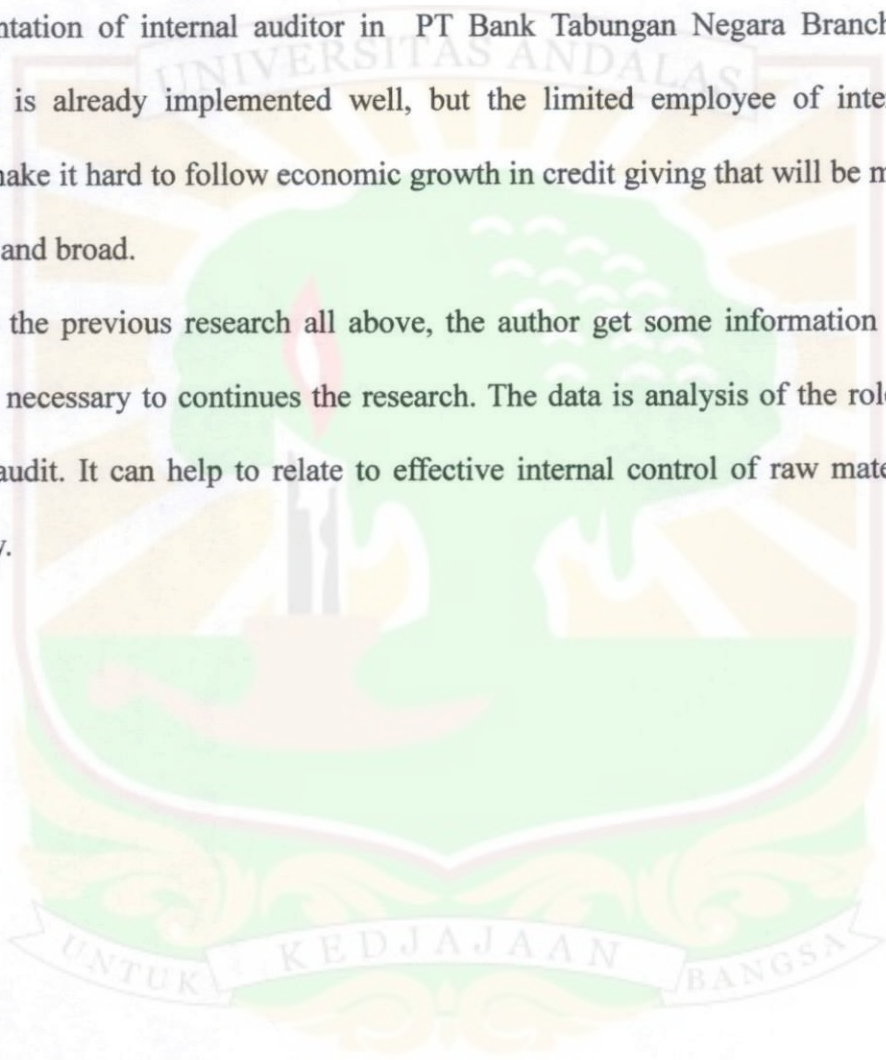
Next research is conducted by Pribowo (2007). The research title is “The role of internal audit in the effectiveness of internal control of credit investments: A Case Study Approach”. The conclusion is that an Internal auditor is implemented and operated well in order to help the company in the effectiveness of internal control of credit investment. The role of internal audit in that research is internal auditor monitored and evaluated credit investment in the company. This research give some understanding to the author about the role of internal audit.

The third, is the implementation of internal audit in credit giving in PT. Bank Tabungan Negara branch of Bandung, East Java, made by Petrisia (2005).

She concludes that implementation of internal auditor in credit giving is good enough. Its mean that internal auditor has done their work. In her thesis she has stated that internal auditor is independent and competent, audit program and

internal audit activities is well conducted by internal auditor, and management has done follow up of internal auditor suggestion. It means that the company has run good internal control and internal control has already sufficient as professional standard of internal auditor. So, this researh helps the author in understanding more for the role of internal auditor. She also state the suggestion that implementation of internal auditor in PT Bank Tabungan Negara Branch in Bandung is already implemented well, but the limited employee of internal auditor make it hard to follow economic growth in credit giving that will be more complex and broad.

In the previous research all above, the author get some information and data that necessary to continues the research. The data is analysis of the role of internal audit. It can help to relate to effective internal control of raw material inventory.



CHAPTER III

RESEARCH METHOD

3.1. Type of Research

This research is an analytical descriptive approach, held with collecting data, arrange and analyzing data in order to make conclusion then advice when it needed. Analytical descriptive is take in order to ascertain and to be able to describe the characteristic of the variable of interest in a situation (Sekaran, 2003).

3.2. Research Object

The object that choosen in this research is the role of intenal audit in the effectiveness of raw materials inventory internal control case study in PT. Nusantara Beta Farma. Internal auditor is an independence appraisal function in an organization to examine and evaluate organization activities. By those definition internal auditor has big role in orgnization function and it can help in effective internal control of raw materials inventory.

This research is choosen include analysis of the role of intenal audit in the effectiveness of raw materials inventory internal control in PT. Nusantara Beta Farma Padang. It means this research analyzes to what extent the role of internal audit in PT. Nusantara Beta Farma able to make the effectiveness of raw materials inventory internal control.

3.3. Sources of Data

Data of this research obtained from primary data. Primary data is obtained from interview to people know for the role of internal audit toward the effectiveness of raw materials inventory internal control in PT. Nusantara Beta

Farma. Secondary data obtained from company's documents, the books and sources related to research.

3.4. Data Collection Method

Data collection techniques that writers use to obtain data are:

Field Research (Field Research). That is the primary data collection by way of review directly to the public accounting firm. Primary data obtained through:

- a. Observations (observation) is to blunt the data in doing by observing and understanding the various symptoms associated with objects which is to know the role of internal audit in the effectiveness of raw materials inventory internal control in PT Nusantara Beta Farma.
- b. Interview (interview) is a way to collect data by conducting interviews with various people who are directly related to the problem under study. In here the purpose is to get information from people in charge the role of internal audit in the effectiveness of raw materials inventory internal control in PT. Nusantara Beta Farma.
- c. Research Library (Library Research)
Is a way to obtain the secondary data that can provide theoretical foundation to support data-primary and secondary data obtained during the research and to support the discussion of identification problems. These data obtained from the books and other references relating to the object under investigation in order to get as many detail information as possible about the role of internal audit in the effectiveness of raw materials inventory internal control in PT. Nusantara Beta Farma.

3.5. Scope of Analysis

The writer limits the scopes of this research which are:

1. This study only to analyze the role of internal audit in PT. Nusantara in Padang.
2. This study only to analyze the role of internal audit in the effectiveness of raw materials inventory internal control in PT. Nusantara Beta Farma in Padang.

3.6. Data Analysis

1. Analyze the role of internal audit in PT. Nusantara Beta Farma Padang.
2. Analyze the effectiveness in using raw materials in PT. Nusantara Beta Farma Padang.
 - a. Identify internal control.
 - b. Identify effectiveness of raw materials inventory internal control.

Such data would be analyzed, including the search for truth against the proposed interview by matching the answers with an analysis of the obtained data such as documents, notes, in support of identifying the changes that occur with the role of internal audit in the effectiveness of internal control of raw materials inventory in PT. Nusantara Beta Farma.

BAB IV

ANALYSIS AND DISCUSSION

4.1 Company Profile

4.1.1 The development of Indonesian Pharmaceutical Industries

Indonesia had been familiar with pharmaceutical science since the colonial times. It is seen in the development of Indonesian traditional medicine from generation to generation among the community.

In the days of Dutch colonialism, Indonesia began to recognize the modern medicine produced by a pharmaceutical industry which was called *Pabrik Kina* "Bandoengsche Fabriek" (now *PT.Kimia Farma* in Bandung). Then a vaccine plant was set up in 1890 which was then transformed into "Pasteur Institute" in 1995 by a public company called *Biofarma*.

From 1921 to the period of independence war, there had been 23 pharmaceutical industries operating in Indonesia. According to the data in 1966, the number increased to 109 medicinal plants. In 2002, it increased further to 199 medicinal plants. Since then, however, the development of Indonesian pharmaceutical industries experienced some hurdles due to poor economic conditions.

The pharmaceutical industries in Indonesia began to revitalize since the dawn of the new order along with the central government's friendly policy on foreign investment in 1967. The policy on national drug in 1983 and the

implementation of Good Manufacturing Practices (GMP) in 1983 to improve the quality played a significant role in boosting Indonesian pharmaceutical industries .

Given these efforts, the pharmaceutical industry in Indonesia is expected to be more advanced and able to compete in both local and international markets.

4.1.2 Brief History of The Establishment of PT.Nusantara Beta Farma

PT. Nusantara Beta Farma is located on Km 25 Padang – Bukittinggi Highway, Pasar Usang. This company has been running since early February 1995. It was previously situated on Jl. Sawahan Dalam IV No.20 Padang which operated in the form of home industry. PT.Nusantara Beta Farma is one of Indonesian pharmaceutical Industries that produce generic drugs. It was founded by Drs. Yusri Umar, Apt in 1979, with the name of PT. Beta Farma Indonesia. On 9 October 1979, the owner proposed a change of name into PT.Nusantara Beta Farma and it was officially inaugurated on 5 November 1979.

The pharmaceutical factory of PT. Nusantara Beta Farma was officially established by the decree of the Minister of Health with the permission of the Directorate General of Food and Drug Administration of the Ministry of Health of the Republic of Indonesia in Jakarta through Head of West Sumatra Provincial Health Office Number 2661/A/SK/PAB/1981 which authorized it to produce drugs in the free and limited free classifications. At that time, it was still located on Jl. Sawahan Dalam IV No.1 Padang with only 5 employees.

Having operated for six years, PT.Nusantara Beta Farma perceived the need of more space for various reasons such as, among others, the expansion of production and administration premises. In its early establishment, the production

site was at the residence of Drs. Yusri Umar, Apt. On 24 January 1985, he filed an application for moving from Jl. Sawahan Dalam IV No.1 Padang to Jl. Sawahan Dalam IV No.20 Padang. It officially had a new address with the decree of Minister of Health Number 503 273 / ER / 1985 dated 1 October 1985. On 12 June 1985, the company began to enjoy a working capital loan from the Bank. Then, on 19 September 1988, it managed to secure the Credit for Small Investment (KIK) from the Bank.

In an effort to improve the quality of drugs in Indonesia, Minister of Health issued a decree No. 43 / Men Kes / SK / II/1988 on the guidelines of the Good Manufacturing Practice (GMP) to the pharmaceutical industries in Indonesia. Given this decree, PT.Nusantara Beta Farma decided to build better facilities and infrastructure. It built a new manufacturing plant at Pasar Usang. Its building permit was issued on 8 December 1992 and the construction started in 1993. The new plant is located on KM 25 Padang Bukittinggi Highway, Pasar Usang Village, Sudistrict of Batang Anai, Padang Pariaman District.

In February 1995, the new plant that met the GMP requirements started operating. Thus the production activities began to move to the new premises at Pasar Usang with powder products. In early August 1995, the entire production moved to Pasar Usang.

In 2002, the top management was held by Ms. Diana Agustin, Apt who is the first daughter of the founder of the company. Many changes took place both in the rules and systems of PT.Nusantara Beta Farma. The new management aimed

to achieve professional and sustainable management to meet the company's vision and mission.

4.1.3 Company's Vision and Mission

Mission :

To produce high quality drugs in accordance with the GMP requirements to earn the trust and loyalty of customers and users.

Vision :

To become a leading pharmaceutical industry in Sumatera.

4.1.4 The Company's Quality Policy

1. Applying a Quality Management system in implementing the GMP.
2. Purchasing raw materials from the suppliers that have been formally approved.
3. Conducting a strict quality control of the raw materials, semi-finished drugs and medicines.
4. Performing a validation program for the entire aspects.
5. Providing trained and competent human resources efficiently in accordance with the GMP guidelines.
6. Improving internal and external communications as well as lowering the level of customers' complaints to a minimum and enhancing after-sales service on an ongoing basis.
7. Ensuring the on time delivery in accordance with the customers' demand.

8. Creating and maintaining a clean, friendly and hygienic working environment.

4.1.5 Building/Premises

Name : PT.NUSANTARA BETA FARMA

Address : KM 25 Padang –Bukittinggi Highway

Village : Pasar Usang

Subdistrict : Batang Anai

District : Padang Pariaman

Province : Sumatera Barat

Land Area : 12.235 m²

Factory Premise Size : 3.856,9 m²

Status : Property Rights

Borders : - East : Padang Bukittinggi Highway
- West : Vacant Land
- North : Residential area
- South : Residential area

4.1.6 The Production Division of Company

The production division is a series of activities that serve to process the raw materials and the auxiliary materials into finished goods which are central to the economy of the company with types of production consisting of:

1. Sub-division of Liquid
 - External fluid drugs
 - Internal fluid drugs
2. Sub-division of powder
3. Sub-division of Ointment
4. Sub-division of Food

4.1.7 The Quality Control of Company

Quality control activities are all controlling efforts made during the manufacture of drugs and are designed to ensure that the products always meet the specification, identification, purity and other characteristics according to the specified standard. The quality control is highly crucial in implementing the production activities as well as affecting the progress of a pharmaceutical industry.

The Quality control division is led by a pharmacist. In general, the quality control has the following tasks :

1. Inspection and testing of the preliminary materials (raw materials and packaging materials)
2. Inspection and testing during the processing
3. Inspection and testing after the packaging (secondary packaging)
4. Re-Inspection and re-testing of the drug.

4.1.8 The Storage of Company

1. The preliminary materials storage
 - a. The packaging materials storage, the primary and secondary packaging
 - b. The raw materials storage, the room-temperature resistant materials, the room temperature non-resistant materials (air conditioned) and flammable materials.
2. The finished drugs storage, the products are ready for the market
3. The quarantine house, a temporary storage for:
 - a. Quarantine of the preliminary materials
 - b. Quarantine of the finished drug

4.1.9 The Company's Waste

There are two types of the waste generated by PT.Nusantara Beta Farma :

1. The Solid waste consisting of :
 - a. Domestic waste (plastic, paper etc.), readily burned

- b. Waste plant (residual talc), this waste can still be used for retreading, bricks and fiber tiles processing.

2. The Liquid waste consisting of :

- a. Used oil (engine oil), this waste is collected and it can be sold as used oil
- b. The waste from cleansing the laboratory and production tools, this waste must undergo a waste treatment (the waste installation) as follows :

The chart of waste treatment above illustrates that all generated liquid waste, after being filtered, flows into the tank. Then it flows into the tub containing calcium oxide which is useful to neutralize the wastewater pH (pH 6-7). When the pH is neutral, the waste is then poured into another tub for erasing process using an *erator* tool that serves to incorporate oxygen into the water. Then it flows into the tub containing plants like algae that serve to remove the chemical bonds existing in the water. Subsequently, the water flows through a shallow and light transparent tub containing algae-like plants to the fish pond. The water is eventually released into the Batang Anai river from the pond.

4.1.10 Organizational Structure

Organizational structure in PT. Nusantara Beta Farma is line organization structure that shows authority and responsibility vertically, it means that each person in the organization unless the worker has had a subordinate. From the organizational structure is seen that the highest power is in the managing director.

In running the activities of company, the managing director delegated authority tasks and responsibility to a director. This director oversees seven sections, each section headed by a manager who is directly responsible to the director. The manager of each division is in charge of its subordinate staff in carrying out the tasks assigned to him/her. The seven divisions are:

1. Personnel
2. Accounting
3. Finance
4. Quality and control
5. Production
6. Sales
7. Purchase



1. Managing Director

He is responsible for the running of all activities of the company with the following main tasks:

- a. Managing and directing all activities of the organization's divisions in both technical and administrative manner.
- b. Reviewing regular reports from the managers and working collaboratively to solve and to settle any arising problems within the organization.
- c. Making decisions regarding the organization's routines and incidental activities.
- d. Giving the production manager instructions on the implementation of drug production.
- e. Paying attention to the employees' prosperity for the progress of the organization.

2. Managers

There are 7 managers in the organizational structure of PT.Nusantara Beta Farma that run the organization's day to day activities :

1) Manager of Personnel

Manager of Personnel has the following authorities and responsibilities :

- a. Recruiting employees
- b. Procuring the office supplies and meeting the administrative needs of the organization's activities.

- c. Ensuring the stock of records on employees, payrolls, wages, incentives, overtime pays and any other staffing needs.

2) Accounting Manager

An Accounting Manager has the following authorities and responsibilities :

- a. Recording all transactions within the organization.
- b. Ensuring the stock of financial information such as balance sheet, income statement, financial position and others.

3) Finance Manager

A Finance Manager has the following authorities and responsibilities :

- a. Assisting Board of Directors in administering the financial matters
- b. Directing the organization's financial policies.
- c. Implementing the financial functions in accordance with the plant's needs
- d. Preparing for budget in cooperation with other divisions to obtain the input data and administering payments and revenues.

4) Quality and Control Manager

Quality and Control Manager supervises a laboratory unit in its activities, with the following authorities and responsibilities :

- a. Qualifying the raw materials, packaging materials for the finished products in accordance with the specified requirements and procedures.
- b. Managing and directing the activities in the chemical laboratory and microbiology laboratory, ensuring quality in Good Manufacturing Practices (GMP).
- c. Being accountable and assuring that all examinations are performed in the correct and approved methods.
- d. Being in charge of inspection on raw materials, packaging materials as well as production process.
- e. Keeping the records of all analysis procedures
- f. Improving the quality control from time to time

5) Production Manager

A Production Manager has the following authorities and responsibilities :

- a. Ensuring a smooth production process and product manufacture in accordance with the specified standard.
- b. Providing technical guidance and encouraging good cooperation among the employees.
- c. Being in charge of drug production which meets the requirements and Good Manufacture Practices within the specified time and production costs.
- d. Acting as a pharmacist being in charge of the production.

- e. Cooperating with Quality Control, Planning and Procurement Divisions in designing the production plan.
- f. Making the routine periodical reports and annual reports for the products already manufactured.

6) Sales Manager

A Sales Manager has the following authorities and responsibilities:

- a. Being in charge of the drug marketing, distribution channel policies and determining the marketing areas.
- b. Doing promotion and advertisements, determining the discounts and credit as well as sorting out prospective buyers.

7) Purchasing Manager

A Purchasing Manager has the following authorities and responsibilities :

- a. Purchasing the required materials for production such as raw or auxiliary materials.
- b. Deciding on the appropriate time for purchasing and selecting the lowest bidding with the best quality from the suppliers.

4.1.11 Internal Audit of PT. Nusantara Beta Farma

The Internal Audit of PT. Nusantara Beta Farma is part of the internal audit within the organization. The auditing is conducted once in six months by an internal audit team formed by the owner or managing director. This internal

division is directly accountable to Board of Directors that it serves as an independent team for the units it audits.

The Internal Audit division is responsible for ensuring that the data presented conform to the real condition on the field. This will facilitate the evaluation and decision-making process of the management.

The Internal Audit division also serves as a source of information or a whistle blower for such cases as grafts, dissipation, fraud, embezzlement etc. At the same time, it checks if each division in the organization works in compliance with the Standard Operation Procedure (SOP). It also evaluates the effectiveness of the organization's internal audit.

In conducting the audit, the Internal Audit Division will first compile the internal audit plan. To have a good and integrated plan, PT. Nusantara Beta Farma creates an internal audit program implemented systematically by the management and the Internal Audit Division. The management and the Internal Audit Division create the annual work program and conduct the weekly audit. Beyond this program, the internal auditors will also carry out the daily audit. The work program contains description on the audit object, the audit schedule and the auditor assignment. The work program is also one of the tools and the controlling standard used by the management to produce an effective and efficient audit.

The internal auditors of PT. Nusantara Beta Farma perform a few important tests in the audit of raw materials :

1. Test of raw materials stock control.
 - a. Random sampling for the raw materials

- b. Comparing the quantity and the unit price for the raw materials on the receipts from the suppliers to the records at hand.
- c. Checking the data on the raw materials movement and existence.
- d. Reviewing the delivery documents, quantity and the raw materials' unit price.
- e. Any important finding is recorded and kept to use by the management in decision making and as the accountability of the internal auditors.

2. Test of raw materials stock balance

- a. Examining and keeping track of each invoice/document related to raw materials from the suppliers. For example, purchasing invoice, production cost records and complete production reports.
- b. Examining the data obtained from raw materials purchasing, production process all the way to production completion.
- c. Comparing physical records of the raw materials to the production plan.
- d. Analyzing any detected slow movement of the raw materials and checking defective or obsolete raw materials.

4.1.12 Raw Materials Inventory Internal Control in PT. Nusantara Beta Farma

The control of the raw materials stock at PT. Nusantara Beta Farma starts from the budgeting of the raw materials made by the Finance manager. The budget produced will be sent to the management. Those being in charge of implementing the budget are : purchasing manager, warehouse manager,

production and accounting management. They should always coordinate with the management as well.

To supervise the effectiveness of internal control for the raw materials, the Internal Audit Division will oversee the controlling process through the standard rules on the raw materials implemented in the organization. The standard rules of the warehouse division are :

1. Available on time.

PT. Nusantara Beta Farma requires that the raw materials be available on time. This means that the raw materials should be available in accordance with the agreement made between PT. Nusantara Beta Farma and the supplier in the order of raw materials. Late stock of raw materials may lead to losses suffered by the organization such as obstructed production and failure in meeting the consumers' demand. Therefore, this standard is of utmost importance in preventing such losses.

2. The raw materials' quality in compliance with the organization standard.

The raw materials highly affect the quality of final products. Nearly the quality of all final products is determined by the raw materials' quality. In other words, the organization's quality standard reflects the quality of the raw materials used by the organization.

3. Standard of quantity/capacity

PT. Nusantara Beta Farma also implements the quantity standard in terms of the raw materials' stock. Prior to ordering the raw materials, PT. Nusantara Beta Farma must check the raw materials in the storage for quantity. PT. Nusantara Beta Farma always makes order for exact need of

the raw materials. Excessive or insufficient stock of raw materials may produce detrimental effects. Insufficient raw materials cannot meet the needs of production process, and excessive stock will incur more expenditures for the organization. For that reason, the standard is also important as it shows how efficient and effective the organization uses the raw materials.

4. Standard of costs.

The cost for purchasing the raw materials is one of the determinant factors in policies on the raw materials stock. The raw materials cost indicates the amount of investment the organization should make for the raw materials stock. Thus the capital cost in the raw materials should be calculated as well.

5. Records keeping and assessment of raw materials based on FIFO system.

Records keeping in the FIFO (First in First out) system means that the cost flow of the raw materials equals the flow of the raw materials' utilization. When a quantity of raw materials purchased at certain cost has depleted, the cost for the next use of raw materials is based upon the next purchasing cost.

There are two types of stock at PT. Nusantara Beta Farma:

- a. The stock for raw materials
- b. The stock for finished goods

The raw materials PT. Nusantara Beta Farma uses in processing the raw materials into the finished goods (drugs) are as follows :

1. Succus, nipagin, sugar to be processed into a liquid drug called OBH
2. Salicil, sulfur, white Vaseline, yellow Vaseline to be processed become Salf
3. Etiket gentian violet to be processed become gentian violet
4. Ac salicil, P coquelicot, P eric, talkum to be processed become salisil talc wangi
5. Aseta glasial to be processed become cuka makan

TABLE 4.1
RAW MATERIALS RECEIPT DATA
DECEMBER 2011

Code	Raw material	Amount of raw material (Mg)	Raw material accepted
BB	succus	500mg	7-12-2011
BBS	sulfur	1000mg	2-12-2011
BBT	talkum	1200mg	8-12-2011
BBA	Acidum salicylicum	750mg	8-12-2011
BBP	P eric	800mg	8-12-2011
BBP	P coquelicot	700mg	8-12-2011

Source: PT. Nusantara Beta Farma, Padang

In table A describe when the company PT. Nusantara Beta Farma accepted the kinds of raw material included the amount of raw material on December 2011.

TABLE 4.2
RAW MATERIAL CONSUMPTION DATA
DECEMBER 2011

Customer	Raw material	Amount of Raw material	Raw Material Accepted
PT. NBF	succus	450mg	18-12-2011
PT. NBF	sulfur	850mg	15-12-2011
PT. NBF	talkum	1100mg	21-12-2011
PT. NBF	Acidum salicylicum	720mg	21-12-2011
PT. NBF	P eric	780mg	21-12-2011
PT. NBF	P coquelicot	690mg	21-12-2011

Source: PT. Nusantara Beta Farma, Padang

In table B PT. Nusantara Beta Farma has put out all their raw materials, so the company reorder the raw materials needed the day before the raw materials actually used up. Table above shows that the amount of raw material received does not match with the raw materials sold. Remaining unused raw materials will be stored in the warehouse as stock when reorder to the raw materials do not correspond to the arrival time of booking.

4.1.13 The Role of Internal Audit in Effectiveness of Raw Materials Inventory Internal Control.

The internal audit of PT. Nusantara Beta Farma plays a very important role in meeting the needs of management and the audit staff. The internal audit prioritizes the goals of the management and the organization over their plans and activities. The Internal Audit Division also plays a significant role in effective internal control of the raw materials at PT. Nusantara Beta Farma.

The followings are the roles of Internal Audit Division in effective internal control of the raw materials at PT. Nusantara Beta Farma:

1. Identifying and minimizing the risks.
2. Overseeing the activities beyond the control of top management.
3. Assisting the decision-making process.
4. Analyzing the future not the past.
5. Assisting the management to manage the organization.

The effectiveness of internal control of the raw materials stock can be seen in how long the raw materials stay at the warehouse. The standard length for the raw materials to stay at the warehouse as specified by PT. Nusantara Beta Farma is 14 days. If the raw materials stay at the warehouse for less than 14 days, it indicates an effective internal control of the raw materials and the other way around. PT. Nusantara Beta Farma set the 14-day standard because the raw materials that are finished within 14 days will generate revenues much sooner for the organization.

TABLE 4.3**Effectiveness of Raw Material Inventory Control****DECEMBER 2011**

Standard of company storage	Raw materials old in the warehouse	Effectiveness	Description
14 days	11 days	1,27	Effective
14 days	13 days	1,07	Effective
14 days	13 days	1,07	Effective
14 days	13 days	1,07	Effective
14 days	13 days	1,07	Effective
14 days	13 days	1,07	Effective
Average of effectiveness		1,10	Effective

Source: data is processed by author

From the table above shows that the raw material inventory internal control in PT. Nusantara Beta Farma on December 2011 is effective, because of the effective formula is $E \geq 1$.

4.2 Analysis and Discussion

4.2.1 Organizational Structure of PT.Nusantara Beta Farma

The organizational structure discussed in this research refers to divisions or sections of the company that are directly related to internal audit of raw material inventory.

The internal audit of PT.Nusantara Beta Farma Pharmaceutical Industries works directly under the Board of Directors. In other words, the internal audit is independent but accountable in providing the audit report to the Board of Directors.

Those dealing directly with internal control of the raw material inventory are the warehouse (storage), inventory section of the finance, accounting, and the store manager as well as the company's operational section.

PT. Nusantara Beta Farma Pharmaceutical Industries is adopting a line organization system in its structure. It is reflected by the location of authority and accountability of each manager from top to bottom. It means that there is a separation of defined functions and responsibilities which can avoid the possible manipulation of a manager who does more than one function.

Given the line organization system, chief executive officer as the top management has full authority in carrying out the coordination and control of all responsibilities and authorities of the divisions under his management.

4.2.2 Internal Audit of PT. Nusantara Beta Farma

Internal audit of PT. Nusantara Beta Farma is performed by an Internal Audit Division elected by the owner and the internal audit division is accountable to the owner.

Internal audit in PT.Nusantara Beta Farma Pharmaceutical Industries is the auditing conducted by internal auditors to examine the financial statements, accounting records, and possible frauds that might happen within PT.Nusantara Beta Farma Pharmaceutical Industries.

TABLE 4.4

Comparison of Internal audit in IIA standard with internal audit in PT.

Nusantara Beta Farma

IIA Standard	Nusantara Beta Farma	Comments result/conclusions
Independence	It serves as an independent team for the units it audits.	The internal audit in PT. Nusantara as an independent team that in accordance with IIA standard that is independence.
Objective assurances	Ensure the data presented conform to the physical condition on the field.	To get objective assurances, internal audit in PT. Nusantara Beta Farma ensure the data presented conform to the physical condition on the field.
Consulting activity designed to add value and improve organization operations	Facilitate the evaluation and decision-making process of the management. Perform a few important	By evaluating the management and decision making process, internal audit in PT. Nusantara Beta Farma can add value

	tests in the audit of raw materials.	for the company and improve organization operations by performing a few important tests in the audit of raw materials.
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The functions of an internal auditor are: serving as the source of information in determining a variety of situations such as leakage, theft, waste, making sure that the work of each division is already in accordance with the Standard Operating Procedures already established in PT. Nusantara Beta Farma Pharmaceutical Industries and evaluating the effectiveness of the organization's internal control.

The functions and responsibilities of internal auditors of PT.Nusantara Beta Farma have not all gone well as they are supposed to be because there are still some shortcomings and weaknesses found in the control performed by the internal auditor. However, the audit conducted is considered quite good because the internal auditors set the auditing program and the audit results are tested again for their validity. The tests performed are:

1. Testing of raw material inventory control
2. Testing of raw material inventory balances

4.2.3 Raw Material Inventory Internal Control in PT. Nusantara Beta Farma

The internal control within PT.Nusantara Beta Farma is a process aiming to preserve and protect assets as well as to achieve efficiencies in the control performed.

The objectives of internal control in PT. Nusantara Beta Farma are:

1. Keeping the organization's assets and records
2. Checking the accuracy of accounting data
3. Promoting the accounting efficiency

The objectives of internal control of PT.Nusantara Beta Farma can be seen from the budgeting process for raw materials demonstrating the realization of the purpose of internal control.

The internal control of PT.Nusantara Beta Farma can be considered quite good in terms of its functional separation of responsibilities. However, in terms of its limits, the internal control is still considered poor due to the onset of errors in judgment and frequent reporting bottlenecks which results in delayed reporting. Thus it can be said that PT.Nusantara Beta Farma has not paid a thorough attention to the predetermined control limits.

In PT.Nusantara Beta Farma, inventory is a raw material being stored for sale or further processing in the production process. Moreover, it is also intended as a way to prevent bottlenecks in the production process due to errors in planning, changes in supply and demand or late order delivery.

The types of inventory used by PT.Nusantara Beta Farma are: raw materials inventory for succus, nipagin, sugar, salicil, sulfur, talcum, aseta glacial and finished goods stocks. This is because PT.Nusantara Beta Farma produces raw materials directly into finished goods.

The standards used by PT.Nusantara Beta Farma are: the punctual availability standard, the standard of raw materials quality, the quantity standard and the standard of cost. All of these standards have yet to run appropriately in particular the punctual availability standard because of frequent delays of raw materials arriving at PT.Nusantara Beta Farma in accordance with the purchase order.

The inventory records:

There are two types of inventory records according to Mulyadi (2001 : 556) as follows:

1. Perpetual inventory method

In this method all output and input of inventory is booked in inventory from the related goods. Nevertheless, estimation of amount inventory available will always updated perpetually. That is will help the company to know about the amount of the inventory available without doing physical examination of stock directly.

2. Physical inventory method

According to this method all input and output of inventory is not recorded at the time when inventory used. Inventory input is recorded at the sales estimation. So, the amount of inventory shows the ending available from related goods only. That is why if a

company wants to know about the amount of updated inventory has to do physical examination to the warehouse.

The inventory records of PT.Nusantara Beta Farma is still rated poorly because it only uses perpetual inventory method which merely looks at the forecast records without calculating physical goods and inventory records. The perpetual inventory method used is the FIFO method which means that the cost flow of raw materials equals the usage flow of raw materials.

4.2.4 The Role of Internal Audit in Effectiveness of Raw Material Inventory

Internal Control

Effectiveness in PT.Nusantara Beta Farma is closely related to the achievement of corporate goals or objectives such as maintaining the corporate assets, checking the reliability and accuracy of accounting data and increasing efficiency in the organization.

Measuring effectiveness has yet to be conducted in PT.Nusantara Beta Farma. Effectiveness is merely assessed from estimates or forecasts and are only based on the results achieved. Thus the role of internal audit in effectiveness is not good enough because it is only based on an estimate not on measuring of the effectiveness. Consequently, the results obtained have not been truly effective. The standard is said to be effective when it has already been proven by an established measuring. For example, the measuring is done by assessing the quality and quantity of raw materials inventory, by looking at the quality of raw materials as well as the quantity of raw materials already produced. In such a way,

an auditor will be able to assess the effectiveness of the raw material inventory.

The quantity of raw materials to be produced must conform to the order.



CHAPTER V

CONCLUSION AND RECOMMENDATION

5.1 Conclusions

Based on the research findings and the discussion presented in previous chapters, the writer can draw the following conclusion:

1. The auditing performed by Internal Audit of PT.Nusantara Beta Farma is said to be good in view of the initial procedure by having a close look at the schedule and the audit programs developed previously that include financial auditing and operational auditing. Then the auditor investigates, learns and observes every single procedure in the sections to be audited and compares them with the Standard Operational Procedure (SOP) in PT.Nusantara Beta Farma Pharmaceutical Industries.
2. The role of internal audit in the effectiveness of raw material inventory internal control is still poor. It is because the effectiveness is only assessed pursuant to estimates or forecasts and not accompanied by the measuring to assess the effectiveness of internal control of raw material inventory.
3. Raw material inventory internal control in PT.Nusantara Beta Farma has yet to run properly. It is yet to be based on: punctuality standard. Moreover, the records used are only based on perpetual inventory that is barely based on estimates or forecasts.

5.2 Recommendation

Based on the analysis and research conducted at PT.Nusantara Beta Farma Pharmaceutical Industries, the writer comes up with the following suggestions:

1. The company needs to have internal auditors who can perform their role and duty properly to achieve an effectiveness of raw material inventory internal control.
2. In raw material inventory internal control, PT.Nusantara Beta Farma should pay attention to the specified standards in implementing an effective control.

5.3 Implications

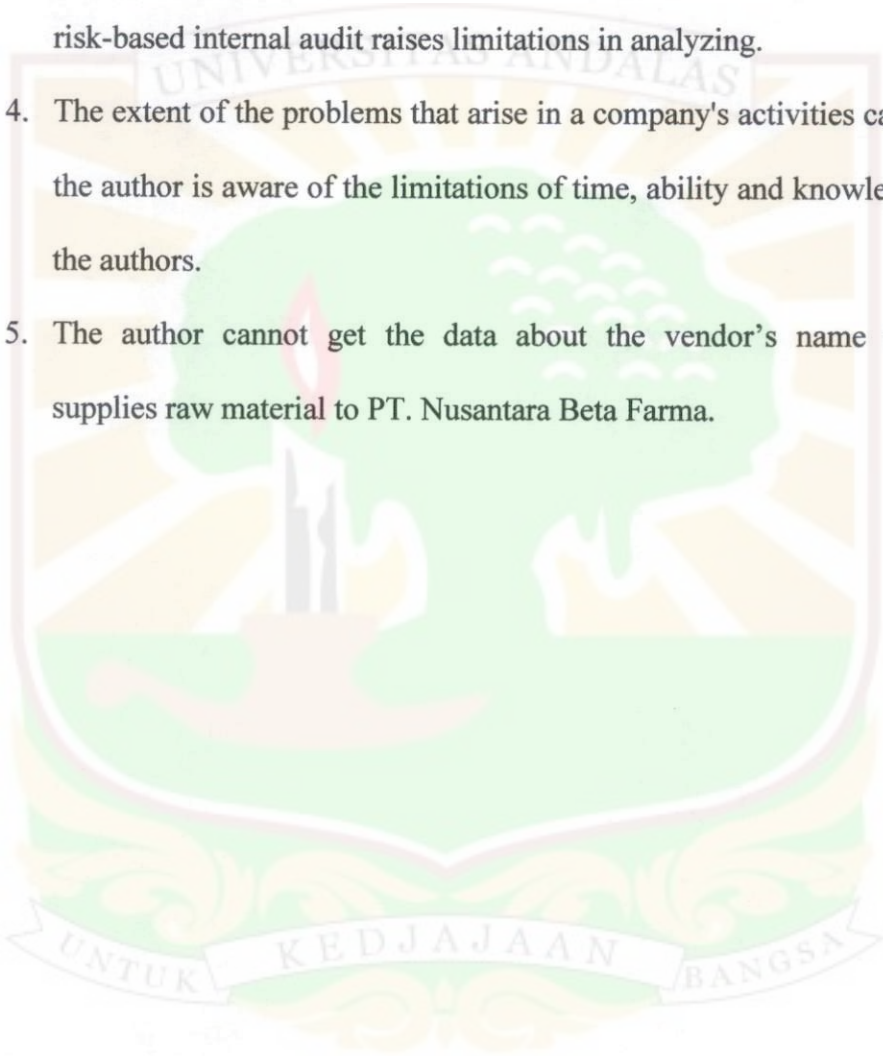
The implication of this research for PT. Nusantara Beta Farma has been implemented good role of internal audit in effectively and hope can improve the effectiveness of internal control, effective internal control of raw material inventory and improve the standards as a whole. For the further research, the author suggest for more deep analysis to the role of internal auditor in effectiveness of internal control of raw material inventory. Then use additional aspect to analyze that need more intention.

5.4 Research Limitations

This study has limitations that may cause interference bias on research results:

1. The restriction on access in the collection of data needed by the author, thus it caused the limitation in analyzing.

2. The authors cannot evaluate and provide input on matters of a technical nature, because this study was only able to collect data then evaluate the role of internal audit in effectiveness of of raw material inventory internal control.
3. Limited of understanding and the number of subjects of research on risk-based internal audit raises limitations in analyzing.
4. The extent of the problems that arise in a company's activities cause the author is aware of the limitations of time, ability and knowledge the authors.
5. The author cannot get the data about the vendor's name that supplies raw material to PT. Nusantara Beta Farma.



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