ROLE OF AUDIT COMMITTEE IN THE FRAUD PENTAGON AND FINANCIAL STATEMENT FRAUD

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Abstract
Financial statements display financial information of entities and their performance in one accounting period. The information should be relevant and reliable, but factors to cause entities intentionally manipulate financial statements to give any individuals or certain groups with material advantages are known as fraud. The research aims to detect financial statement fraud through Fraud Pentagon, with Audit Committee as a moderating variable. Variables applied in this research are a dependent variable in form of Financial Statement Fraud, an independent variable in form of Fraud Pentagon consisting of Pressure, Opportunity, Rationalization, Competence or Capability and, Arrogance factors, and Audit Committee as a moderating variable. This research is correlational research tested by Multiple Regression Analysis. Meanwhile, this research analyzes 49 manufacturing companies listed on the Indonesia Stock Exchange (IDX) during 2016-2018 as the research sample and conducts 149 observations through a purposive sampling method. The research finds out that Pressure, Opportunity, and Rationalization determine Financial Statement Fraud concerning the existence or inexistence of moderation by the size of the Audit Committee. Other factors (i.e., Capability and Arrogance) most likely are insignificant to Financial Statement Fraud. This research suggests that corporate management should cautiously take into account the Pressure factor measured by financial stability, the Opportunity factor measured by effective monitoring, and the Rationalization factor measured by the change in auditor. Those three aspects are highly significant to Financial Statement Fraud. Besides, corporate management should also enhance the effectiveness of the Audit Committee because this variable can magnify the effect of Pressure, Opportunity, and Rationalization factors on Financial Statement Fraud.

Keywords: Financial Statement Fraud, Pressure, Opportunity, Rationalization, Capability, Arrogance, Audit Committee

JEL Classification: M42, D4, G3
INTRODUCTION

Financial statements disclose corporate financial performance, appropriate for an accounting period, and are validate corporate management responsibility to stakeholders (PSAK 1, 2018). Stakeholders take decisions and act on grounds of financial statements. Relevance and precise disclosure are two fundamental information characteristics underscoring the conceptual framework of financial reporting. Precisely-disclosed financial statements feature comprehensive, neutral, error-free information. Financial statements contain error-free information processes and elucidate phenomena accurately.

Fraud may occur if any of the individuals in corporate management is committed to material manipulation over financial statements. The Association of Certified Fraud Examiners (ACFE) theorizes fraud as conscious acts against prevailing laws for specific reasons—manipulating disclosed reports. Individuals inside or outside organizations may commit to fraud for one or collective benefits, and fraud is certainly a violation of other parties.

Enron's energy-generated to involve with Arthur Andersen's Accounting and Tax Consulting was committed to financial statements fraud of USD600,000,000 profits amid the Company's in default performance. Apart from Enron's 2020 fraud case, fraud committed by PT Garuda Indonesia and PT Kimia Farma gave a glimpse of the accounting scandal in Indonesia. In April 2019, PT Garuda Indonesia (Persero) was accused of manipulating its 2018's financial statements to disclose USD809 million earnings in contrast to 2017's financial statements to account for a USD216.58 million of loss. Ministry of Finance to find Garuda Indonesia's violation against the standardized Financial Statements and to act in unison with Financial Service Authority (OJK) and Indonesian Stock Exchange (IDX) gave sanctions to Garuda Indonesia and its public accounting consultant. Another to PT Garuda Indonesia, PT Kimia Farma's fraud-committed acts of 2017 was another example of a fraud case in Indonesia.

Financial statements contain material misstatement if the financial statements contain significant misstatements that have individually or overall impacts, which may result in financial statements not being presented fairly, in all material respects, by generally accepted accounting principles in Indonesia. Misstatements can occur as a result of mistakes or fraud (SA seksi 312 PSA 04). Based on scandalous acts with financial statements unveiled that numerous entities intentionally conduct efforts to manipulate materially financial statements to produce accounting information to bring benefits to individuals or certain groups related to such entities.

Yesiari and Rahayu’s research (2017) on financial statement fraud elaborated that external pressure and rationalization are proven to be significant variables to financial statement fraud. Conversely, financial stability, financial targets, change in auditor, personal financial needs, nature of the industry, ineffective monitoring, and capability are insignificant variables to financial statements fraud. Another research by Annisya (2016) acknowledged that the financial-stability variable measured by the ratio of changing total assets is a positive significance to fraudulent financial statements. Their research proved external pressure variable measured by leverage ratio, financial target measured by return on assets, nature of industry measured by inventory change ratio, audit opinion shown by an Unqualified opinion with an explanatory, and capability measured by the change in Board of Directors are most likely significant to fraudulent financial statements.

Furthermore, Zaki (2017) in his research to apply the fraud diamond model for the independent variable and dependent variable of fraudulent financial statements measured by Altman Z-score, P-value, and Beneish M-score. The research found the significant relevance
gap between the Fraud Diamond model and the Fraud Triangle Model in assessing fraudulent possibility, albeit insignificant effects of Fraud Diamond Model. The research, indeed, unveiled that Fraud Diamond Model is a precise indicator for possible fraud in Egyptian financial statements.

Meanwhile, researches on good corporate governance by Miftah and Murwaningsari (2018) as well as by Handoko and Ramadhani (2017) described fraudulent financial statements committed by an independent board of commissioners. Their researches concluded that an independent audit committee and company size are irrelevant contributors to plausible financial statement fraud; conversely, the financial expertise of the audit committee highly contributes to any fraudulent financial statements.

The underlining reason to analyze IDX-listed manufacturing companies is stocks of those companies are publicly traded. Should they commit to fraud in reporting their financial statements, impacts are publicly appealing. Manufacturing companies whose sales target are subject to substantial profits for corporate management and stakeholders are prone to fraud acts committed by corporate managers as any downturn in sales to cause sliding profits is the main culprit in fraud. This research contributes to enriching literature in the form of empirical facts about the role of the audit committee relating to the correlation between fraud pentagon and financial statement fraud.

A few differences from the prior research results encourage the researcher to re-conduct research to re-test the effects of fraud pentagon to financial statement fraud. This research also develops further from prior research by adding the audit committee variable. Prior researches tested the significance of fraud pentagon—pressure, opportunity, rationalization, capability, and arrogance—to financial statement fraud. Moreover, research on good corporate governance was an additional affirmation to the audit committee as a moderating variable explaining how fraud pentagon correlates to financial statement fraud. The audit committee is a relevant variable to such correlation because of its responsibilities and authorities over managerial monitoring to ensure any decisions in compliance with the company's prevailing regulation and governance concerning any unprecedented backdrop. The researches adapted to updated data as they adopted data of manufacturing companies listed on the Indonesia Stock Exchange (IDX) during 2016-2018.

LITERATURE REVIEW

The agency theory elucidates the tangible correlation between shareholders as the principal and management as the agent. Management as a party whose performance is binding on the contractual agreement is subject to shareholders' review and hold responsibility for its performance before shareholders. Jensen and Meckling (1976) reasoned an agency relationship as follows:

“... agency relationship as a contract under which one or more person (the principals) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent”.

Jensen and Meckling (1976) theorized that agents are most likely to act on behalf of their interests as their interests are pretty different from the interest of either the corporate management or stakeholders. The distinct interests may trigger agency conflict to involve Moral Hazard and Adverse Selection. Moral Hazard occurs as agents breach the binding working contracted stated in the agreement, while Adverse Selection may occur as principal/stakeholders are not well aware of the basis of agents' decision—reliable information obtained or agents’ incompetent performance.
Fraud is inextricably bonded to the agency theory as confirmed by Statement of Auditing Standards No. 99: Fraud is an on-purpose act of misleading financial statements subject to audit review. Association of Certified Fraud Examiners (ACFE) defines financial statement fraud as a fraudulent act committed by corporate management using disclosing misleading financial statements to cause any economic losses suffered by investors and creditors. F-Score Model is one of measure to detect financial statement fraud.

The F-score model totals two variables—accrual quality and financial performance (Skousen et al., 2009). The Crowe's Fraud Pentagon consisting of 5 elements (i.e., pressure, opportunity, rationalization, capability, and arrogance). Fraud arises when the pressure to actualize certain purposes is hindered by incapability; accordingly, the circumstance is a potent driver for fraudulent acts (Albrecht et al., 2012:34). Financial stability, external pressure, personal financial need, and financial target determine pressure. Meanwhile, the opportunity to give a sense of safe circumstances to individuals with fraudulent tendencies opens the plausibility of fraudulent acts. Opportunity is measured by the nature of the industry and ineffective monitoring.

Rationalization is a mechanism to validate unethical practices (Albrecht et al., 2012:56) and is measurable by the change in auditor and total accruals to total assets. Wolfe and Hermanson (2004) mentioned that capability is an individual's trait to play a key role in fraudulent practices. Position, intelligence and creativity, confidence, coercion, deceit, and immunity to stress are some measures to determine capability. Crowe-Horwath (2011) added arrogance featuring superiority and privilege or greediness in individuals’ traits. Arrogance blinds individuals so that they consider that internal control, corporate policies and procedures do not apply to them.

Organization for Economic Cooperation and Development (OECD) defines corporate governance as the system by which business distribution rights and responsibilities among different participants in the corporation such as the board, the managers, shareholders, and other stakeholders, and spell out rules and procedures for making decisions on corporate affairs. The establishment and practices of the audit committee are regulated in the Regulation of Financial Service Authority Number 55/POJK.04/2015. The audit committee is incorporated and holds responsibilities to the Board of Commissioners as the committee ensures that the functions and duties of the Board of Commissioners run smoothly. The audit committee consists of at least three people: one of Independent Commissioner, one of the external party, and one of Public Company. The precondition for its efficient performance is smooth communication among the board of commissioners, directors, internal and external auditors.

The Effect of Pressure on Financial Statement Fraud

Albrecht et al. (2012: 34) explained pressure to hinder individuals from accomplishing their purposes is a cause of fraud, and the company's stable financial performance is an indicator of pressure. SAS No. 99 reasons that managers prone to fraudulent practices of manipulating financial statements when their financial stability or profitability are unstable amid the unprecedented economic, industrial, and operational circumstances. Financial statement fraud committed by the management proportionally correlates to the growth in corporate assets. Thus, financial stability is represented using percentage in changing total assets (Skousen et al., 2009). A higher percentage of changing total assets necessarily means higher fraudulent practices of manipulating financial statements. The theory is validated with research by Sihombing (2014) that finds financial stability as a significant contributor to financial statement fraud. A research (Becker, et al., 2006) theorizes that higher pressures on
individuals most likely cause greater chances of academic fraud. Based on the elaboration, the following hypothesis is formulated:

**Ha1: Pressure contributes positively to financial statement fraud.**

### The Effect of Opportunity on Financial Statement Fraud

In studies of fraud (Albrecht et al., 2012), the opportunity is defined as a safe circumstance to allow individuals committed to fraudulent practices. Opportunity is resulted from lenient monitoring to give managers an opportunity for any fraudulent practices. Zaini et al. (2015) provided the explanation that an individual with a fraudulent motive should not actualize the motive into practice if the circumstance is unsupportive, in reverse circumstance applies. The elaboration results in the following hypothesis:

**Ha2: Opportunity contributes positively to financial statement fraud.**

### The Effect of Rationalization on Financial Statement Fraud

A rationalized mechanism allows individuals to justify unethical conduct (Albrecht et al., 2012:26). Statement on Auditing Standard (SAS) No. 99 stated that the auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud. The former auditors are most likely capable of detecting fraudulent practices committed directly or indirectly by the management. Changes in auditors necessarily mean a higher level of fraudulent practices. Research by Yesiariani and Rahayu (2017) confirmed the hypothesis as the research found that changes in auditors most likely imply manipulated financial statements. Indeed, Zaki (2017) in his research also confirmed that a higher level of rationalized mechanism means higher fraudulent practices committed by individuals. The aforementioned elaboration results in the hypothesis as follows:

**Ha3: Rationalization contributes positively to financial statement fraud.**

### The Effect of Capability on Financial Statement Fraud

Capability/Competence explains that employees are pretty capable of ignoring internal control, creating a secretive strategy, and monitoring social circumstances to find the plausible opportunity of satisfying one's interests (Crowe-Horwath, 2011). Wolfe and Hermanson (2004), furthermore, stated that individuals' capabilities are specific traits to master fraudulent acts with the existence of the other three aspects.

Changes in board of directors portray the extent of capability level as the changes account for handing down authority from the former board of directors to the new ones, purposes of which better improve former management's performance. Nevertheless, the changes may lead to a stressful period and greater plausibility of fraudulent practices.

Researches by Sihombing (2014) and Zaini et al. (2015), indeed, confirmed that the greater plausibility of fraud on grounds of changes in the board of directors. Both studies found that factors to spark fraud are not merely pressure and opportunity as one's incapability of taking fraudulent practices is also matters most. Conversely, higher capabilities necessarily mean greater chances of turning fraudulent motives into practices. The elaborated passages of capability's effects come out in the following hypothesis:

**Ha4: Capability contributes positively to financial statement fraud.**
The Effect of Arrogance on Financial Statement Fraud

Crowe-Horwath (2011) explained that arrogance is an individuals’ superiority traits over their privileges as they are aware that their privileges make them immune to internal control and corporate policies. Arrogance is a lack of conscience and superiority over internal control immunity. Prior study (Aprilia, 2017) analyzed that the frequent appearance of CEO's pictures in a company's annual report indicates arrogance level as more CEO's pictures show much intention of owning public acclamation and arrogance. Fraud pentagon lists arrogance as one of its elements. The described theory of arrogance formulate a hypothesis as follows:

Ha5: Arrogance is significant to financial statement fraud.

The Effect of Audit Committee as Moderating Variable of Fraud Pentagon towards Financial Statement Fraud

The good corporate governance minimizes conflict agency as its prevailing practices integrate distinct interests of corporate owners and the management. The audit committee is one of the internal mechanisms in good corporate governance and established by the board of commissioners. Both parties hold responsibilities for and authorities of monitoring the management performance. A company with an effective audit committee ensures that corporate management is pretty capable of coming up with a decision in compliance with prevailing good corporate governance regulations, despite pressure occurs. The monitoring by the Board of Commissioners and Audit Committee is performed to integrate mutual interests. The increasing size of audit committee necessarily means stricter monitoring to diminish fraud, despite pressures on corporate management. Prior researches also revealed that Board Of Commissioners as one of the good corporate governance mechanisms weaken the inextricable correlation among financial targets, ineffective monitoring changes in auditors, and changes in directions over fraud (Panungkas, Ghozali, & Achmad, 2018). The above elaboration develops into hypothesis as follows:

Ha6a: Audit Committee intensifies the Pressure effect on financial statement fraud.

The opportunity arises due to lenient monitoring and widens the chances of fraudulent acts committed by managers. Thus, strict monitoring by the audit committee and the board of commissioners over management performance narrows the plausibility of financial statement fraud. Research by Diany and Ratmono (2014) as cited by Yesiariani and Rahayu (2017) stated that ineffective monitoring correlates positively to financial statement fraud. Based on the above elaboration, the following hypothesis is inferred:

Ha6b: Audit Committee increases Opportunity effect on financial statement fraud.

Murtanto and Umar (2017) stated that proximity is significant to plausible fraud as proximity rationalizes and even validates any of the unethical acts committed by individuals or groups (Albrecht et al., 2012:56). The independent commissioners and Audit Committee's strict monitoring over corporate management minimize any fraudulent practices through early detection of financial statement fraud. Accordingly, the hypothesis below takes into account:

Ha6c: Audit Committee intensifies the Rationalization effect on financial statement fraud.
Wolfe and Hermanson (2004) explained that the CEO, Board of Directors, and head of divisions are susceptible to fraudulent practices as their privilege gives them capabilities of directing or influencing others as well as taking advantage of the circumstances to smooth their fraudulent acts. The effective monitoring by the Audit Committee and Board of Commissioner narrows plausibility of fraud regardless of management's capability of taking fraudulent motives into acts. Thus, such a hypothesis results:

\[ \text{Ha}_6: \text{Audit Committee increases the Capability effect on financial statement fraud.} \]

Arrogance is a superiority or greediness trait embedded in fraudulent perpetrators. Lacking conscience, the perpetrators are confidence of their immunity over companies' internal policies and regulations (Horwath, 2011). Board of Commissioners and Audit Committee’s main role of monitoring arrogant management ensure that the managers comply with prevailing regulations and good corporate governance. The increasing size of the Audit Committee leverage effective and stricter monitoring as well as minimizing chances of fraud. Aprilia. (2017) in his research described that the number of CEO's pictures appears in a company's annual report indicate CEO's arrogant level. High-level arrogance triggers fraud as the CEO internalizes that any corporate internal control is incapable of restricting his acts. The elaborated passages result in the following hypothesis:

\[ \text{Ha}_6: \text{Audit Committee intensifies the Arrogance effect on financial statement fraud.} \]

**METHOD**

This type of research is hypothesis-testing research. The independent variable used in this study is the Fraud Pentagon Fraud in the form of pressure, opportunity, rationalization, capability, and arrogance variables. Meanwhile, the dependent variable used in this study is financial statement fraud which is measured using the F-Score Model. This study also employs a moderating variable in the form of the size of the Audit Committee, functioning as one of the internal mechanisms in Good Corporate Governance. This study employs the control variable in the form of financial performance as measured by leverage, Return on Assets, Return on Sales, and Total Accruals to Total Assets.

This data source of this research is secondary data. The secondary data is obtained from www.IDX.com in the form of annual reports published by manufacturing companies listing on the Indonesia Stock Exchange during 2016-2018. The research sample was selected using a purposive sampling technique with the criteria of presenting financial statements in Indonesian Rupiah units. Based on the sampling technique above, a total of 147 observations from 49 companies were obtained.

This research employs techniques of Multiple Regression Analysis and Moderating Regression Analysis on panel data using the following models:

**Model 1**

\[
F\text{-SCORE}_{it} = \beta_0 + \beta_1 \text{PRES}_{it} + \beta_2 \text{OPT}_{it} + \beta_3 \text{RTZ}_{it} + \beta_4 \text{CAP}_{it} + \beta_5 \text{ARG}_{it} \\
+ \beta_6 \text{LEV}_{it} + \beta_7 \text{ROA}_{it} + \beta_8 \text{ROS}_{it} + \beta_9 \text{TATA}_{it} + \varepsilon_{it}
\]
Model 2

\[ F\text{-SCORE}_{it} = \beta_0 + \beta_1 \text{PRES}_{it} + \beta_2 \text{OPT}_{it} + \beta_3 \text{RTZ}_{it} + \beta_4 \text{CAP}_{it} + \beta_5 \text{ARG}_{it} + \beta_6 \text{PRES}^{\cdot} JKA_{it} + \beta_7 \text{OPT}^{\cdot} JKA_{it} + \beta_8 \text{RTZ}^{\cdot} JKA_{it} + \beta_9 \text{CAP}^{\cdot} JKA_{it} + \beta_{10} \text{ARG}^{\cdot} JKA_{it} + \beta_{11} \text{LEV}_{it} + \beta_{12} \text{ROA}_{it} + \beta_{13} \text{ROS}_{it} + \beta_{14} \text{TATA}_{it} + \varepsilon_{it} \]

Explanation:

F-SCORE: Financial Statement Fraud
PRES: Pressure
OPT: Opportunity
RTZ: Rationalization
CAP: Capability
ARG: Arrogance
LEV: Leverage
ROA: Return on Assets
ROS: Return on Sales
TATA: Total Accruals to Total Assets
JKA: Size of Audit Committee

\( \beta_0 \) : Constants
\( \beta_1 - \beta_{14} \) : Coefficient of Variables

\( i \) : cross-section
\( t \) : time
\( \varepsilon \) : error term

LEV, ROA, ROE, TATA: control variables

Variable measurement of this research is described as follows:

**Financial Statement Fraud**

This research employs the dependent variable in the form of Financial Statement Fraud using the Fraud Score Model (F-score). The F-Score model is the sum of two variable components in the fraud score model, namely accrual quality and financial performance (Skousen et al., 2009). The formula for the F-Score model is written as follows:

\[ \text{F-score} = \text{Accrual Quality} + \text{Financial Performance} \]

**Accrual Quality (RSST)**

\[ \text{Accrual Quality} = \frac{\Delta WC + \Delta NCO + \Delta FIN}{ATS} \]

**Financial Performance**

\[ \text{Financial Performance} = \text{Change in Receivables} + \text{Change in Inventories} + \text{Change in Cash Sales} + \text{Change in Earnings} \]

Explanation:

WC (Working Capital) = (Current Assets – Current Liability)
NCO (Non-Current Operating Accrual) = (Total Assets – Current Assets – Investment and Advances) – (Total Liabilities – Current Liabilities – Long Term Debt)

FIN (Financial Accrual) = Total Investment – Total Liabilities
ATS (Average Total Assets) = (Beginning Total Assets + Ending Total Assets)/2

\[ \text{Change in Receivables} = \frac{\Delta \text{Receivables}}{\text{Average Total Assets}} \]

\[ \text{Change in Inventories} = \frac{\Delta \text{Inventories}}{\text{Average Total Assets}} \]
\[
\begin{align*}
\text{Change in Cash Sales} &= (\frac{\Delta \text{Sales}}{\text{Sales}(t)}) - (\frac{\Delta \text{Receivables}}{\text{Receivables}(t)}) \\
\text{Change in Earnings} &= (\frac{\text{Earnings}(t)}{\text{Average Total Assets}(t)}) - (\frac{\text{Earnings}_{t-1}}{\text{Average Total Assets}_{t-1}})
\end{align*}
\]

**Pressure**
Pressure (pressure) is an impulse or motivation or goal to be achieved but limited by the inability to achieve which can cause someone to commit fraud (Albrecht et al., 2012: 34). In this research, financial stability is measured by examining changes in company assets of the current year compared to the prior year (Sihombing, 2014). Below is the formulation of the ratio of changes in assets:

\[
PRES: \frac{(\text{TOTAL ASSET}_t - \text{TOTAL ASSET}_{t-1})}{\text{TOTAL ASSET}_t}
\]

**Opportunity**
Opportunity is a situation that allows a person to commit fraud and is considered safe by fraudulent behavior (Albrecht et al., 2012: 34). In this research, the opportunity is measured by the percentage of board members belonging to an external party as indicated by the formulation as follows (Sihombing, 2014):

\[
\text{OPT} = \frac{\text{Number of independent commissioner}}{\text{Size of the board of commissioners}}
\]

**Rationalization**
Rationalization is a mechanism carried out by individuals that allow individuals to justify unethical behavior (Albrecht et al., 2012: 56). In this research, rationalization is measured by the change in auditors of a company as an endeavor to eliminate traces of fraud found by previous auditors. Auditor turnover is measured using a dummy variable (Sihombing, 2014), in which:

a. if there is a change in the public accountant office during 2016-2018, code 1 is written; and
b. if there is no change in the public accountant office during 2016-2018, code 0 is written.

**Capability**
Capability/competence is the expertise of employees to ignore internal controls, develop concealment strategies, and observe social conditions to meet their interests (Crowe-Horwath, 2011). In this study, the capability is measured by changes in directors during the period of research, in which:

a. if there is a change in company directors during 2016-2018, code 1 is written; and
b. if there is no change in company directors during 2016-2018, code 0 is written.

**Arrogance**
Arrogance is the nature of superiority for possessing certain rights or the greediness of the perpetrators of crime in which he/she thinks that neither internal controls nor company policies and procedures apply to him/her (Crowe-Horwath, 2011). In this study, arrogance is measured by the frequent number of CEO's pictures (Aprilia, 2017), defined as the frequency of CEO photos displayed on the company's annual report that can represent the level of arrogance or superiority the CEO may have.

**Moderating variable**
The **moderating variable** used in this study is the Audit Committee. The Audit Committee is one mechanism in good corporate governance established by the Board of
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Commissioners to assist the monitoring process in the company. In this research, the Audit Committee is measured based on the size of Audit Committees (Cadbury, 2004). Meanwhile, the control variables used in this study are as follows:

Leverage

Leverage is the amount of debt used to finance/buy company assets. The higher the value of leverage shows that the company's financial performance is not in good condition. Leverage is formulated as follows:

\[
LEV = \frac{\text{TOTAL LIABILITIES}}{\text{TOTAL ASSETS}}
\]

Return on Assets

Return on Assets (ROA) is a part of profitability ratios in the analysis of financial statements or measurements of company performance (Skousen et al., 2009). ROA is used to measure the effectiveness of the company in generating profits by utilizing existing assets in the company. ROA can be calculated using the following formula:

\[
\text{ROA} = \frac{\text{PROFIT AFTER TAX}_{t-1}}{\text{TOTAL ASSETS}}
\]

Return on Sales

A good company will endeavor to reduce the number of receivables and increase the company's cash collection (Sihombing, 2014). Since receivables require subjective judgment in estimating uncollectible receivables, this situation can put some pressure on managers to manipulate financial statements on uncollectible accounts receivable. This study employs a total receivables ratio compared to sales with the following formula:

\[
\text{ROS} = \left(\frac{\text{RECEIVABLES}_t}{\text{SALES}_t}\right) - \left(\frac{\text{RECEIVABLES}_{t-1}}{\text{SALES}_{t-1}}\right)
\]

Total Accruals to Total Assets

The assessment and decision making of the company involve company management whose subjectivity will be reflected in the company's accrual value (Skousen et al., 2009) as measured by the amount of accrual value compared to the total company assets using the following formula:

\[
\text{TATA} = \frac{\text{NET PROFIT} - \text{OPERATING CASH FLOW}}{\text{TOTAL ASSETS}}
\]
RESULT

Table 1. Descriptive Statistics

| Variable                      | Mean    | Min     | Max     | SD     |
|-------------------------------|---------|---------|---------|--------|
| F-Score                       | -0.077914 | -8.048583 | 7.243884 | 0.995204 |
| Pressure                      | 0.116553 | -0.160617 | 1.030520 | 0.170857 |
| Opportunity                   | 0.397285 | 0.000000  | 0.800000 | 0.113724 |
| Rationalization               | 0.204082 | 0.000000  | 1.000000 | 0.404407 |
| Capability                    | 0.428571 | 0.000000  | 1.000000 | 0.496564 |
| Arrogance                     | 3.299320 | 0.000000  | 24.000000| 3.201915 |
| Size of Audit Committee       | 3.068027 | 2.000000  | 5.000000 | 0.301357 |
| Leverage                      | 0.370862 | 0.076894  | 0.807311 | 0.182078 |
| Return On Assets              | 0.104875 | 0.000782  | 0.920997 | 0.132969 |
| Receivable to Sales           | 0.001603 | -1.914705 | 1.956126 | 0.231714 |
| Total Accrual to Total Assets | -0.001234 | -0.166482 | 0.795560 | 0.107840 |

Note: The dependent variable in the form of financial statement fraud is measured by an F-score. The independent variables are pressure, opportunity, rationalization, capability, and arrogance. The moderating variable is the size of the audit committees. The leverage, Return on Assets, Return on Sales, and Total Accruals to Total Assets are control variables.

Table 1 above shows that the Financial Statement Fraud has an average value of -0.077 which means the average fraud on the financial statements is low, as it is shown by the average F-score below 1. The F-score of the sample company shows heterogeneous data because the average score (-0.077) is smaller than the standard deviation (0.995).

The pressure variable has an average asset change of the sample company which is quite stable at 11.65%. The average assets change of the sample companies shows heterogeneity because the average value (0.116) is smaller than the standard deviation (0.170). Regarding the opportunity variable, the number of independent commissioners compared to the size of the company's board of commissioners shows an average score of 39.7%. In other words, there is a homogeneity because the average score (0.397) is greater than the standard deviation (0.113).

The rationalization variable has the lowest score of 0 (no change in the auditor) and the highest score of 1 (a change of auditor). The average change of auditors during the observation period of the sample company shows heterogeneity because the average score (0.204) is smaller than the standard deviation (0.404). Accordingly, the capability variable has the lowest score of 0 (no change of director) and the highest score of 1 (a change of director) during the observation period. It demonstrates heterogeneity because the average score (0.428) is smaller than the standard deviation (0.496).

The arrogance variable has an average score of 3,299 which means that the average sample company has a few pictures of the CEO incorporated in the annual reports. Data describing the number of CEO photos of 49 companies during the observation period 2016-2018 shows a pattern of homogeneity because the average score (3,299) is greater than the standard deviation (3,201). The size of the Audit Committee has the lowest score of 2 people and the highest score of 5 people with an average size of Audit Committee in 49 companies during 2016-2018 consists of 3 (three) members. Since the average score (3,068) is greater than the standard deviation (0.30), the size of the Audit Committee of the sample companies shows a homogeneous pattern.
Table 2. Partial Test (Financial statement fraud)

\[ F-\text{SCORE}_{it} = \beta_0 + \beta_1 \text{PRES}_{it} + \beta_2 \text{OPT}_{it} + \beta_3 \text{RTZ}_{it} + \beta_4 \text{CAP}_{it} + \beta_5 \text{ARG}_{it} + \beta_6 \text{LEV}_{it} + \beta_7 \text{ROA}_{it} + \beta_8 \text{ROS}_{it} + \beta_9 \text{TATA}_{it} + \epsilon_{it} \]

| Variable         | Coefficient | sig      |
|------------------|-------------|----------|
| Pressure         | 0.449122    | 0.0000 (**) |
| Opportunity      | 0.487594    | 0.0001 (**) |
| Rationalization  | 0.112731    | 0.0015 (**) |
| Capability       | 0.016249    | 0.5286   |
| Arrogance        | -0.034999   | 0.0000   |
| Leverage         | -0.261956   | 0.0004   |
| ROA              | -0.018572   | 0.8862   |
| ROS              | -3.413601   | 0.0000   |
| TATA             | 0.200450    | 0.1111   |
| Sum square resid weighted statistics | 41.04549 |          |
| sum square resid unweighted statistics | 59.89076 |          |
| DW weighted      | 3.203606    |          |
| DW unweighted    | 2.306155    |          |
| Adjusted R-Square | 0.920473   |          |
| P-Value F statistic | 0.000     |          |

Note: Leverage, Return on Assets, Return on Sales and Total Accruals to Total Assets belong to control variables. The significance level uses a 5% margin of error (**) p < 0.05

Table 2 above demonstrates that the value of sum square residual weighted statistics is smaller compared to the sum square residual weighted statistics. Therefore, it can be concluded that in the two models above there is no violation of the classical assumption of heteroskedasticity. The autocorrelation test results show that both DW weighted and unweighted values are in the inconclusive area and not containing autocorrelation (closer to having no autocorrelation). Therefore, this model does not break the assumption of autocorrelation.

The result of the Goodness of Fit Model test shows that the F-score model without moderating the Audit Committee has an adjusted R-Squared value of 92.05%. This result can be interpreted that the variation of the pressure, opportunity, rationalization, capability, and arrogance variables, as well as control variables, in explaining the financial statement fraud is 92.05% and the remaining 7.95% is explained by other factors not contained in the model, provided with the assumption of ceteris paribus.

The result of the simultaneous test shows that the Financial Statement Fraud model which has not been moderated by the Audit Committee has a statistic sig F value of 0.000 (smaller than \( \alpha = 0.05 \)). This result can be interpreted that the variation of the pressure, opportunity, rationalization, capability, and arrogance factors in a model that has not been moderated simultaneously by the size of the Audit Committee has a significant influence on the Financial Statement Fraud variable, assuming ceteris paribus. The results of hypothesis testing prove that:

a. **Pressure** has a positive and significant effect on financial statement fraud with a coefficient of 0.449122 with a significance of 0,000 (0,000 / 2), smaller than \( \alpha = 0.05 \).
b. **The opportunity** has a positive and significant effect on financial statement fraud, with a coefficient value of 0.487594 with a significance of 0.00005 (0.0001 / 2), smaller than $\alpha = 0.05$

c. **Rationalization** has a positive and significant effect on financial statement fraud with a coefficient value of 0.112731 with a significance of 0.00075 (0.0015 / 2), smaller than $\alpha = 0.05$

d. **The capability** has no significant effect on financial statement fraud because its coefficient value is 0.016249 with a significance of 0.2643 (0.5286 / 2), greater than $\alpha = 0.05$

e. **Arrogance** has no significant effect on financial statement fraud because its coefficient value is negative at 0.034999 with a significance of 0.0000 (0.0000 / 2). Since the coefficient sign of the Arrogance variable is contrary to the theory, Ho fails to be rejected, meaning that arrogance factor statistically has no positive and significant effect on financial statement fraud.

The result of statistical test shown in Table 2 also proves that the control variables consisting of leverage, Return on Assets, Return on Sales, and Total Accruals to Total Assets have a significance value above 0.05 which infers that based on statistics, the control variables have no significant effect on financial statement fraud.

### Table 3.

**Partial Test (Financial statement fraud with Moderating Variable of Audit Committee)**

| Variable                  | Coefficient | sig          |
|---------------------------|-------------|--------------|
| Pressure*Audit Committee  | 0.150610    | 0.0000 (**)  |
| Opportunity*Audit Committee | 0.138146   | 0.0032 (**)  |
| Rationalization*Audit Committee | 0.041461 | 0.0012 (**)  |
| Capability*Audit Committee | 0.005010   | 0.5607       |
| Arrogance*Audit Committee  | -0.007736   | 0.0001       |

**Sum square resid weighted statistics**

41.80976

**Sum square resid unweighted statistics**

61.92159

**DW weighted**

3.166715

**DW unweighted**

2.284444

**Adjusted R-Square**

0.901750

**P-Value F statistic**

0.000

**Note:** The significance level uses margin of error 5% (**p < 0.05**)

Table 3 above shows that the value of sum square residual weighted statistics is smaller than the sum square residual weighted statistics. Therefore, it can be concluded that the three models above do not break the classical assumption of heteroskedasticity. The result of the autocorrelation test shows that both DW weighted and unweighted values are in the area that does not contain autocorrelation and is inconclusive (closer to having no autocorrelation). It shows that this model does not break the assumption of autocorrelation.

The result of the Goodness of Fit Model test shows that the F-score model with a moderating variable, namely the size of the Audit Committee, has an adjusted R-Squared value of 90.18%. This can be interpreted that variations in pressure, opportunity, rationalization, capability, and arrogance factors moderated by the Audit Committee variable are capable of...
explaining the financial statement fraud variable by 90.18% and the remaining 9.82% is explained by other factors not contained in both models, assuming *ceteris paribus*. The result of the simultaneous test shows that the Financial Statement Fraud model which has been moderated by the Audit Committee has a statistic sig F value of 0.000 or smaller compared to $\alpha = 0.05$. This can be interpreted that the variation of pressure, opportunity, rationalization, capability, and arrogance in the model which has been moderated by the size of the Audit Committee simultaneously have a significant influence on the Financial Statement Fraud variable, assuming *ceteris paribus*. Table 3 above describes the result of hypothesis testing as follows:

a. The coefficient value of the Pressure*Audit Committee is 0.150610 with a significance of 0.0000 (0.0000 / 2), smaller than $\alpha = 0.05$ resulting in the rejection of Ho. Based on statistics the size Audit Committee can strengthen the correlation between Pressure and Financial Statement Fraud.

b. The coefficient value of the Opportunity*Audit Committee is 0.138146 with a significance of 0.0016 (0.0032 / 2), smaller than $\alpha = 0.05$ resulting in the rejection of Ho. Based on statistical evidence the size of the Audit Committee increases the influence of Opportunity on Financial Statement Fraud.

c. The coefficient value of the Rationalization*Audit Committee is 0.041461 with a significance of 0.0006 (0.0012 / 2), smaller than $\alpha = 0.05$ resulting in the rejection of Ho. Based on statistics the size of the Audit Committee strengthens the effect of Rationalization on Financial Statement Fraud.

d. The coefficient value of the Capability*Audit Committee is 0.005010 with a significance of 0.28035 (0.5607 / 2), greater than $\alpha = 0.05$ so that Ho fails to be rejected. In other words, based on statistical evidence the Audit Committee does not enlarge the influence of Capability on Financial Statement Fraud.

e. The coefficient value of the Arrogance*Audit Committee is negative at 0.007736 with a significance of 0.00005 (0.0001 / 2). However, since the sign of the Arrogance coefficient is negative or opposing to the theory, Ho fails to be rejected. It means that the size of the Audit Committee statistically does not strengthen the Arrogance effect on Financial Statement Fraud.

**DISCUSSION**

The findings of this research indicate that pressure has a positive and significant effect on financial statement fraud, Opportunity has a positive and significant effect on financial statement fraud and rationalization has a positive and significant effect on financial statement fraud. So, the findings of this research indicate that Pressure, Opportunity, and Rationalization have a positive effect on Financial Statement Fraud either they are not moderated or moderated by the Audit Committee. The pressure which has a proxy on the financial stability is proven to have a positive effect on fraudulent financial statements, making the results of this study consistent with the findings of research conducted by Annisyia (2016). Managers facing pressure related to financial stability tend to commit fraud because their profitability is challenged by economic situations.

Capability and arrogance have no significant effect on financial statement fraud. Since the coefficient sign of the Arrogance variable are contrary to the theory, Ho fails to be rejected, meaning that arrogance factor statistically has no positive and significant effect on financial statement fraud. In contrast, this study also proves that Capability and Arrogance factors do not affect Financial Statement Fraud. Similar to research findings conducted by Sihombing...
(2014), the Capability variable does not influence Financial Statement Fraud. It is likely because of effective supervision by the Board of Commissioners on the performance of the Board of Directors. As a result, a change in the Board of Directors does not create an opportunity for financial statement fraud. Regarding the Arrogance variable which is also not proven to affect financial statement fraud, it is consistent with the result of prior research conducted by Saleh (2019). The measurement used is probably not appropriate. Instead of measuring the frequent appearance of manager pictures in the financial statements, other instruments of measurement need to be developed.

Similar results are obtained with or without moderation by the size of the Audit Committee. Moreover, the result of this study is also in line with Aprilia's finding (2017) that Opportunity affects financial statement fraud. Weak supervision provides an opportunity and encourages managers to commit fraud in presenting financial statements, both with and without the moderation of the Audit Committee. Furthermore, Rationalization has a positive effect on financial statement fraud whether it is moderated or not by the size of the Audit Committee. The higher the rationalization, the higher the possibility of someone at the management level performing manipulation.

CONCLUSION

Based on the results of data testing, it can be concluded that pressure has a positive and significant effect on financial statement fraud with a coefficient of 0.449122 with a significance of 0.000. The opportunity has a positive and significant effect on financial statement fraud with a coefficient value of 0.487594 with a significance of 0.00005. Rationalization has a positive and significant effect on financial statement fraud with a coefficient value of 0.112731 with a significance of 0.00075. The capability has no significant effect on financial statement fraud because its coefficient value is 0.016249 with a significance of 0.2643. Arrogance has no significant effect on financial statement fraud because its coefficient value is negative at 0.034999 with a significance of 0.0000, the coefficient sign of Arrogance variable is contrary to the theory, Ho fails to be rejected.

Furthermore, the size of the Audit Committee increases the influence of Pressure, Opportunity, and Rationalization variables significantly on Financial Statement Fraud. Nevertheless, the Audit Committee does not multiply the effect of Capability and Arrogance variables on Financial Statement Fraud.

The implications of this research are: 1) Company management must pay attention to the Pressure aspect as measured by financial stability, the Opportunity aspect as measured by the effectiveness of monitoring, and the Rationalization aspect as measured by the change of auditors because these factors greatly affect the Financial Statement Fraud. 2) Besides, management also needs to increase the effectiveness of the Audit Committee because this variable can increase the influence of Pressure, Opportunity, and Rationalization on the Financial Statement Fraud. 3) The average sample of manufacturing companies listed on the Indonesia Stock Exchange commits fraudulent financial statements at a minor level. The limitation in this study is the value of fraud on the financial statements measured by the value of the F-Score shows a negative number (-0.077914 < 1), meaning that the average sample company may perform manipulation of financial statements at minor level. The research might produce different conclusions if the sample used were companies in other sectors with the potentials of major fraudulent financial reports. Based on these limitations, it is recommended for further research to use a sample of companies other than manufacturing sectors to compare the findings with the results of this study. Financial service companies are recommended to examine for further research because the level of fraud in the financial sector in Indonesia
reaches 43.1 percent, which ranks second highest in Southeast Asia after Vietnam at 58.2 percent (AppsFlyer Report, 2019).

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