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LITERATURE STUDY: ACCURACY OF FRAUD TRIANGLE THEORY ANALYSIS IN IDENTIFYING FINANCIAL STATEMENT FRAUD

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Abstract

The focus of this study is to identify what components are used in identifying fraud in financial statements using the perspective of fraud triangle theory and to find out whether the fraud triangle theory is accurate in detecting fraud in financial statements. This is important to do because there are still many cases of financial statement fraud and will have an impact on decision-making by stakeholders. This scientific work uses a qualitative approach. Data analysis uses literature study techniques. The results of the study show that factors that can detect financial statement fraud include Financial Stability, Financial Targets, Personal Financial Needs, External Pressure, Nature of Industry, Ineffective Monitoring, Auditor Change and Audit Committee. These factors have been proven to have an effect on the occurrence of financial statement fraud so that the Fraud Triangle theory is accurate in detecting financial statement fraud.

Keywords: Fraud Triangle, Financial Statement Fraud, Opportunity, Pressure, Rationalization

Introduction

Financial statements as a product of a series of accounting recording processes are very useful for economic decision-making for stakeholders (Ulupui, et.al., 2021). The information contained in the financial statements includes the amount of assets, liabilities, equity, income, expenses, and cash flow of the company. In compiling and presenting financial statements, there are characteristics that must be met which are generally regulated in the Financial Accounting Standards (SAK). All financial transactions and other events and conditions that give rise to the recognition of each heading in the financial statements must be presented honestly and reasonably.

Sometimes the data displayed by financial statements contains inconsistent information that raises question marks and needs to be traced to the cause (Sukamulja, 2022). This can happen because there is a difference of interest between management and investors or a conflict of interest which is commonly called an agency problem (Jensen & Smith, 1985). Investors as principals are interested in getting high investment returns while management acts as an agent aiming to get a large profit on the results of their work, in the process the agent will try to manipulate the data in the financial statements to achieve its goals (Abbas, Mulyadi & Fatika, 2020). This can lead to fraud in financial statements. Therefore, in assessing financial statements, several adjustments are needed because financial statements are optional, there is the potential for incorrect reporting, inconsistent reports, unreported information, and reported without any supporting information (Sukamulja, 2022).

According to the Association of Certified Fraud Examiners (ACFE) (2020), financial statement fraud is an act of misusing, eliminating or hiding important information from financial statements. Fraud can be financial or non-financial, ACFE divides fraud into three groups, namely corruption, asset misappropriation and financial statement fraud. According to Donald R. Cressey (1953), fraud arises due to three things, namely pressure, opportunity/ opportunity and rationalization known as the Fraud Triangle theory. According to Aini & Sukanto (2021) there are reasons that cause someone to cheat. The existence of pressure on individuals and opportunities that provide opportunities for someone to access assets or authorize control procedures carried out by the company often triggers the occurrence of fraud. Rationalization occurs when fraudsters consciously make decisions by putting their personal interests above class (rationalization). In addition, the position and authority to authorize provide opportunities to commit fraud.

Pressure is divided into financial and non-financial pressure. Financial pressures such as urgent needs, debt payment obligations and high lifestyles. Meanwhile, non-financial pressures such as a person's lack of discipline and the influence of drug addiction. Opportunities are created when a person is in a position to be a confidant of the company and lack of effective internal control of the company. Then the last is rationalization (rationalization) which is related to the thoughts or attitudes of a person who seeks validation or justification for his actions before committing fraud. Rationalization is needed to secure his position as an employee trusted by the company (Indriani & Rohman, 2022).

According to Skousen et al. (2009) in Aini & Sukanto (2021), the components of the fraud triangle theory cannot be analyzed directly, therefore consideration is needed to use variables and proxies in measuring them. Dwijayani, Sebrina & Halmawati (2019) explained that pressure is projected in four factors, namely financial stability, external pressure, personal financial needs and financial targets (SAS No. 99). The next component is opportunity represented by the nature of industry, ineffective monitoring and organizational structure (SAS No. 99). Rationalization is a search for justification from fraudsters before committing their crimes (Irwandi, Pujiati & Rahmawati, 2022). Rationalization can be described through the auditor turnover cycle, audit opinion and accrual totals (Sidauruk & Abimanyu, 2022).

Several previous studies related to financial statement fraud analysis from the perspective of fraud triangle theory have been carried out and have yielded different conclusions. The research of Dwijayani, Sebrina & Halmawati (2019) which aims to obtain empirical evidence that supports the fraud triangle theory in an effort to trace the occurrence of financial statement fraud resulted in the finding that the financial targets factor has an impact on the level of fraud in financial statements while other factors have no effect. With the objectives of the study in line, the results of Irwandi, Pujiati & Rahmawati (2022) indicate that financial stability has a considerable effect on the occurrence of financial statement fraud while other variables do not. Another study by Sidauruk & Abimanyu (2022) concluded that apart from the nature of the industry, the factors that had an impact on the fraudulent actions of financial statements proved to have no effect. Different results were obtained in the research of Abbas, Mulyadi & Fatika (2020) where the variables that have the potential for financial statement fraud are external pressure and auditor change. Similar results were obtained from the research of Tiapandewi, Suryandari & Arie (2020) which obtained the results of auditor change and audit commitee giving sufficient effects financial statement fraud. The next study concluded that what has the potential to trigger financial statement fraud is the variables of financial stability and the nature of industry (Indriani & Rohman, 2022). In line with the study, Ramdany, Harmenawati & Samukri (2021) also concluded that financial stability, financial targets and the nature of industry have a significant effect on financial statement fraud.External pressure, ineffective monitoring and financial stability have a significant impact on the occurrence of financial statement fraud in the research conducted by Aini & Sukanto (2021). In contrast to other studies, the results obtained by Sabatian & Hutabarat (2020) indicate that what has a meaningful effect on the occurrence of financial statement fraud is rationalization. Lestari & Nuratama (2020) agrees with the study that in addition to rationalization, the nature of industry also has an impact on financial statement fraud. From several samples representing previous research related to the use of fraud triangle theory to analyze financial statement fraud, different conclusions were obtained. There are variables that have an effect in one study but not in another.

Based on the observation of previous research that obtained inconsistent research results related to the factors that affect the occurrence of financial statement fraud from the perspective of fraud triangle, the author is interested in raising this theme as a topic in this scientific paper. This scientific paper aims to understand: 1) what factors are used in identifying fraud in financial statements through the perspective of fraud triangle theory, as well as; 2) to find out whether the fraud triangle theory is accurate in identifying fraud in the presentation of financial statements based on observations of the research results obtained.

This scientific work is useful both practically and theoretically. Practical benefits include being able to broaden the horizons for financial report users in particular and the public in general to be more careful and careful in reading financial statements because there are indications of fraud in the financial statements. The theoretical benefit is to provide additional information that is useful for further research in analyzing fraud in financial statements.

Methods

This scientific work uses a qualitative approach. The qualitative approach is a descriptive study and in the process does more analysis (Wekke, et al., 2019). In a qualitative approach, the form of data collected as research material can come from previous studies. According to Hasan et al. (2022), qualitative research is research that is needed when a problem has been quantitatively researched but has not been solved. A qualitative approach is carried out when a problem has not found a bright spot, the goal is to find out the meaning that has not been revealed or confirm the truth of the theory and research a paradigm that continues to develop (Darmalaksana, 2020).

According to Moleong (2021) there are eight types of qualitative research, one of which the author will use in this writing is the document study method. Document study is an activity that prioritizes the analysis or interpretation of material written based on the theme discussed. Research with this type of method can also be used to explore a person's thoughts or opinions that are poured into published books or articles or journals (Hasan et al., 2022).

To obtain quality, accurate and in accordance with adequate standards, it is necessary to use good data collection methods. The study took data from secondary sources. According to Aisya & Astuti (2022), secondary data is sourced from readings and other sources such as official government and private documents and publications from various organizations, one example is the results of studies such as scientific journals.

The first stage of writing this scientific paper is to know the type of literature needed. The literature sources that the author uses in this scientific work come from scientific journals, previous research results, and related books and articles. The next stage is to review and collect library materials. The author collects and selects journals related to the topic of scientific papers and then examines starting from the author, year of writing, objectives, results and content of the research. The last stage is to present the literature studies that have been carried out and pour it through scientific papers by making citations both directly and indirectly.

Results and Discussions

The three aspects that trigger fraud are pressure, opportunity and rationalization called the fraud triangle (Donald Cressey, 1953). Based on SAS No. 99 in Dwijayani, Sebrina & Halmawati (2019) four types of pressure conditions that trigger fraud include financial stability, external pressure, personal financial needs and financial targets. Meanwhile, the three conditions that cause the existence of opportunities to commit fraud are the nature of industry, ineffective monitoring and organizational structure. Furthermore, the conditions that cause fraud from rationalization factors are the auditor turnover cycle, audit opinion and accrual totals (Skousen, Smith & Wright, 2009) in (Sidauruk & Abimanyu, 2022). Previous research has proven that some of these conditions have a significant influence on the occurrence of fraud in financial statements which can be explained as follows:

Financial Stability

According to Irwandi, Pujiati & Rahmawati (2022) financial stability is a situation that indicates that the business financial situation is stable. When a company is threatened in terms of economy, industry and operations, management is forced to engineer financial statements. When the financial situation is unstable, there is a high possibility of management committing fraud, on the other hand, when financial stability increases, the possibility of the company committing financial statement fraud is lower.

The condition of the assets owned by the company can be used to assess the financial stability of the company. In a study conducted by Irwandi, Pujiati & Rahmawati (2022), ACHANGE which shows a comparison of asset changes over a two-year period, shows the level of financial stability. This ratio is obtained by subtracting the total assets of the current year by the total assets of the previous year, then the result is divided by the total assets of the previous year. The results of the study show that the total assets of the objects studied have changed significantly from the previous year. The existence of a negative value in financial stability is a signal or warning for business entities regarding the potential for fraud in their financial statements (Irwandi et al., 2022).

If the company's assets decrease, it will affect potential investors and negative assumptions will arise from the public due to the company's financial instability. Management does everything possible to produce financial statements that look stable and tend to increase even by committing dishonest acts such as manipulating the value of the company's assets (Indriani & Rohman, 2022). When a company's financial position is more unstable, the likelihood of them cheating on financial statements will also increase (Aini & Sukanto, 2021). Research by Irwandi, Pujiati & Rahmawati (2022), Indriani & Rohman (2022), Ramdany, Harmenawati & Samukri (2021) and Aini & Sukanto (2021) came to the same conclusion that financial stability affects the level of financial statement fraud.

Financial Targets

Financial targets are one of the pressure conditions given by directors or shareholders to fulfill both short-term and long-term obligations (Indarto & Ghozali, 2016 in Ramdany, Harmenawati & Samukri, 2021). Management tries to meet its financial obligations, but sometimes those obligations cannot be fulfilled immediately. This causes management to use shortcuts such as manipulating financial statements to report good financial performance (Ramdany et al., 2021).

Return of Assets (ROA) can be used to proximate the company's financial targets in the next period. According to Ramdany et al. (2021), companies with high yields and ROA that increase in each period will increase stock prices and attract investors. A study conducted by Ramdany et al. (2021) concluded that the larger the targeted ROA, the greater the potential for management to engineer financial statements. Financial statements manipulated by management will make the company display the results of achievement according to the financial targets that have been set. Ramdany et al. (2021) and Dwijayani, Sebrina & Halmawati (2019) concluded that the financial targets set by companies have a significant effect on management's tendency to act fraudulently on financial statements.

Personal Financial Needs

According to SAS No. 99 in Sari & Lestari (2020), personal financial needs are a situation when a company's finances are affected by the director's personal financial situation. This is because management can act as the owner and executor of the company's operations at the same time, so they can commit fraud to get dividends and high stock returns. Skousen, et al. (2009) using the proxy of ownership in the firm hold by insider (OSHIP) to determine the influence of personal financial needs (Sari & Lestari, 2020). OSHIP is calculated by dividing the number of shares owned by executives by the number of outstanding shares. The research by Sari & Lestari (2020) shows that the need for personal finance has a major impact on financial statement fraud, so this factor can be used to identify fraud. The more shares owned by internal parties, the more likely it is that the management will commit fraud.

External Pressure

External pressure is the amount of pressure on management to meet the requirements or expectations of third parties (Aini & Sukanto, 2021). According to SAS No. 99, financial statement fraud may occur when there is excessive external pressure. Quoting the opinion of Skousen et al. (2009) in Aini & Sukanto (2021), one of the pressures directed at the management is the need to obtain funding through additional debt or financing from other sources from external parties with the aim of keeping the company competitive. The incurrence of corporate debt will automatically give rise to the obligation to pay off its debts. If the company's leverage ratio is relatively high, it means that the company has large debts and high credit risks. This triggers management to report high profitability by increasing its profit so that it looks able to pay off its long-term obligations. That is the gap for management to engineer the financial statements it presents.

The result of the research by Aini & Sukanto (2021) is that the variable external pressure contributes to financial statement fraud because management is forced to meet the expectations of third parties, causing management to manipulate its financial statements. In addition, a similar study conducted by Abbas, Mulyadi, Basuki & Fatika (2020) proved that in this study, external pressure proxied with leverage (LEV) affects fraud in financial statements.

Nature of Industry

Situations within the company, such as weak internal control over an account, can support fraud. One of them is monitoring the nature of the industry which can be seen from the number of receivables and sales (Indriani & Rohman, 2022). According to Sari et al. (2020), the nature of industry is a component of risks caused by the economic environment and company policies at the operational location. Financial statements contain several accounts whose balance is determined through assessment, deliberate errors when estimating the value of uncollectible receivables balances are an opportunity for management to commit fraud (Lestari & Nuratama, 2020). Therefore, the nature of industry is proxied by the rate of change in receivables compared to sales (RECEIV). Sidauruk & Abimanyu (2022) explained that it is not ideal for the company's industrial conditions to encourage management to manipulate financial statements by displaying cash flows that are larger than receivables. Management conducts significant estimation and analysis of the calculation of receivables balances whose value and estimates are carried out in an unobjective manner by reducing the amount of receivables balances to prevent the value of receivables from becoming too large. In addition to accounts receivable, Irwandi, et al. (2019) explained that there is a desire to generate high investment returns to investors and obtain additional incentives from sales results, encouraging management to use financial statements as a way to hide financial problems that actually occur by manipulating profits and increasing sales. Research conducted by Sidauruk & Abimanyu (2022), Indriani & Rohman (2022), Ramdany, Harmenawati & Samukri (2021) and Lestari & Nuratama (2020) resulted in the conclusion that the nature of the industry has an impact on financial statement fraud.

Ineffective Monitoring

Ineffective monitoring is a condition when a business entity lacks sufficient supervisory units to oversee business operations (Aini & Sukanto, 2021). For example, the ineffectiveness of the board of directors and the audit committee in overseeing the company's internal control and financial reporting. According to Kusumawardhani (2013) in Aini & Sukanto (2021), financial statement fraud is influenced by the ineffectiveness of supervision. The presence or absence of an independent board of commissioners or an audit committee tasked with detecting fraud indicates the company's internal oversight. Effective supervision can reduce cheating. Entrusting the assignment to an external party to become a board of commissioners allows for independent supervision because in general, the external board of commissioners is not related to management, shareholders, or other internal parties (Aini & Sukanto, 2021).

According to Aini & Sukanto (2021), a study by Beasley (1996) stated that the incorporation of an external board of commissioners in a company can increase the efficiency and effectiveness of management supervision aimed at stopping fraudulent reports finance. Research by Aini & Sukanto (2021) came to the conclusion that ineffective monitoring contributes to the possibility of financial statement fraud.

Auditor Change

Rationalization is one of the factors that cannot be ruled out for the occurrence of fraud. Rationalization is often associated with the behavior and nature of a person who always justifies himself from actions that are actually not good (Tiapandewi, Suryandari & Susandya, 2020).

The results of the research by Tiapandewi et al. (2020) resulted in the conclusion that auditor change has an influence on financial statement fraud. Management will more often replace auditors to cover up its fraudulent actions from possible detections made by the old auditor against the company's financial statements. Another study by Abbas, Mulyadi Basuki & Fatika (2020) also came to the same conclusion that auditor change affects the occurrence of financial statement fraud.

Audit Committee

According to Damayanti (2015) in Tiapandewi, Suryandari & Susandya (2020) that the existence of an audit committee in a company has a function to assist the board of commissioners in supervising the performance of the preparation of financial statements carried out by management. In essence, the main task of the audit committee is to provide assistance to the board of commissioners in carrying out monitoring tasks on management performance. The existence of an audit committee is one of the company's efforts to reduce financial statement fraud, so when there are more audit committees in the company, the level of financial statement fraud will decrease (Tiapandewi et al., 2020). Therefore, the results of the study by Tiapandewi et al. (2020) concluded that the audit committee has an influence on fraudulent presentation of financial statements.

The three components in the Fraud Triangle theory, namely Pressure, Opportunity and Rationalization, have an influence in encouraging someone to commit fraud. From the results of the previous research described above, there are a number of factors that are used as variables in detecting fraud through the three components of the Fraud Triangle. The variables Financial Stability, Financial Targets, Personal Financial Needs and External Pressure are factors used to measure how influential

The Pressure component can cause financial statement fraud. Meanwhile, Nature of Industry and Ineffective Monitoring represent the Opportunity component which measures the influence of opportunities or opportunities in encouraging someone to commit fraud. Then the last component, namely Rationalization, which is represented by the variables Auditor Change and Audit Committee. Each of these variables has proven to be influential in identifying fraud in the presentation of financial statements.

Conclusion

From the perspective of the fraud triangle, fraud in financial statements can be detected through various factors including financial stability which is reflected by changes in total assets (ACHANGE), financial targets are proxied by the rate of return on assets (ROA), personal financial needs which can be assessed from the level of share ownership by the company's internal parties (OSHIP), external pressure proxied by the ratio of the company's ability to pay off its long-term debt (LEVERAGE), the nature of industry can be seen from the value of the ratio of changes in receivables to sales (RECEIV), ineffective monitoring related to the existence or absence of an effective supervisory unit within the company, auditor change which is shown by how often the company changes auditors and the last Audit Committee , which consists of an audit committee team that oversees the company's operations.

These factors represent each of the three components of the Fraud Triangle. Financial Stability, Financial Targets, Personal Financial Needs and External Pressure represent the components of Pressure.

Nature of Industry and Ineffective Monitoring are the variables of the Opportunity component and the third is Rationalization which is represented by the variables Auditor Change and Audit Committee.

Based on the literature studies that have been conducted in previous studies, it is found that each factor used to identify financial statement fraud as mentioned in the previous paragraph, is proven to have an effect/influence on the cases of financial statement fraud that occur. So that it can be concluded that the fraud triangle theory is accurate in identifying fraud in financial statements.

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