

Determinants of Pentagon Fraud in Detecting *Financial Statement Fraud* and Company Value

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ABSTRACT

Purpose of this study was to analyze the determinants of fraud pentagon, namely pressure, opportunity, rationality, capability and arrogance of fraudulent financial statements and value. company. The research sample was 66 manufacturing industrial companies indicated to report financial fraud. Methods of data analysis using regression with panel data. The results showed: Positive pressure on fraudulent financial statements, the more widely used to obtain finance, making outsiders, insiders and financial targets, the greater the fraudulent financial statements; Positive opportunities for financial statement fraud. This shows that there is no factor in the false financial statements; Positive arrogance against fraudulent financial statements. This shows that as arrogance increases, fraudulent financial reports will increase.

The deviation from negative financial statements to financial reports, the greater the company's profits and profits will increase in the long run; Positive pressure on firm value, the more opportunities to get gross profit margin, net cash flow, total managerial ownership, return on assets, firm value will increase; Negative company opportunities for firm value. It shows that nothing bigger and ineffective will improve company performance; Positive rationalization of fraudulent financial statements, so that the greater the ratio to get the amount of accruals to total assets, the greater the firm value; The ability to have a positive relationship with company value. This shows that the determining factor or controlling the running of the company so that the value of the company will increase; Positive attitude towards company value. This shows that increasing arrogance will increase the value of the firm; positive pressure on financial reports, greater amounts of financial information to obtain, costs from outside parties, other parties within and financial targets so that fraudulent financial statements will be greater to increase company value; Positive opportunities for financial reports. This shows that nothing is greater than the job and the ineffectiveness of a good commissioner and fraudulent financial reports will be increasingly bigger to increase the value of the company; A positive rationalization of firm value through fraud in financial statements, so that the greater the total accruals to total assets, the greater the fraudulent financial statements will increase firm value; Financial reporting capabilities. This shows that the greater the value of ownership increases through waning financial statements; Pride against corporate value from fraudulent financial statements. This shows that the more money will increase.

1. INTRODUCTION

Fraud is an intentional act and is carried out for personal or other purposes. Regarding financial reporting, fraud is defined as a deliberate act that results in material misstatement in financial reporting (Generally Accepted Audit Standards - GAAS, 2016) Rezaee (2002) states that in the last two decades, financial statement fraud has increased substantially. Increased fraud in financial reports on the one hand can benefit business people because they can overestimate their financial results and financial condition so that their financial statements look good in the public eye.

Financial statement fraud detection does not always get the bright spot due to various underlying motivations and the many methods for committing financial statement fraud (Brennan and McGrath, 2007). Corporate governance is often associated with fraudulent financial reporting. This statement is proven by the research of Dechow et al. (1996) who found that the highest incidence of fraud occurs in companies that are weak in corporate governance, such as companies that are more dominated by insiders and tend not to have audits (Skousen et al., 2009). The findings of Dechow et al. (1996) reinforced by Dunn (2004) who concluded that cheating is more likely to occur when there is a concentration of power in the hands of insiders (Skousen et al. 2009).

To provide solutions to weaknesses in fraud detection procedures in the world, American of Auditing Standards No. 99 (SAS No. 99) regarding Fraud Considerations in Financial Statement Audits in October 2002 (Skousen et al., 2009). The objective of the issuance of SAS No.99 is to increase the effectiveness of auditors in detecting fraud by assessing the risk factors for fraud. The fraud risk factors adopted in SAS No. 99 are based on Cressey's (1953) fraud risk factors theory. This adoption is supported by professional accountants, academics, and various institutions (Skousen et al., 2009).

Unsuccessful financial statement fraud can develop into a major scandal that costs many parties (Skousen et al., 2009). Thus, this study is intended to detect financial fraud statements using pentagon fraud analysis with reference to research conducted by Crowe Howarth (2011). Crowe Howarth's research in 2011 succeeded in developing a fraud prediction model that has increased substantially compared to other fraud prediction models. Research conducted to detect financial fraud statements using pentagon fraud analysis is still rare in Indonesia. The elements in Crowe's fraud pentagon theory cannot only be investigated and thus require variable variables. The component of the fraud triangle cannot be examined directly, so researchers must develop variables and proxies to measure it (Skousen et al., 2009). Independent variables that can be used in this study include: financial stability, external pressure, personal financial needs, financial targets, nature of the industry, effective monitoring, and rationalization.

financial statement fraud, there are development factors that are analyzed to predict financial statement fraud. Wolfe and Hermanson (2004) develop the fraud triangle to become a diamond fraud by adding a capability factor, which ultimately adds to the Arrogance projected by the many CEO images. These five factors are indicated to have triggered an increase in fraud, especially in recent years.

Research Objectives

The purpose of this study was to examine and analyze: pentagon fraud affects financial statement fraud and firm value.

2. LITERATURE REVIEW

The importance of this study can be explained as follows, namely the need for an empirical study of the results of research that analyzes the effectiveness of the risk factors for fraud as adopted in SAS No. 99 in predicting financial statement fraud. This study uses the theory of Cressey, SAS No. 99 and previous studies (such as Skousen et al., (2009), Wolfe and Hermanson (2004), and others) and attempted to develop dimensions and indicators to predict financial statement fraud behavior using diamond factor fraud, namely: 1) pressure (pressure); 2) opportunities (opportunities); 3) rationalization; and 4) ability. Furthermore, added by researcher Crowe (2011) the factors that cause fraud consists of five elements, namely: pressure,

opportunity, rationalization opportunities, competence, and arrogance. The five elements are better known as Crowe's deception pentagon theory.

3. HYPOTHESIS DEVELOPMENT

Pressure Factors with Financial Stability Dimensions as Variables to Detect Fraud Financial Statements

SAS No. 99, managers face pressure to commit financial statement fraud when financial stability and / or profitability is threatened by economic, industrial or entity operating situations (Skousen et al., 2009). Loebbecke et al (1989) Bell et al. (1991) show that in cases where the company experiences growth that is below the industry average, management will manipulate financial reports to improve the company's prospects (Skousen et al., 2009). Research conducted by Skousen et al. (2009) proved that the greater the ratio of changes in the total assets of a company, the higher the probability of fraud in the company's financial statements.

Pressure Factors with External Presence Dimensions as a variable to detect fraudulent financial statements.

Companies often experience pressure from outside parties. One of the pressures often experienced by company management is the need to obtain additional debt or external sources of financing to remain competitive, including research and development funding or capital expenditures (Skousen et al., 2009). The need for external financing is related to cash generated from operating and investing activities (Skousen et al, 2009), which in this study is proxied by the ratio of free cash flow. Research conducted by Skousen et al. (2009) proved that the higher the company's free cash flow ratio, the lower the company's probability of committing fraud.

Pressure Factors with Dimensions of Personal Financial Needs as Variables to Detect Fraudulent Financial Statements

Dunn (2004) states that when executives have a significant financial role in the company, their personal financial needs will be threatened by the company's financial performance (Skousen et al., 2009). Some of the shares owned by company executives will influence management policies in disclosing the company's financial performance. Therefore, the variable personal financial needs is proxied by the ratio of share ownership by insiders. Research conducted by Skousen et al. (2009) proved that when the ratio of insider ownership in a company is low, the likelihood of fraud in the company is high.

Pressure Factors With Target Financial Dimensions As Variables To Detect Fraudulent Financial Statements

In carrying out their performance, company managers are required to perform their best so that they can achieve the planned financial targets. Comparison of income to total assets or Return on Assets is a measure of operational performance that is widely used to show how efficiently assets have worked (Skousen et al., 2009). ROA is often used in assessing manager performance and in determining bonuses, wage increases, etc. Summerris and Sweeney (1998) report that ROA is significantly different between fraudulent firms and non-fraudulent firms (Skousen et al., 2009). Therefore, Return On Assets is used as a proxy for the target financial variables.

Return On Asset is used to measure company management in obtaining profit (profit) as a whole. The greater the ROA obtained, the greater the level of profit achieved by the company and the better the company's position in terms of asset use (Dendawijaya, 2005).

Research by Carlson and Bathala (1997) in Widyastuti (2009) proves that companies that have large profits (measured by profitability or ROA) are more likely to carry out earnings management than companies that have small profits. However, the results of the study from Skousen et al. (2009) do not corroborate the evidence that ROA affects financial statement fraud. This study tries to prove that ROA has a positive effect on fraudulent financial statements.

H1: Pressure influencing financial statement fraud

Factors for Opportunity with Industrial Natural Dimensions as Variables for Detecting Fraudulent Financial Statements

The company's current assets and fixed assets are highly susceptible to fraudulent acts. Asset engineering current such as cash, accounts receivable, inventory, prepaid expenses can be done by playing with the size of the asset components. Fixed asset engineering utilizes the depreciation method and determines the estimated economic life that the company chooses and uses.

Geriesh (2003) found that companies that engage in accounting fraud often conduct transactions with related parties.

Opportunity Factors with Ineffective Monitoring Dimensions as Variables to Detect Fraud Financial Statements Fraud

Or fraudulent practices can be minimized, one of which is a good monitoring mechanism. Independent commissioners are believed to be able to increase the effectiveness of company supervision.

The Beasley (1996) study concluded that the inclusion of the board of commissioners from outside the company increases the effectiveness of the board in supervising management to prevent fraudulent financial reporting. The results of this study are corroborated by research conducted by Dechow et al. (1996) Dunn (2004) who examined the relationship between the composition of the board of commissioners and financial statement fraud. The results prove that fraud is more common in companies that have fewer external board members (Skousen et al., 2009). Research results from Skousen et al. (2009) do not corroborate the evidence that the ratio of the independent board of directors affects financial statement fraud.

H2: opportunities to influence Fraud Financial Statements

Reasoning Factor with Total Accrual Dimensions as Variables to Detect Fraud Financial Statements. Full rationalization with subjective assessment of the company. Subjective assessment and corporate decision making will be reflected in the company's accrual value (Skousen et al., 2009).

Total accruals will affect financial statement fraud because accruals are strongly influenced by management decision making in the rationalization of financial statements (Beneish, 1997). Therefore, rationalization will be proxied by the ratio of Total Accruals (TATA). The total accrual ratio can be calculated using the accrual calculation formula by Beneish (1997), namely: TATA (Total assets divided by total accruals).

H3: rationalization affects the statement of financial fraud.

The capability factor with majority ownership to detect financial statements Fraud ability is defined as the ability of fraudsters to find out and avoid the internal control system, the ability to handle stress for fraudulent acts that have been committed and self-assurance that ensures that their actions will not known to anyone. (Wolfe and Hermanson, 2004). Personal positions or functions within the organization provide the ability to create or exploit fraud. Beasley, et al. (1999) found that 70% of CEOs of public companies indicated that accounting fraud indicates that organizations are not applying sufficient checks and balances to reduce the CEO's ability to influence and perpetuate fraud. This study uses majority ownership as a group of owners who have share ownership of more than 50% (Classens, 2003), are considered capable shareholders so as to avoid the internal control system, the ability to handle stress over fraud

actions that have been taken and self-assurance that ensures self-assurance. it would not be known to anyone.

H4: ability to influence financial statement fraud

The effect of arrogance with the dimensions of the CEO's image in detecting Fraud Financial Statements

A CEO tends to want to show everyone the status and position they have in the company because they do not want to lose their status or position (or feel they are not considered), this is consistent with one of the elements presented by Crowe (2011). A high level of arrogance can lead to fraud because

with the arrogance and superiority of a CEO, the CEO feels that any internal control will not apply to him because of his status and position.

H5: Arrogance affects financial loss

4. RESEARCH METHODOLOGY

The big design of this study is to analyze the components of fraud with fraudulent financial statements and their effect on firm value. This study uses an observation method on secondary data of manufacturing companies listed on the Indonesia Stock Exchange with a certain population whose data collection was carried out in the 2012 to 2016 period as many as 66 companies during the 2012-2016 period. The analysis tool used is Pls analysis using panel data.

		Original Sample (O)	T Statistics (O / STDEV)	
H1	pressure -> cheating	0.502	9,155	Accepted H1
H2	opportunity -> cheating	0.161	4.830	Accepted H2
H3	rationalization -> cheating	0.856	9.164	Accepted H3
H4	ability -> cheating	0.128	1.105	Rejected H4
H5	Arrogance -> fraud	0.067	3.513	Accepted H5
H6	fraud -> firm value	-0.116	3.160	Accepted H6
H7	pressure -> firm value	0.520	4.155	Accepted H7
H8	opportunity -> firm value	-0.850	7.830	Accepted H8
H9	rationalization -> firm value	0.161	5.164	Accepted H9
H10	ability -> firm value	0.502	2.105	Accepted H10
H11	Arrogance -> firm value	0.067	3.513	Accepted H11
H12	pressure -> firm value	0.462	8.155	Accepted H12
H13	through fraud	0.831	3.830	Accepted H13
H14	opportunity -> company value through fraud	0.062	8.164	Accepted H14
H15	rationalization -> firm value through fraud	0.487	2.105	Accepted H15
H16	ability -> firm value through fraud	0.067	3.513	Accepted H16

Table above shows:

1. The pressure affects the fraudulent financial statements of 0.502 because the t stat is 9,155 > t table 1.96. This shows that the greater the pressure, the greater the fraudulent financial statements.
2. Opportunity to influence financial statement fraud is 0.161 because t stat is 4,830 > t table is 1.96. This shows that the bigger the chance, the bigger the fraudulent financial statements.
3. Rationalization affects the fraudulent financial statements of 0.856 because the t stat is 9,164 > t table 1.96. This shows that the greater the rationalization, the greater the fraudulent financial reporting.
4. The ability has no effect on fraudulent financial statements of 0.128 because the t stat is 1.105 < t table 1.96. This shows that capability is not dominant in determining fraudulent financial statements.
5. Arrogance affects financial statement fraud by 0.067 because the t statistic is 3.513 > t table 1.96. This shows that the greater the arrogance, the greater the fraudulent value of financial statements.

6. Falsification of financial statements affects the firm value -0,116 because the t stat is 3,160 > t table 1,96. This shows that the bigger the fraudulent financial statements, the lower the firm value.
7. Pressure affects the firm value 0.520 because the t stat is 4.155 > t table 1.96. This shows that the greater the pressure, the greater the value of the company.
8. Chances of influencing firm value -0,850 because t stat is 7,830 > t table 1,96. This shows that the bigger the opportunity, the greater the value of the company.
9. Rationalization affects firm value with 0.161 because t stat is 5.164 > t table 1.96. This shows that the greater the rationalization, the greater the firm value.
10. The ability to influence firm value is 0.502 because the t stat is 2.105 < t table 1.96. This shows that the greater the capability, the company value will also increase.
11. Arrogance affects the firm value of 0.067 because the t statistic is 3.513 > t table 1.96. This shows that the greater the arrogance, the greater the value of the company.
12. Pressure affects firm value through fraudulent financial statements of 0.462 because tstat 8.155 > t table 1.96. This shows that the greater the pressure through fraudulent financial statements, the greater the value of the company.
13. Chances of influencing firm value through fraudulent financial statements by -0.161 because t stat 4,830 > t table 1.96. This shows that the greater the opportunity through fraudulent financial statements, the value of the company will also decrease.
14. Rationalization affects firm value through financial statement fraud 0.062 because t stat is 8.164 > t table 1.96. This shows that the greater the rationalization through fraudulent financial reporting, the greater the firm value.
15. The ability to influence firm value through fraudulent financial statements is 0.487 because the t stat is 2.105 < t table 1.96. This shows that the greater the ability through fraudulent financial statements, the greater the value of the company.
16. Arrogance affects firm value through a financial statement deficit of 0.067 because the t statistic is 3.513 > t table 1.96. This shows that the greater the arrogance, the greater the value of the company through financial statement fraud.

5. CONCLUSION

1. Pressure has a positive effect on fraudulent financial statements, so the greater the pressure to obtain financial stability, pressure from outside parties, the percentage of insider ownership and financial targets, the greater the financial statement fraud.
2. Opportunities have a positive effect on fraudulent financial statements. This shows that the greater the increase in accounts receivable and the ineffective supervision of the independent board of commissioners, the greater the fraudulent financial statements.
3. Rationalization has a positive effect on fraudulent financial statements, so that the greater the ratio for obtaining total accruals to total assets, the greater the fraudulent financial statements.
4. The ability does not affect the fraudulent financial statements. This shows that majority ownership is not a factor that causes fraudulent financial statements.
5. Pride has a positive effect on fraudulent financial statements. This indicates that improvement. arrogance, fraudulent financial reports will increase.
6. Fraudulent financial statements have a negative effect on fraudulent financial statements, so the greater the earnings management, the firm's value will decrease in the long run
7. Pressure has a positive effect on firm value, so the greater the pressure to get gross profit margins, net cash flow, the amount of managerial ownership, return on assets, firm value will increase.
8. Opportunities have a negative effect on firm value. This shows that the greater the increase in bad debts and the ineffective supervision of the independent board of commissioners, the lower the firm value.
9. Rationalization has a positive effect on fraudulent financial statements, so the greater the rationalization for obtaining total accruals on total assets, the greater the firm value.

10. Ability has a positive effect on firm value. This shows that majority ownership is a determining factor or controls the running of the company so that the company value will increase.
11. Pride has a positive effect on firm value. This shows that increasing arrogance will increase the value of the company.
12. Pressure has a positive effect on firm value through fraudulent financial reports, so the greater the pressure to obtain financial stability, pressure from outside parties, the percentage of insider ownership and financial targets, the greater the fraudulent financial statements will increase the firm's value.
13. Opportunities have a positive effect on firm value through fraudulent financial reporting. This shows that the greater the increase in accounts receivable and the ineffective supervision of the independent board of commissioners, the greater the fraudulent financial statements will increase firm value.
14. Rationalization has a positive effect on firm value through financial statement fraud, so that the greater the rationalization for obtaining total accruals on total assets, the greater the fraudulent financial statements will increase firm value.
15. The ability to influence firm value through fraudulent financial reports. This shows that the greater the majority ownership, the value of the company will increase through a lack of financial reports.
16. Pride affects corporate value through fraudulent financial reporting. This shows that the more arrogance, the value of the company through financial statement fraud will increase as well.

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