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AUDIT COMMITTEE EFECTIVENESS AS FRAUD PREVENTION MECHANISMS

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ABSTRACT

This study aims to examine the effect of audit committee effectiveness on financial statement fraud. This research type is explanatory research. The research population is property and real estate sector companies listed on the Indonesia Stock Exchange (IDX) during 2020–2022. The sampling method used is a purposive sampling with a total sample of 141 annual reports. The data collection method used content analysis on annual report. This study used logistic regression analysis assisted by EViews13 software. The results showed that the effectiveness of the audit committee, proxied by financial expertise, accounting expertise, and the number of audit committee meetings had negative and significant effect on financial statement fraud. This study contributes by strengthening agency theory, where the findings prove that the effectiveness of the audit committee can overcome agency conflicts and minimize financial statement fraud. Practically, this research contributes to regulators to develop policies regarding the work guidelines of the audit committee as a supervisory body for the financial reporting process and to investors to be able to improve investment decision strategies by analyzing the audit committee structure as a party that ensures the reliability of financial statements which are the basis for corporate decision making.

Keyword: **Audit, Governance, Financial Statement, Fraud**

ABSTRAK

Tujuan penelitian ini adalah untuk menguji pengaruh efektivitas komite audit terhadap kecurangan laporan keuangan. Jenis penelitian ini adalah penelitian eksplanatoris. Populasi penelitian merupakan perusahaan sektor properti dan real estat yang terdaftar di Bursa Efek Indonesia (BEI) selama tahun 2020-2022. Metode sampling yang digunakan adalah metode purposive sampling dengan jumlah sample 141 laporan tahunan. Metode pengumpulan data menggunakan konten analisis pada laporan tahunan. Penelitian ini menggunakan analisis regresi logistik yang dibantu dengan EViews13. Hasil penelitian menunjukkan bahwa efektivitas komite audit yang diproksikan dengan keahlian keuangan, keahlian akuntansi dan jumlah rapat berpengaruh negatif dan signifikan terhadap kecurangan laporan keuangan. Penelitian ini memberikan kontribusi dengan memperkuat teori agensi, dimana temuan membuktikan bahwa efektivitas komite audit dapat mengatasi konflik keagenan dan meminimalisir dilakukannya kecurangan laporan keuangan. Secara praktis, temuan penelitian ini memberikan kontribusi kepada regulator untuk mengembangkan kebijakan mengenai pedoman kerja komite audit sebagai badan pengawas proses pelaporan keuangan dan kepada investor untuk dapat meningkatkan strategi keputusan berinvestasi dengan menganalisis struktur komite audit sebagai pihak yang dapat memastikan keandalan laporan keuangan yang merupakan dasar pengambilan keputusan perusahaan.

Kata Kunci: **Audit, Tata Kelola, Laporan Keuangan, Kecurangan**

Introduction

Companies listed on the Indonesia Stock Exchange (IDX) are required to publish annual reports every year. The annual report provides users with information on the financial condition, performance, and results of the company's operational activities as a basis for decision-making. Thus, such a report should be prepared in accordance with the Statement of Financial Accounting Standards (PSAK) No. 1. Accurate financial information can be used as a basis for making decisions and predicting the reliability of alternative scenarios made by

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management (VanAuken et al., 2017). The annual report is also referred to as an accountability report of the board of directors and the board of commissioners in managing and supervising a public company for one financial year.

The annual report consists of an overview of the company's performance, financial statements and prospects for the upcoming year. Management wants to present the company in a positive light to compete in the industry when financial statements are issued. The importance of information in financial statements encourages management to present financial statements in good condition, thereby increasing the risk of fraudulent practices (Yang et al., 2017). Management engages in deceptive and untrustworthy financial statement fraud by manipulating the substantive amounts within the financial statements. Such actions will undoubtedly cause harm to numerous parties and have a negative impact on the company itself.

According to the Association of Certified Fraud Examiners (ACFE, 2022), financial statement fraud refers to a deliberate action that contravenes legal regulations, involving the manipulation and dissemination of deceptive reports to external entities with the aim of gaining personal or collective advantages. Instances of fraudulent activity in financial statements can manifest through several means, such as intentional falsification, manipulation, or modification of data included within accounting records or other supporting documents. The credibility of financial statements as a means of evaluating a company's future prospects can be undermined by the presence of falsified financial statements, leading to a decline in public trust (Omar et al., 2017).

The factor that can reduce financial statement fraud is the effectiveness of the audit committee. The effectiveness of the audit committee is related to audit committee members who have sufficient resources to protect the interests of stakeholders by ensuring the reliability of financial reporting, internal control, risk management and strict monitoring (Abdillah et al., 2019). Audit committees can ensure the financial integrity of the company and have a negative impact on fraud and improve the reliability of financial reporting (Mousavi et al., 2022, and Razali and Arshad, 2014). The effectiveness of the audit committee in carrying out its duties can be seen through various indicators and proxies. This study examines the effectiveness of the audit committee through the financial expertise, accounting expertise owned, and the number of meetings held by the audit committee. The financial expertise owned by the audit committee is an expertise that focuses on financial management in the company's operational activities, while accounting expertise focuses on the financial reporting cycle and regulatory standards (Dwiharyadi, 2017, and Trautman, 2013). Understanding of finance and accounting will make it easier for the audit committee to conduct supervision such as assessing financial information, compliance with financial reporting standards and detecting anomalies in the financial reporting process. Furthermore, regular meetings are conducted by the audit committee to monitor the adequacy and effectiveness of the internal control system which discusses the quality and appropriateness of financial statements, internal controls, and the financial reporting process. Regular meetings by the audit committee, the likelihood of financial statement fraud and risks in the organization will be reduced (Mousavi et al.,2022). Thus, the more financial

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expertise, accounting expertise and the number of meetings on the audit committee, the financial statement fraud will decrease.

Research related to the effectiveness of the audit committee proxied by financial expertise, accounting expertise and the number of meetings has been conducted in previous studies. Research on financial expertise conducted by Badolato et al., (2014) shows the results of financial expertise have a significant impact on earnings management. Research by Abernathy et al., (2014) states that financial expertise possessed by the audit committee will improve the quality of financial reporting and be able to prevent financial statement fraud. Mousavi et al., (2022) also showed that financial expertise can reduce the likelihood of financial statement fraud and money laundering. A similar result was also obtained by Khoufi and Khoufi (2018) who showed that financial statement fraud tends to decrease when audit committee members have more financial expertise. However, research by Mclaughlin et al., (2021), Marzuki et al., (2019), and Dwiharyadi (2017) did not find the effect of financial expertise owned by the audit committee on financial statement fraud.

Research on the effect of accounting expertise on financial statement fraud has been conducted by Ghafran and O'Sullivan (2013) which states that audit committees who have accounting expertise are able to improve the quality of financial reporting. Research by Krishnan and Visvanathan (2007) states that accounting expertise provides stricter supervision and results in higher financial statement conservatism. Dwiyanti and Astriena (2018) show that audit committees that are proficient in accounting are more competent to find earnings management practices of a company that tend to lead to fraud. The results of other studies show a negative effect of accounting expertise owned by the audit committee on financial statement fraud (Chang and Sun, 2009, and Nelson and Devi, 2013). However, these results are not in line with research by Beasley (1996) and Dwiharyadi (2017) who found no effect of accounting expertise owned by the audit committee on financial statement fraud and earnings management.

Research on the number of audit committee meetings as a proxy for the effectiveness of the audit committee on financial statement fraud has mixed results. Several studies have shown a negative effect on the number of meetings held by the audit committee on financial statement fraud (Abbott et al., 2000; Anichebe et al., 2019; Razali and Arshad, 2014; Wiralestari et al., 2019). The results of these studies explain that the more often meetings are held, the problems and findings faced by the audit committee will be resolved more quickly, so that the likelihood of financial statement fraud will be reduced. However, these results contradicted with research by Mclaughlin et al., (2021) and Sharma and Iselin (2012) who found a positive relationship between the number of audit committee meetings and financial statement fraud. The study states that companies that experience problems tend to hold meetings more often, so that the more frequent meetings indicate that the audit committee finds many findings related to financial statement fraud.

The existence of research gaps in previous research results needs to be studied more thoroughly in order to prevent financial statement fraud to the fullest. Research gaps in previous studies can be due to differences in the use of measurements and differences in population. In previous studies, the measurement of financial expertise and accounting expertise was often measured through the educational background of

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the audit committee (Chang and Sun, 2009; Krishnan and Visvanathan, 2007; Marzuki et al., 2019; Mousavi et al., 2022; Nelson and Devi, 2013). In addition, in previous studies (Anichebe et al., 2019; Mousavi et al., 2022; Razali and Arshad, 2014) financial statement fraud variables tend to use M-Score and Z-Score.

This study was conducted to answer the research gap in previous studies. The difference offered in this study is to consider the audit committee work experience as a measurement of financial expertise and accounting expertise. Prior studies neglect the audit committee's work experience, which is directly related to its responsibilities and duties as a supervisor. The audit committee's responsibilities and duties require its members to understand financial management, financial reporting, and accounting standards. Research by Badolato et al., (2014) propose that measuring audit committee expertise is more appropriate using work experience in finance and accounting separately. The measurement has been applied and has a negative effect on earnings management. This study adopts the measurement to examine the effect of audit committee financial expertise and audit committee accounting expertise on financial statement fraud. In addition, this study uses F-Score for its measurement. This measure was taken with reference to research by Aghghaleh et al. (2016) who found that the F-Score measurement has a higher accuracy (73.71%) than M-Score (69.51%) and has a lower error rate (26.83%) than the M-Score measurement (30.49%). The data analysis technique used in this research is logistic regression analysis.

This study contributes by strengthening agency theory, where the findings in this study are able to prove that the effectiveness of the audit committee as seen from financial expertise, accounting expertise, and the number of audit committee meetings can overcome agency conflicts and minimize financial statement fraud. Practically, this research contributes to regulators, especially the Financial Services Authority (OJK), to develop policies regarding the audit committee work guidelines on Financial Services Authority Regulation Number 55 of 2015 related to the obligation to fulfill the minimum requirements for the number of audit committee members who have expertise in finance and accounting, as well as the number of meetings that must be fulfilled. Thus, the audit committee as the supervisory body of the financial reporting process will be able to be more effective in carrying out its duties. The contribution to investors is to be able to improve investment decision strategies by analyzing the structure of the audit committee with regard to the reliability of financial statements, the resolution of risks faced by the company, and the protection of investors.

Literature Review

Agency Theory

According to Jensen and Meckling (1976) introduction of agency theory, agency relationships arise when shareholders (the principal) sign into a cooperation contract with management (the agent) to hire and delegate their authority in decision-making. The relationship between shareholders and management often conflicts because of differences in interests between the two. Management tends to want profits for their performance, while shareholders focus on improving financial performance (Jensen and Meckling, 1976). Besides, information asymmetry between the two often occurs because management, as someone directly involved in the company, has more information than shareholders (Eisenhardt, 1989). This

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information asymmetry makes it easier for management to hide some information that is not known by shareholders, thus encouraging financial statement fraud (Mousavi et al., 2022). Therefore, the effectiveness of supervision of audit committee is needed as a tool that can reduce opportunistic attitudes and prevent financial statement fraud (Razali and Arshad, 2014). This role reflects the principles of agency theory and the need to monitor managers to reduce their opportunities for obtaining individual interests from the company (Beasley et al., 2009; Fama and Jensen, 1983).

Financial expertise as a proxy for audit committee effectiveness will increase the audit committee's knowledge in supervising the financial reporting process. The expertise owned will make it easier for the audit committee to assess whether the financial information presented by the manager reflects the actual condition of the company and there is no information asymmetry between management and shareholders. Furthermore, the accounting expertise owned by the audit committee will also increase the ability of the audit committee as the company's supervisory body. The expertise owned will make the audit committee more careful and thorough when reviewing and complying with financial reporting standards. Thus, the principal's trust in the agent's delegation of the duties assigned will increase. The findings and monitoring process will be discussed and followed up through regular meetings held by the audit committee. Agency conflicts, including possible conflicts of interest, will be discussed by the audit committee at the meeting, so that conducting the meeting will reduce the conflict of interest between the agent and the principal. Therefore, regular audit committee meetings will help the audit committee more quickly and responsively deal with conflicts and protect the interests of shareholders. Thus, the existence of audit committee effectiveness can reduce agency conflicts, and the likelihood of financial statement fraud will also be reduced.

Audit Committee Effectiveness

The board of commissioners, as the supervisory board, forms an audit committee to help carry out its duties and functions. The establishment and guidelines for the work of the audit committee are regulated in Financial Services Authority Regulation Number 55 of 2015. Some of the responsibilities and duties of the audit committee include reviewing financial information, ensuring compliance with regulations, providing recommendations for the appointment of accountants, reviewing the implementation of internal auditors, overseeing the implementation of follow-up on findings, and others.

Audit committee effectiveness is an audit committee member who has sufficient resources to protect the interests of stakeholders by ensuring the reliability of financial reporting, internal control, risk management and strict monitoring (Abdillah et al., 2019). In this study, the effectiveness of the audit committee is proxied by accounting expertise, financial expertise and the number of meetings conducted by the audit committee. Audit committee financial expertise is work experience in financial positions that use financial statements (Badolato et al., 2014).

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Audit committee financial expertise is the knowledge of the audit committee that focuses on financial management in the company's operational activities (Dwiharyadi, 2017, and Trautman, 2013). Having expertise in finance will increase the ability of the audit committee to supervise the company, especially in assessing the financial information presented by management in the financial reporting process which will be used by external parties, especially shareholders, to see the company's financial condition. In addition to financial expertise, accounting expertise is also needed by the audit committee. Audit committee accounting expertise is work experience in specialized accounting positions (Badolato et al., 2014). Accounting expertise focuses on the financial reporting cycle and regulatory standards (Dwiharyadi, 2017, and Trautman, 2013). Audit committees with accounting expertise will be able to review financial reports and ensure compliance with financial reporting standards more carefully and thoroughly. Another proxy is the audit committee meeting which is defined as a forum or place to discuss various findings, problems and risks faced by the company (Mclaughlin et al., 2021). Regular audit committee meetings will make the audit committee quicker and more responsive in resolving problems, findings, and reviewing conflicts of interest that may occur. Thus, the more audit committee members with financial expertise, accounting expertise and holding regular meetings will be able to increase the effectiveness of the audit committee as a supervisor and minimize the likelihood of financial statement fraud.

Financial Statement Fraud

Financial statement fraud is an intentional misrepresentation of a company's financial condition that can be achieved through the deliberate misstatement or omission of a value or amount in the financial statements to deceive users of the financial statements (ACFE, 2022). Misstatements can result from acts of manipulation, falsification, or making changes in accounting records (Mark F et al., 2017). Manipulated financial statements may cause substantial losses to investors and reduce public trust. Financial statement fraud may occur due to a poor internal control system, abuse of duties and authority, and ineffective monitoring or supervision of the company.

Hypothesis Development

Audit Committee Financial Expertise, and Financial Statement Fraud

This study uses agency theory as the main theoretical basis to examine the relationship between audit committee effectiveness and financial statement fraud. The first proxy for audit committee effectiveness in this study is the audit committee's financial expertise. Agency theory emphasizes that the principal and agent relationship involves the transfer of trust and duties to the agent with the assumption that the agent has an opportunistic nature and is looking out for their own interests which are contrary to the interests of the principal, where this relationship creates a conflict of interest (Jensen and Meckling, 1976). Shareholders make an assessment of the company's performance during one period through the financial statements made by management. In this situation, shareholders are unable to know whether the financial statements made by management reflect the

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actual conditions. Currently the audit committee is present as a bridge between management and shareholders. The audit committee is intended to monitor the financial reporting process and restrict opportunistic reporting and protect the interests of shareholders (Badolato et al., 2014). The expertise owned by the audit committee makes the audit committee more able to detect anomalies in the financial information needed by shareholders. The audit committee's ability to detect these anomalies will also increase the effectiveness of its monitoring in overseeing management attitudes and behavior. Thus, audit committee supervision accompanied by financial expertise will increase the effectiveness of its monitoring and make management more careful in conducting financial reporting, so the likelihood of fraud will be reduced.

Professionalism and financial expertise owned by the audit committee are closely related to the effectiveness of its supervision. The audit committee, which has the duty and responsibility to be able to assess the company's financial information, of course requires financial expertise. Financial expertise is the expertise or knowledge of the audit committee that focuses on financial management in the company's operational activities (Dwiharyadi, 2017,and Trautman, 2013). Based on financial expertise, the audit committee will be able to analyze financial information and determine whether the information is in accordance with the actual state of the company. Thus, the financial expertise possessed by the audit committee will be able to identify anomalies that exist in the financial reporting process, so that the audit committee effectiveness will be increasing and the likelihood of fraudulent financial statements will be reduced.

Abernathy et al., (2014) state that financial expertise owned by the audit committee improves the quality of financial reporting and is able to prevent fraud. Khoufi and Khoufi (2018) show that financial statement fraud tends to decrease when audit committee members have more financial expertise. Badolato et al., (2014) show that audit committees with financial expertise have a negative effect on earnings management. Research by Mousavi et al., (2022) provides results that audit committees with financial expertise are able to reduce financial statement fraud and money laundering. Thus, the hypothesis in this study is:

H1: Audit committee financial expertise has a negative effect on financial statement fraud

Audit Committee Accounting Expertise, and Financial Statement Fraud

The relationship between audit committee accounting expertise and financial statement fraud is explained by agency theory. Jensen and Meckling (1976) state that agency relationships arise when there is a cooperation contract between shareholders (principals) to hire and delegate their authority in decision making with management (agents). In agency theory, management is assumed to have an interest in obtaining maximum profit for their performance, while shareholders focus on improving financial performance. Management as the party inside the company, of course, knows more information about the company than the shareholders. Hence, information asymmetry and conflict of interest occur. This information asymmetry makes it easier for management to hide information that is not known by shareholders and prioritize their personal interests, which encourages

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financial statement fraud. The audit committee as a supervisory body can reduce agency conflicts if it supervises effectively. The effectiveness of the audit committee in conducting supervision can be seen from the expertise they have. By having accounting expertise, of course, the audit committee will be able to supervise effectively more carefully and thoroughly. Having accounting expertise, audit committees can detect anomalies when management wants to take advantage of the information asymmetrical situation by hiding financial information for personal interests in financial reporting. Numbers in financial reporting that appear unreasonable will also be more easily detected by audit committees with accounting expertise due to their understanding of financial reporting standards. Therefore, the agency conflict between shareholders and management will be reduced and the likelihood of financial statement fraud is also minimized.

To fulfill the duties and responsibilities of the audit committee appropriately, it is crucial to ensure its effectiveness in performing its duties. This efficacy becomes apparent through the members' expertise, which leads to a better mastery of financial reporting. The audit committee is required to have the expertise to understand the complexity of financial reporting and be able to assess the quality of financial reporting (Krishnan and Visvanathan, 2007). Therefore, the audit committee requires accounting expertise in carrying out its duties. Accounting expertise focuses on the cycle and standards of financial reporting rules (Dwiharyadi, 2017, and Trautman, 2013). Understanding the standard financial reporting rules will make it easier for the audit committee to detect unusual or anomalous numbers in the financial statements. So, when financial statement fraud occurs, the audit committee, with an understanding of reporting standards and the complexity of financial statements, will be able to detect the fraud (Dwiyanti and Astriena, 2018). Thus, the accounting expertise of the audit committee can reduce the likelihood of financial statement fraud.

Prior research by Ghafran and O’Sullivan (2013) states that accounting expertise provides better audit quality and influences financial statement fraud. Krishnan and Visvanathan (2007) show that audit committee accounting expertise provides stricter supervision and results in better conservatism. Dwiyanti and Astriena (2018) show that audit committees that are proficient in accounting are more competent to find earnings management practices of a company that tend to lead to fraud. Chang and Sun (2009) and Nelson and Devi (2013) show that audit committee accounting expertise can reduce the likelihood of financial statement fraud. Thus, the hypotheses in this study are:

H2: Audit committee accounting expertise has a negative effect on financial statement fraud

Audit Committee Meetings, and Financial Statement Fraud

Agency theory is used to explain the relationship between audit committee meetings and financial statement fraud. In agency theory, management as an agent has its own interests to benefit as much as possible from the results of its performance and the existence of information asymmetry makes them want to cover up information that is not known by shareholders (Jensen and Meckling, 1976). This will increase the risk of manipulation in the financial statements. The

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risk of financial statement fraud can be detected by the effectiveness of the audit committee in carrying out its duties and responsibilities. The number of meetings held by the audit committee can show the effectiveness of the audit committee. The manipulation will be detected by the audit committee through regular audit committee meetings (Razali and Arshad, 2014). Findings in the financial statements and possible conflicts of interest are also discussed through audit committee meetings. Thus, audit committee effectiveness as seen in meetings held by the audit committee can reduce agency conflicts between management and shareholders.

A variety of risks in the company can be detected and resolved by the effectiveness of the audit committee in conducting its supervision. The audit committee reviews and evaluates the adequacy of the effectiveness of the internal control system through regular meetings (Mousavi et al., 2022). By holding regular audit committee meetings, the detection of potential fraud will be more easily detected and improve the audit committee's supervision of the financial reporting process (Alice and Christian, 2022). Also, audit committees that always hold meetings will be able to continue to monitor managers and oversee the reporting process because with frequent meetings, it is less likely for managers to manipulate financial reporting (Nurliasari and Achmad, 2020). When supervising financial reporting, the audit committee will find the findings, problems and risks faced by the company. This was conveyed at a meeting held by the audit committee. Findings and anomalies in financial reports will be more easily detected by holding regular meetings. Thus, audit committee meetings can reduce the possibility of fraudulent financial statements. Anichebe et al., (2019) found that the audit committee meeting was able to reduce the occurrence of financial statement fraud. Another study by Wiralestari et al., (2019) and Nurliasari and Achmad (2020) states that the more often the audit committee meetings are held, the less likely financial statement fraud will be committed. Razali and Arshad (2014) found that a high number of audit committee meetings will reduce the likelihood of financial statement fraud being committed. Thus, the hypothesis in this study is:

H3: The number of audit committee meetings has a negative effect on financial statement fraud

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Research Method

Type of Research

This type of study is explanatory research. Explanatory research is research that examines the causal relationship between research variables using hypothesis testing (Sekaran and Bougie, 2016). The variables of this study are audit committee financial expertise, audit committee accounting expertise, number of audit committee meetings, and financial statement fraud. This study aims to examine the effect of audit committee effectiveness proxied by audit committee financial expertise, audit committee accounting expertise and the number of audit committee meetings on financial statement fraud.

Type and Source of Data

This type of study data is quantitative. The source of data research is secondary data, namely researchers get data indirectly. Researchers obtained data in

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the form of annual reports from the Indonesia Stock Exchange (IDX) and the websites of each property and real estate sector company.

Population and Sample

The population in this study were 81 property and real estate sector companies listed on the Indonesia Stock Exchange (IDX) in 2020-2022. The sampling technique was carried out by purposive sampling, which is a sample selection technique based on specific criteria. The following criteria were applied in the selection of the sample shown in the table 1:

Table 1. Sample selection criteria

	Description	Companies
	Total Population	81
	Sample Criterias:	
1.	Property and real estate companies that not remained listed on the IDX or delisting between 2020 and 2022.	(8)
2.	Property and real estate sector companies that did not publish annual financial reports consecutively during 2020–2022.	(21)
3.	Data related to the audit committee in accordance with the research variables was not available in complete form.	(5)
		47
	Total sample (3 years)	141

Source: Processed data, 2023

Based on sampling with several criteria applied, a sample of 47 companies was obtained with a total of 141 annual report analysis units as samples in this study.

Data Collection Method

The data collection method in this study uses content analysis which is carried out in several stages such as (1). Determination of the sample. The sample in this study is property and real estate companies in 2020-2022. (2). Data collection in the form of annual reports through the Indonesia Stock Exchange and the respective company websites. (3). Content analysis and tabulation of annual report data and financial reports by looking at data in accordance with the variables in the study, namely financial statement fraud, audit committee work experience and the number of meetings held by the audit committee during one period. (3). Data analysis using logistic regression. (4). Data interpretation.

Operational Definitions and Measure of Variables

Audit Committee Financial Expertise

Audit committee financial expertise is work experience in a financial position that uses financial reports (Badolato et al., 2014). This variable is seen from the proportion of audit committees with financial expertise adopted from the research by Badolato et al. (2014). The measurement scale of this study uses nominal scale. The following is the formula used in this study.

FINEXP = Total audit committee members with financial expertise

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Audit Committee Accounting Expertise

Audit committee accounting expertise is work experience in an accounting-specific position (Badolato et al., 2014). This variable is seen from the proportion of audit committees with accounting expertise adopted from the research by Badolato et al. (2014). The measurement scale of this study uses nominal scale. The following is the formula used in this study.

ACCEXP = Total audit committee members with accounting expertise

The Number of Audit Committee Meetings

The number of audit committee meetings is a forum or place to discuss various findings, problems and risks faced by the company (Mclaughlin et al., 2021). This variable is seen from the number of meetings held by the audit committee during one period adopted from research by Mousavi et al., (2022). The measurement scale of this study uses a nominal scale. The following is the formula used in this study.

MEETS = The number of audit committee meetings in one period

Financial Statement Fraud

Financial statement fraud is a misstatement that occurs in the financial statements due to manipulation, falsification, or alteration of accounting notes (Mark F et al., 2017). Measurement of financial statement fraud in this study uses the F-Score Model. This model sums two components, namely accrual quality and financial performance. companies are predicted to commit financial statement fraud if the F-score value is more than 1, whereas companies with an F-score value of less than 1 cannot be predicted to commit financial statement fraud (Dechow et al., 2011). The measurement scale of this study uses ratios. The following is the formula used in this study.

F-Score = Accrual Quality + Financial Performance

Accrual quality proxied by accruals RSST

$$\textbf{RSST Accrual} = \frac{\Delta WC + \Delta NCO + \Delta FIN}{\text{Average Total Asset}}$$

a. **WC** = (Current Asset-Cash short term investment) – (Current liabilities-short term debt)
b. **NCO** = (Total assets - Current assets – Investment and advances) – (Total liabilities – Current liabilities – Long term debt)
c. **FIN** = Short term investment + Long term investment) – (Long term debt + Short term debt + Preferred Stock)
d. **ATS**= (Beginning total assets + End total assets)/2

The financial performance calculation formula is as follows:

Financial performance = change in receivable + change in inventories + change in cash sales + change in earnings

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Analysis Techniques

Regression Logistic Analysis

The regression analysis used in this study is logistic regression with the EViews13 data processing tool. This model is used because the dependent variable in this study is a dummy variable. This analysis technique does not require normality test and classical assumption test, and ignores heteroscedasticity (Ghozali, 2017). As a pre-test, goodness-of-fit test and model accuracy test will be conducted. Before conducting the prerequisite test, descriptive statistical analysis is carried out to see a description of the data seen from the mean, standard deviation, maximum, and minimum (Ghozali, 2017). In this study, we will look at the data description of the audit committee financial expertise, audit committee accounting expertise, number of audit committee meetings, and financial statement fraud.

The first prerequisite test is the goodness-of-fit test is conducted to test the fit of the data with the model (Ghozali, 2017). This test uses Hosmer and Lemeshow's. If the Hosmer and Lemeshow's test results (HL-Statistic) show a number greater than 0,05, then the model in this study is said to be fit. The next prerequisite test is model accuracy test is conducted to show how well the model predicts and as a measure of model accuracy (Ghozali, 2017). This test is seen from the expectation-prediction evaluation table. If the results on % Correct shown are close to 100%, then the use of models and variables is more accurate and correct. Next. the Z statistical test is conducted to test whether each independent variable in the study significantly affects the dependent variable (Gujarati et al., 2012). If the probability of Z count is less than 0.05, then the proposed hypothesis is accepted.

Result

Descriptive Analysis

Descriptive analysis is carried out to see a description of the data seen from the mean, standard deviation, maximum, and minimum. In this study, descriptive analysis explains the financial expertise of the audit committee, the accounting expertise of the audit committee, and the number of audit committee meetings. The descriptive analysis result described in table 2, as follows:

Table 2. Descriptive analysis result

	N	Min	Max	Mean	Std. Deviation
FRAUD	141	0	1	0,170	0,377
FINEXP	141	0	2	0,489	0,605
ACCEXP	141	0	3	1,063	0,872
MEETS	141	0	16	5,276	3,174
Valid N (listwise)	141				

Source: Processed data, 2023

Results in table 2 reported that the mean value for the financial statement fraud is 0.17. This indicates that the sample of companies selected in this study has a low likelihood of fraud. The audit committee’s financial expertise shows a minimum value of 0, a maximum of 2, and an average of 0,489. The average audit committee's financial expertise means that the financial expertise owned by audit committees in Indonesia tends to be low. This result is not in

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accordance with Financial Services Authority Regulation Number 55 of 2015, which states that the audit committee must have at least one member with a financial background. Thus, there are still many companies that do not comply with this minimum regulation.

The audit committee's accounting expertise shows a minimum value of 0, a maximum of 3, and an average of 1,063. The average audit committee accounting expertise means that the accounting expertise owned by the audit committee in Indonesia has met the minimum standards contained in Financial Services Authority Regulation Number 55 of 2015, which states that the audit committee must have at least one member with an accounting background. Therefore, although there are still companies that have not fulfilled this regulation, the average company has followed it. The number of audit committee meetings shows a minimum value of 0, a maximum of 16, and an average of 5,76. The average number of audit committee meetings means that the meetings held by the audit committee in Indonesia have met the minimum standards set out in Financial Services Authority Regulation Number 55 of 2015, which states that the audit committee holds regular meetings at least once every three months or four times a year. Although there are still companies that have not fulfilled these rules, the average company has held more meetings than the minimum standards that have been determined.

Goodness-of-fit Test

The goodness-of-fit test is a pre-test in logistic regression. This test is conducted to test the fit of the data with the model. The test in the study assessed using the Hosmer-Lemeshow is explained in table 3

Table 3. Goodness-of-fit Test Result

Goodness-of-Fit Evaluation for Binary Specification
Andrews and Hosmer-Lemeshow Tests
Equation: UNTITLED
Grouping based upon predicted risk (randomize ties)

	Quantile of Risk		Dep=0		Dep=1		Total	H-L
	Low	High	Actual	Expect	Actual	Expect	Obs	Value
1	0,002	0,017	14	13,855	0	0,1450	14	0,147
2	0,017	0,030	14	13,653	0	0,347	14	0,356
3	0,030	0,060	12	13,346	2	0,654	14	2,905
4	0,060	0,091	12	12,899	2	1,101	14	0,796
5	0,091	0,113	12	12,611	2	1,390	14	0,298
6	0,113	0,191	12	11,963	2	2,038	14	0,001
7	0,219	0,257	12	10,824	2	3,176	14	0,562
8	0,257	0,257	14	10,396	0	3,604	14	4,853
9	0,257	0,335	9	9,787	5	4,214	14	0,210
10	0,376	0,638	6	7,433	9	7,567	15	0,547
		Total	117	116,766	24	24,234	141	10.676

H-L Statistic	10,676	Prob. Chi-Sq (8)	0,221
Andrews Statistic	46,919	Prob. Chi-Sq (10)	0,000

Source: Processed data, 2023

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Prob (H-L Statistic) has a value of 0,221 (>0,05) indicating the model in this study has no difference between the data and the model, so it can be concluded that the model in this study is fit.

Model Accuracy Test

The model accuracy test is conducted to show how well the model predicts and as a measure of model accuracy. This test is seen from the expectation-prediction evaluation table. The model accuracy result described in table 4, as follows:

Table 4. Model Accuracy Test Result

Expectation-Prediction Evaluation for Binary Specification
Equation: UNTITLED
Success cutoff: C = 0.5

	Estimated Equation			Constant Probability		
	Dep=0	Dep=1	Total	Dep=0	Dep=1	Total
P(Dep=1) <=C	116	16	132	117	24	141
P(Dep=1)>C	1	8	9	0	0	0
Total	117	24	141	117	24	141
Correct	116	8	124	117	0	117
% Correct	99,15	33,33	87,94	100,00	0,00	82,98
% Incorrect	0,85	66,67	12,06	0,00	100,00	17,02
Total Gain*	-0,85	33,33	4,96			
Percent Gain**	NA	33,33	29,17			
	Estimated Equation			Constant Probability		
	Dep=0	Dep=1	Total	Dep=0	Dep=1	Total
E (# of Dep=0)	100,40	16,37	116,77	97,09	19,91	117,00
E (# of Dep=1)	16,60	7,63	24,23	19,91	4,09	24,00
Total	117,00	24,00	141,00	117,00	24,00	141,00
Correct	100,40	7,63	108,03	97,09	4,09	101,17
% Correct	85,81	31,79	76,61	82,98	17,02	71,75
% Incorrect	14,19	68,21	23,39	17,02	82,98	28,25
Total Gain*	2,83	14,77	4,86			
Percent Gain**	16,63	17,80	17,21			

*Change in "% Correct" from default (constant probability) specification
**Percent of incorrect (default) prediction corrected by equation
Source: Processed data, 2023

If the result in % Correct is close to 100%, then the use of models and variables is more accurate and correct. In this study, the results show the results of 85.81%, thus the models and variables in this study are accurate.

Z-Statistic Test

This hypothesis testing was carried out with EViews13 software. To see if the hypothesis accepted or not can be seen from the significance of the number on the Z-Statistic. This study uses a significance level of 0.05 (5%). The result of hypothesis test described in table 5, as follows

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Table 5. Hypothesis Test Result

Dependent Variable: Y
Method: ML - Binary Probit (Newton-Raphson / Marquardt steps)
Sample: 2020 2022
Included observations: 141
Convergence achieved after 6 iterations
Coefficient covariance computed using observed Hessian

Variable	Coefficient	Std. Error	z-Statistic	Prob.
C	0,353	0,329	1,073	0,283
X1	-0,683	0,272	-2,515	0,012
X2	-0,559	0,184	-3,041	0,002
X3	-0,111	0,046	-2,446	0,014
McFadden R-squared	0,177	Mean dependent var		0,170
S.D. dependent var	0,377	S.E. of regression		0,344
Akaike info criterion	0,808	Sum squared resid		16,181
Schwarz criterion	0,891	Log likelihood		-52,944
Hannan-Quinn criter.	0,842	Deviance		105,889
Restr. deviance	128,655	Restr. log likelihood		-64,328
LR statistic	22,766	Avg. log likelihood		-0,376
Prob (LR statistic)	0,000			
Obs with Dep=0	117	Total obs		141
Obs with Dep=1	24			

Source: Processed data, 2023

The results of hypothesis test on table 5 shows: The audit committee financial expertise variable gives a result of 0,012 (<0,05). Thus, the financial expertise of the audit committee has a negative significant effect on financial statement fraud. Therefore, H1 is accepted. (2) The audit committee accounting expertise variable shows a significance value of 0,002 (<0,05), so that the audit committee accounting expertise has a negative significant effect on financial statement fraud. So, H2 is accepted. (3) The variable number of audit committee meetings shows a significance value of 0,014 (<0,05), so that the number of audit committee meetings has a negative significant effect on financial statement fraud. Therefore, H3 is accepted.

The value of McFadden R-squared shows the ability of the model in the study to explain the dependent variable. In this study, McFadden R-squared shows a value of 0,177. This number indicates that the independent variables in this study can explain the dependent variable by 17,7%, while the rest is explained by other variables outside the research model.

Discussion

Audit Committee Financial Expertise, and Financial Statement Fraud

The results showed that audit committee expertise had a negative and significant effect on financial statement fraud. This means that the more audit committees with financial expertise, the less financial statement fraud will occur. These results support agency theory, where the audit committee is intended to limit opportunistic reporting and safeguard the interests of shareholders (Badolato et al., 2014). Audit committees with financial expertise are able to better assess financial information and minimize information asymmetry between agents and principals, thereby reducing agency conflicts between the two.

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This result indicates that the audit committee with financial expertise is able to increase the effectiveness of the audit committee in supervising the company's financial reporting process. The audit committee will find it easier to assess the financial information presented by management and determine whether the information reflects the actual situation. The financial expertise owned by the audit committee will make management more careful in reporting the company's financial information and reduce the risk of fraud. Thus, the effectiveness of the audit committee as seen from the financial expertise possessed by the audit committee will reduce the likelihood of fraudulent financial statements.

In Indonesia, it is stated in the Financial Services Authority Regulation No. 55 of 2015 that the audit committee is expected to have at least 1 member with financial expertise. The audit committee must also understand the company's financial statements and business to fulfill its duties and responsibilities. This is related to the ability to assess the financial information presented by management, so as to ensure that the reports presented are in accordance with the actual circumstances. Thus, the interests of shareholders will also be protected. With these duties and responsibilities of the audit committee, investors must pay attention to the expertise owned by the audit committee in the company before making investment decisions. The audit committee's expertise allows investors to ensure the reliability of financial statements, the quality of management, and risk management by the company.

This result are in line with research by Abernathy et al., (2014) that the financial expertise of the audit committee can improve the quality of financial reporting and prevent financial statement fraud. The research is also in line with the results obtained by Khoufi and Khoufi (2018) who show that financial statement fraud tends to decrease when the audit committee has more financial expertise. The results also support the research by Mousavi et al., (2022), Badolato et al., (2014), and Abbott et al., (2004) who show that the financial expertise of the audit committee has a negative effect on financial statement fraud. On the other hand, the results of the study reject several research results which state that financial expertise has no effect on financial statement fraud (Dwiharyadi, 2017; Marzuki et al., 2019; Mclaughlin et al., 2021). This difference in results may be due to differences in measurement of the financial expertise variable as seen from educational background (Marzuki et al., 2019) and the use of financial statement fraud measurement through earnings management (Dwiharyadi, 2017).

Audit Committee Accounting Expertise, and Financial Statement Fraud

The results showed that the audit committee's accounting expertise had a negative and significant effect on financial statement fraud. This means that the more audit committee members with accounting expertise, the less financial statement fraud will occur. These results support agency theory, where audit committee supervision based on expertise will be able to provide tighter supervision on opportunistic behavior owned by management (Razali and Arshad, 2014). Audit committees with accounting expertise can review and ensure compliance with financial reporting standards. So, when management wants to take advantage of the asymmetrical information situation and use it to fulfill individual

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interests, the audit committee with accounting expertise will be easier to detect and protect the interests of shareholders. Thus, the accounting expertise of the audit committee can reduce the conflict of interest between management and shareholders.

These results indicate that the effectiveness of the audit committee as seen through accounting expertise is able to reduce the likelihood of financial statement fraud. Audit committees with accounting expertise are able to review and comply with the financial reporting process according to financial reporting standards more carefully and thoroughly. Therefore, financial reporting made by management will be scrutinized and monitored more thoroughly, so that if there is a deliberate error, the audit committee is able to detect it. Thus, the effectiveness of the audit committee as seen from accounting expertise is able to reduce the likelihood of financial statement fraud.

The ability of the audit committee to be able to review the compliance of the financial reporting process with financial reporting standards carefully and thoroughly can be achieved by the existence of accounting expertise. Financial Services Authority Regulation Number 55 of 2015 states that the audit committee must understand financial reporting standards and legal regulations. The accounting expertise owned by the audit committee will make the audit committee more scrutinize and be able to avoid management's opportunistic attitude in the financial reporting process. Thus, management will maintain its attitude and financial statement fraud will be minimized. Effective supervision by the audit committee will result in good quality financial reports, so that investors can assess the company according to the conditions that actually occur in the company before making investment decisions.

These results are in line with research by Krishnan and Visvanathan (2007) who found that accounting expertise will provide tighter supervision on financial reporting. This result also support research by Ghafran and O'Sullivan (2013) who state that accounting expertise will provide higher audit quality and produce higher quality financial reports. The result also supporting Dwiyanti and Astriena (2018) who found that audit committees that are proficient in accounting are more competent to find earnings management practices of a company that tend to lead to fraud. In addition, it also supports research by Chang and Sun (2009) and Nelson and Devi (2013) who prove that audit committee accounting expertise has a negative effect on financial statement fraud. However, this study rejects the results of research by Dwiharyadi (2017) and Beasley (1996) who found that there is no effect of audit committee accounting expertise on financial statement fraud. This difference in results may be influenced by differences in the use of measurement of financial statement fraud variables.

Audit Committee Accounting Expertise to Financial Statement Fraud

The results showed that the number of audit committee meetings had a significant negative effect on financial statement fraud. This indicates that the more meetings held by the audit committee, the less financial statement fraud will occur. These results support agency theory, where management who has its own interests and manipulates the financial statements will be detected by the audit committee

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through regular audit committee meetings (Razali and Arshad, 2014). During supervision of financial reporting, the audit committee will find findings, problems and risks faced by the company. This was conveyed at the meeting held by the audit committee, including potential conflicts of interest that exist in the company. Thus, the audit committee meeting will be able to reduce agency conflicts between management and shareholders.

This result shows that the effectiveness of the audit committee as seen through the number of meetings held by the audit committee is able to reduce the likelihood of financial statement fraud. This indicates that company risks and findings in the financial reporting process found by the audit committee which are discussed through meetings in order to be resolved more quickly are able to overcome financial statement fraud. An audit committee that meets regularly will make management more careful, because the audit committee will discuss anomalies and their suspicions at the meeting. So, if management commits fraud, the audit committee will find it faster. Thus, financial statement fraud will be reduced.

The number of audit committee meetings mentioned in the Financial Services Authority Regulation Number 55 of 2015 is at least once in three months or four times a year. The meetings discuss findings, company risks, potential conflicts of interest, and the financial reporting process. By conducting regular meetings, it will make the audit committee's supervision of the financial reporting process tighter. So, non-compliance or anomalies in the financial statements will be easily and quickly detected by the audit committee. Thus, the number of meetings held by the audit committee is able to increase the effectiveness of its supervision of management and reduce the likelihood of fraudulent financial statements. The number of audit committee meetings can be analyzed by investors before making investment decisions. Investors will get an overview of how well the audit committee supervises the company, especially the supervision of the financial reporting process.

The results of this study support research conducted in previous researchers who found that the more often the audit committee meets, the stricter the supervision will be carried out and the financial statement fraud in the company will decrease (Abbott et al., 2000; Anichebe et al., 2019; Nurliasari and Achmad, 2020; Razali and Arshad, 2014; Wiralestari et al., 2019). However, this result contradicts the research by Mclaughlin et al. (2021) and Sharma and Iselin (2012) who in contrast found a positive effect of the number of audit committee meetings on the perpetration of fraudulent financial statements. The difference in results can be caused by the measurement of the financial statement fraud variable.

Conclusion

The results of this study prove that the audit committee effectiveness proxied by audit committee financial expertise, audit committee accounting expertise and the number of audit committee meetings affect financial statement fraud. This indicates that the more financial expertise, accounting expertise, and the number of meetings in the audit committee will lead to better supervisory effectiveness and reduce the likelihood of financial statement fraud. Thus, to reduce

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the likelihood of fraudulent financial statements, companies must pay attention to the composition and effectiveness of the audit committee.

Limitation

The limitation of this study is the small sample size which is influenced by the number of companies that do not present annual reports on the Indonesian Stock Exchange (IDX) and the company's website properly. In addition, the R-squared value in this study tends to be small.

Suggestions

Future research is expected to seek companies that present annual reports and company data consistently on the Indonesia Stock Exchange (IDX) and the company's website. Researchers may also consider other variables that may affect the effectiveness of audit committee monitoring, such as the busyness of the audit committee, audit independence, and audit tenure.

Implication

This study makes a theoretical contribution to agency theory. The findings in this study are able to prove that an audit committee that carries out its duties and responsibilities effectively will be able to overcome agency conflicts and minimize financial statement fraud. This study also provides implications for regulators to develop policies regarding audit committee work guidelines related to the obligation of audit committee members to have expertise in finance and accounting, as well as the number of meetings that must be fulfilled as the effectiveness of the audit committee in carrying out its duties. The implication for investors is that before making investment decisions, it is hoped that investors can analyze the structure of the audit committee in the company. This analysis aims to provide insight and ensure the reliability of financial statements, how the company deals with the risks faced, and how the company protects investors.

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