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Financial Statement Fraud Analysis: Financial Stability, External Pressure and Auditing Quality

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ABSTRACT

Fraudulent on financial statements is increasing nowadays. The impact is not only felt by investors but also affects global economic stability. This research aims to collect empirical data to determine whether financial stability, external pressure, and audit quality partially and simultaneously influence financial statement fraud. The research objects are companies from the property and real estate sector listed on the Indonesia Stock Exchange, in 2020-2022. Multiple regression analysis was used to test the hypothesis on this research's panel data. The results of data processing indicate that external pressure has a positive effect on financial report fraud, while audit quality and financial stability do not influence financial report fraud.

Keywords: Financial Stability, Audit Quality, External Pressure, Fraudulent Statement Reporting.

ABSTRAK

Penipuan laporan keuangan semakin meningkat saat ini. Dampaknya tidak hanya dirasakan investor tetapi juga mempengaruhi stabilitas perekonomian global. Penelitian ini bertujuan untuk mengumpulkan data empiris untuk mengetahui apakah stabilitas keuangan, tekanan eksternal, dan kualitas audit berpengaruh secara parsial dan simultan terhadap kecurangan laporan keuangan. Objek penelitiannya adalah perusahaan sektor properti dan real estate yang terdaftar di Bursa Efek Indonesia pada tahun 2020-2022. Analisis regresi berganda digunakan untuk menguji hipotesis pada data panel penelitian ini. Hasil pengolahan data menunjukkan bahwa tekanan eksternal berpengaruh positif terhadap kecurangan laporan keuangan, sebaliknya kualitas audit dan stabilitas keuangan tidak memiliki pengaruh terhadap kecurangan laporan keuangan.

Kata Kunci: **Stabilitas Keuangan, Kualitas Audit, Tekanan Eksternal, Kecurangan Laporan Keuangan**

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Introduction

Fraud in companies has caused losses to various interested parties. Fraud will be difficult to eliminate when society can accept wrong behavior and is willing to make peace and accept it (Xu et al., 2017). The cause of fraud is an important thing that company have to settled (Maulidi & Ansell, 2020). According to a survey conducted by the Association of Certified Fraud Examiners (ACFE, 2020), financial statement fraud is the type of fraud that causes extraordinary losses to the organization.

However, detecting financial statement fraud issues is complicated task. Cases of fraud in financial reporting involving big corporation and public accounting firms have occurred. The biggest cases ever occurred comprehend the Enron Corporation and the public accounting firm Arthur Andersen. Enron is one of the largest corporations in the energy sector. Disregarding Enron, there are various international corporations embroiled in financial cases such as World Com, Xerox, Merck, Tyco and Walt Disney. . In Indonesia, cases of fraud in financial reporting occurred at Lippo Bank and Kimia Farma companies which also involved public accounting firms.

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Kusumawardhani (2013) stated that special attention must be paid to fraudulent financial reporting behavior thus fraud can be detected and even eliminated. The development of a method for detecting financial report fraud by Skousen et al., (2008) called the fraud triangle. Skousen et al., (2008) stated that the fraud triangle theory is useful to detect fraudulent financial reporting. Various factors causing fraud are grouped into three causal factors, including (1) pressure, (2) opportunity and (3) rationalization.

Prior research by Skousen et al., (2008) stated that the element in fraud triangle framework cannot be observed directly, but need to be developed and proxies for their measurement. Rationalization is the last element of the fraud triangle, and also the most challenging element to measure in detecting fraud. The important role of financial reports is in the context of decision making for interested parties. In this case, the auditor's role is as a party who provides opinions and confidence regarding the fairness of the company's financial statements. Auditing of financial reporting provides assurance that the financial reports do not have material misstatements and provide an opinion on the fairness of the accountability given by management for assets in the Company (Koroy, 2008).

Insights from previous research studies about fraud theory models in financial statement fraud. Study by Mekonnen et al., (2015) argue that fraud is committed if someone has the intention and opportunity to commit a criminal act. Execute a fraud requisite ability and there will consistently be a legitimize for the perpetrator of the fraud. Stated another way, the factors cause fraud proposed by Mekonnen et al., (2015) used to detect the fraud in a company. Moreover, Study conducted by Vousinas, (2019) shows that the most significant element caused someone to commit fraud is ego. In the the fraud pentagon it is defined as arrogance.

Phenomenon related to fraudulent financial reporting occur in property and real estate sectors company. One of the cases involved PT Bakrieland Development, Tbk in 2019. PT Bakrieland Development Tbk did not record long-term liabilities. The company was warned by the Indonesian Stock Exchange (BEI) for failing to report its financial reports in 2018 and not paying the late fines that had to be paid. Finally, the IDX decided to stop trading in ELTY shares and increase the fine of IDR 150 million. Other case, state-own enterprises, PT Waskita Karya, Tbk had manipulation of financial report in 2009. Company recorded Rp 1 trillion contract as revenue and acknowledge the projects had been completed. However, it was only Rp300 billion completed (Rahadiana, 2009).

PT Hanson International Indonesia, which is also part of the property and real estate sector, has been involved in a case of manipulating financial reports. The Financial Services Authority in its statement stated that PT Hanson International was proven to have manipulated the 2016 financial statements. During the examination it was found that irregularities in presentation were related to the sale of plots with a gross value of IDR 732 billion which caused a sharp increase in PT Hanson International's income. Therefore, PT Hanson International Tbk was given a sanction by the OJK of IDR 500 million and an order to redraw the 2016 financial statements.

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The large number of these case phenomena indicates that fraudulent financial reporting is increasing in occurrence in property and real estate sectors companies. The auditor as an independent party must consider several factors regarding the possibility of fraud in the Company's financial reporting. Therefore, detection of fraudulent financial reporting should be prevented.

Previous studies have discussed financial statement fraud. In research conducted by Ahmadiana, N.S.S., Novita (2018), Herdiana, R. & Sari (2016), Tessa, C. G., & Harto (2016), Aprilia (2017), Chantia et.al., (2021) financial stability proven capable of predicting opportunities for companies to commit fraud in financial reporting. However, Ulfah et al., (2020) deny this, the results of their research showed that financial stability has no effect on fraud in financial reporting.

Furthermore, external pressure has a significant negative effect on financial report fraud, which means that the more the company's needs are met, the lower the indication of financial report fraud. This is proven in research by Norbarani & Rahardjo (2012), Agustina & Pratomo (2019), Chantia et.al., (2021), Tessa, C. G., & Harto (2016), and Anggraini, W.R., Suryani (2021). However, research by Herdiana, R. & Sari (2016) states that external pressure has no effect on detecting financial statement fraud.

This research focuses on analyzing factors that influence fraudulent financial reporting. Based on existing research phenomena and inconsistencies, the main problem in this research can be formulated as follows: Do variables in the form of financial stability, audit quality and external pressure partially or simultaneously influence financial statement fraud? How to analyze the influence of financial stability variables, audit quality and external pressure on financial statement fraud. Based on cases fraudulent action in financial reporting This research focus on property and real estate sector

For this reason, the aim of this research is to test and analyze:

1. How does financial stability affect financial statement fraud?
2. How does audit quality influence financial statement fraud?
3. How does external pressure influence financial statement fraud?

Literature Review

According to the American Institute Certified Public Accountants (AICPA, 2002) fraud is negligence or deliberate action resulting in misleading material misstatements in financial statements. Meanwhile, according to Anthony & Govindarajan (2001) states that fraud is a misstatement of material facts and is committed by one party to another party with the aim of deceiving, which can harm interested parties. Meanwhile, according to Elliot & WillinghM (1980), it shows that financial statement fraud is the same as management fraud where financial statement fraud is carried out deliberately by managers which can cause losses for investors and creditors. The definition above shows that fraud has a broad definition as can be seen from several categories of fraud. Anthony & Govindarajan (2001) show that based on case law, fraudulent acts must comply with five conditions such as: (1) misstatement, (2) material facts, (3) intent, (4) justifiable reliance, and (5) damage or loss.

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In agency theory, a cooperation contract between two or more individuals, business owners or stockholders which mandates another party, namely the agent or management (Jensen & Meckling (1976), to provide services to the owner and gives authority to the agent to make the best decisions to the owner, but company management on the other hand also wants to maximize their welfare. With supervision by the owner and management by parties who understand how to run a business, the agency relationship must be able to increase the value of the company. However, what happens is the opposite, management can use authority This is solely to maximize their interests.

The fraud triangle is an idea about the causes of fraud, first demonstrated by Cressey (1954). This research was conducted in the field of social psychology, starting from a model that explains three elements that cause fraud. This theory was carried out through a interviews series with 113 people who had been sentenced to embezzlement of company money called "breach of trust". The model is explained in terms of the fraud triangle, where each one signifies represents pressure, opportunity and rationalization. This model explains fraud in a holistic way. Generally, public accountant has become use this model as a tool to understand the risk factors someone to commit financial fraud. The first elements is pressure, which can be divers, including lifestyle, economic demands and others someone has pressure to commit fraud. The second element is opportunity, it is an opportunity that can trigger fraud. Opportunities appear because fraudsters believe that their activities will not be discovered. Opportunities can occur due to weak internal controls such as lack of supervision from management. Skousen et al., (2008) stated that the last factor is rationalization, which is a component of the fraud triangle as the most challenging to measure. Rationalization is closely related to a person's personality and character. This is an important element of deception, where the creators seek justification for their actions.

Financial stability

Financial stability is the result of the company's efforts to maintain or maintain the stability of the economic condition of the company. A relatively fine financial reporting condition will entice the attention of investors and the public in general. If problems arise with financial stability, management of the company will try to make financial conditions look better. This condition can pressure management to carry out various methods, including cheating in financial reports. According to SAS N0.99 (AICPA, 2002), when economic, industrial and other conditions threaten the financial stability and profitability of a company, managers are under pressure to commit fraud and manipulate financial reports.

Companies with better financial stability are less likely to engage in fraudulent earnings reporting practices. In other words, companies with good financial stability will ideally be able to prevent themselves from manipulating profits in their financial reports. Research on the relationship between financial stability produces a positive relationship with financial statement fraud (Kurniawan & Trisnawati, 2021). According to (Loebbecke et al., 1989) management will manipulate financial reports if business growth is below the

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industry average. Ahmadiana, N.S.S., Novita (2018) shows that financial stability influences financial statement fraud. Chantia et.al., (2021)also show that stressed management will commit fraudulent financial reporting due to unstable financial conditions. Research by Anggraini, W.R., Suryani (2021) states that financial stability has no effect on the practice of fraudulent financial reporting. So management resorted to fraud to cover up poor financial conditions. Meanwhile, according to Norbarani & Rahardjo (2012) there is no significant influence between financial stability and financial statement fraud.

H1: Financial stability influences financial statement fraud

Audit quality

A financial report audit is an activity to ensure that the financial reports presented are free from errors and prepared in accordance with generally accepted accounting standards and principles. Ultimately, the audit results ensure that interested parties in the company and users of financial reports will not be harmed by the audit results. According to Andriani & Nursiam (2017) audit quality is defined as the auditor's ability to find and report errors in the presentation of financial reports as well as violations of the accounting methods applied (DeAngelo, 1981). According to Alim et al., (2007), audit quality is when the auditor can guarantee that there are no mistakes or errors and fraud in financial reporting and that the audit results are disclosed independently.

Audit is an element or part that creates efficiency in the capital market. Audits can also increase the credibility of financial information and create better corporate governance. Audit quality can be assessed by the external auditor who carries out the audit process. The quality of the auditor's audit depends on whether the auditor complies with the Public Accountant Professional Standards (SPAP) and is able to assess the client's business risks Alim et al., (2007). Auditors who are members of the Big4 are considered more trustworthy in carrying out the process of examining financial reports.

Research by Bloomfield & Shackman (2008) found a positive relationship between auditor quality and the restatement of company financial reports, where the results showed that with the presence of Big 4 auditors, good quality auditors were able to provide good results in the restatement of audited financial reports. Palmrose (1988) research results found that big 8 auditors had higher audit quality than non-big 8 auditors in detecting fraud and conveying their opinions in the auditor's report.

H2: Audit quality influences financial statement fraud

External pressure

Efforts to fulfill third party expectations are a form of external pressure on management (Skousen & Kevin, 2015). Funding for operations is a third-party type of company. When a company's performance is poor, there will be a decrease in the flow of incoming funds. However, when the inflow of funds increases, management will be more responsible because it must meet the expectations of third parties by explaining the company's conditions as best as possible. To remain competitive, businesses require external sources of financing or additional

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debt. This can cause management to manipulate earnings. Research on external pressure influencing financial report fraud was conducted by Skousen & Kevin, (2015) and Noor et al., (2015).

External pressure is a condition when management faces meeting the requirements or expectations of third parties. According to Skousen et al., (2008), managers may perceive pressure to obtain additional equity or debt financing to keep the company competitive. On the other hand, the company is required to pay the debt it has taken. A company is considered capable of repaying debts if its business runs smoothly and does not experience losses. Companies with high leverage ratios have large debts and high credit risk. Company management often reports high profitability because the Company has a lot of debt. Therefore, the Company committed fraud in financial reporting by increasing the Company's profits.

External pressure is one of the factors faced by management in the financial reporting process (Skousen & Kevin, 2015). External pressure comes from funding for business activities from third parties. When a company's performance is poor, there will be a decrease in the flow of incoming funds. However, when the inflow of funds increases, management will be more responsible because it must meet the expectations of third parties by ensuring good conditions for the company. To remain competitive, businesses require external sources of financing or additional debt. This can cause management to manipulate earnings. According to (Skousen & Kevin, 2015) and Noor et al., (2015), this external pressure causes management to tend to commit fraud in the company's financial reporting. So the research hypothesis can be described as follows:

H3: External pressure influences financial statement fraud

Research Method

This research is a causative panel research. This research seeks to explain the influence of financial stability, audit quality and external pressure on detecting fraudulent financial statements. Since the development of property and real estate sectors in Indonesia tends to increase. The research sample of this study was selected companies listed on the IDX in the property and real estate sector for the 2020-2022 period. The criteria of chosen sample based on the reports By ACFE stated that the property and real estate sectors have a high tendency to conduct fraud in financial reporting (ACFE, 2018). The sampling technique was carried out using a purposive sampling method with a sample of companies that met predetermined criteria.

This research consists of 4 (seven) variables, namely one dependent variable and 3 independent variables. The definition and operation of each variable will be explained in detail as follows.

Dependent Variable

The dependent variable in this research is financial statement fraud which can be measured using the fraud score model. Where the variable components in the F-Score are accrual quality and financial performance. According to Rini &

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Achmad (2012) the sum of these two components can well predict the risk of financial statement fraud, so the model can be formulated with the following equation

F-Score = Accrual Quality + Financial Performance

Accrual Quality can be proxied by RSST Accrual which can describe all non-cash and non-equity changes in a company's balance sheet. According to Hugo (2019) RSST Accrual can be calculated using following equation:

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

Information:

WC (Working Capital) = (Current Assets – Current Liabilities)

NCO (Non-Current Operating) = (Total Assets – Current Assets – Investment and Advances) – (Total Liabilities – Current Liabilities – Long Term Debt)

FIN (Financial Accrual) = (Total Investment – Total Liabilities)

ATS (Average Total Assets) = (Beginning Total Assets + End Total Assets) /2

Independent Variable

Financial Stability explains the financial condition of a company where a company with a stable condition is assessed by the asset change ratio.

Measurement: (Total Assets.t - Total Assets.t-1): Total Assets

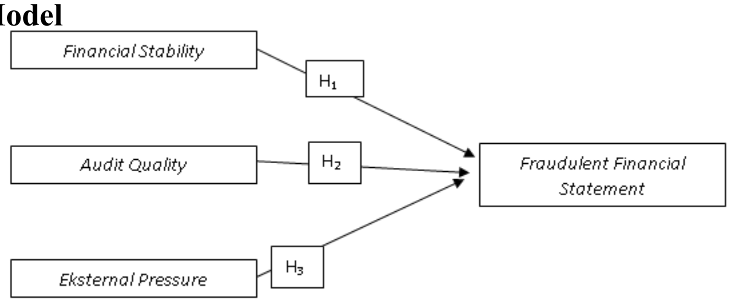
Audit Quality represented by the auditor's reputation. Big Four auditors are considered to produce higher audit quality than non-Big Four auditors

Measurement: Using dummy 1 for companies audited by big four auditors and 0 if the company is audited by a non-Big Four auditor

External Pressure represented by leverage or the comparison between total debt and total assets.

Measurement: Leverage: Total debt/total assets

Research Model



To analyze and test the data obtained, this research began with descriptive statistical analysis, classical assumption testing, and hypothesis testing. Then, for statistical analysis the mean and standard deviation are used.

The analysis technique used in this research is multiple linear regression which consists of one dependent variable and three independent variables:

FSCOREt = β0 + β1FinSta + β2AUDQUA + β3EXTPRES + εi

Information:

ß0 = Regression constant coefficient

ß1,2,3 = Regression coefficient for each variable

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FSCOREt	= Accrual Quality
FINSTA	= Financial Stability
AUDQUA	= Audit Quality
EXTPRES	= External Pressure
ε	= Error

Result and Discussion

Table 1. Regression Coefficient Variable

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	-49361333.352	93434051.539		-.528	.041
	X1	-275037956.101	605491034.634	-.087	-.454	.653
	X2	269649426.656	202251407.777	.870	1.333	.354
	X3	-89279699.553	83839703.967	-.202	-1.065	.043

a. Dependent Variable: Y

The influence of financial stability on financial statement fraud

The results of the hypothesis test show a coefficient value of negative 0.087 with a significance of 0.653, so it is found that financial stability has no effect on financial statement fraud. This shows that when the condition of a company's assets is stable, the possibility of financial statement fraud occurring will be less.

The results of this research correspond with the study by Adnovaldi, Y & Wibowo (2019). Companies that achieved high profits in the previous period will see increased profitability in the following period. The study conducted by Wahyuni, (2014) also shows the similar results. Consequently, management does not need to feel pressured when the company's targets are set at higher levels. The paper stated that Substantial earnings can drive up stock prices. If earning high, investors believe the stock price is also high. Therefore, it implies that the dividend payment will increase. Management avoids setting an excessively high profit target to prevent dividend payments from being excessively high.

Information about the company will spread quickly due to the increase in company assets which also attracts public attention. Companies that have increasing assets will gain the trust of the government, society, investors and creditors in the hope of obtaining a high rate of return (Solechan, 2009). Companies will be more careful in reporting the Company's financial condition in their financial reports. Therefore, the company will maintain its reputation by reducing practices related to earnings management, so that the public does not know about the company's fraudulent practices. The company will continue to improve its image to ensure that the information disseminated is reliable and encourages investors to invest.

The research results are in line with research by Lou & Wang (2009), Chtourou et al., (2001), Norbarani & Rahardjo (2012). However, research Skousen et al., (2008) and Rusli, (2009) shows that management performance is

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influenced by changes in company assets. When the company's average growth is lower than the industry average, managers tend to commit financial report fraud, but this research obtained different results. The research results show that managers do not manipulate financial reports to improve the company's financial condition. The research results are in accordance with Loebbecke et al., (1989). According to the manager, the act of manipulating financial reports will worsen the company's financial condition in the future.

The influence of audit quality on financial statement fraud

The table testing the effect of audit quality on fraudulent financial reporting shows a significance value of 0.354, with a beta value of negative 0.870. Therefore, hypothesis H2 is rejected. This means that audit quality has no influence on financial statement fraud.

The results of research conducted by Tsipouridou & Spathis, (2012) and Yasar, A., (2013) show that there are no significant differences between companies audited by BIG4 and non-BIG4 auditors in terms of fraud or earnings management. Large public accounting firms will not be better than smaller accounting firms if they do not provide opinions independently. The Enron Andersen case, for example, shows that KAP Anderson, when he was Enron's auditor, worked in a leading accounting firm and on a large business scale. However, the audit of Enron was not carried out independently.

The use of BIG4 and non-BIG4 KAPs still needs to be considered as a measurement of audit quality. The use of BIG4 and non-BIG4 KAPs as audit quality measurements has an effect that is not much different as a proxy for audit quality audit (Lawrence et al., 2011). In Indonesia, the case that occurred at PT Sunprima Nusantara Pembinaan (SNP) Finance, where the financial report was audited by KAP Deloitte (KAP BIG4), presented financial reports that were not in accordance with the actual situation of the company. There were indications that KAP had made negligence when auditing the financial statements of the Columbia Group subsidiary company (CNBC Indonesia, 2018). Therefore, BIG-4 KAP cannot be a guarantee that there will be better audit quality compared to non-BIG4 KAP.

The influence of external pressure on financial statement fraud

The hypothesis test shows that the coefficient value of the external pressure variable is positive 0.202 with a significance of 0.043. So, it can be concluded that external pressure has a negative impact on financial statement fraud. The more external pressure a company experiences, the greater the possibility that the company will commit fraudulent financial statements. When the company lacks cash, it faces pressure to secure external financing, which may lead it to engage in fraudulent financial reporting to ensure the financing gets approved. The results of this study corroborate research conducted by Skousen et al., (2008), (Sari S.T, 2016), Widarti (2015), Tiffani (2015).

Excessive pressure on management to meet the requirements or expectations of third parties is called external pressure. According to SAS No. 99, financial statement fraud may occur when there is excessive external pressure on

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company management. Skousen et al., (2008) stated that one of the challenges that business operations often face is the need to obtain additional debt or external sources of financing so that the company remains competitive, including financing for capital expenditures and research and development Persons, (1999) stated, high leverage (LEV) is associated with the possibility that the company will violate credit agreements and a lower chance of obtaining a loan to obtain additional capital. Lou & Wang (2009) strengthens this statement by saying that when a company faces external pressure, the risk of financial reporting misstatements will be higher.

Conclusion

From the analysis that has been carried out, it can be concluded that financial stability has no influence on fraudulent financial statements. Apart from that, it was found that audit quality had no influence on financial statement fraud and external pressure had a negative effect on financial statement fraud.

Limitation

The limitation of this study had only used data obtained from IDX in the period 2020-2022. This limits other sources of information that might be useful in finding the influence of company commit fraud in financial reporting. The existence of an ethics committee in the company that can mitigate the existence of fraud. This research only looks at the behavior of fraudulent financial reports of companies only in the property and real estate sectors.

Suggestions

From the research that has been conducted, future research would be better to consider using other model such as fraud hexagon. Apart from that, further research could use samples from other industrial sector company and extend the observation period beyond 2022 to remove potential bias. Regulators, in this case the government, are also advised to assess the best policies for the interests of users of the Company's financial reports.

Implication

It is hoped that the research results can be used as consideration for stakeholders of in property and real estate sectors company in making decisions because there are several factors that cause companies to commit financial report fraud. This study may give reference for investors, academics, companies, auditors and the government. Investors and users of financial reports are expected to better understand and analyze the factors that cause fraudulent financial reporting before deciding to invest, because high financial targets in a company are likely to cause fraud. Auditors can be more careful in providing audit opinions regarding financial reports to avoid several frauds that are difficult to detect. Apart from that, companies need to consider when committing financial report fraud. This is because fraudulent financial statements have a negative impact on company value.

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