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The Effect of Hexagon Fraud on the Potential Fraud Financial Statements with the Audit Committee as a Moderating Variable

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ABSTRACT: This study aims to obtain empirical evidence of the influence of the six elements of fraud hexagon theory on potential financial statement fraud by involving the audit committee which acts as a moderating variable in the financial statements of state-owned companies listed on the Indonesia Stock Exchange in 2016-2020. Potential financial statement fraud is measured using the f-score model. The research sample was obtained by the purposive sampling technique. Data analysis methods and techniques include descriptive statistics, evaluation of the SEM-PLS model, and hypothesis testing. The results show that financial pressure has a positive effect on potential financial statement fraud, effective monitoring has a negative effect on potential financial statement fraud, while related party transactions, CEO education, CEO narcissism, and political connection do not affect potential financial statement fraud. The role of the audit committee as a moderating variable is only able to weaken the relationship between financial pressure and potential financial statement fraud.

KEYWORDS: Fraud Hexagon Theory, Financial Statement Fraud, Audit Committee

INTRODUCTION

Financial reports are a medium of communication between management and several stakeholders, such as shareholders, customers, suppliers, employees, and the government. The financial statements present financial information and the condition of the company that is used as a basis for making decisions by stakeholders. Based on the agency theory proposed by Jensen & Meckling (1976) explains the relationship between management and shareholders, where management acts as an agent and shareholders act as principals or owners of the company. Opportunistic attitudes, agency conflicts, and management bonus schemes based on the company's financial performance motivate management to commit financial statement fraud.

The Association of Certified Fraud Examiners (ACFE) Indonesia Chapter conducted the Indonesia Fraud Survey in 2016 and 2019. The fraud survey was grouped into three groups of cases, namely corruption, misappropriation of assets, and fraudulent financial statements. The survey results showed that cases of financial statement fraud increased from 2% to 9.2%. Corruption cases have increased from 67% to 69.9%. Meanwhile, cases of asset misappropriation decreased from 31% to 20.9%. Cases of fraudulent financial statements have increased significantly, which is as much as four times.

Cases of fraudulent financial statements in Indonesia often occur from State-Owned Enterprises (BUMN). Several cases of fraudulent financial statements of state-owned companies, namely PT Kimia Farma in 2002 (Tempo, 2003), PT Waskita Karya in 2009 (Tempo, 2009) and 2018 (Tribun News, 2020), PT Timah in 2015 (Oke Finance, 2016), PT Garuda Indonesia in 2019 (CNN Indonesia, 2019) and PT Asuransi Jiwasraya in 2020 (Oke Finance, 2020). Fraudulent financial statements result in material and non-material losses. Based on the results of the 2019 Indonesia Fraud Survey from the ACFE Indonesia Chapter, several organizations experienced material losses. The most losses were borne by government organizations of 48.5% of the total material losses, the second-largest loss was borne by state-owned enterprises (BUMN) at 31.8%, the third-largest loss was borne by private company organizations by 15.1%, then institutional organizations non-profit that bear a loss of 2.9%, and finally other organizations with a total loss of 1.7%. The consequences arising from fraudulent practices are not only in the form of material losses but in the form of non-material losses. Practitioners or academics, begin to question the credibility of a company's financial statements and the performance of a Public Accounting Firm. The chain of trust that is being built among economic actors is slowly being eroded.

The fraud triangle theory proposed by Cressey is the first point of view to detect the implementation of fraudulent financial statements. There are three angles to the fraud triangle that are the cause of fraudulent practices, namely pressure, opportunity, and rationalization (Skousen et al., 2008). The second theoretical development was carried out by Wolfe and Hemerson in 2004 by expanding the scope of elements, namely capability. The second theory consists of four elements and is referred to as the fraud diamond theory (Wolfe & Hermanson, 2004). The third theory development was carried out by Crowe Horwath in 2011 by changing the capability element to competency and adding an arrogance element. The third theory consists of five elements and is referred to as the fraud pentagon theory (Horwarth, 2011). The latest theoretical development was carried out by Vousinas in 2019 by Replacing the elements of pressure and arrogance into stimulus and ego and adding one element, namely collusion. The latest theory consists of six elements and is referred to as the fraud hexagon theory, this theory is also referred to as the S.C.C.O.R.E Model (Vousinas, 2019). This study uses the fraud hexagon point of view in detecting fraud in financial statements.

The risk of financial statement fraud can be minimized through internal control. The role of the audit committee is expected to be an element of optimal internal control to create an effective company internal control system to prevent various frauds, especially financial statement fraud. This statement is reinforced by the research of Handoko & Ramadhani (2017); Kamarudin & Ismail (2014); Prasetyo (2014) who tested the effect of audit committee attributes on the risk of financial statement fraud. The existence of an audit committee in a BUMN company is regulated in Law No. 17 of 2003 concerning BUMN Article 70 which states that the board of commissioners and the supervisory board of BUMN are obliged to form an audit committee. This study involves the role of the audit committee as a moderating variable in the direct relationship between elements of the fraud hexagon theory and the potential for fraudulent financial statements.

Referring to the results of the ACFE survey, cases of financial statement fraud from state-owned companies, several previous studies, and the fraud hexagon theory, the researchers are interested in researching the effect of the six elements of the fraud hexagon theory on the potential for fraudulent financial statements with the audit committee as a moderating variable. The research contributions consist of four contributions. First, the use of the latest fraud detection theory compared to previous fraud detection theories, namely the fraud hexagon theory by Vousinas (2019). Second, using the related party transaction indicator on the rationalization element according to the suggestion of Hasnan et al. (2013). Third, using the CEO education indicator on the capability element following the advice of Abdullahi & Mansor (2015) by considering the nature of the capability element inherent in management, so that capability can be measured using the characteristics of the CEO. Using the measurement of the Audit Committee Financial and Accounting Expertise (ACFAE) to measure the audit committee variables, because based on OJK Regulation No. 55/POJK.4/2015 the audit committee is tasked with assisting the supervisory system of management when presenting the company's financial statements so that audit committee members must have financial and financial expertise. accounting to carry out the supervisory function.

LITERATURE REVIEW

Agency theory explains that shareholders as company owners (principals) do not manage the company's business directly, but delegate business management tasks to management (agents) (Jensen & Meckling, 1976). Management manages the company's business in the interests of the shareholders, and management must be able to account for the tasks delegated by the shareholders. The desire to get high returns from investments that have been invested (return on investment) is in the interests of shareholders (principals). The principal also has an obligation to the agent namely, to provide financial compensation for his work in managing the company's business. This difference in interest is the origin of the conflict of interest.

Financial statements are the result of a series of accounting processes that are prepared and presented by management as a form of accountability to shareholders (Astuti et al., 2019). The company's financial statements are a source of information that can reflect the financial condition and performance of the company in a certain period (Trisanti, 2020a). Meanwhile, according to The Association of Certified Fraud Examiners (ACFE) fraud is an unlawful act that aims to manipulate and present untrue reports or other actions carried out by executors inside or outside the organization for their interests or the interests of certain groups with full awareness and resulting in losses. either directly or indirectly. So that financial statement fraud according to the American Institute of Certified Public Accountants (AICPA) is a deliberate act to omit material facts, presenting accounting data that plunges users of financial statements so that it can affect the judgment of users of financial statements when making decisions.

This study examines the effect of the six elements of the fraud hexagon theory Vousinas (2019) on the potential for fraudulent financial statements involving the audit committee as moderation. Fraud hexagon theory is also called S.C.C.O.R.E Model, which is an acronym for stimulus, capability, collusion, opportunity, rationalization, and ego. Stimulus is another term for pressure which is representative of the pressure experienced by someone until that person commits fraud. Capability is a person's ability to know which area opportunities and conditions are like being able to commit fraud. Collusion is an agreement between two or more parties who agree to harm a third party, such as an act of fraud on the rights of the third party. Opportunity is an opportunity for certain individuals or groups to commit fraud that can be detected through general information and technical skills. Rationalization is the attitude of someone who justifies the act of cheating before the person commits fraud through the office and how to commit fraud as consideration. Ego is another term for arrogance, which is an attitude of superiority to other people and/or to situations so that they feel that the rules in the environment do not have to be obeyed.

The audit committee is a form of supervision effort so that the company's internal control and internal audit are carried out properly, to prevent and reduce the potential for fraudulent financial statements. The audit committee is part of the board of commissioners whose task is to assist the supervision of the board of commissioners on the financial reporting implementation system to the presentation of the company's financial statements (Ika & Mohd Ghazali, 2012). The audit committee is expected to be able to reduce improper accounting measurements and management fraud (Trisanti, 2020b).

HYPOTHESIS DEVELOPMENT

Financial Pressure on Stimulus Elements Affects Potential Financial Statement Fraud

The financial pressure experienced by management was created because the company set targets too high. The company's financial performance will be considered good by stakeholders if the financial targets set by the board of directors can be met, therefore management will work as effectively and efficiently as possible. Based on agency theory Jensen & Meckling (1976) explains that if management succeeds in achieving the set targets, shareholders will appreciate management's performance by giving bonuses. Return on Assets (ROA) is a measure of operating performance that is useful for assessing management performance in determining management compensation (Skousen et al., 2008). However, this compensation calculation mechanism is often misused by management. Lokanan & Sharma (2018); Ozcelik (2020) proved that financial pressure measured using the ROA ratio proved to have a positive relationship with financial statement fraud. Based on this explanation, the researcher formulated the first hypothesis, namely:

H_1: Financial pressure has a significant positive effect on potential financial statement fraud

Effective Monitoring on Opportunity Elements Affecting Potential Financial Statement Fraud

The effective monitoring system implemented by the company will help management to achieve optimal performance because management knows that the tasks carried out as agents are always supervised by shareholders as owners of the company. So that an effective monitoring system will prevent and reduce opportunities for management to commit fraud. One of the efforts to create an effective supervisory system is to establish a board of commissioners that includes independent commissioners. Independent commissioners are tasked with monitoring the performance of the company's management. So, the ratio of the number of independent commissioners (BDOUT) can be used to measure effective monitoring. Kusumawardani (2018); Lokanan & Sharma (2018) prove that effective monitoring as measured by the number of independent commissioners has a negative relationship with financial statement fraud. Based on this explanation, the researcher formulated the second hypothesis, namely:

H_2: Effective monitoring has a significant negative effect on potential financial statement fraud

Related Party Transaction on Rationalization Element Affects Potential Financial Statement Fraud

Rationalization is a view that views unethical actions as fair, including financial statement fraud. Management often views transactions with related parties as internal transactions (still in one entity). So that management often rationalizes fraudulent actions in related party transactions. This study focuses on related-party sales transactions because they are complex transactions, the main transaction being one of the largest items, and the most relevant to the value in the financial statements (Marchini et al., 2018; Rasmussen, 2013). Chen et al. (2011); El-helaly et al. (2020) have examined the relationship of related party transactions with earnings management, in which several techniques in earnings management are used by fraudsters to commit financial statement fraud but violate applicable accounting standards. Based on this explanation, the researcher formulated the third hypothesis, namely:

H_3: Related party transactions have a significant positive effect on potential financial statement fraud

CEO Education on Capability Elements Positively Affects Potential Financial Statement Fraud

Capability is the ability and capacity of a manager to commit fraudulent actions in the company environment. Not everyone in the company can commit financial statement fraud. Relevant capability is required to conduct financial statement fraud. One way to obtain certain abilities that are often done by humans is through education, therefore capability can be measured using CEO education. Ying & Mei (2014) suspect that if a manager or director has higher education, the possibility of financial statement fraud will be higher. Based on this explanation, the researcher formulated the fourth hypothesis, namely:

H_4: CEO education has a significant positive effect on potential financial statement fraud

CEO Narcissism on Arrogance Elements Positively Affects Potential Financial Statement Fraud

Arrogance is a greedy and superior attitude that assumes that an organization's internal control is not effective for someone who is arrogance, so that person is more likely to commit fraud. The higher a person's position in the company, the more arrogant that person tends to be. The study of Tessa G & Harto (2016) suggests that CEOs tend to emphasize to others about the position and status of the position they have at the company they work for because they do not want to lose their position and status. The CEO's way of showing their position and status is by including their photo on the company's annual report. Based on this explanation, the researcher formulated the fifth hypothesis, namely:

H_5: CEO narcissism has a significant positive effect on potential financial statement fraud

Political Connection on Collusion Elements Affects Potential Financial Statement Fraud

Collusion is the act of making certain agreements dishonestly by two or more people for the personal interests of the parties involved in the agreement. Collusion in the company can be identified through the political connections owned by company officials (Shleifer

& Vishny, 1994). Political connections can provide benefits for companies in terms of making it easier to borrow funds from banks, avoiding tax payments, to obtaining projects or contracts from the government which is carried out in a way that tends to be dishonest or fraudulent. The study of Matangkin et al. (2018) has used the political connection to measure collusion and obtained results that prove that political connections have a significant positive effect on fraudulent financial statement acts. Based on this explanation, the researcher formulated the sixth hypothesis, namely:

H_6: Political connection has a significant positive effect on potential financial statement fraud

Audit Committee Moderates Relationship between Fraud Hexagon Theory Elements and Potential Financial Statement Fraud

The audit committee is a form of corporate governance that aims to minimize agency conflicts. An effective audit committee within the company can ensure that the company's management has made decisions based on the applicable corporate governance regulations in any situation and condition (Lastanti, 2020). The seventh hypothesis to the twelve hypotheses, researchers suspect that the existence of an audit committee in the company will weaken the relationship between the elements of fraud hexagon theory and financial statement fraud, except for hypothesis eight. In the eighth hypothesis, it is suspected that the audit committee acts as a moderating variable that strengthens the significant negative relationship between effective monitoring and financial statement fraud. Dewi & Anisykurlillah (2021); Lastanti (2020); Wailan'an (2019) have examined the role of the audit committee as a moderator on the relationship between the influence of fraud theory on financial statement fraud. Based on this explanation, the researchers formulated the seventh to twelve hypotheses, namely:

H_7: The audit committee weakens the influence of financial pressure on potential financial statement fraud.

H_8: The audit committee strengthens the effect of effective monitoring on potential financial statement fraud.

H_9: The audit committee weakens the influence of related party transactions on potential financial statement fraud.

H_{10}: The audit committee weakens the influence of CEO education on potential financial statement fraud.

H_{11}: The audit committee weakens the influence of CEO narcissism on potential financial statement fraud.

H_{12}: The audit committee weakens the influence of political connection on potential financial statement fraud.

RESEARCH FRAMEWORK

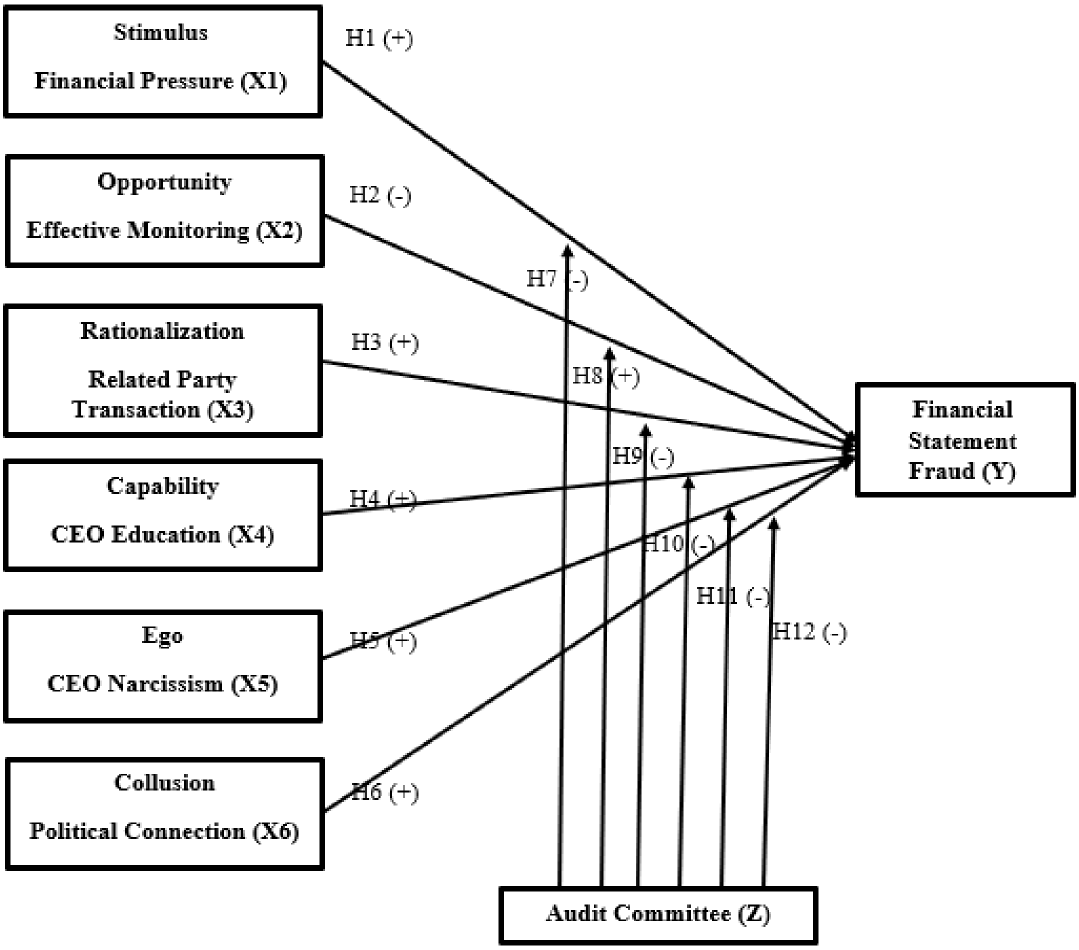


Table 1. Variables, Operational Definition, and Measurement

Variables	Reference	Measurement
Potential Financial Statement Fraud (Y)	Dechow et al. (2011); Richardson et al. (2005)	$F-Score = accrual\ quality + financial\ performance$
Financial Pressure	Skousen et al. (2008)	$ROA = \frac{net\ income}{total\ assets}$
Effective Monitoring (X1)	Skousen et al. (2008)	$BDOUT = \frac{total\ independent\ commissioners}{total\ commissioners}$
Related Party Transaction (X2)	Habib et al. (2017)	$RPT\ Sales = \frac{total\ related\ party\ transaction}{total\ sales}$
CEO Education (X3)	Ying & Mei (2014)	1=postgraduate degree, 0=bachelor's degree
CEO Narcissism (X4)	Horwarth (2011)	$FNOP = the\ frequent\ number\ of\ CEO\ picture\ in\ the\ annual\ report$
Political Connection (X5)	Matangkin et al. (2018)	$Political\ connection = \frac{total\ commissioners\ connected\ to\ politics}{total\ commissioners}$
Audit Committee (Z)	Badolato et al. (2014)	$ACFAE = \frac{total\ audit\ committee\ members\ with\ financial\ and\ accounting\ expertise}{total\ audit\ committee}$

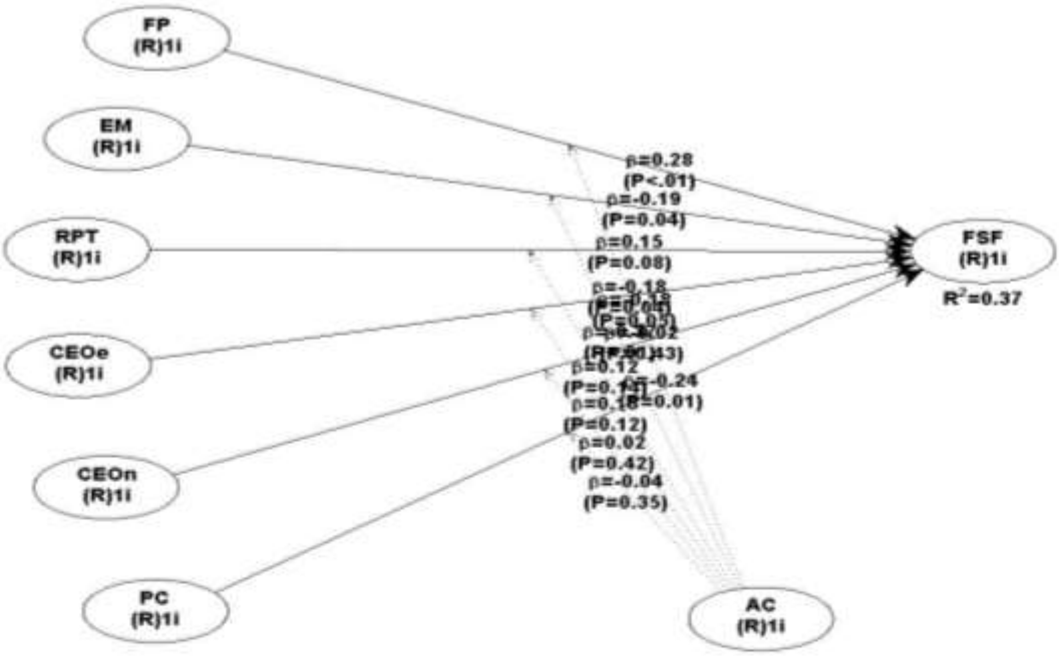
RESEARCH RESULTS AND DISCUSSION

The population of this study is state-owned companies listed on the Indonesia Stock Exchange in 2016-2020. The research sample was obtained using a purposive sampling technique with three criteria so that 80 data were obtained from the annual report of BUMN companies listed on the IDX in 2016-2020.

Table 2. Sample Selection Results

No	Description	Number of Company
1	State-owned companies listed on the IDX 2016-2020	20
2	Non-financial state-owned companies	(4)
3	State-owned companies that present complete data on research variables from two years before the research period (2014-2020)	-
Companies that meet the criteria for sampling		16
The number of observations used in this study (16x5)		80

The research data of 80 data were processed using warpPLS version 7.0 so that the results of hypothesis testing were obtained as follows:



Tabel 3. Hypothesis Testing Results

Hypothesis	Prediction	P-value (α=5%)	Path Coefficient	Decision
H1=FP→FSF	+	0.004	0.282	Accepted
H2=EM→FSF	-	0.035	-0.193	Accepted
H3=RPT→FSF	+	0.081	0.151	Not Accepted
H4=CEOEdu→FSF	+	0.045	-0,182	Not Accepted
H5=CEONar→FSF	+	0.426	-0.021	Not Accepted
H6=PC→FSF	+	0.011	-0.243	Not Accepted
H7=FP*AC→FSF	-	0.050	-0.176	Accepted
H8=EM*AC→FSF	+	<0.001	-0.365	Not Accepted
H9=RPT*AC→FSF	-	0.139	0.118	Not Accepted
H10=CEOEdu*AC→FSF	-	0.124	0.125	Not Accepted
H11=CEONar*AC→FSF	-	0.418	0.023	Not Accepted
H12=PC*AC→FSF	-	0.347	-0.043	Not Accepted

Testing the first hypothesis in a p-value of 0.004 and a path coefficient value of 0.282, so the decision made was to support the first hypothesis. This decision is in line with the research of Fitri & Syukur (2019); Supri et al. (2018). Financial targets are often used as the basis for bonus schemes for management to measure management performance. The bonus scheme based on management's financial performance is one of the triggering factors for management to practice fraudulent financial statements.

The results of testing the second hypothesis indicate that effective supervision has a negative effect on the potential for fraudulent financial statements as evidenced by a p-value of 0.035 and a path coefficient value of -0.193, so the decision made is to support the second hypothesis. This decision is in line with Kusumawardani (2018); Lastanti (2020); Ozcelik (2020); Pusphita & Yasa (2018). OJK Regulation No. 33/POJK.04/2014 Regarding the Board of Directors and Board of Commissioners of Issuers or Public Companies, the proportion of independent commissioners to the board of commissioners is at least 30%. The research data shows that on average the sample companies have a total proportion of independent commissioners to the board of commissioners of 36.16%. This number shows that in general state-owned companies have complied with the applicable regulations.

Testing the third hypothesis, in a p-value of 0.081 and a path coefficient value of 0.151, so the decision made was to reject the third hypothesis even though the direction of the path coefficient was under the research hypothesis. Chen et al. (2011) show that related party transactions have a positive effect on earnings management. However, based on the results of this study, shows that related party transactions do not affect the risk of financial statement fraud. The third hypothesis is not supported because there is a dividing line that distinguishes the nature between earnings management and financial statement fraud, namely generally accepted accounting standards (Md Nasir et al., 2019).

The fourth hypothesis is rejected because testing the fourth hypothesis produces a p-value of 0.045 and a path coefficient value of -0.182, although the p-value is less than 0.05, the direction of the path coefficient is not under the research hypothesis. This hypothesis is not supported because the CEO education measurement adapted from Ying & Mei (2014) only considers the educational background of the president director, while for fraudulent financial reporting practices in large entities that implement a comprehensive accounting information system, financial statement fraud perpetrators cannot act. fraud alone, considering that all research samples are large companies.

Testing the fifth hypothesis in a p-value of 0.426 and a path coefficient value of 0.021, so the decision made was to reject the fifth hypothesis. This decision is in line with Aviantara (2019); Damayani et al. (2017); Lastanti (2020); Sari et al. (2020). According to Damayani et al. (2017), the frequency of the appearance of CEO photos in annual reports has two sides, namely negative and positive sides. The negative side shows a person's arrogance, superiority, and arrogance over the position and position they have. The positive side shows a sense of confidence in skills, principles, and norms that are held, and concern for others. So that the use of the frequency of occurrence of CEO photos in the annual report to measure the element of arrogance is not appropriate.

The results of testing the sixth hypothesis show that political connections do not affect the potential for fraudulent financial statements as evidenced by a p-value of 0.011 and a path coefficient value of -0.243, so the decision made is to reject the sixth hypothesis even though the p-value is less than 0.05 but the direction the path coefficient is not under the research hypothesis. State-Owned Enterprises companies have close political connections due to the authority of the Ministry of State-Owned Enterprises to assign state officials from several ministries, the Indonesian National Armed Forces, and the Indonesian National Police as members of the board of commissioners of State-Owned Enterprises companies to carry out the supervisory function of the directors to protect the interests of the state. One of the efforts of the Ministry of State-Owned Enterprises can be said to be successful in assigning state officials to carry out a supervisory function on state-owned companies, in line with the second hypothesis in this study.

The seventh hypothesis is supported because testing the seventh hypothesis produces a p-value of 0.05 and a path coefficient value of -0.176, so the decision made is to accept the seventh hypothesis. This decision is in line with the research of Dewi & Anisykurlillah (2021); Wailan'an (2019). OJK Regulation No.55/POJK.04/2015 has regulated the minimum number of audit committee members in a company, namely three audit committee members with at least one person having accounting and/or finance expertise. The research data shows that all state-owned companies in the research sample have complied with OJK Regulation No.55/POJK.04/2015, so that the supervision of the audit committee in state-owned companies has been running according to the rules.

Testing the eighth hypothesis, in a p-value of <0.001 and a path coefficient value of -0.365, so the decision made was to reject the eighth hypothesis even though the p-value was less than 0.05 but the direction of the path coefficient was not under the research hypothesis. The ninth hypothesis testing in a p-value of 0.139 and a path coefficient value of 0.118, so that the decision made was to reject the ninth hypothesis. Testing the tenth hypothesis, in a p-value of 0.124 and a path coefficient value of 0.125, so the decision made was to reject the tenth hypothesis. The eleventh hypothesis testing in a p-value of 0.418 and a path coefficient value of 0.023, so the decision made was to reject the eleventh hypothesis. Testing the twelfth hypothesis, in a p-value of 0.347 and a path coefficient value of -0.043, so the decision made was to reject the twelfth hypothesis even though the direction of the path coefficient was under the research hypothesis. The decision of the last five hypotheses is in line with the research of Indriyani & Suryandari (2021); Lastanti (2020). The audit committee as measured by the comparison of the number of audit committee board members with accounting and/or finance expertise to the number of audit committee board members does not yet represent how effective the supervision carried out by the audit committee board is, so that the audit committee board's supervisory function is less effective in increasing the effectiveness of supervision. Against the risk of fraudulent financial statements.

CONCLUSION, LIMITATIONS, AND SUGGESTIONS

This study aims to obtain empirical evidence of the influence of the six elements of the hexagon theory Vousinas (2019) on the potential for fraudulent financial statements of state-owned companies listed on the IDX in 2016-2020. This study involves an audit committee that acts as a moderator on the direct relationship between variables from the elements of the Hexagon theory of fraud and financial statement fraud. The results show that not all elements of the fraud hexagon theory affect the potential for fraudulent financial statements, only financial pressure has a positive effect on fraudulent financial statements and effective monitoring has a negative effect on fraudulent financial statements, henceforth related party transactions, CEO education, CEO narcissism, and political connection does not affect fraudulent financial statements. The role of the audit committee as a moderating variable is only able to weaken the direct relationship between financial pressure and financial statement fraud.

This study has several limitations that are expected to be improved or completed by researchers in the future. This study only focuses on the risk of fraudulent financial reporting practices in state-owned companies, so the results of the study cannot describe the relationship between elements of the theory of fraud hexagon, financial statement fraud, and audit committees in companies other than state-owned companies listed on the IDX. This study uses the type of secondary data that is not appropriate to measure subjective variables, while in the fraud hexagon theory there are two subjective elements, namely elements of rationalization and arrogance. The use of comparison of the number of commissioners involved in politics with the number of commissioners is not appropriate to measure the political connection variable because the research sample is a state-owned company, so the government has the right to supervise state-owned companies.

Some suggestions that researchers can convey for the benefit of further research, namely that further researchers can use research samples of private companies and state-owned enterprises in all industrial sectors except the financial industry so that research results can describe the relationship between elements of the fraud hexagon theory, potential fraud in financial statements, and audit committees. Advanced researchers can use a primary data approach to measure subjective variables, use the number of audit committee meetings to measure the audit committee variable, the number of cooperation projects between companies and the government to measure the political connection variable, use a comparison of the number of boards of directors involved in political connections with the number of the board of directors to measure the political connection variable, using the corporate good governance variable as a moderating variable on the direct relationship between the variables of the fraud hexagon theory element and the potential for fraudulent financial statements, and using the fraud triangle theory to examine the potential for fraudulent financial statements in state-owned companies.

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