



## **Consequences of Fraud Factors on Accounting Fraud of Regional Apparatus**

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### **Abstract**

The purpose of this study is to understand the influence of compensation suitability, money ethics, and internal control systems on accounting fraud committed by local officials. This research was conducted with a quantitative descriptive approach using a correlation approach, and samples were taken using a sampling technique by criteria. Data for this study was collected through filling out a questionnaire distributed to staff members of the Regional Work Unit (SKPD). The SmartPLS (Partial Least Square) program is used to model the data to be analyzed. The study found that money ethics had a positive effect, while the internal control system and the appropriateness of compensation had a negative effect on accounting fraud among regional officials.

**Keywords:** Accounting Fraud, Compensation Suitability, Money Ethics, Internal Control System

### **Introduction**

In the current era of globalization, every country has unique methods and systems in achieving national goals, including Indonesia. Currently in Indonesia, regional autonomy is being implemented, where each region is given the right, authority, and responsibility to manage government affairs and the interests of the local community, in accordance with laws and regulations ranging from the provincial to sub-district levels. However, the spirit of regional autonomy seems to have caused many negative impacts. According to Khudori (2014), one of the main problems is the emergence of "institutional crimes", both from the executive and the legislature. One of the violations that often occurs is fraud in accounting related to corruption (Wilopo, 2006). According to Sulistiyo (2014), corruption among bureaucrats is difficult to avoid, because political scandals involving power and bureaucracy are very influential.

The study of accounting fraud related to corruption is an important topic, because the handling of accounting fraud requires better, more comprehensive, and integrated efforts. Therefore, it is important to research the main reasons behind accounting fraud. It is important to gather more comprehensive information about the factors that lead to accounting fraud.

According to Dito (2010), one of the main aspects that is closely related to accounting fraud is the appropriateness of compensation given to employees for their contributions to the organization. By providing appropriate compensation, the likelihood of accounting fraud can be reduced, so that individuals can feel satisfied with their income and avoid unethical practices or fraud for personal gain. However, accounting fraud can sometimes arise not only from compensation issues, but also from an obsession with wealth. As revealed by Sloan (2002), an interest in money can encourage individuals to prioritize financial gains in their lives, so they see accounting fraud as acceptable (Lau, Choe, and Tan, 2013). Those who crave money intensely often tend to behave deviantly within organizations (Tang and Chiu, 2003), as they are driven by a desire to pursue additional wealth. Tang (2002) argues that the ethical view of money is directly related to accounting (fraud). This means that individuals who place a high value on money (strong money ethics) are more prone to engaging in unethical accounting fraud compared to those with lower money ethics.

To combat this (fraudulent) accounting behavior, a strong internal control system within the company is needed (Wilopo, 2009). Such a system is expected to help reduce accounting fraud, as effective internal controls can significantly assist organizations in reducing the incidence of fraud (Fauwzi, 2011). The problem of this study is that there are still differences in the results of research on accounting factors (fraud) in Indonesia, namely the variable of compensation suitability. According to Thoyibatun (2009) the variable of compensation suitability affects accounting fraud (fraud), but the results of Fauwzi (2011) research state that compensation suitability does not affect accounting fraud (fraud).

Agency Theory, in this study, the concept model is based on agency theory (Jensen and Meckling, 1976). This is considered appropriate because the main purpose of the study is to ascertain the components that affect accounting fraud and other components of fraud, which plays a role in preventing and eradicating accounting fraud, Sulisityo (2014).

### **The Effect of Compensation Suitability on Accounting (Fraud)**

According to attribution theory, a person's actions in an organization are influenced by causal attribution (Waworuntu, 2013). The fraudulent actions that a person commits are caused by the desire to maximize personal profits, because basically humans work to make money to meet their life needs. So, employees work to show their loyalty to the company, in the hope that the company will reward those employees. One way for management to improve performance, motivate, and improve employee performance is by providing compensation (Mathis and Jackson, 2000 in Dito, 2010).

Reimbursement is a component of the cost paid by an organization to employees. For employees, compensation is a factor that determines the level of well-being, while for organizations, compensation is a cost component that affects the level of efficiency and profitability. Therefore, organizations need to be careful in controlling and designing compensation so that both interests can be accommodated. It is a challenge for organizations to create a compensation system that is able to motivate employees to achieve optimal performance. Leopold (2000).



The act of accounting fraud is triggered by an individual's dissatisfaction with the rewards received from their work. It is hoped that with the right compensation system, individuals will feel satisfied so that they do not take actions that are detrimental to the organization, including committing accounting fraud, because an appropriate compensation system is expected to reduce the desire to commit fraudulent acts. Based on the explanation above, the following research hypothesis can be drawn:

Ha1: There is an effect of compensation appropriateness on accounting fraud (fraud) of regional apparatus.

#### **The Effect of Money Ethics on Accounting Fraud (Fraud)**

According to Tang (2002), those who love money very much/money ethics) consider it very important and tend to be less ethical compared to those who have low money ethics. As a result, having a lot of money allows some individuals to better meet their needs and achieve a better quality of life. As a result, they aim to earn more money to maintain their lifestyle. A person's love for money drives them towards unethical actions (Tang, 2002), such as engaging in accounting fraud.

When a person puts financial gain and wealth as a top priority, they may feel that unethical actions are justified. Those who are heavily driven by money or put it in front of their values may consider accounting fraud to be morally acceptable. Previous research has shown that money ethics significantly and directly influences fraudulent behavior, as Lau, Choe, and Tan (2013) have noted, as they consider fraud to be prevalent. This shows that the greater a person's desire for money, the higher the likelihood of engaging in accounting fraud. From this explanation, the following research hypothesis can be formulated:

Ha2: There is an influence of money ethics on accounting fraud (fraud) of regional apparatus

#### **The Influence of the Internal Control System on Accounting (Fraud)**

Attribution theory suggests that the actions of a leader or authority figure are shaped by the causal factors (Green and Mitchell, in Waworuntu, 2013). Thus, a control system is needed to minimize the causes of accounting fraud (fraud). The internal control system is supposed to help reduce dishonest acts committed by employees as some employees may commit dishonest acts to increase personal gain. One example of dishonest behavior is committing accounting fraud (fraud).

Accounting fraud can occur if there is an opportunity to do so. A great opportunity to increase the frequency of accounting fraud. This opportunity can be minimized with an effective internal control system, Agoes (2013). The efficient implementation of internal controls can reduce or even completely eliminate the opportunity to commit accounting fraud. From this explanation, the research hypothesis can be formulated:

Ha3: There is an influence of the internal control system on accounting fraud (fraud) of regional apparatus



## **Method**

### **Research Methods and Types of Data and Data Sources**

The research method used is a quantitative descriptive approach with a correlational perspective. The type of research carried out is hypothesis testing research, which examines phenomena reviewed from the relationship between variables (causal research). The type of data in this study is subject data, namely research data that contains opinions, attitudes, experiences, or traits of individuals or groups participating in the research (respondents). The source of data for this research includes primary data in the form of opinions, attitudes, experiences, or characteristics of the respondents (subjects) of the research, and the tool used is a questionnaire or survey.

### **Data Collection Methods**

The data collection method is carried out by distributing directly or by using postal facilities (mail survey) and e-mail survey. In order to ensure the effectiveness and efficiency of the questionnaire design, a pilot test was conducted to determine the time needed to complete the questionnaire and assess the validity and reliability of the questionnaire.

### **Sampling Techniques**

The sample determination technique in this study uses the Purposive Sampling technique. The Purposive Sampling method is a technique for determining samples with consideration. The selection of the research sample was based on the following considerations:

1. The Head of SKPD as the official who uses the budget is tasked with: compiling the RKA SKPD, compiling the DPA-SKPD.
2. The head of the SKPD can delegate part of his authority to the head of the work unit in the SKPD as the power of attorney for the budget user/power of attorney for the user of goods. The authority of the head of SKPD is delegated to one level below the head of SKPD.

### **Data Analysis Techniques**

Before the data is analyzed, the data is first assessed for quality, including reliability and validity tests using SPSS software version 23.0 (Statistical Product and Service Solution). Reliability testing aims to evaluate questionnaires that serve as measurement variables or constructs. The reliability assessment was carried out through the Cronbach Alpha test. A construct is considered reliable if it obtains a Cronbach Alpha value of  $\geq 0.60$  (Nunnaly, 1967 in Ghozali 2011).

In this study, data analysis uses the Partial Least Square (PLS) method which is run with SmartPLS software. PLS is a type of structural equation model (SEM) that focuses on components or variants. According to Ghozali (2006), PLS is an alternative method that moves from a covariation-based SEM approach to a variance-based framework. Covariant-based SEM analysis usually tests causality or theory, while PLS is more predictive-oriented. Ghozali's (2006) research states that PLS is considered a strong analytical technique because of its minimal dependence on assumptions (Will, 1985). For example, the data does not need to be normally distributed, and a large sample size is not necessary. In addition to confirming the



theory, PLS can also explain whether there is a relationship between latent variables. PLS can simultaneously analyze constructs created with reflective and formative indicators, this cannot be done with a covariance-based SEM as it will result in an unidentified model. In the analysis with PLS, there are 2 things that are done, namely:

1. Assessing the outer model or measurement model

There are three criteria to assess the outer model, namely Convergent Validity, Discriminant Validity and Composite Reliability. The convergent validity of the measurement model with reflective indicators is assessed based on the correlation between the score items/component scores calculated with PLS. Individual reflex measures are said to be high if they correlate more than 0.70 with the constructed being measured. However, according to Chin, 1998 (in Ghazali 2006) for the initial stage of research from the development of a loading value measurement scale of 0.5 to 0.6 is considered quite adequate. The following is the formula for calculating AVE:

$$AVE = \frac{\sum \lambda_i^2}{\sum \lambda_i^2 + \sum I \text{var}(\epsilon_i)}$$

Where  $\lambda_i$  is the component loading to the indicator to  $\text{var}(\epsilon_i) = 1 - \lambda_i^2$ . If all indicators are standardized, then this measure is equal to the Average Communalities in blocks. Fornell and Larcker, 1981 (in Ghazali 2006) stated that this measurement can be used to measure the reliability of the component score of latent variables and the results are more conservative than composite reliability. It is recommended that the AVE value must be greater than the value of 0.50. Composite reliability indicator blocks that measure a construct can be evaluated with two measures, namely internal consistency developed by Wert et.al 1979 (in Ghazali 2006).

2. Assessing the Inner Model or Structural Model.

Testing the inner model or structural model is carried out to see the relationship between the structure, significance value and R-square of the research model. The structural model was evaluated using R-square for dependent constructs, Stone-Geisser Q-square test for predictive relevance and t-test and significance of structural path parameter coefficients. The effect of the magnitude of  $f^2$  can be calculated by the following formula:

$$f^2 = \frac{R^2_{\text{included}} - R^2_{\text{excluded}}}{1 - R^2_{\text{included}}}$$

Where  $R^2_{\text{included}}$  and  $R^2_{\text{excluded}}$  are the R-squares of the dependent latent variable when the predictor of the latent variable is used or excluded in the structural equation. In addition to looking at the R-square value, the PLS model is also evaluated by looking at the Q-Square predictive relevance for the construction model. Q-Square predictive relevance measures how well the observation value is generated by the model as well as the estimation of its parameters. A Q-Square predictive relevance value greater than 0 indicates that the model has a predictive relevance value, while a Q-Square predictive relevance value of less than 0 indicates that the model lacks predictive relevance.

## Results and Discussion

### Result For Inner Weights

The importance of the value for rejecting and accepting the suggested hypothesis is  $\pm 1.96$ . According to the results of the estimates to evaluate the structural model, it is clear that the suitability of compensation has a negative impact on accounting fraud ( $2,922 > 1.96$ ). Ethical standards regarding money have a positive impact on accounting fraud ( $9,221 > 1.96$ ). The internal control system has a negative impact on accounting fraud ( $-2,654 < -1.96$ ).

Table 1. Result For Inner Weights

Information	original sample estimate	Mean subsamples	of Standard deviation	T-Statistic	Hypothesis
Compensation Conformity -> Accounting Fraud	-0.285	-0.266	0.098	2.922	Accepted
Money ethics -> Accounting fraud	0.583	0.583	0.063	9.221	Accepted
Internal Control System -> Accounting Fraud	-0.580	-0.572	0.040	14.631	Accepted

Source : SmartPLS 2023 Output

### Testing the Structural Model (Inner Model)

The higher the R-square, the greater the independent variable can explain the dependent variable so that the better the structural balance. The following table is the result of the R-square estimation using SmartPLS.

Table 2. R-Square Value

Variable	R-square
Compensation Suitability	
Money ethics	
Internal Control System	
Accounting Fraud	0.685

Source : SmartPLS 2023 Output





The table above shows the R-square values for the accounting fraud construct. A higher R-square value indicates that the independent variable makes a more significant contribution to explaining the dependent variable, resulting in a more effective structural equation. The R-square value for the accounting fraud variable is 0.685, which shows that 68.5% of the accounting fraud constructs are due to compensation suitability, money-related ethical behavior, and the efficiency of the internal control system. The rest, 31.5%, was associated with other variables that were not covered in this study.

### **Hypothesis Testing**

#### **Effect of Compensation Suitability on Accounting Fraud**

This study shows that compensation suitability has a negative impact on accounting fraud. This shows that when employees receive appropriate compensation, the likelihood of accounting fraud becomes lower. For employees, compensation that meets their expectations becomes essential to their well-being, encouraging them to work effectively. This will ultimately reduce behavior that violates ethical and moral standards (Dallas, 2002). Therefore, companies need to create a compensation system that is appropriate and feasible for the business, because fair compensation will encourage employees to work as well as possible. On the other hand, if a company fails to compensate employees in accordance with their expectations, this can encourage unethical behavior, as employees may try to meet their needs through alternative means, which contributes to accounting fraud (Lee et al., 2009).

#### **The Direct Influence of Money Ethics on Accounting Fraud**

The results of this study show that attitudes towards money greatly affect accounting fraud positively. This implies that individuals with strong money ethics are more likely to engage in accounting fraud, as they perceive it as acceptable and common behavior, prioritizing money above all else, and therefore viewing accounting fraud as morally acceptable. This finding is in line with research conducted by Lau, Choe, and Tan (2013), which found that individuals with high financial ethics consider accounting fraud to be ethical. In addition, the results of this study are in line with previous research by Tang (2002) and Tang and Chiu (2003).

#### **The Effect of the Internal Control System on Accounting Fraud**

The results of this study show that the implementation of the internal control system has a negative impact on accounting fraud. This shows that the increased implementation of internal control systems in companies can reduce the likelihood of employees being involved in accounting fraud, because the incidence of fraud is influenced by the availability of opportunities (Glifandi, 2011). This opportunity can be minimized through the implementation of effective internal controls. These findings are in line with the insights provided by agency theory. Agency theory describes an organization as a contractual relationship between managers and principals, which is characterized by the existence of varying interests on both sides. If a party's interests are threatened in its ability to be met, it can lead to deviant behavior, which indicates the need for a structure that can restrain the manager's actions. In addition, the



implementation of an effective internal control system ensures sufficient assurance related to the accuracy of financial statements, legal compliance, and operational effectiveness and efficiency, thereby helping to reduce the incidence of accounting fraud (Mulyadi and Puradiredja, 1998 in Fauwzi, 2011).

## **Conclusion**

The suitability of compensation has a negative effect on accounting fraud in regional apparatus. Money ethics has a significant positive effect on accounting fraud in regional apparatus. The internal control system has a negative effect on accounting fraud in regional apparatus.

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