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DIAMOND THEORY IN ACTION: STRATEGIES TO DETECT AND DETER FINANCIAL FRAUD IN THE ERA OF COVID-19

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Abstract: The purpose of this research is to ascertain how financial statement fraud in manufacturing firms in the goods and consumer industry sector is affected by diamond fraud analysis using a beneish model. Diamond fraud with pressure (financial stability, financial targets), with opportunity (industry nature), with rationalization (change of auditors), with capability (change of director), and covid. Purposive sampling is the methodology that is used (method using certain criteria). 184 manufacturing businesses in the goods and consumer sector that were listed on the Indonesia Stock Exchange in 2018–2021 made up the study's sample. The multiple regression model from IBM SPSS 26.0 was used in this study. The results of this research show that while the nature of industry variables has a significant impact on financial statement fraud, financial stability, financial targets, rationalization, capability, and covid do not have a significant impact.

Keywords: Financial Stability, Financial Target, Nature of Industry, Rationalization, Capability, Covid and Fraud Financial Statement

INTRODUCTION

Background to the study

Financial statement information is crucial since it may describe the state and performance of the business. Many people find that high-quality information is helpful while making financial decisions. Investors and other interested parties use profit information as a gauge for how well money are employed in an enterprise, as shown by the rate of return, and as a sign of rising well-being. The tendency of outside parties (investors) to focus more on profit information as a measure of firm performance and the existence of information asymmetry will push management to alter the way profit information is displayed, a practice known as profit management (Amin, 2018). Financial statements can be said to be accepted by interested parties if they meet the requirements, one of which is relevant. The components in financial statements in Indonesia have been prepared more and more fully (comprehensively), but there are still loopholes in the financial statements that can be used as opportunities and places for parties who have the authority to commit *fraud* on financial statements for personal interests. So that the financial statements cannot be said to be relevant anymore. The

practice of fraud in financial statements itself is known as *fraudulent financial statements* (Khoirunnisa & Amaroh, 2020). According to the Indonesian Accounting Association (2011), the purpose of the statements is to provide information about the company's financial position, performance, and cash flow, which is helpful for most users of financial statements and demonstrates the manager's accountability for the resources he or she entrusts. However, in practice, there are still certain businesses that are unable to provide financial statements that satisfy the requirements. Fraud done by managers to obtain personal and class benefits is one of the causes. According to Thiesen (2020) circumstances that are referred to as financial fraud instead focus on adding or omitting information that is meant to mislead rather than actual financial statement errors. Financial fraud includes two types: false financial reporting-related misstatements, and asset-related misstatements.

Study Aim and Objective

The objective is to determine how diamond fraud and the theories of covid and diamond fraud are related. This study outlines a set of goals that are consistent with the goals of the research to:

1. Analyze the relationship between fraudulent financial statements and fraudulent diamonds.
2. Analyze the relationship between fraudulent financial statements and covid

Research Hypotheses

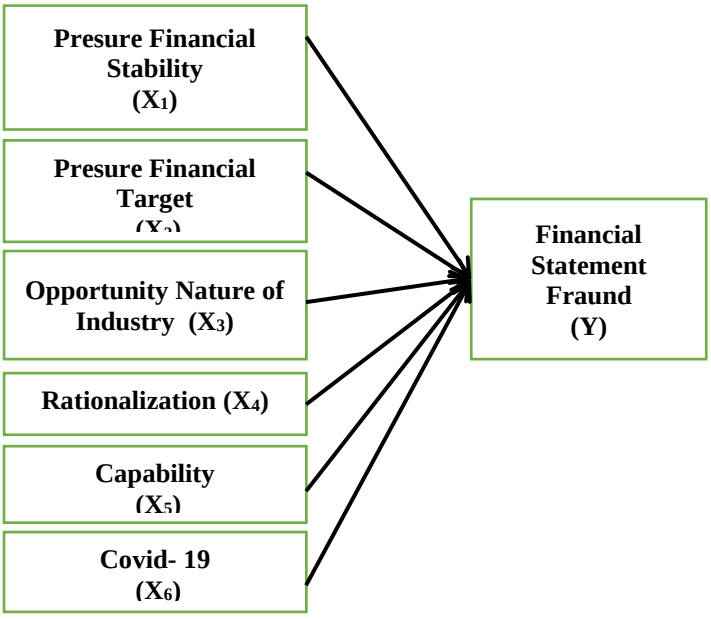
The hypotheses formulated are as follows:

H_1: Financial Stability does not significantly correlate with Fraud Financial Statement
H_2: Financial Target significantly correlate with Fraud Financial Statement
H_3: Nature of Industry does not significantly correlate with Fraud Financial Statement
H_4: Rationalization does not significantly correlate with Fraud Financial Statement
H_5: Capability significantly correlate with Fraud Financial Statement
H_6: Covid significantly correlate with Fraud Financial Statement

Conceptual Framework

In this study six variables, namely: financial stability, financial target, nature of industry, rationalization, capability, covid (the independent variable) and fraud financial statement (the dependent variable).

Conceptual Framework on Fraud Diamond and Covid between Fraud Financial Statement



LITERATURE STUDY

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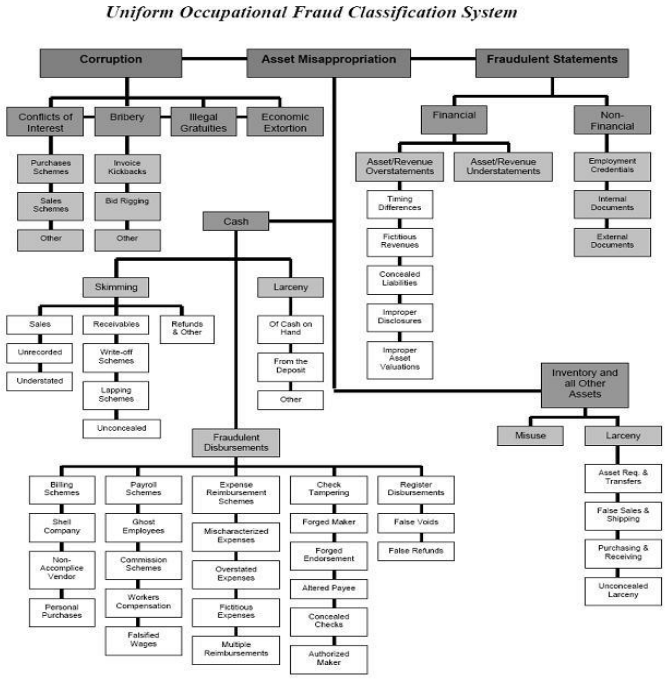
Agency Theory

According to Jensen & William H (1988) In this view, an agency relationship is a contract wherein the agent has the authority to make decisions on behalf of the principle and is used to carry out a certain task for the principal's advantage. Because each side has different interests, there may be an information asymmetries between shareholders and organizations.

Asymmetric information will result in charges known as agency costs. In order to make sure that the management's actions are in line with their desires, the principle attempts to reduce asymmetric information to its most basic form. There are three types of agency costs: (a) costs associated with monitoring the agent's activities; (b) costs associated with ensuring that the principal and agent's interests are aligned in accordance with the contract; and (c) costs associated with decisions made by the agent that are not in the principal's best interests (Jensen & William H, 1988).

Fraud

Fraud according to Setiawan et al., (2020) that results in reporting inaccuracies in financial accounts, or a deliberate act of concealing the truth and using corporate resources inappropriately for one's own benefit. Fraud is described as "deliberate fraud that compels a person to give up his legal property rights or rights" by Webster's New Dictionary. One of the associations in the USA with a focus on fraud prevention and eradication is the Association of Certified Fraud Examinations (ACFE). The Association of Certified Fraud Examiners (ACFE) Gates et al., (2017) designed a diagram known as a "fraud tree" that details fraud methods used in the workplace. In the diagram, ACFE categorizes cheating into 3 categories, namely:



Source: (Gates et al., 2017)

1) Corruption

Corruption is fraud committed by an employee who uses his position of power inside the organization to violate his own or his superiors' obligations in order to gain immediate personal benefits. Due to the fact that numerous parties are covering for one another in practice, this fraud is difficult to spot.

2) *Asset Missappropriation*

Since it is tangible and calculable, asset misuse is the fraud that is most easily identified. When an employee unlawfully and selfishly utilizes corporate resources, fraud happens. This strategy also involves taking or stealing the company's assets.

3) *Financial* Statement Fraud

Financial statement fraud is the deliberate use of financial engineering in the presentation of financial statements by senior managers or executives of a firm to conceal its true financial situation. This finance, often referred to as window dressing, is done to make the company's financial performance appear strong to users of financial statements.

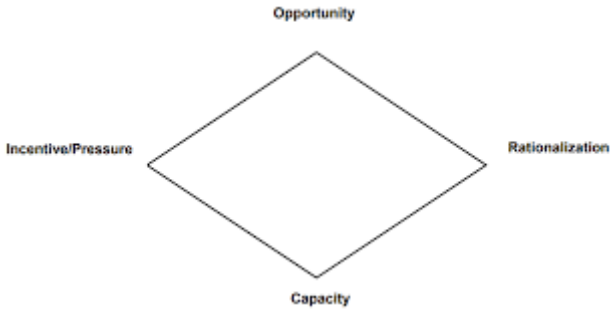
Fraud Financial Statement

According to financial accounting standards in the book at the start of 2011 "The financial condition and financial performance of a business are shown in financial statements in an organized manner. When making economic decisions, the majority of readers of financial statements find information regarding an entity's financial situation, financial performance, and cash flow to be helpful. According to Diansari & Wijaya (2019) A mistake or deliberate omission in the disclosure of financial statements with the intent to harm financial statement users is referred to as fraudulent financial reporting. According to Gates et al., (2017) Financial statement fraud is the intentional misrepresentation of the financial position of an organization. It might be accomplished through purposeful falsifications, the elimination of value, or disclosures in financial statements intended to mislead readers of financial statements. In order to produce financial statements that do not follow widely accepted accounting rules, financial statement fraud is used. If intentions are tangible, they have the power to sway people's decisions (Diansari & Wijaya, 2019).

Fraud Model

Fraud Diamond Theory (Teori Segiempat Kecurangan)

Wolfe & Hermanson (2004) The new theory explains that there are four elements that drive a person to cheat by adding the capability component to Cressey's (1953) theory. The term "diamond fraud" refers to these four elements. The following picture serves as an illustration of the theory:



Sumber : (Wolfe & Hermanson, 2004)

Wolfe & Hermanson (2004) argue that if no one is capable of carrying out cheating in detail, cheating won't happen. The first factor that prevents someone from engaging in cheating is pressure. Once under pressure, the perpetrator looks for opportunities or ways to relieve the strain. If the cheating has been rationalized, the culprit must then determine whether he is capable of carrying out the fraud. This competence include both his knowledge of cheating as well as his position inside the organization.

The various capabilities are linked to fraudster characteristics:

a. *Position* and function

A person's role and position within a corporation may give them the opportunity to commit fraud.

b. *Brains/intelligence and creativity* (kecerdasan dan kreativitas)

A person's with greater intelligence or inventiveness can quickly identify the company's shortcomings.

c. *Confidence and ego* (confidence and ego)

Fraudsters must be highly skilled at persuasion in order to recruit more people into their criminal enterprise and increase their own authority.

d. *Coercion* skills

As fraudsters to increase the number of people involved in the criminal enterprise and increase their own authority, it is crucial that they are skilled at persuasion.

e. *Effective* lying

The fraudster must be skilled at lying convincingly in order for his deception to go undetected.

f. *Immunity* to stress

A fraud has a high level of complexity, therefore the perpetrator who is unable to take care of himself can become stressed. As a result, the perpetrator must be able to prevent himself from becoming stressed.

METHODOLOGY

Purposive sampling is used in this study's sampling technique, which involves selecting samples based on the researcher's own criteria rather than at random. The research conducted will be used to define the selection criterion. using a sample of criteria:

a. Manufacturing companies engaged in the goods and consumption industry during the 2018-2021

b. During the time of the research the company is listed on Indonesia Stock Exhange

c. Publishes complete financial reports and annual report during 2018-2021

Regression Equation as follows:

$$M - SCORE = \alpha + \beta 1NIG + \beta 2ROA + \beta 3RECEIVABLE + \beta 4AUDCHANGE + \beta 5DCHANGE + \beta 6CVD + \varepsilon$$

Where as follows:

M-SCORE= *FraudelentFinancial Statement*

NIG= Financial Stability

ROA= Financial Target

RECEIVABLE= Nature of Industry

AUDCHANGE= Rationalization

DCHANGE= Capability

CVD= Covid

ε = *Erro*

Dependent Variable

In this research, the dependent variable (Y) is a fraudulent financial statement. The 1999-adopted Beneish Model was used to calculate the fraudulent financial statement (Beneish, 1999). As for the formula as follow:

$$\boldsymbol{M - Score = -4.48 + 0.920\,DSRI + 0.528GMII + 0.404AQI + 0,892SGI + 0.115DEPI - 0.172SGAI - 0.327LVGI + 4.697TATA}$$

Following are details for each ratio: Index of Days' Sales in Receivables 1. (DSRI). This ratio is used to compare a year's worth of sales days in the form of receivables to the year before. The likelihood of financial statement tampering increases with DSRI. The formula on the DSRI is as follow:

$$\text{DSRI} = \frac{\frac{Net\ Receivables\ t}{Sales\ t}}{\frac{Net\ Receivables\ t-1}{Sales\ t-1}}$$

1. *Gross Margin Index* (GMI)

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This ratio is used to determine the gross profit margin when comparing one year to the next. The GMI formula is as follows:

$$GMI = \frac{\frac{(Sales\ t-1-COGS\ t-1)}{Sales\ t-1}}{\frac{(Sales\ t-COGS\ t)}{Sales\ t}}$$

2. *Asset Quality Index* (AQI)

This ratio compares current assets, buildings, land, and equipment with total assets to represent changes in the risk of asset realization. The AQI formula is as follows:

$$AQI = \frac{\frac{(1-(Current\ Asset\ t+Fixed\ Asset\ t))}{Total\ Asset\ t}}{\frac{(1-(Current\ Asset\ t-1+Fixed\ Asset\ t-1))}{Total\ Asset\ t-1}}$$

3. *Sales Growth Index* (SGI)

This ratio is used to analyze revenue growth from the prior year to the current year. The SGI formula is as follows:

$$SGI = \frac{Sales\ t}{Sales\ t-1}$$

4. *Depreciation Index* (DEPI)

Comparing the current year's cost of depreciation and the gross values of buildings, land, and equipment to the prior year's. DEPI formulas as follows:

$$SINCE = \frac{\frac{Depreciation\ t-1}{Depreciation\ t-1+Fixed\ Asset\ t-1}}{\frac{Depreciation\ t}{Depreciation\ t+Fixed\ Asset\ t}}$$

5. *Sales, General and Administrative Expenses Index* (SGAI)

This ratio is used to compare the current year's sales and administrative costs to the prior year's sales. The SGAI formula is as follows:

$$SGAI = \frac{\frac{SGA\ expenses\ t}{Sales\ t}}{\frac{SGA\ expenses\ t-1}{Sales\ t-1}}$$

6. *Leverage Index* (LVGI)

This ratio is used to assess the firm's long-term risk and the financial health of the company. LVGI formula is as follows:

$$LVGI = \frac{\frac{Total\ Liabilities\ t}{Total\ Asset\ t}}{\frac{Total\ Liabilities\ t-1}{Total\ Asset\ \ t-1}}$$

7. *Total Accruals to Total Assets Index* (TATA)

Accounting profits that are not cash profits are measured using this ratio. The TATA formula is as follows:

$$TATA = \frac{Income\ from\ operations\ t-Net\ cash\ flow\ providen\ by\ operating\ activities\ t}{Total\ Asset\ t}$$

Independent Variables

The variable that influence the dependent variable (Y), known as the independent variable (X), often has a positive or negative impact. The following are the independent variables included in this study:

a. Financial Stability

A condition that shows the company's stable financial condition is financial stability. (Herdiana & Sari, 2018). The risk of fraud will increase with a company's larger net income ratio. The ratio of net income (NIG), calculated using the following formula, serves as a proxy for the study's changeable financial stability (이명걸 & YoungGyu Ahn, 2014):

$$\boldsymbol{NIG(Net\ Income\ Growth)} = (\boldsymbol{current\ net\ income - previous\ net\ income})/(\boldsymbol{previous\ net\ income})$$

b. Financial Targets

The financial pressure placed on management to meet the financial statement set by the director or management is known as financial target (Sabatian & Hutabarat, 2020). It is the responsibility of the company manager to manage the goals that have been set for success. Financial goals are approximated by ROA using the following formula (이명걸 & YoungGyu Ahn, 2014):

$$\boldsymbol{ROA = \frac{Pendapatan\ bersih}{Total\ aset}}$$

c. Nature of Industry

An optimum situation for a corporation in an industry is determined by its nature (Annisya et al., 2016). Estimates and arbitrary judgments are used to determine a particular account's balance (Skousen et.al, 2009). When estimating uncollectible receivables for accounts receivable and inventories, subjective judgment is necessary (Summers & Sweeney, 2013). Therebefore, this study uses a proxy for the ratio of total receivable, with the formula as follow (Herdiana & Sari, 2018):

$$\boldsymbol{Receivable = \frac{Receivable\ t}{Sales\ t} - \frac{Receivable\ t-1}{Sales\ t-1}}$$

d. Rationalization

According to research, when companies replace auditors, audit failure and litigation rise (Skousen et.al, 2009). Then in research, rationalization is proxied by the change of auditor measured by dummy variables. If the company changes the auditor during the 2018-2021 periode, it is given code 1, and if the company does not change the auditor, it is given code 0 (Fabiolla et al., 2021).

e. Capability

Changes in the board of directors may result in a stressful moment where fraud opportunities are increased. This study uses DCHANGE, or the turnover of corporate directors, as a stand-in for capacity. Directors' change is evaluated using a dummy variable. Companies that change directors between 2018 and 2021 are assigned code 1, while those that don't are assigned code 0 (Annisya et al., 2016).

f. Covid

Covid is a current phenomenon, therefore covid greatly affects fraudulent financial statements. This study using a dummy variable. Companies for 2018–2019 are given code 0, while those for 2020–2021 are given code 1 (Sunitha, 2020).

RESULD AND DISCUSSION

Descriptive Statistic

Table 2 explaines about an overview of the data seen from the minimum, maximum, average, and standard deviation of the tested variables as follows:

	N	Minimum	Maximum	Mean	Std.Deviation
Financial Stability	184	-2248.65372	13.19232	-21.4731273	191.3513241
Financial Target	184	-0.21398	4.1632	0.0914404	0.032998788
Nature of Industry	184	-2.03806	4.89271	0.0667789	0.65665262
Rationalization	184	0	1	0.48	0.051
Capability	184	0	1	0.15	0.355
Covid	184	0	1	0.5	0.501

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Fraud Financial Statement	184	-6.94099	22.76937	-1.8239747	3.21722615
Valid N (listwise)	184				

Table 2

Source : SPSS 26

The following findings of descriptive statistical tests are shown in Table 2 above:

1. Variable financial stability with the 184 has the lowest value -2248.6537 and the highest value of 13.1923 which mean of -21.47% of the collected company data for individual financial stability and the value of the standard deviation (deviation) is quite large that is 191.351 (standard deviation > mean);
2. The variable financial target with the 184 data have a mean value of 0.09% of the firm data gathered for individual financial targets and a standard deviation (deviation) value of 0.3299 (standard deviation > mean); the lowest value is 0.219 and the highest is 4.163;
3. The nature of idnusrty with the 184 data have a range of values between -2.038 and 4.8292, with a mean value of 0.06% for individual nature of industry and a rather high standard deviation value of 0.6566 (standard deviation > mean);
4. The variable rationalization with the 184 data points, with the lowest value being 0 and the highest being 1, with a mean of 0.48% of the firm data obtained for individual rationalization, and a standard deviation value of 0.501 (standard deviation > mean);
5. The variable capability with the 184 have a range of 0 to 1, with a mean value of 0.15% of the company data collected for individual rationalization, and a standard deviation value of 0.355 (standard deviation > mean);
6. The variable covid with the 184 data have a range of 0 to 1, with a mean of 0.50% of the company data gathered for individual rationalization, and a large enough standard deviation (deviation) value of 0.501 (standard deviation > mean);
7. The variable fraud dfinancial statement with the 184 data have a range from -6.9409 to 22.7693, with a mean of -1.8239% of the gathered company data for individual rationalization. The value of the standard deviation (deviation), however, is quite high at 3.2172 (standard deviation > mean);

Normality Test

The normality test is performed to see whether the research model's residuals have a normally distributed distribution. The outcome of the Central Limit Theorem (CLT) method's normality test. The results of the normality test in this study show that there were 184 samples used in the study, which means that 184 samples is larger than 30 samples (184 > 30). The data can be said to be regularly distributed as a result of this.

Multicollinearity Test

The table below shows the results of the multicolonierity test:

Table 3

	Tolerance	VIF
(Constant)		
Financial Stability	0.973	1.028
Financial Target	0.951	1.051
Nature of Industry	0.995	1.005
Rationalization	0.980	1.020
Capability	0.964	1.037

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Covid	0.966	1.036

Source: SPSS 26

The described explanation leads to the conclusion that none of the variables in this study, including financial stability, financial target, industry type, rationalization, capability, and covid-19, have any relationship to one another. This conclusion is supported by the acquisition of Tolerance values of each variable > 0.10 and VIF values of each variable 10.

Heteroscedasticity test

The Spearman Rho test was used to analyze heteroscedasticity in this study. The significant value of each independent variable evaluated with the residual absolute value of the dependent variable can be used to determine the Spearman Rho test, as was covered in the previous chapter. The table below shows the results of the Spearman Rho test:

Table 4

		Unstandardized Residual
Financial Stability	Correlation Coefficient	-0.017
	Sig. (2-failed)	0.816
	N	184
Financial Target	Correlation Coefficient	0.136
	Sig. (2-failed)	0.065
	N	184
Nature of Industry	Correlation Coefficient	0.101
	Sig. (2-failed)	0.174
	N	184
Rationalization	Correlation Coefficient	0.122
	Sig. (2-failed)	0.098
	N	184
Capability	Correlation Coefficient	0.008
	Sig. (2-failed)	0.915
	N	184
Covid	Correlation Coefficient	-0.071
	Sig. (2-failed)	0.335
	N	184

Source : SPSS 26

The significance of the independent variables, which include financial stability, financial target, industry type, rationalization, capability, and COVID-19, has a significance value > 0.05, which indicates that there is no heteroscedasticity in the research regression model.

Autocorrelation Test

The table below shows the results of the autocorrelation test:

Table 5

Model Summary[b]

Model	R	R Square	Durbin-Watson
1	0.267[a]	0.071	1.841

Source: SPSS 26

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The Durbin Watson (DW) value obtained from the table above is 1.841, which indicates that there is no autocorrelation (1.8264<1.841<2.1736) in the regression model of this study. This is the outcome of the autocorrelation test.

F Test

These are the F test results:

Table 6

ANNOVA [a]

Model	Mean Square	F	Sig.
Regression	22.515	2.265	.039[b]
Residual	9.938		

Source: SPSS 26

It is significant table 6 above that independent variables like financial stability, financial aim, industry type, rationalization, capacity, and covid can all have an immediate and considerable impact on financial statement fraud. This is demonstrated by the significant value in the preceding table (0.039 < 0.05).

R Test & R-*Square* (Determination Coeficient)

Results of the R & R-Square Test are shown in the table below:

Table 7

Model Summary[b]

Model	R	R Square	Adjusted R Square
1	0.267[a]	0.071	0.040

Source: SPSS 26

According to the table above, the link between the independent factors of financial stability, financial target, industry type, rationalization, capability, and correlation to the dependent variable of falsified strong financial statements has a R value of 0.267. The above said table also displays the adjusted R-Square value of 0.040, which indicates that 40% of the dependent variable of fraudulent financial statements is explained by independent variables of financial stability, financial target, nature of industry, rationalization, capability, and covid, while the remaining 60% is explained by other factors not included in the research model.

Hypothesis Test (T-Test)

Hypothesis test result (t test) can be seen from table below:

Table 8

[b]		Sign.	Information
(Constant)	-1.886	0.000	
Financial Stability	0.000	0.917	rejected
Financial Target	0.429	0.554	rejected
Nature of Industry	1.29	0.000	accepted
Rationalization	-0.082	0.862	rejected
Capability	-0.119	0.859	rejected
Covid	-0.019	0.968	rejected

Source: SPSS 26

Seen from table above, the following result are obtained:

1. Financial Stability does not significantly influence fraudulent financial statement
2. Financial Target does not significantly influence fraudulent financial statement

3. Nature of Industry has a significant positive effect toward the fraudulent financial statement
4. Rationalization does not significantly influence fraudulent financial statement
5. Capability does not significantly influence fraudulent financial statement
6. Covid does not significantly influence fraudulent financial statement

CONCLUSSION

It can be inferred that just a small number of independent factors analyzed for use to analyze the fraudulent financial statement, such as nature of industry, can significantly affect the fraudulent financial statement. This is because the independent variables utilized as proxies are less directly tied to financial statement data and instead are more focused on human behavior. The following are the limitations of this study: A manufacturing company that was incorporated on the Indonesia Stock Exchange (BEI), where the business has a track record of good corporate governance, serves as the study's first example. As a result, the significant proportion of independent variables in the study's findings had no impact on fraudulent financial statements; both of the Beneish models were appropriate for manufacturing companies, which made up the study's sample of manufacturing companies; third, the variable used to proxy fraudulent financial statements by the Beneish M-Score has multiple iterations and a wide range of ratios, making it time-consuming to calculate the score for the company. Therefore, it is anticipated that the following study will be able to accomplish a number of tasks, including: The following are some implications of future study on the findings of previous research, according to the research that has been done: For academic purposes, it is hoped that this research's findings will serve as a guide for future studies and serve as justification for the creation of additional diamond fraud measurement variables. A follow-up study could then make use of additional proxies or the fraud hexagon theory to produce more convincing results.

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