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FINANCIAL REPORTING MANIPULATION ON MINING COMPANIES IN INDONESIA: FRAUD DIAMOND THEORY APPROACH

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Atiek Sri Purwati[1]✉, Yonathan Daya Persada[2], Roni Budianto[3], Eko Suyono[4], Sofiatul Khotimah[5]
[1245]Universitas Jenderal Soedirman
[3]Universitas Sultan Ageng Tirtayasa
✉[1]aisyaatieksp@yahoo.com
Jl. HR Boenyamin No.708, Grendeng, Purwokerto Utara, Banyumas, Jawa Tengah, Indonesia

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Abstract
Forensic accounting helps to discover fraud practices where the fraud diamond theory is one of the popular theories in this issue. It puts concerns on budget priorities, financial stability, inefficient monitoring, replacement of auditor and directors. As the dependent variable, financial statement manipulation funded by income control is used. The nine mining entities listed on the Indonesian Stock Exchange in 2017-2019 were chosen using the purposive sampling method, resulting in 27 observations. By using the multi-linear regression method, This study showed that financial targets and financial stability affect the occurrence of fraud in financial reports. Oppositely, insufficient monitoring, replacement of auditors and directors have no impact on the fraudulent reporting.

INTRODUCTION

Fraud is an act committed by a person in an organization to take advantage of himself or a group of people. Fraud is a knowingly fraudulent activity intended to achieve wrongful benefits or deprive victims their rights (Herawati, 2017; Basri et al., 2020; Fitriyah & Novita, 2021). Fraudulent activity may occur at individual, group, or even corporate level. A lot of studies have been done on corporate fraud and the resulting theoretical framework. The inference drawn from most fraud-related research is that the cost of fraud prevention is always more cost-effective than fraud detection. Reducing fraud, is less costly and more efficient than finding it after the incident. Typically, when fraud is found, the money is long gone and there is no chance of recouping even a small portion of the loss.

Fraudulent financial reporting is the act of knowingly misrepresenting a company's financial results for the intent of making a profit (Suyono & Farooque 2019; Martins & Junior, 2020; Gozali et al., 2021; Yanthi et al., 2021). The misrepresented information is either an oversight or a deliberate attempt to misinterpret the business's actual economic and financial health. Income is improperly administered whether the financial statements are unfairly governed or viewed outside the legal system (Svabova et al., 2020; ACFE (Association of Certified Fraud Examiners), 2016). Wells (2011) states that fraud can include any or a portion of the financial reporting processes. These may be generated by managers, who are concerned with performance, such as income, and

Volume 14, No. 1, April 2022, Page. 115-121

to hide the firm's true efficiency. The fraud often targets executive pay, compensation, and equity holdings. There are stories of trustworthy companies involved in fraudulent reporting (Martins & Junior, 2020; Yanthi et al., 2021). Fraudulent reporting has resulted in substantial losses as seen in table 1.

Table 1. Total Losses And Percentage Of Fraud

Type of fraud	2012		2014		2016	
	US Dollar	%	US Dollar	%	US Dollar	%
Misappropriation of assets	120.000	86,7	130.000	85,4	125.000	835
Dishonesty	250.000	33,4	200.000	36,8	200.000	35,4
Information asymmetry	1.000.000	7,6	1.000.000	9,0	975.000	9,6

Source: ACFE Report to Nations (2016)

In Indonesia fraud involving financial statements have occurred, and large companies such as PT Ancora Mining Service was involved (Pristine, 2011; Gozali et al., 2021) The scandal stemmed from the financial institution's accounting practices that helped them to minimize taxes. The case demonstrates the ineffectiveness of auditing to deter fraud and the lack of effectiveness of financial reporting. Also, a false financial reporting by PT Timah that was accused of falsely certifying a financial report for the first semester of fiscal 2015. This fraudulent financial report was intended to cover up the ongoing poor results of PT Timah (Afrianto, 2016). Two of these cases as examples of fraud in mining companies in Indonesia where complex financial transactions tend to cause fraud. Therefore, it indicates that the possibility of fraud in mining companies with more complex financial transactions is highly likely to occur.

Spathis (2002) offers details on the key cause factors that can be used in deception on company financial statements. People who are aware of their risk for being captured are more likely to be caught (Kranacher & Richard, 2011; Fitriyah & Novita, 2021). This article illustrates fraud vulnerabilities inherent in businesses. Fraud Diamond needs motivation, rationalization, capability, and pressure. Fraud Diamond is the synthesis of an incentivized scenario, motivation, and rationalization. The mining sector is, in fact, the second-lowest sector that has encountered fraud cases relative to other sectors. Despite being extremely costly and dangerous, the degree of fraud is small. Therefore, this industry (i.e, mining) is attractive to study. The aim of this research is to discover whether there is a link between financial targets, financial stability, successful monitoring and the change of auditors on the occurrence (frequency) of fraudulent financial reporting by Indonesian mining companies.

To reach our financial targets, managers must perform well, and their efforts will be rewarded. To assess an organization's operational efficiency, authors used the proxy of ratio of earnings to dollar-value of assets or Return on Assets (Skousen et al., 2009). Return on Assets is used to determine the effectiveness of management's ability to make money for the company. The greater the return on assets, the greater the profit and the more advantageous it is for the company to own and use assets (Dendawijaya, 2005). If the ROA does not show a positive result, this means that their overall ability to generate profit has not been able to grow, which means that their invested capital assets have not been able to generate profit. Management refers to the value of the effectiveness achieved in the previous year when determining financial targets for the following year. Thus, it can be determined whether the amount generated in the current year exceeds the estimated target.

This research examines how the ROA measures agency theory. Shareholders (principal) hope to make a profit for the company, while management (agent) are given a bonus. Management is the group that runs the business to the best of its ability. Management is not in a position to disclose the company's current condition to be responsible for it. The incentive to meet financial goals to achieve a pay hike contributes to company workers' propensity to commit financial statement fraud. Firms with higher income are more likely to engage in earnings management (Mittoo & Yan, 2020).

The term financial stability refers to a situation whereby the company's financial condition is safe. If management considers a company's finances precarious, management will take various actions to cover the companies' uncertain financial position (Skousen et al., 2009). Moreover, Loebbecke et al., (1989) demonstrated that management manipulate financial reports to retain public opinion of the business. The overall amount of assets held by the company is a primary determinant of what the company does. Companies that have a lot of assets will generate income for investors. Alternatively, if the reduction in net assets results in a loss, investors, creditors, and shareholders will be affected. Companies that face financial uncertainty, operation problems, and poor profitability tend o manipulate financial data to make the companies look more profitable than they actually are. Therefore, the company's management commits fraud by preventing disclosure of poor financial conditions by financial statements. Fudging the asset numbers suggests major financial reporting fraud. Findings by Skousen et al., (2009), Martantya (2013) and Sihombing (2014), as well as Tessa & Harto (2016) illustrate the impact of financial security on financial fraud. The research shows that if a company experiences below average growth by manipulating the company's financial statements, management will boost the company's prospects. Although other studies have found conflicting results, research by Norbarani (2012), Martins & Junior (2020), Pardosi (2015) and Yesiriani & Isti (2016) indicate that a lack of financial stability has a negative impact on financial statement fraud.

The presence of a poor control system offers an incentive for agents to deviate from normal activities and participate in dishonest behaviors. Good management minimizes illegal activities in the workplace. The enforcement board's presence is viewed as increasing the efficacy of company oversight. Getting outside directors on the board enhances the board's efficiency in supervising management because it prevents management from falsifying financial statements. This opinion is supported by research conducted by (Dechow et al., 1995) who examined the relationship between the composition of the board of commissioners and financial statement fraud and proved that fraud was more prevalent in companies that had less external board members. Another study by (Skousen et al., 2009) compared various independent board of commissioners and did not conclude that the ratio of independent board of commissioners has an impact on financial statement fraud.

Replacing auditors in the business can mean fraud because the previous auditor may have found fraud by management, either directly or indirectly. With the replacement of auditors, fraud will become more likely. Unharmonious relationships between the previous auditor and management are suggestive of fraud (Suyono & Farooque, 2019). The auditor change mechanism will minimize fraud and make it hard to detect (Putri et al., 2017). Moreover, Loebbecke et al., (1989) found that 36% of fraud within a sample of audited companies occurred within the first two years of an auditor's tenure.

Capability complements Cressey's fraud triangle model. The capacity of someone to commit fraud is determined by capability. Wolfe and Hermanson (2004) noted that roles of CEO, director and other division leaders may provide the opportunity to build or take advantage of opportunities to commit fraud. There are political agendas and conflicts of interest that enter the picture as you discuss corporate board changes. The changes in directors demonstrate the rationalization process (Wolfe & Hermanson, 2004) and concluded from the results of their research that changes in directors may imply fraud. Board of directors adjustments that do not have a positive effect on the company should not be made without due thought. Since this may be a business move to undermine directors who are suspected to be aware of the fraud. So changes in the board of directors require transition time to ensure the initial output is not optimum. After a change in the board of directors, a tension phase may trigger opportunities for fraud. Therefore, Wolfe & Hermanson (2004) supports Pardosi argument (2015), nothing that changing chief executive has a major impact on financial statement fraud. Results from Laksito & Septia (2015), as well as Yesiriani & Isti (2016) claim that capacity is negatively linked to financial statement fraud.

METHOD

As the dependent variable of this study is financial fraud which is measured by the level of earnings management following (Dechow et al., 1995). Meanwhile, the independent variables are financial target, financial stability, ineffective monitoring, auditor replacement, and director replacement. Financial target is measured by using return on asset (ROA), financial stability by using changes in total assets for the last 2 years, meanwhile, ineffective monitoring is measured by the ratio between a number of independent commissioners compared to total a number of commissioners. Moreover, auditor replacement is measured by a dummy variable, where 1 is given if there is an auditor switch during the research period and 0 if otherwise. Similarly, director replacement is measured by a dummy variable, where I is given if there is director replacement during the study period and 0 if otherwise. This study explores theoretical principles through the use of quantitative data and uses multiple regression analysis to interpret this data. The study population is public companies in the mining company category listed on the Indonesia stock market in 2017-2019. The sampling technique used was purposive with specific criteria: first, the companies have consecutively published their audited annual report in 2017-2019; second, the companies financial reports contain information on all variables under study. There were 44 mining companies that were consistently listed on the market during 2017-2019, and they have published financial reports consecutively during the period. Nine companies met the criteria. However, 35 of them did not meet both criteria leave only nine companies for analysis. Nine companies for three years made up to 27 observations. The data was then statistically analysed.

RESULTS

The descriptive statistical analysis of the data for all variables can be seen in Table 2. The vector Y (fear of the financial statements) has an average value of -0.243, meaning that mining firms have committed fraud in the financial statements with a trend of growing income has the lowest score of -0.228 and a highest of 0.082. A standard deviation that exceeds the average value indicates high fluctuations in the variable financial statement fraud data during the observation period.

Financial targets (X1) are the amount of profit the company must achieve. Based on table 2, it is known that the average X1 mining company is -0.25 with a lower score of -1.571 and a maximum value of 0.196 with a standard deviation of 0.300 from the average. The standard deviation value that exceeds the average value indicates the high fluctuation of the financial targets (X1) variable data during the observation period.

Financial stability (X2) is a condition that illustrates an organization's financial position in a stable state. The average X2 mining enterprise is considered to be 0.118 based on Table 2, with a value of at least -0.614 and a maximum value of 1.502, with an average standard deviation of 0.336. Standard deviation value that exceeds the average value indicates a high fluctuation in financial stability (X2) variable data during the observation period.

The phenomenon of fraud is one of the consequences of inadequate oversight or control to provide agents or supervisors with an ability to perform defiantly by committing fraud in financial reports. Ineffective monitoring (X3) in table 4 has an average of 0.383 with the lowest value of 0.200 and a maximum value of 0.500. X3 has a standard deviation of 0.091, which is smaller than the average, which implies that effective monitoring is around the mean value.

Table 2. Description Of Univariate Data

	N	Min	Max	Mean	Std. Dev
Y	27	-.228	.082	-.024	.079
Fin. target	27	-1.571	.196	-.025	.300
Fin. stability	27	-.614	1.50	.118	.336
Ineffective monitor	27	.200	.500	.383	.091
Auditor replacement	27	0	1	.100	.305
Manager replacement	27	0	1	.470	.507
Valid N (listwise)	27				

Source: Output Of Descriptive Statistic From SPSS

The regression analysis used in this study to evaluate the hypothesis consists of a change of director (DCHANGE), financial stability (ACHANGE), effective monitoring (BDOUT), financial goals (ROA) and change of auditors (AUDCHANGE) for 2017-2019 mining company financial statements fraud. Table 3 shows the findings of the Multiple Regression Analysis.

Table 3. Multivariate Data Analysis Results

Model		Unst.Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	.150	.056		2.657	.015
	Fin. targets	.119	.056	.470	2.134	.045
	Fin. stability	.216	.051	.962	4.260	.000
	Ineffective Monitoring	-.480	.146	-.533	-3.280	.004
	Auditor replacement	-.051	.038	-.208	-1.351	.191
	Manager replacement	-.015	.026	-.094	-.566	.577

a.Dependent Variable: Y

Source: Output of SPSS

The first hypothesis implies that financial targets (ROA) influence manipulation in financial statements (earnings management). The test results for hypothesis 1 suggest that the t-value of the variable financial targets (ROA) is 2.134, whereas the t-table value is 0.68581 with α = 0.05 and df (n-k) 27-5 = 22. Based on these observations, it can be shown that the t-count is greater than the value of the t-table (2.134> 0.068581), so it can be inferred that fraud of financial statements caused by variable financial objectives (ROA). Hypothesis 1 (H1), which notes that financial priorities affect fraud in financial statements, is therefore acknowledged.

The second hypothesis notes that financial stability (ACHANGE) influences fraud in financial statements (earnings management). The test results for hypothesis 2 reveal that the calculated t of the variable financial stability (ACHANGE) is 4.260, where 0.68581 is the t-table value with alpha = 0.05 and df (n-k) 27-5 = 22. Based on these observations, it can be shown that the t-count is higher than the t-table value (4,260> 0.068581), it can be implied that fraud of financial statements is caused by variable financial targets (ROA). Therefore, Hypothesis 2 (H2), which states that financial stability affects financial statement fraud is accepted.

The third hypothesis notes that efficient monitoring (BDOUT) influences fraud in financial statements (earnings management). The testing results for hypothesis 4 show that the t-count value of the effective monitoring variable (BDOUT) is -3.280, while the t-table value with α = 0.05 and df (n-k) 27-5 = 22 is 0.68581. Since the t-count is smaller than the t-table value (-3.280 <0.68581); it can be inferred that the efficient monitoring factor does not impact the fraud of financial reports. On this premise, Hypothesis 3 (H3), which states that ineffective monitoring influences financial statements fraud, is rejected.

The fourth hypothesis states that change in auditor affects financial statement fraud (earnings management). The testing results for hypothesis 4 show that the t-value of the variable change in auditor is -1.351 while the t-table value with α = 0.05 and df (n-k) 27-5 = 22 is 0.68581. Based on these findings, it can be shown that the t-count is lower than the t-table value (-1.351 <0.68581), and it can be implied that the auditor's variable adjustment does not impact the fraud of the financial statements. On this premise, Hypothesis 4 (H4), which implies that the auditor's amendment affects fraud in financial statements, is rejected.

The fifth hypothesis states that change in director (DCHANGE) affects financial statement fraud (earnings management). The testing results for hypothesis 5 show that the t-count value of the variable change in director (DCHANGE) is -0.566, while the t-table value with α = 0.05 and df (n-k) 27-5 = 22 is 0.68581. Based on these results, it can be identified that the t-count is lower than the value of the t-table (-0.566 <0.68581), thus, it is assumed that director replacement has no significant influence on fraudulent financial reporting act. Hence the hypothesis 5 (H5) was not supported.

DISCUSSION

Based on the results of financial targets measured using ROA, financial targets affect financial statement fraud. Therefore, the higher the company's financial target, seen from the increase in ROA, will encourage the company to commit fraud by committing financial statement fraud. Pressure, which is one of the diamond theory fraud factors, can be detected by this variable. An undue pressure was put on management to make earnings meet the company's financial goals, which induced earnings management. This data is consistent with Widyastuti (2009) and Suyono & Farooque (2018) which showed that businesses that have significant revenues are more likely to participate in earnings management. The research results by (Norbarani, 2012) and Nugraha & Henny (2015) also show the same results, where the financial targets that are proxied by ROA influence the occurrence of fraudulent financial reporting.

As determined by the total asset turnover ratio, financial stability influences the fraud in financial statements based on the results. Martantya (2013) stated that management is always under pressure to display whether the firm can use its assets properly to produce income and supports this outcome. Management commits fraud using financial reports as a means of covering up the company's dire financial condition. Excessive pressure on management is conforming with the fraud diamond theory of pressure. One way is to change the appearance of the total assets to their liking. Companies manipulate income whenever their performance is threatened by financial stability or economic conditions. The percentage change in total assets indicates fraudulent financial statements. A study by Skousen et al., (2009), Sihombing (2014), and Tessa & Harto (2016), who previously found that financial stability induces fraud in financial reports, also confirm the findings of this article.

Based on the institutional makeup of the independent board of commissioners, inadequate monitoring would not affect fraudulent financial reporting. A fraud diamond component is an opportunity detected through insufficient monitoring and was not proved in this analysis. Opportunities may arise in organizations that have inadequate controls, are poorly run, or due to the nature of positions. The board's role in carrying out the supervisory function of the company's operations has not been running correctly, and the appointment and presence of the board of commissioners may only be made to fulfil company regulations. This result is

Volume 14, No. 1, April 2022, Page. 115-121

supported by Norbarani (2012), Pardosi (2015), and Putri et al., (2017) who in their research concluded that independent commissioners did not affect financial statement fraud.

Rationalization can be a difficult part of fraud detection. The audit documentation process also relies on the quality of the auditors. Research results suggest that auditor replacement does not have an impact on fraud. Many businesses did not change their auditors during the 2017 to 2019 period.

Capability, one of the elements in the fraud diamond theory, can be proxied by companies act of replacing their auditors. New auditors are expected to bring a better work atmosphere in terms of fraud detection. Frauds that generally large in number are not possible if there is no person with superior capabilities. Characteristics related to capabilities include position, understanding, and ego. The study confirms the view that director replacement does not influence fraudulent financial reporting. Few firms in this study changed their directors during the 2017-2019 period, and the results for only the observational data were less than ideal. Contrarily, Wolfe & Hermanson (2004) argued that capability is one of the factors that influence fraud and changes in directors, indicating that fraud.

CONCLUSION

Referring to the result of the analysis, the following conclusions are drawn: first, financial targets significantly influence the act of fraudulent financial reporting practices. Similar finding also applies to financial stability. On the other hand, the other three variables (i.e., ineffective monitoring, auditor, and manager replacement) do not stimulate managements' moral hazard in the form of fraudulent financial reporting. With its limitations, such as the relatively small number of samples, this study contributes to developing the knowledge related to financial reporting, particularly in fraudulent financial reporting and factors affecting it. Moreover, the result of this study adds value to the existing references in the following manners: first, this research leads to the advancement of theory of fraud diamond (Wolfe & Hermanson, 2004). This study further reinforces the notion that financial targets and financial stability could be used for fraud in financial reports. Investors are expected to understand variable financial targets and financial stability better so that this research can be used as an early detection tool for detecting fraud in the company's financial statements to make effective decisions. Second, for the advancement of scientific accounting knowledge, this study may provide a new insight that may be useful in elucidating the concept of financial targets and financial stability of fraud diamonds to identify financial statements fraud. This study is expected to become an encouragement for further studies for other parties.

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