

The Effect of Nature of Industry, Financial Stability, Ineffective Monitoring, and Changes in Company Directors on Indications of Fraudulent Financial Statements

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Article Info	Abstract
Received : 2023-10-01 Accepted : 2023-10-02 Published : 2024-01-12	Fraudulent financial statements are part of corporate management fraud. It is conducted based on the financial condition of the organization for the purpose of misleading users of financial statements by omitting values or amounts in the disclosure of financial statement documents. Therefore, it will mislead the stakeholders who are investing in the company. This study aims to analyze the effect of the nature of the industry, financial stability, ineffective monitoring, and changes in company directors on indications of fraudulent financial statements. The research population is manufacturing sector companies listed on the Indonesia Stock Exchange (IDX) for the 2017–2019 period, which are listed on the website www.idx.co.id . There are as many as 183 companies. The sampling method used is the purposive sampling method. The companies that meet the sampling criteria are 76. The analysis tool uses multiple linear regression. The results of this study shows that the nature of the industry has a positive effect on indications of fraudulent financial statements, financial stability has a positive effect on indications of fraudulent financial statements, and ineffective monitoring has a positive effect on indications of fraudulent financial statements. Meanwhile, the changes in company directors has no effect on indications of fraudulent financial statements.
Key words: nature of industry; financial stability; ineffective monitoring; changes in company directors; fraudulent financial statements	

INTRODUCTION

Financial reports are used by internal and external stakeholders in making decisions and showing accountability for using resources entrusted to management (IAI, 2015). Therefore, the information provided must be complete, clear, and able to accurately describe economic events that affect the company's financial results. The purpose of a company's financial statements is to show or demonstrate that the company's condition and profits are good. Many companies arbitrarily manipulate securities reports and distort the information contained in the income statement in order to provide their companies with good information and conditions (RisdaWanty, 2015). Falsification of financial statements is a form of fraud. According to the Treadway Commission, fraudulent financial statements refer to any action that intentionally deviates from company records, including misapplication of accounting standards, which results in materially misleading financial statements (Hasnan et al., 2013). This action makes the company's financial statements irrelevant to the data and information contained and causes misstatements and other errors that are detrimental to financial statement users, creditors, and investors. The factor that distinguishes fraud from error is whether the behavior underlying the misstatement of financial statements is intentional or unintentional (IAI, 2017).

Fraudulent financial statements are also common in Indonesia to cover up deficiencies in financial statements by making them more attractive to readers and other users. There are several fraud cases that have occurred in Indonesia, such as the case of PT Garuda Indonesia Tbk (Pratiwi, H., 2019). Companies that are state-owned and very complex can experience fraud. In the case of PT Garuda Indonesia Tbk, the misstatement of financial statements in 2018 regarding the cooperation agreement for the provision of connectivity services with PT Mahata

Aero Teknologi amounts to \$890.85 thousand dollars, or equivalent to IDR 11.33 billion (Kurnia, T., 2019). Likewise, other companies, such as PT Tiga Pilar Sejahtera Food, have overstatements of their 2017 annual financial statements of up to 4 trillion in trade receivables, group fixed asset inventories, IDR 662 billion in sales, and IDR 329 billion in EBITDA (Ernst & Young Indonesia, 2019).

Fraudulent financial reporting can result in losses and damage to a company's reputation, leading to lawsuits and fines (Nurliasari & Achmad, 2020). Therefore, predicting and preventing accounting fraud is important for businesses and their stakeholders. The fraud triangle is a concept used to explain the factors that influence the occurrence of fraud in an organization. The fraud triangle concept consists of three elements: pressure, opportunity, and rationalization (Cressey, D, 1953). The fraud triangle concept was first introduced by an accountant named Donald Cressey in 1953, and it still remains a relevant concept in today's business world.

In financial statements, the possibility of high misstatements can be caused by certain factors. One of them is an error in recording transactions that are directly recorded in the financial statements. It can also be caused by inadequate internal control and budgeting processes. Material misstatements can occur due to errors in the assessment, calculation, and recording of the company's financial transactions. This is also caused by factors external to the company, such as external pressure to achieve certain targets. In addition, according to ACFE (2014), the general reasons someone commits accounting fraud include encouraging investment with the release of shares, showing an increase in earnings per share, which can ultimately increase bonuses and dividends, covering up the inability to generate cash flow, concealment, covering up negative public perceptions of organizational performance, obtaining financing or obtaining more favorable financing terms, demanding higher prices for acquisitions, demonstrating compliance with financing agreements, achieving corporate goals, and failure to achieve good results for bonus purposes. Institutional ownership has impact toward firm performance, family's ownership does not impact toward firm performance, ownership concentration has impact toward firm performance and dividend policy has impact toward firm performance (Teguh et al, 2022).

This research was conducted based on the inconsistency of the results of previous studies regarding the effect of the nature of industry on indications of fraudulent financial statements. In the concept of the nature of industry, according to SAS 99 (AICPA, 2002), there are a number of conditions inherent in the nature of the industry that can provide opportunities for management to prepare financial statements that contain fraud. From agency theory, this can be applied to principals who try to encourage management to reduce the total amount of receivables, meaning that the level of receivables is lower than sales. This is in line with research conducted on the effect of the nature of industry, where Sihombing et al. (2014) concluded that the nature of industry has an effect on fraudulent financial statements. Meanwhile, research conducted by H. Adam Afiezan et al. (2021) concluded that the nature of industry has no effect on indications of fraudulent financial statements.

Then, on the financial stability variable, Skousen et al. (2009) show that the higher the ratio of changes in total assets of a company, the greater the possibility of fraudulent financial reporting by the company. If the company's total assets have suddenly and significantly changed from period to period in the absence of any appropriate increase in operational performance (a comparable increase in sales, net income, or transactions that can be supported), this may indicate that changes in assets may have been manipulated to improve the appearance of the company's financials. This is in line with research conducted on the effect of financial stability by Skousen et al. (2017), which resulted in the conclusion that financial stability has an effect on indications of fraudulent financial statements. Meanwhile, research conducted by Wahyuni et al. (2017) concluded that ineffective monitoring and financial stability have no effect on indications of fraudulent financial statements.

Furthermore, the ineffective monitoring variable refers to ineffective internal control in the company. According to the Committee of Sponsoring Organizations of the Treadway Commission (COSO, 2013), it indicates that there are weaknesses or failures in the application of internal control that allow undetected risks or fraud due to supervisory failures in certain

areas, which usually occur due to either weaknesses in the design or application of internal control in the company. This can be caused by a lack of understanding of the risks and needs of appropriate supervision, a lack of employee qualifications or training, and a lack of adequate information systems (COSO, 2013). This is in line with research conducted on the effect of ineffective monitoring by Septriani, Y., and Handayani, D. (2018), which concluded that ineffective monitoring has an effect on indications of fraudulent financial statements. Meanwhile, research conducted by Wahyuni et al. (2017) concluded that ineffective monitoring and financial stability have no effect on indications of fraudulent financial statements.

Lastly, the variable changes in company directors every year can be an indication of fraudulent financial statements. Firstly, if the replacement of the company's directors occurs after the disclosure of fraudulent financial statements that harm the company or other parties, it can raise suspicion that the changes in directors is related to concealing fraud or avoiding responsibility. Secondly, if the replacement of the company's directors occurs with significant changes in the financial statements, such as a drastic decrease in revenue, a large change in net income, or a sudden change in accounting methods, it may lead to suspicions of financial statement manipulation. Thirdly, if the replacement of directors and the transfer of the company occur after an audit that indicates fraudulent financial statements or an internal investigation that highlights unethical practices, then it may indicate the existence of previous fraudulent acts. This is in line with research conducted on the effect of changes in directors by Amira B, Khusnatul Z, and Ardyan FM (2018), which resulted in the conclusion that the changes in company directors has an effect on indications of fraudulent financial statements. Meanwhile, research conducted by Chyntia Tessa (2016) concluded that the changes in company directors has no effect on indications of fraudulent financial statements.

The existence of high fraud cases that occur in Indonesia's financial statements, especially in the manufacturing sector due to fraud, and the number of fraud cases that are difficult to detect Research on indicators of fraudulent financial statements in Indonesia is commonly used, but researchers make a difference, which is with the period from 2017 to 2019, the addition of one variable, namely 'changes in company directors', to expand the research sample from previous studies, which mostly used the three variables above as samples, and also from the selection of sectors that are generally studied in the fields of real estate and finance, where researchers choose the manufacturing sector that has been listed on the Indonesia Stock Exchange (IDX). Manufacturing companies have diverse sectors, a very broad range, and a larger scale. This can be generalized so that the test can be compared between one company and another.

This study aims to analyze the effect of the nature of industry, financial stability, ineffective monitoring, and changes in company directors on indications of fraudulent financial statements in manufacturing sector companies listed on the Indonesia Stock Exchange for the 2017–2019 period.

LITERATURE REVIEW

1. Agency Theory

Agency theory describes an agency relationship between owners and managers (Jensen & Meckling, 1976). According to Eisenhardt (1989), agency theory is a study related to planning and supervising managerial activities in the context that the principal (company owner) has different interests from the agent (manager). This contractual relationship allows a conflict of interest between shareholders and managers (Ross, Westerfield, and Jaffe, 2010). In Jensen and Meckling's (1976) research, it was found that an agency relationship exists when one or more principals hire an agent to perform obligations and delegate decision-making authority to the manager. Therefore, the manager is obliged to carry out the orders given by the principal.

This theory explains that information asymmetry creates problems between owners and managers. Managers who are given trust are supposed to work for the owners, but in reality, they work for their own interests. The conflict of interest between the two companies forces management to look for ways to improve company

performance in the hope of being recognized by the owner in the form of higher compensation. This is done by managers related to the conflict of interest that exists in the company, causing managers to face a number of pressures (pressure) from shareholders to improve the company's performance for the better, which makes the manager get appreciation (compensation) from shareholders for the performance performed. Because management has easy access to information, they have the opportunity to commit accounting fraud (Rani, 2016).

In agency theory, management manipulating financial statements can have a negative impact on the company's financial statements in several aspects. This allows the company to experience both internal and external losses. According to research from Eisenhardt (1989), internal and external mechanisms of supervision and control can reduce conflicts that occur between principals (company owners) and agents (managers). The mechanism of supervision and control has procedures so that the agent (manager) can comply with the interests of the principal.

2. Fraud Triangle Theory

The fraud triangle, also known as the fraud triangle, is a concept used to describe the factors that influence the occurrence of fraud in an organization. The fraud triangle concept consists of three elements: pressure, opportunity, and rationalization. Financial reporting fraud using the fraud triangle can occur in various business sectors and scales, from small-scale to multinational companies. A fraud triangle is a concept that explains the factors that cause someone to cheat in a company or organization.

The fraud triangle concept was first introduced by an accountant named Donald Cressey in 1953, and it has remained a relevant concept in today's business world. According to Albrecht (quoted from the National Whistleblowing Center), the fraud triangle states: (1) some sort of perceived pressure, (2) a perceived opportunity, and (3) some sort of motivation to cheat. The fraud triangle concept consists of three main components: pressure, opportunity, and rationalization. Pressure and pressure are factors that cause people to commit fraud (Bologna JC, 2020). The pressure can be financial, such as personal financial problems, increasing debt, or other financial needs. Opportunities are circumstances or conditions that allow someone to commit fraud. Opportunities can arise when individuals have unrestricted access to money or organizational resources, or when supervision and internal controls are weak. Rationalization is the method an individual uses to justify an act of fraud or deception.

3. Fraud

Fraud generally refers to fraudulent activities for personal gain or harm to others. According to Johnston et al. and Oktavia (2014), fraud is an intentional activity involving errors by certain parties that result in the misrepresentation of financial statements. On the other hand, Albrecht et al. (2016) define fraud as the act of someone trying to gain an advantage over others by making false statements in a deceptive manner. The Association of Certified Fraud Examiners explains fraud as a scam by individuals or organizations who know that the mistake can result in some losses to individuals, entities, and other parties (Ernst & Young LLP, 2009). Many cases of fraud have occurred in Indonesia. No exception occurs in large companies and even in small and medium business lines. Fraud can also occur in all sectors in Indonesia, such as the real estate sector, sharia, and even manufacturing.

2.2 Fraud Perpetrators

Fraud perpetrators are individuals or groups who commit fraud. The perpetrators of fraud themselves are people within the company. This is because individuals within the company can access information within the company and use this information to commit illegal acts. Because people internal to the company understand the system and

controls, it is difficult to detect fraudulent acts committed by people internal to the company (Widjaja, 2013).

2.2 Types of fraud

According to Albrecht (cited by Nguyen, 2008), fraud can be grouped into five types: First, employee embezzlement or occupational fraud is the type of offense committed by subordinates against their superiors this type of fraud is committed by subordinates, either directly or indirectly, by deceiving their superiors. Second, management fraud, this is a type of fraud committed by management against shareholders, creditors, and other parties that depend on financial statements. this type of fraud is committed by management by providing false information, such as financial information. Third, investment scams, this is a type of fraud by individuals on investors. this type of fraud is committed by individuals by tricking investors into investing their money in the wrong investments. Fourth, vendor fraud is type of fraud is committed either by organizations or individuals offering goods or services to companies that do so. this type of fraud is committed by organizations by overpricing goods and services or not shipping goods even though the payments have been made. Fifth, customer fraud is type of fraud is committed by customers of organizations or companies that sell goods or services. this type of fraud is committed by the client by deceiving the seller by lying to the seller if the items offered to the client are unsuitable or by accusing the seller of not providing more than it should.

2.2 Fraud Tree

The Association of Certified Fraud Examiners (ACFE), an international organization that is an association of forensic accountants in the United States, describes fraud in the form of a fraud tree, which describes the branches of fraud in the work relationship. As well as branches and twigs (Tuanakotta, 2012).

The fraud tree consists of three main branches: corruption, asset misappropriation, and fraudulent statements. Corruption is often associated with other actions, such as collusion and nepotism. Conflicts of interest are often encountered in various forms, such as those owned by officials (rulers) and their families who are suppliers or partners of government institutions and in the business world (Tuanakotta 2012).

Asset misappropriation is called theft in everyday language. However, legally, the unlawful (illegal or unlawful) taking of assets by a person authorized to control or monitor the property is called embezzlement (Tuanakotta, 2012). Asset misappropriation includes the act of stealing a company's assets when the effect of the fraud is to substantially prevent the financial statements from being reported in accordance with Generally Accepted Accounting Principles (GAAP) (SAS 99, 2002). Based on GAAP (SAS 99, 2002), fraudulent financial statements are intentional reports that are intended to mislead users of financial statements when the effect is to make the financial statements substantially invisible. This fraud involves misrepresentation or misstatement (both overstatement and understatement), which consists of financial and non-financial.

4. Fraudulent Financial Statements

Fraudulent financial statements or financial reporting fraud is part of corporate management fraud. According to ACFE (2014), financial statement fraud is the deliberate presentation of an organization's financial condition for the purpose of misleading users of financial statements by omitting values or amounts in the disclosure of financial statement documents. According to ACFE (2014), common reasons for someone to commit accounting fraud include encouraging investment with the release of shares, showing an increase in earnings per share, which can ultimately increase bonuses and dividends, covering up the inability to generate cash flow, concealment, covering up negative public perceptions of organizational performance, obtaining financing or obtaining more favorable financing terms, demanding higher prices for acquisitions, showing compliance with financing agreements, achieving corporate goals, and failure to achieve good results for bonus purposes.

Therefore, it is important for the company to prevent and control fraud in the financial statements that occur in the company. To prevent fraudulent financial statements, the F-score model is used. The F-score model is a fraud detection method in the form of a probability scale, red flag, or signal of possible earnings management or misstatement (Dechow et al., 2011). Joseph Piotroski's research (2000) explains the relationship between the F-score model and empirical analysis of historical data. In measuring the F-score model, measurements are used using accrual quality and financial performance in financial statements. This shows the quality of the financial statements.

Hypothesis Development

The Effect of the Nature of Industry on Indications of Fraudulent Financial Statements

In the financial statements, there are certain accounts whose balances were determined by the company based on estimates, such as bad debt accounts and obsolete inventory accounts. Things like this will encourage investors to invest their funds in the company. According to Summers and Sweeney (1998), management focuses on these two accounts when they intend to manipulate financial statements. In inventory, there is a ratio of inventory to sales, which can provide an overview of how the company manages inventory. Meanwhile, in bad debt, there is a ratio of current receivables to sales, which can give an idea of how the company collects money from sales.

The receivables used in measuring are the net receivables owned by the company, which have been reduced by the allowance for bad debts. This is done because the accounts receivable ratio provides an overview of the efficiency and financial risks associated with bad debts and inventory in the industry. According to SAS 99 (AICPA, 2002), there are a number of conditions inherent in the nature of the industry that can provide opportunities for management to prepare financial statements that contain fraud. One of these industry traits is that financial accounting involves subjective judgments, making it difficult to justify calculations such as accounting for assets, liabilities, revenues, and expenses. These subjective judgments are usually accounts whose values are based on estimates, such as bad debts and inventories (Yossi Septriani, 2018). Siddiq (2017) explains that accounts receivable and inventory require management to make subjective estimates or judgments in estimating the amount of accounts receivable and obsolete inventory that are due.

By allowing companies to estimate the value of receivables, this opens up opportunities for companies to use these accounts to manipulate financial statements (Skousen et al., 2009). This is because principals want their company's cash flow to be smooth, especially for its core activities such as sales. On the other hand, it becomes clear to the management of the company over time that management cannot fulfill the wishes of the principal; they will commit financial statement fraud, which greatly increases the estimated amount of bad debts affecting the accounts receivable account (AICPA, 2002). This means that the higher the value of the nature of the industry influence variable, the higher the fraudulent financial statement. This is supported by research (Yossi Septriani, 2018), which states that the nature of industry variables as measured by the accounts receivable ratio positively affects indications of fraudulent financial statements. Based on the description above, the hypothesis is as follows:

H1: The nature of industry has a positive effect on indications of fraudulent financial statements.

The Effect of Financial Stability on Indications of Fraudulent Financial Statements

Financial stability means a situation where the financial position is stable, and if the financial position deteriorates, there is a risk of fraud by company management. Companies are said to have a stable financial position when they are able to meet their financial obligations in the long term and have sufficient capacity to meet their operational needs (Ross, SA, Westerfield, RW, Jordan, BD, & Daff, D, 2018). Companies can also be declared to have good financial stability if they have effective financial management, good risk control, and transparency in financial reporting (Brigham, EF, & Houston, JF, 2018).

Based on Brealey, R. A., Myers, S. C., & Allen, F. (2017), the company's financial stability is measured based on the increase in total assets from year to year. Total assets describe the assets owned by the company, which include current and non-current assets. High changes in total assets show that the company is in good condition. The high change in the company's total assets is expected to provide high profits for creditors and investors. However, high changes in total assets also put pressure on the company to be able to generate returns in accordance with the total assets available (Ni Kadek Dwi Susianti, 2015). When the company's financial stability is threatened, management faces pressure to commit financial statement fraud (Skousen et al., 2009). Financial instability in a company can encourage management to manipulate total assets. This causes fraud in management's financial statements, especially regarding assets.

As a result, manipulation of total assets is often carried out with the aim of manipulating the company's financial statements to make them look more stable or better than they really are. Financial instability in a company can encourage management to manipulate total assets. In No. SAS 99, when financial stability or profitability is poor or below average due to economic, industry, or business unit circumstances, managers feel pressure to commit fraud on financial statements (Skousen and Twedt, 2009). This causes fraud in management's financial statements, especially regarding assets. Usually, growing companies need more assets to develop their businesses. The increase in asset changes is often used by management as financial reporting fraud (Aprilia et al., 2017), where these assets can be classified as fraud. This is supported by research conducted by Bawekes et al. (2018), and Septriyani & Handayani (2018) show that financial stability has a positive effect on fraudulent financial statements. Based on the description above, the hypothesis is as follows:

H2: Financial stability has a positive effect on indications of fraudulent financial statements

The Effect of Ineffective Monitoring on Indications of Fraudulent Financial Statements

Ineffective monitoring describes a company situation where the control unit is not running properly. Based on research by Peter B. Lorange (2002), ineffective monitoring is the inability of the supervisory system to accurately collect and analyze relevant data, so that it is unable to identify existing problems or errors. Ineffective monitoring refers to ineffective internal control within the company. According to SAS No. 9, it explains that a weaker supervisory system leads to higher fraudulent financial statements. According to the Committee of Sponsoring Organizations of the Treadway Commission (COSO, 2013), it shows weaknesses or failures in the application of internal controls that allow undetected risks or fraud to occur. Supervisory failures in certain areas usually occur due to weaknesses in the design or implementation of internal controls in the company. This can be caused by a lack of understanding of the risks and the need for appropriate controls, a lack of employee qualifications or training, and a lack of adequate information systems (COSO, 2013).

The existence of financial statement manipulation carried out by management in ineffective monitoring conditions is based on a feeling of encouragement to improve the company's image or show better performance in reality (Beneish, M. D., & Vargus, M. E., 2002). In a situation of ineffective monitoring, management hopes that the manipulation will not be detected, and the falsified results may benefit the company's reputation or management's own personal interests (Klein, A. (2002). In some cases, management may feel pressure to manipulate financial statements to match market and shareholder expectations. If existing controls are not effective in understanding and assessing these targets, management may feel compelled to manipulate financial statements to achieve desired goals.

Therefore, the supervision of independent commissioners is needed to ensure the integrity and reliability of the company's financial statements. According to Law No. 40 of 2007 on Limited Liability Companies, independent commissioners are selected based on their knowledge and experience in finance, accounting, and corporate governance. This knowledge allows them to understand the complexity of financial statements and detect potential fraud. The existence of a high number of independent commissioners in the company can increase the supervisory function so that it can reduce the possibility of fraud in the financial statements. This allows them to carry out supervisory duties independently and oversee management with

objectivity. This is supported by the results of research by Rahmawati et al. (2020), which show that ineffective monitoring has a positive effect on fraudulent financial reporting. Based on the description above, the hypothesis is as follows:

H3: Ineffective monitoring has a positive effect on indications of fraudulent financial statements

The Effect of the Company's Directors on Indications of Fraudulent Financial Statements

According to Fred R. and Forest R. (2015), the changes in directors is a process where shareholders or company owners decide to replace incumbent board members with new individuals. Changes in company directors can be an attempt by the company to improve the performance of the previous directors by changing the composition of the company's directors or recruiting new directors who are considered more qualified than the previous directors (Judge, W. Q., & Zeithaml, C. P., 1992). On the other hand, the replacement of directors can be an attempt by the company to get rid of directors who may be aware of fraud committed by the company, and the replacement of new directors requires an adjustment period so that the initial performance is not optimal (Dalton, D. R., Daily, C. M., Johnson, J. L., & Ellstrand, A. E., 1999). New directors moving into the company may not have a deep understanding of the new company's accounting and control systems. This lack of understanding can lead to ignorance and negligence in financial reporting that can be exploited in fraud. Thus, the presence of new directors often results in instability and chaos in the company's organizational structure. This can create an opportunity for irresponsible individuals to manipulate the financial statements, such as by falsifying or concealing transactions.

According to Wolfe and Hermanson (2004), the changes in directors is a form of conflict of interest. Conflicts of interest occur when individuals or groups have interests that conflict with the interests of the company or other stakeholders. Conflicts of interest can arise as a result of internal competition among board members for power, influence, or control over the company. This kind of competition can destabilize the company's directors and lead to board turnover. In addition to factors from organizational politics (office politics), board turnover can also occur because the company is experiencing a period of stress (Stress Period), such as decreased financial performance, financial pressure, and increased competition, which can create an environment that triggers the risk of financial statement fraud (Dalton, D. R., Daily, C. M., Johnson, J. L., & Ellstrand, A. E., 1999).

Based on research from Cohen, JR, Krishnamoorthy, G., and Wright, AM (2002), there is a relationship where the changes in directors can be an indication of financial statement fraud. First, if the changes in directors occurs after the disclosure of fraudulent financial statements that harm the company or other parties, it can lead to the suspicion that the changes in directors is related to hiding fraud or avoiding responsibility. Second, if the changes in directors is followed by significant changes in the financial statements, such as a drastic decrease in revenue, a large change in net income, or a sudden change in accounting methods, it may raise suspicions of financial statement manipulation. Finally, if the changes in directors and the company move occur after an audit finding that indicates financial statement fraud or an internal investigation that highlights unethical practices, then it may indicate the existence of previous fraudulent acts. This is supported by research by Devy (2017) and Putriasih (2016), which states that the variable changes in directors has a positive and significant effect on financial statement fraud. Based on the description above, the hypothesis is as follows:

H4: The changes in the company's directors has a positive effect on indications of fraudulent financial statements

METHODS

In conducting this research, the type of research used is quantitative. This type of data uses secondary data to make calculations that describe the processed data. The research population is manufacturing sector companies listed on the Indonesia Stock Exchange (IDX) for the period 2017–2019, which are listed on the website www.idx.co.id. There are as many as 183 companies. The sample criteria are, first, manufacturing companies listed on the Indonesia Stock Exchange (IDX) consecutively during 2017–2019. Second, manufacturing companies publish the required annual report during 2017–2019. Third, manufacturing companies that earn

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profits consecutively during 2017–2019. Fourth, manufacturing companies that present financial statements in rupiah currency. Furthermore, the companies that meet the sampling criteria are 76. The sampling method used is the purposive sampling method. The purposive sampling method is a sampling method in accordance with the required sample requirements (Sugiyono, 2017). The analysis tool uses multiple linear regression tests. The documentation observation technique is through the financial statements of sample companies, books, articles, websites, and other scientific journals. Definition of operational variables and measurement show at table 1.

Table 1. Definition of Operational Variables and Measurements

Variable	Definition	Indicator	Scale
Indications of Fraudulent Financial Statements (Y) (Chistopher J. Skousen, 2009)	This type of fraud is characterized by the intention to deliberately commit financial statement fraud or an error in the amount of financial statement disclosure with the intention of deceiving users of financial statements (Johnstone et al., 2014).	$F\text{-Score} = \text{Accrual Quality} + \text{Financial Performance}$ Accrual quality is proxied by RSST accrual, and financial performance is proxied by the total increase in changes in accounts receivable, changes in inventory accounts, changes in credit sales accounts, and changes in EBIT.	Ratio
Nature of Industry (X ₁) (Chistopher J. Skousen, 2009)	The nature of industry is an ideal condition for an industrial company. There are certain accounts in the financial statements, the balance of which is determined by the company. Summers and Sweeney (1998) point out that accounts receivable and inventory require subjective judgment when evaluating bad accounts. Summers and Sweeney (1998) also found that managers focus attention on these two accounts when they intend to	RECEIVABLE $= \frac{\text{Receivable } t}{\text{Sales } t} - \frac{\text{Receivable } t - 1}{\text{Sales } t - 1}$	Ratio

	manipulate financial statements.		
<i>Financial Stability</i> (X ₂) (Chistopher J. Skousen, 2009)	Financial stability is a condition when a company's finances are unstable. The company's financial stability is reflected in the state of its assets. Total assets describe the assets and wealth owned by the company (Skousen et al., 2009).	$\text{ACHANGE} = \frac{\text{Total assets } t - \text{Total assets } t - 1}{\text{Total assets } t - 1}$	Ratio
<i>Ineffective Monitoring</i> (X ₃) (Chistopher J. Skousen, 2009)	Ineffective monitoring describes a situation where the company does not have an effective control unit to monitor company activities. It is generally believed that the independent company's commissioners has a very important role in monitoring upper management (Skousen et al., 2009).	$\text{BDOUT} = \frac{\text{Number of Independent Commissioners}}{\text{Total Number of Company's Commissioners}}$	Ratio
The Changes in Company Directors (X ₄) (David T.Wolfe, 2004)	The changes in company directors is a process where shareholders or company owners decide to replace incumbent board members with new individuals (Fred R & Forest R, 2015).	The changes in company directors uses a dummy variable; if the company makes a replacement of directors during 2017–2019, it is given code 1 (one); if the company does not make a changes in company directors during 2017–2019, it is given code 0 (zero).	Nominal

RESULT AND DISCUSSIONS

1. Descriptive Analysis of Data

The results of the descriptive test in this study include the minimum value, maximum value, and mean value of one dependent variable and the independent variable. The purpose of this study is

to provide an overview of the dependent variable data in the form of indications of fraudulent financial statements as well as independent variables in the form of the nature of the industry, financial stability, ineffective monitoring, and changes in company directors. The following are the results of descriptive statistical tests:

Table 2. Descriptive Statistical Test Results

Descriptive Statistics					
	N	Minimum	Maximum	Mean	Std. Deviation
Nature of Industry	76	0.0824	0.9327	0.141004	0.0918477
Financial Stability	76	0.9951	1.0510	0.101977	0.2549013
Ineffective Monitoring	76	0.0000	1.0000	0.5855	0.1792
The Changes in Company Directors	76	0.0000	1.0000	0.596495	0.2997192
Fraudulent Financial Statement	76	3.5229	2.0649	0.967693	0.9012486
Valid N (listwise)	76				

Source: SPSS 24 Output

At table 2 show, the results of the descriptive statistical analysis show that the number of observations in the study (N) is 76, obtained within a period of 3 years. Based on table 2, it can be seen that the nature of the industry variable obtained a maximum value of 0.9327, a minimum value of -0.0824, an average value (mean) of 0.141004, and a standard deviation of 0.091847. The financial stability variable obtained a maximum value of 1.0510, a minimum value of -0.9951, an average value (mean) of 0.101977, and a standard deviation of 0.2549013. The ineffective monitoring variable obtained a maximum value of 1.0000, a minimum value of 0.0000, an average value (mean) of 0.5855, and a standard deviation of 0.1792. The variable changes in company directors obtained a maximum value of 1.0000, a minimum value of 0.0000, an average value (mean) of 0.59649, and a standard deviation of 0.2997192. This means that the data is fully capable of explaining the entire thing. Not only that, the results of the standard deviation value can show the level of risk taken. If the result of the standard deviation value is smaller than the average value, the performance can be said to be good.

2. Classical Assumption Test

The classical assumption test is carried out in order to obtain regression results that can be accounted for and have unbiased results. The classic assumption test in this study consists of a normality test, a multicollinearity test, a heteroscedasticity test, and an autocorrelation test. The following are the results of the classic assumption test:

2.2 Normality Test

The normality test is used to determine whether the residual value is normally distributed or not. A good regression model is one that has a normal distribution. A regression equation is said to pass normality if the significance value of the Kolmogorov-Smirnov test is greater than 0.05. The following are the results of the normality test:

Table 3. Normality Test Results

One-Sample Kolmogorov-Smirnov Test		
		Unstandardized Residual
		76
N		0.0000000
Normal Parameters ^{a,b}	Mean	0.89239316
	Std.	0.100

Deviation		
Most Extreme Differences	Absolute	0.092
	Positive	-0.100
	Negative	0.100
Test Statistic		
Asymp. Sig. (2-tailed)		0.200 ^c

Source: SPSS 24 Output

Based on table 3 above, it can be seen that the significance of the Kolmogorov-Smirnov value, which is above the 0.05 confidence level, is 0.20. This shows that the data is normally distributed.

2.2 Multicollinearity Test

The multicollinearity test aims to determine whether there is an intercorrelation (strong relationship) between the independent variables. A good regression model is characterized by no intercorrelation between independent variables. One of the most accurate ways to test for multicollinearity can be seen from the variance inflation factor (VIF) and tolerance value. If the VIF value is < 10 and the tolerance value is > 0.10 , then there is no multicollinearity. The following are the results of the multicollinearity test:

Table 4. Multicollinearity Test Results

Coefficients ^a			
Model		Collinearity Statistics	
		Tolerance	VIF
1	<i>Nature of Industry</i>	0.966	1.035
	<i>Financial Stability</i>	0.890	1.123
	<i>Ineffective Monitoring</i>	0.991	1.010
	<i>The Changes in Company Directors</i>	0.911	1.097

a. Dependent Variable: *Fraudulent Financial Statement*

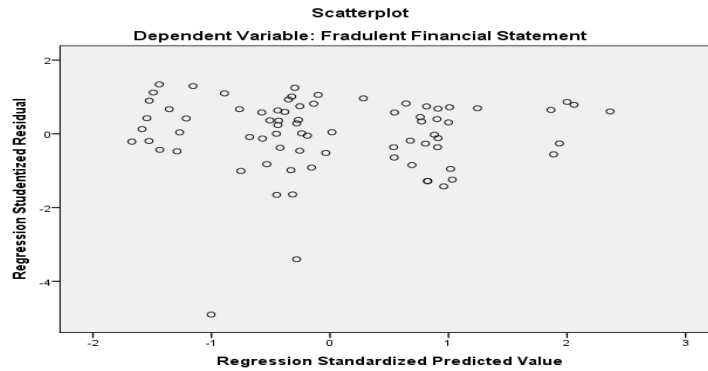
Source: SPSS 24 Output

Based on table 4 above, it can be seen that there are no multicollinearity symptoms between independent variables because all variables have a tolerance value greater than 0.10 and a VIF value smaller than 10.

2.3 Heteroscedasticity Test

The heteroscedasticity test aims to test whether in the regression model there is an inequality of variance from the residuals of one observation to another. A good regression model is one with homoscedasticity, not heteroscedasticity. The method used to detect the presence or absence of heteroscedasticity is testing using a scatter plot. The following are the results of the heteroscedasticity test:

Table 5. Heteroscedasticity Test Results



Source: SPSS 24 Output

Based on Table 5 above, it can be seen that there is no clear pattern or does not form a certain pattern, and since the points are above the number 0 on the Y axis, it can be concluded that there is no heteroscedasticity.

2.4 Autocorrelation Test (Durbin Watson)

The autocorrelation test serves to show the effect of data from previous observations in regression. The test results will help predict whether the model is biased or can provide autocorrelation-free regression prediction results. To determine whether there is autocorrelation in the regression model data, the Durbin-Watson test (DW test) can be used.

Table 6. Autocorrelation Test Results

Model Summary ^b					
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	0.140 ^a	0.020	-0.036	0.9171866	2.139

a. Predictors: (Constant), *Changes in Company Directors, Nature Of Industry, Ineffective Monitoring, Financial Stability*
b. Dependent Variable: *Fraudulent Financial Statement*

Source: SPSS 24 Output

Table 6, it can be seen that the Durbin-Watson value (d-count) is 2.139. With a significance of 0.05, N = 76, and the number of independent variables k = 4, the value of dU = 1.7399 is obtained, and the value of dL = 1.5190. Then the value (4-dL) = 2.481 value (4-dU) = 2.2601 so that the value of dU < dW < 4-dU = 1.7399 < 2.139 < 2.2601. Based on these results, it can be concluded that there is no autocorrelation.

3. Multiple Linear Regression Analysis

The model used to analyze the effect of independent variables on the dependent variable is a multiple linear regression model (multiple regression method). This model was chosen because this study was designed to examine the independent variables that affect the dependent variable.

Table 7. Multiple Linear Regression Analysis Results

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	1.206	0.293		4.111	0.000
<i>Nature of Industry</i>	0.141	1.173	0.014	0.120	0.005
<i>Financial Stability</i>	0.004	0.520	0.026	0.407	0.020
<i>Ineffective Monitoring</i>	0.002	0.026	0.011	0.093	0.000

<i>Changes in Company Directors</i>	-0.402	-0.280	-0.141	1.244	0.260
a. Dependent Variable: <i>Fraudulent Financial Statement</i>					

Source: SPSS 24 Output

Table 7, show, multiple linear regression analyses obtained positive and negative values. If the value of the multiple linear regression analysis is positive, it means that the relationship between the independent variable and the dependent variable is directly proportional. Meanwhile, if the value of multiple linear regression analysis is negative, the relationship between the independent variable (variable X) and the dependent variable (variable Y) is inversely proportional. The regression equation in this study is as follows:

$$Y = 1.206 + 0.141 X_1 + 0.004 X_2 + 0.002 X_3 + 0.402 X_4 + e$$

Based on the multiple linear regression equation in this study, it can be concluded: β_0 is a constant value without being affected by any variable, which means that the level of fraudulent financial statements in manufacturing companies is 1.206. In β_1 of nature of industry is 0.141 is a value that shows a positive relationship between the independent and dependent variables. Where there is a one-unit increase in the nature of industry variables, the possibility of fraudulent financial statements will be greater. In β_2 of financial stability is 0.004 is a value that shows a positive relationship between the independent and dependent variables. With every one-unit increase in the financial stability variable, the possibility of fraudulent financial statements will be greater. In β_3 of ineffective monitoring is 0.002 is a value that shows a positive relationship between the independent and dependent variables. With every one-unit increase in the ineffective monitoring variable, the possibility of fraudulent financial statements will be greater. In β_4 of changes in company of directors is -0.402 is a value that shows a negative relationship between the independent and dependent variables. Every one-unit increase in the variable changes in company of directors lowers the possibility of fraudulent financial statements.

3.1 Partial Test (t Test)

In this study, if each significance coefficient of the independent variable has a value smaller than 5% (0.05), which is set as the degree of confidence, it can be concluded that the independent variable partially has a significant effect on the dependent variable. The following are the results of the t test:

Table 8. Partial Test Results (t Test)

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	1.206	0.293		4.111	0.000
<i>Nature of Industry</i>	0.141	1.173	0.014	0.120	0.005
<i>Financial Stability</i>	0.004	0.520	0.026	0.407	0.020
<i>Ineffective Monitoring</i>	0.002	0.026	0.011	0.093	0.000
<i>Changes in Company Directors</i>	-0.402	-0.280	-0.141	1.244	0.260
a. Dependent Variable: <i>Fraudulent Financial Statement</i>					

Source: SPSS 24 Output

Based on table 8, the t test results indicate that the nature of industry variable on fraudulent financial statements obtained a significance value of 0.005, which is smaller than the confidence level of 5% (0.05), indicating that H_{01} is rejected and H_{a1} is accepted. These results indicate that the nature of industry variables has a positive effect on fraudulent financial statements. This means that the higher the nature of the industry, the more fraudulent financial

statements will increase. Furthermore, the variable financial stability on fraudulent financial statements obtained a significance value of 0.020, which is smaller than the confidence level of 5% (0.05), indicating that H_{02} is rejected and H_{a2} is accepted. These results indicate that the financial stability variable has a positive effect on fraudulent financial statements. This means that the higher the financial stability, the more fraudulent financial statements will appear. Furthermore, the variable ineffective monitoring on fraudulent financial statements obtained a significance value of 0.000, which is smaller than the confidence level of 5% (0.05), indicating that H_{03} is rejected and H_{a3} is accepted. These results indicate that the ineffective monitoring variable has a positive effect on fraudulent financial statements. This means that the higher the ineffective monitoring, the more fraudulent financial statements will increase. Last, the variable changes in company directors on fraudulent financial statements obtained a significance value of 0.260, which is greater than the confidence level of 5% (0.05), indicating that H_{04} is accepted and H_{a4} is rejected. These results indicate that the changes in company directors has no effect on fraudulent financial statements.

3.2 Test Coefficient of Determination

The coefficient of determination (R^2) are zero and one. The low value (R^2) indicates that the ability of the independent variables to explain the variation in the dependent variable is very limited, while the value (R^2) which is close to one explains the ability of the independent variables to provide the information needed to predict the variation of the dependent variable.

Table 9. Coefficient of Determination Analysis Results

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.726 ^a	0.602	0.575	0.9171866
a. Predictors: (Constant), <i>Changes in Company Directors, Nature of Industry, Ineffective Monitoring, Financial Stability</i>				

Source: SPSS 24 Output

Based on table 9, the magnitude of the influence of the independent variables on the dependent variable indicated by the total determination value R square of 0.602 means that 60.2% of variations in fraudulent financial statements are influenced by variations in nature of industry, financial statements, ineffective monitoring, and changes in company directors while the remaining 39.8% are explained by other factors.

3.3 Simultaneous Test (F Test)

In this study, if each significance coefficient of the independent variable has a value smaller than 5% (0.05), which is set as the degree of confidence, it can be concluded that the independent variable simultaneously has a significant effect on the dependent variable.

Table 10. Simultaneous Test Results (F Test)

ANOVA ^a					
Model		Sum of Squares	df	Mean Square	F
1	Regression	1.191	4	0.298	3.544
	Residual	59.727	71	0.841	
	Total	60.919	75		

a. Dependent Variable: *Fraudulent Financial Statement*

b. Predictors: (Constant), *Changes in Company Directors, Nature of Industry, Ineffective Monitoring, Financial Stability*

Source: SPSS 24 Output

Based on Table 10, the effects of the independent variable on the dependent variable is indicated by the Sig value of $0.02 < 0.05$. In addition, the calculated F value on SPSS 24 is 3.544 and the F table value is 2.73. Based on this analysis, it can be concluded that $F_{\text{count}} > F_{\text{table}}$ ($3.544 > 2.73$), and it can be concluded that the variables of nature of industry, financial stability, ineffective monitoring, and changes in company directors simultaneously or together have a significant effect on the dependent variable, namely fraudulent financial statements.

DISCUSSION

Discussion

The Effect of the Nature of Industry on Fraudulent Financial Statements

The nature of the industry affects fraudulent financial statements. Accounts receivable is one of the accounts whose amount is determined or influenced by the company's estimates and subjectivity. For this reason, based on SAS No. 9, there is a possibility of fraudulent financial statements in accounts receivable. The results of this study indicate that the nature of industry has a significant positive effect on fraudulent financial statements. An increase in the company's accounts receivable can be an indication that the company's cash turnover is not good and will reduce the amount of cash for its operational activities. Limited cash can be an encouragement for management to manipulate financial statements.

If the company wants to attract investors, then one of the efforts to achieve this goal is to manipulate the amount of accounts receivable, either by manipulating the due date or by eliminating long-term receivables (Subramanyam and Wild, 2008). The increase in the company's accounts receivable from the previous year can be an indication that the company's cash turnover is not good. The large number of accounts receivable owned by the company will definitely reduce the amount of cash that the company can use for its operational activities. Limited cash can be an encouragement for management to manipulate financial statements.

The effect of the nature of the industry on fraudulent financial statements may vary based on the characteristics of each industry. Some industries may have a higher risk of financial fraud due to the complexity of their operations, stricter regulations, or other characteristics. However, keep in mind that this trait is not absolute, and financial fraud can occur in various types of industries (Hope & Thomas, 2013).

The results of this study are consistent with research conducted by Ayu Fitaloka (2021), Surbakti Karo-Karo (2022), Terzaghi (2017), and Kennedy Sihombing (2014), which states that the nature of industry has a significant effect on fraudulent financial statements. The subjectivity of the trade receivable assessment allows fraud in the financial statements. However, the results of this study are not in line with research conducted by H. Adam (2021), Wahyuni (2017), Muhammad Iqbal (2016), and Yossi Septriani (2018), which states that the nature of industry variables has no significant effect on fraudulent financial statements.

The Effect of Financial Stability on Fraudulent Financial Statements

Financial stability has a significant effect on fraudulent financial statements. Overall, the financial condition of the companies used as research samples in the last three years is in a conducive economic condition, so company management does not have the urge to commit fraudulent financial statements. Financial stability, as measured by the level of change in assets, is proven to have a positive influence on fraudulent financial statements. Assets are one indicator that illustrates how much the company's wealth is, so changes in assets that occur have an important meaning in the possibility of fraudulent financial statements. Changes in assets are an indicator used to describe whether the company's condition is stable or unstable.

When the company has instability, as evidenced by the rise and fall of assets that are too significant, it will put pressure on management. This is because managers or company management have the responsibility to maintain the company's financial stability. Therefore, if there is company financial instability, company management has failed to fulfill its responsibilities in an effort to maintain the company's financial stability, which will affect the assessment of management performance (Riandani & Rahmawati, 2019). On that basis,

company management will commit financial statement fraud by manipulating the amount of assets so that the performance of management is considered successful by interested parties in the company. The results of this study are in line with research conducted by Yossi Septriani (2018), Surbakti Karo-Karo (2022), and Muhammad Iqbal (2016), which states that financial stability affects fraudulent financial statements. However, the results differ from the research by Wahyuni and Gideon Setyo Budiwitjaksono (2017), which states that financial stability has no effect on indications of fraudulent financial statements.

Regression analysis results reveal that corporate social responsibility and tax avoidance are positively associated, corporation with high corporate social responsibility disclosure are less likely to engage in tax avoidance. Family ownership, on the other hand, affects tax avoidance negatively which means that family firms engage in more tax avoidance than non-family firms. Audit quality has a significant positive effect on tax avoidance but does not affect the relationship of family ownership to tax avoidance (Santi and Elivia, 2022)

The Effect of Ineffective Monitoring on Fraudulent Financial Statements

Ineffective monitoring has a significant positive effect on fraudulent financial statements. The ineffectiveness of supervision or inadequate monitoring in a company can contribute to fraudulent financial statements. Lack of proper supervision allows individuals within the company to carry out fraudulent practices or manipulate financial data without being detected. Good supervision is needed to prevent and detect fraudulent financial statements (Abdullahi et al., 2015).

When controls are ineffective, this creates a gap where individuals with bad intentions can manipulate financial data to support their goals. The lack of strict supervision and the lack of a strong internal control system make it difficult to detect or prevent fraudulent practices such as misrepresentation of information, inflation of revenue, or omission of costs (Andayani, 2010). Therefore, companies must have a good supervisory mechanism to minimize the risk of fraudulent financial statements.

This is in line with research by Kusumosari (2020) and Lestari & Henny (2019) showing that supervisory ineffectiveness has a positive effect on financial statement fraud. Based on agency theory, the principal wants the manager to do his job well so that the principal authorizes the company's commissioners to oversee the manager's performance. However, if the supervision of the company's commissioners is ineffective, the manager has the opportunity to commit fraud in the financial statements. The results of this study are in line with research conducted by Annisu (2019) and Putri (2017), which states that ineffective monitoring has a positive effect on fraudulent financial statements. However, the results of this study differ from research conducted by Ayu Fitaloka (2021) and Wahyuni (2019), which state that the ineffective monitoring variable has no effect on fraudulent financial statements.

The Effect of Changes in Company Directors on Fraudulent Financial Statements

The change of company directors does not affect fraudulent financial statements. This is because stakeholders or directors make changes to the composition of the company's directors not to hide fraud but to obtain a more competent company's directors to manage company resources (Wolfe & Hermanson, 2004). Changes in company directors can be caused by several things, such as the expiration of the company's directors' term of office, personal resignation, or death of directors. In addition, the replacement of directors who are more competent in their fields will improve the company's performance for the better in the future (Aprialiani et al., 2017).

There is supervision from the company's commissioners regarding the performance of each director and the recruitment of more competent directors. Changing the company's company's directors is a process in which members of the company's directors, such as executive directors, non-executive directors, or members of the company's directors, are replaced by new individuals. Changing the company's company's directors (capability) is one component of the fraud hexagon theory (Abdullahi et al., 2015). The company's directors is the party responsible for running

the company and is the top management group. The replacement of old directors with new ones is usually carried out in an effort to improve corporate governance in order to prevent or reduce the occurrence of fraudulent financial statements.

If board changes are carefully made and effective oversight is maintained, these changes may not have a direct impact on fraudulent financial statements. The organizational culture underlying business practices can also play a role. Board changes may not directly change the organizational culture that enables fraudulent practices (Agusputri & Sofie, 2019). As board changes are carried out with transparency and clear regulations, their impact may be more controlled.

This study provides support for the results of research from Indriani & Terzaghi (2017) and Nabila Nuha (2021), which state that changes in the company's directors have no positive effect on financial statement fraud. However, it does not support research conducted by Yossi Septriani (2018), Suryani (2019), and Anggraini et al. (2019), which state that capability proxied by changes in directors has a positive effect on fraudulent financial statements.

Conclusion

The nature of industry has a positive effect on fraudulent financial statements. The large number of accounts receivable owned by the company will reduce the amount of cash available for company operations. Cash limitations can encourage management to make fraudulent financial statements. Furthermore, financial stability has a positive effect on fraudulent financial statements. Financial instability often creates external and internal pressure on companies to maintain or improve financial performance. Such pressure can encourage management to manipulate financial statements. Furthermore, ineffective monitoring has a positive effect on fraudulent financial statements. Lack of proper supervision allows companies to commit fraud or manipulate financial data without being detected. Lastly, changes in the company's directors have no effect on fraudulent financial statements. Stakeholders or managers change the composition of the board, not to conceal fraud but to ensure that company resources are controlled by a more competent board.

Suggestion

Based on this research, there are several suggestions for further research that can add other variables that affect the encouragement of fraudulent financial statements, such as external pressure, financial targets, personal financial need, and rationalization. For further research, they can add a longer observation period so that there is a greater opportunity to provide an overview of the influence of the fraud diamond in detecting fraudulent financial statements in a company. Future research is expected to add independent variables as financial test tools used to detect fraudulent financial statements outside the fraud hexagon theory in order to obtain more accurate and valid results. This research is also expected to be a source of reference for future researchers who take titles related to the fraud triangle or fraudulent financial statements.

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