

CHAPTER 1

INTRODUCTION

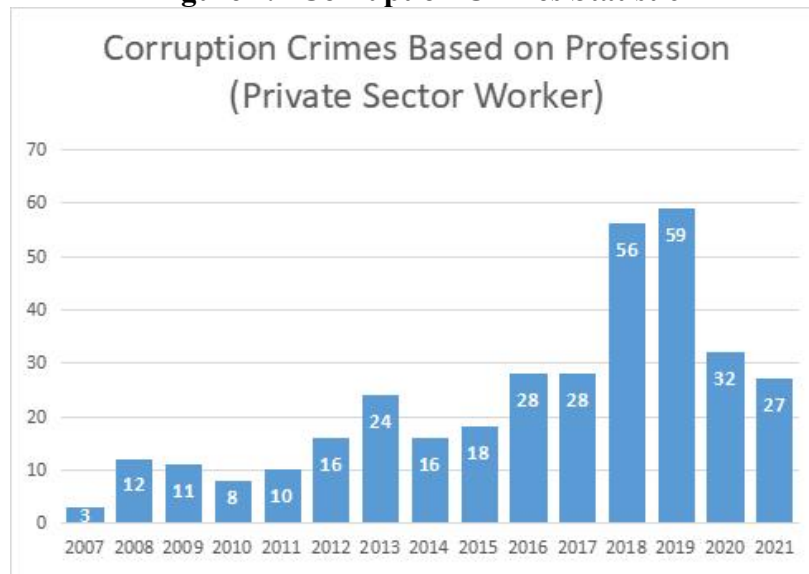
1.1 Background

Accounting scandals are scandals that occur when company executives or the government manipulate financial statements intentionally (Nickolas, 2015). Accounting scandals have occurred in a number of countries worldwide. Examples of the world's largest accounting scandals include the Enron Scandal, which lost investors \$74 billion, and the auditing and accounting firm Arthur Andersen, which had to be dissolved, as well as many other parties that faced consequences such as job loss.

In Indonesia, there is also a big accounting scandal, namely the Jiwasraya scandal, which has been in the spotlight for not being able to pay the maturing JS Saving Plan policy. As a result of this scandal, the Attorney General's Office estimates that the potential state losses will reach Rp 13.7 trillion. Alnajar (2020) defines top management fraud as a fraud committed by CEOs and CFOs where the true purpose of the organization is covered in terms of protecting self-interests. Embezzlement, internal trading, and corruption are all examples of fraud. Top management may also participate in window dressing or financial statement manipulation. The Audit Board of the Republic of Indonesia (BPK) found that Jiwasraya did window dressing in 2006. Directors are related to management and are involved in preparing financial reports. This is why the Jiwasraya fraud case is included in the top management fraud case.

As a consequence of the accounting scandals that occurred in Indonesia, there is concern that there may be several cases of fraud. According to statistics from the Corruption Eradication Commission (KPK), corruption crimes committed by private workers keep rising each year, despite a recent decrease.

Figure 1.1 Corruption Crimes Statistic



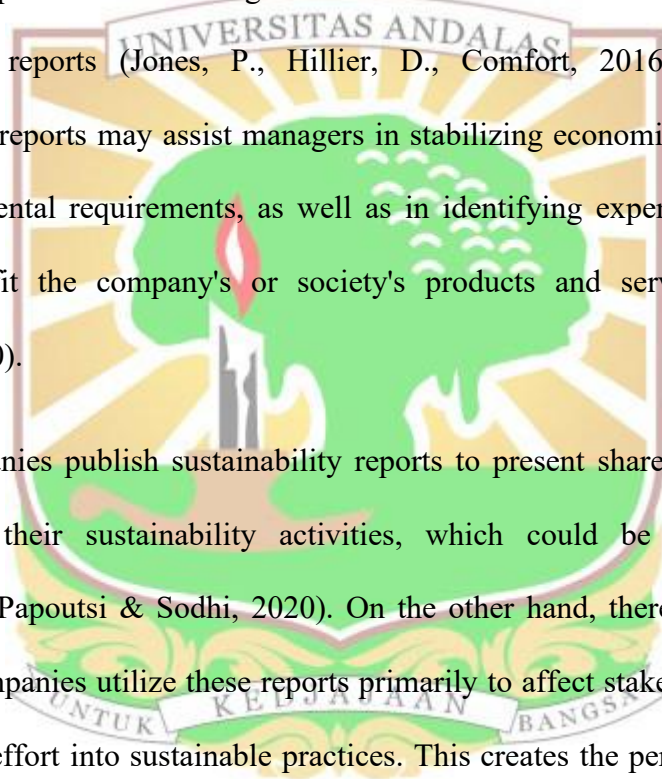
Source: Corruption Eradication Commission (KPK), 2021

The finance and accounting fields are particularly vulnerable to fraud. According to a brief dictionary search, fraud is defined as unlawful or unethical deception committed for financial or individual benefit. The Association of Certified Fraud Examiners (ACFE, 2020) defines fraud as "an acts of fraudulent activity perpetrated by an individual or entity who is aware that the action may result in a negative advantage for the individual or entity". As a criminal offense, fraud includes deception, cunning, and unfair behavior that defrauds someone else (Simeunovic, N; Grubor, G; Ristic, 2016). Ernst & Young (2009) discovered cases of fraud committed by the company's owner or the board of directors.

Furthermore, ACFE discovered that more than half of the offenders of fraud were management.

In addition to its financial performance, a company's evaluation also considers its environmental and social performance. Therefore, it is important to have a sustainability report that is designed to complement the financial report (Şahin & Çankaya, 2020). Sustainability reporting has grown in popularity in recent years prior to the emergence of environmental and corporate social responsibility reports (Jones, P., Hillier, D., Comfort, 2016; Uyar, 2016). Sustainability reports may assist managers in stabilizing economic growth, social and environmental requirements, as well as in identifying expenses that do not directly benefit the company's or society's products and services (Şahin & Çankaya, 2020).

Companies publish sustainability reports to present shareholders with an overview of their sustainability activities, which could be used to show performance (Papoutsi & Sodhi, 2020). On the other hand, there are some who argue that companies utilize these reports primarily to affect stakeholders without putting more effort into sustainable practices. This creates the perception that the company's sustainability report may not accurately reflect its actual sustainability performance in order to influence stakeholder perceptions (Herbohn, 2014; Mahoney, 2013). Therefore, this research explores the concept of "sustainability fraud", which is described as manipulation done by sustainability managers in relation to their sustainability-related activities.



According to KPMG (2020), sustainability fraud can take several forms, ranging from excessive compensation to misleading reporting, in order to get higher ranks, which results in a greater reputation and, as a result, a higher share price. Incorrect or incomplete performance data might also result in (more beneficial) capital access and thus be fraudulent. There are several factors that can contribute to fraud. According to Cressey (1953), fraud has always been characterized by three conditions: pressure, opportunity, and rationalization, commonly referred to as the "fraud triangle." These three conditions considerably raise the risk of fraud happening in such a variety of situations.

Internal control is one strategy for preventing the possibility of fraud. Internal control can be defined as rules and guidelines in existence to provide reasonable assurance that a particular entity's objectives will be met. According to COSO (2020), internal control is a procedure that is conducted by the board of directors, managerial staff, and other staff of an organization with the objective of providing assurance of the effectiveness and efficiency of activities and adherence with relevant standard and guidelines.

Previous research by Stanmeier (2015) showed that sustainability managers are generally under increasing pressure and have manipulative opportunities as a result of inadequate management systems. In addition, understanding the pressures, opportunities, and justifications that drive sustainability managers to manipulate sustainability initiatives may impact the degree to which they rely toward this information.

Previous research has studied fraud in financial accounting, but there has been few research that has explored fraud in sustainability accounting. In addition, among studies that discuss fraud in sustainability reporting, there is no research that discusses the factors that affect performance in preventing fraud in sustainability reporting. Therefore, this research is expected to fill a gap in the literature by assessing the factors that affect fraud prevention performance in sustainability reporting.

1.2 Research Question

Considering the importance of preventing fraud in the sustainability report, a study is conducted to identify the factors that influence fraud prevention performance and the effectiveness of internal controls in minimizing or preventing fraud in the sustainability report. This study examines industrial manufacturing companies that are registered on the Indonesian Ministry of Industry. Industrial manufacturing companies were selected as the sample of research as a result of their influence on the social, economy, and particularly the environmental aspects. Furthermore, considering the above background, there are several formulations of the problems identified in this study, including the following:

1. What is the effect of determinants of fraud prevention performance in sustainability reporting on fraud prevention performance in sustainability reporting?
2. What is the effect of perceived internal control effectiveness on fraud prevention performance in sustainability reporting?

3. What is the effect of determinants of fraud prevention performance in sustainability reporting on perceived internal control effectiveness?

4. What is the intervening effect of perceived internal control effectiveness on the relationship between the determinants of fraud in sustainability reporting and fraud prevention performance in sustainability reporting?

1.3 Research Objectives

In accordance with the formulation of the problem above, the objectives of this research are:

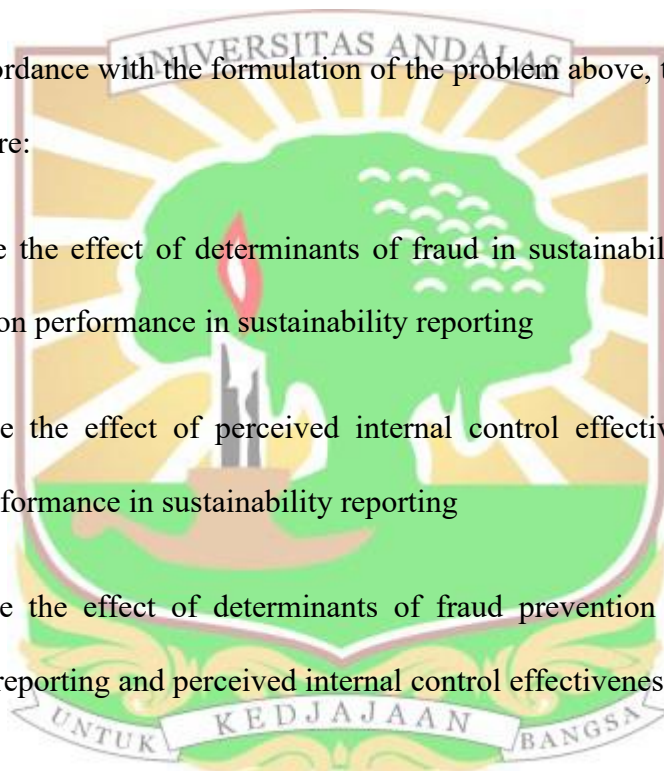
1. To examine the effect of determinants of fraud in sustainability reporting on fraud prevention performance in sustainability reporting

2. To examine the effect of perceived internal control effectiveness on fraud prevention performance in sustainability reporting

3. To examine the effect of determinants of fraud prevention performance in sustainability reporting and perceived internal control effectiveness

4. To examine the intervening effect of perceived internal control effectiveness on the relationship between determinants of fraud prevention performance in sustainability reporting and fraud prevention performance in sustainability reporting

1.4 Research Benefits



The benefit of this research is that it can be used as a guideline for more research. Additionally, it is intended that this research will be beneficial to readers in terms of determining the causes of fraud in sustainability reporting and understanding how internal control might contribute to decreasing and preventing fraud. This research is expected to provide the following benefits:

1. Institution

This research can be used to measure and evaluate companies' performance in terms of fraud prevention in sustainability reporting.

2. Academics

This research can be used as supporting material or reference in developing further research.

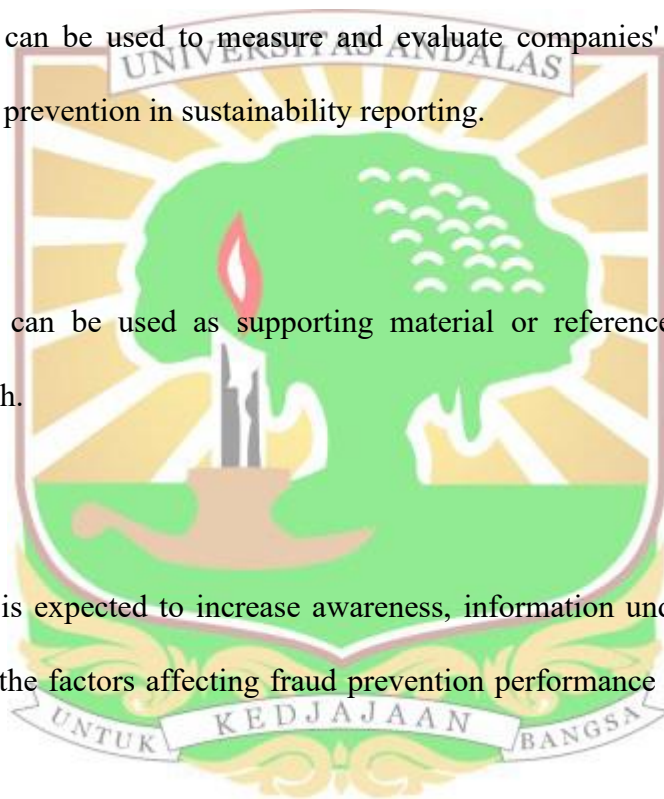
3. Readers

This research is expected to increase awareness, information understanding, and references on the factors affecting fraud prevention performance in sustainability reporting.

4. Researcher

This research is expected to increase researcher's knowledge and understanding into the factors that can influence fraud prevention performance in sustainability reporting.

1.5 Writing Systematic



In this study, researchers conducted a structured discussion through systematic writing. The systematics of writing aims to provide a concise and clear description of the research in order to make it easier for the reader to understand the writing of this research. Each chapter is described in outline as follows:

CHAPTER I: INTRODUCTION

The introduction chapter contains an overview of the research, including the research's background, the formulation of the problem, the research's objectives and benefits, and the research's structure.

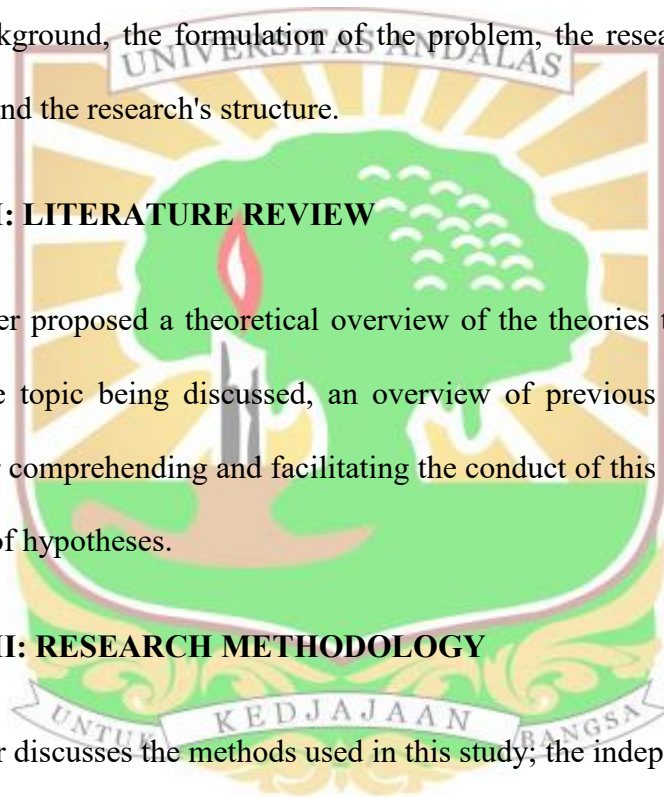
CHAPTER II: LITERATURE REVIEW

This chapter proposed a theoretical overview of the theories that support and connect to the topic being discussed, an overview of previous research, and a framework for comprehending and facilitating the conduct of this research and the development of hypotheses.

CHAPTER III: RESEARCH METHODOLOGY

This chapter discusses the methods used in this study; the independent variables, mediating variables, and dependent variables included in the study, as well as their corresponding measurements; the types and sources of data; data collection methods; and data analysis methods that include data analysis test tools for testing hypotheses.

CHAPTER IV: RESULT AND DISCUSSION



This chapter consists of a brief explanation of information about the object of research, data analysis, interpretation of the results of the data that has been analyzed, and discussion of the research.

CHAPTER V: CLOSING

Closing is the final chapter of this research which outlines the conclusions of the research, the limitations of the authors, and the authors' suggestions.

