

Influence Of Pentagon Fraud On Fraudulent Financial Reporting: Ministry Of Timor-Leste

Caetano Carceres Correia¹, Siti Munawaroh²

¹Faculty of Economics, Universidade da Paz -UNAPZ, Timor Leste

²Faculty of Economics and Business, Universitas Muhammadiyah Berau, Indonesia

Email: Samlac_72@yahoo.com, Siti010890@gmail.com

Abstract

Keywords:

*Pentagon Fraud, Pressure,
Opportunity, Rationalization,
Capability, Arrogance,
Fraudulent Financial Reporting*

This study aims to examine how pentagon fraud can affect financial reporting fraud in Timor-Leste ministries. This study was conducted in 8 Timor-Leste ministries with a sample of 88. The analysis technique used in this study was simple regression using SPSS. The results of the study indicate that with a significance level of 5% (percent), pentagon fraud has a positive effect on financial reporting fraud. This indicates that the higher the pentagon fraud, the higher the financial reporting fraud in Timor-Leste ministries. The results of the study indicate that pentagon fraud has an influence on financial reporting fraud. Based on the results of interviews with respondents in Timor-Leste ministries, many people still use opportunities to commit financial reporting fraud, this is due to the lack of supervision from auditors to identify several opportunities that will be used by irresponsible people to commit financial reporting fraud.

INTRODUCTION

Timor Leste is currently also struggling to avoid actions that violate humanitarian rules and codes of ethics by eradicating acts of corruption that easily occur in every country, because if these unethical actions become more rampant it will cause the country's development to be hampered because government funds are not available. Used as best as possible, and can only be utilized by certain parties.

In order to fulfill reporting system standards and the aim of creating internal audit reporting system governance at Inspeção Geral do Estado (IGE) Timor Leste is transparent, accountable and responsible, one of the Inspectorate's obligations is to carry out accountability reporting on Internal Audit results to realize quality Inspeção Geral do Estado (IGE) Audit report results.

Corruption is a phenomenon that does not only occur in the political complex but occurs in all activities carried out by everyone, especially at the level of politicians who have the opportunity to occupy a certain position. The phenomenon of corruption is a big challenge for every country, because it often involves people who have power in institutions or in managing public finances. Revealing is also often difficult to prove because it is done neatly and there is cooperation from several people, as well as protection by people in power.

Corruption is an act of fraudulent financial reporting. According to Australian Auditing Standards (2000), fraudulent financial reporting is an intentional act of material misstatement to mislead financial report information. This can result in errors in decision making by users of financial report information. Mean while in SAS No. 99 (2003) Fraudulent financial reporting is defined as an intentional misstatement or omission in amounts or disclosures in financial reports that is designed to harm users of financial statements.

Then in the Timor-Leste ministry, according to (Tilman, 2022), there is no single standard based on accounting and auditing standards in the Timor Leste government, and also the inspectorate which is usually based on a decision letter from the respective ministry. In line with (Jaime, 2022) states that each ministry or institution uses its own standards/measures to carry out audits, until now there are no general standards set by the Timor Leste government. According to (Lista, 2022) states that accounting and audit standards depend on the work environment, in Timor Leste until now there are no standards to standardize the supervision system and work of government internal auditors. Temporary auditors, IGE and auditors have a network between the ministries, respectively -each carries out its activities/work based on legal attribution or statutory regulations that support the institution concerned, such as legal attribution from IGE based on statutory regulation n.022/20 status Inspeccão Geral do Estado, in addition to using the legal basis that other things to guarantee the quality of the auditor's work, such as regulations regarding the status of the *Função Publico*, Timor Leste Civil Law, and others. When it comes to standards of uniformity norms, because at IGE the auditors between ministries also adopt good international practices from the International Organization of Supreme Audit Institutions-INTOSAI.

Apart from the lack of one standard that can be applied to all Timor-Leste ministries, all audit results from Timor-Leste ministries are diverse. According to (Tilman, 2022) there are differences in reporting systems between one institution and another, the reason is that there is no standard accounting system and the time to make reports only refers to financial use according to the items. Therefore, adequate provision or training in related fields is needed. Then according to (Lista, 2022) stated the difference in the results of the auditor's report between IGE and the Ministry's network.

With the conditions in the Timor-Leste ministries as described above, it can be said that fraud in financial reports is very risky in every Timor-Leste ministry. Fraud can be detected through several theories, the fraud triangle theory presented by Cressey (1953) which describes 3 causes of financial statement fraud, including pressure, opportunity and rationalization. Then in 2004, Wolfe and Hermanson put forward the fraud diamond theory which was a development of the fraud triangle theory previously proposed by Cressey (1953) by taking into account the fourth element, namely capability. Meanwhile, the most recent theory that can be used to discover fraud is the pentagon fraud theory. Crowe (2011) developed the pentagon fraud theory from the previous theory, namely by adding two new elements, including competence and arrogance, so the pentagon fraud theory became five elements, including pressure, opportunity, and rationalization. rationalization), ability (competence) and arrogance (arrogance).

Tessa and Harto (2016) say that even someone who is not under pressure can also act fraudulently. Rationalization is an important element in the occurrence of fraud because the perpetrator feels that his action is correct and does not violate the rules so that the perpetrator takes advantage of his position to carry out this action. Opportunity is one of the factors causing fraud due to the low level of supervision within the company environment and misuse of power rights. Competence (competence has a similar meaning to capability). The Fraud Pentagon can find potential financial statement fraud. Cases of fraud that still occur in the country and other countries prove that fraud schemes are very difficult to detect before experiencing huge losses. Based on the situation that occurred in the Timor-Leste ministry, the author is interested in further research regarding pentagon fraud in dealing with fraudulent financial reporting in the Timor-Leste ministry.

METHODS

The research approach in this study uses a quantitative approach. The research method used is the explanatory research method. The population in this research is the Auditor Team in all ministries in Timor Leste, totaling 88 ministries in Timor Leste. The unit of analysis in this research is the inspectorate auditor staff for each ministry with a total of 88 internal auditors). The data collection method in this research uses a questionnaire method and looks at the organization's financial reports.

Two types of analysis were carried out to obtain results in accordance with the research objectives, namely: (1) Descriptive analysis to explain the characteristics of the variables studied to support problem solving to obtain operational advice; and (2) Analysis through simple regression equation modeling using SPSS in order to answer the problem formulation and answer the hypothesis.

RESULTS AND DISCUSSION

Of the 88 total questionnaires submitted to respondents, the number of questionnaires returned was 82 questionnaires with a return rate of 93.18 %.

Data analysis

1. Normality test

One-Sample Kolmogorov-Smirnov Test

		Unstandardized Residuals
N		88
Normal Parameters ^{a, b}	Mean	.0000000
	Std. Deviation	1.29917445
Most Extreme Differences	Absolute	.143
	Positive	,070
	negative	-.143
Statistical Tests		.143
Exact Sig. (2-tailed)		,062

a. Test distribution is Normal.

b. Calculated from data.

This is indicated by the Kolmogrov-Smirnov value which has a significant value of 0.062. Where the results show that the level of significance in this research is above $\alpha = 5\%$ or 0.05 ($0.062 > 0.05$). This means that the data for all the variables used are normally distributed.

2. Simple Regression Test

Coefficients^a

Model		Unstandardized Coefficients		Standardized	t	Sig.
		B	Std. Error	Coefficients Beta		
1	(Constant)	-.758	,657		-1,153	,252
	Pentagon Fraud	,960	,169	,537	5,688	,000

a. Dependent Variable: Fraudulent Financial Reporting

From the simple regression equation above, a constant value of 0.10 is obtained. This value can be interpreted as meaning that if the Fraudulent Financial Reporting (Y) variable is not influenced by the independent variables because Fraud Pentagon (X) has a value of zero, then the average size of the Fraudulent Financial Reporting (Y) variable will be 0.10.

The regression coefficient β_1 has a positive value, meaning that if the Fraud Pentagon variable (X) increases by one unit, then the Fraudulent Financial Reporting variable (Y) will increase by 0.960.

In simple regression testing, there are four types of tests, namely

a. Correlation Analysis (R)

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.537 ^a	,288	,279	1.30727

a. Predictors: (Constant), Pentagon Fraud

Based on the table above, the R number is 0.537. This shows that there is a strong relationship between Pentagon Fraud and Fraudulent Financial Reporting.

b. Simultaneous Regression Coefficient Test (F Test)

ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	55,296	1	55,296	32,357	,000 ^b
	Residual	136,716	80	1,709		
	Total	192.012	81			

a. Dependent Variable: Fraudulent Financial Reporting

b. Predictors: (Constant), Pentagon Fraud

Based on the table above, the Fcount value is 32.357 with a Sig value of 0.000. This shows that the Fcount value of 32.357 is greater than Ftable 2.32 and the Sig value is smaller than 0.05. Thus H0 is rejected. This means that Pentagon Fraud has a significant positive influence on Fraudulent Financial Reporting.

c. Partial Regression Coefficient Test (T' Test)

Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	-.758	,657		-1,153	,252
Pentagon Fraud	,960	,169	,537	5,688	,000

a. Dependent Variable: Fraudulent Financial Reporting

With $df = nk - 1 = 82 - 1 - 1 = 80$, we get a t-table of 1.664. From the table above, it can be seen that the t-count value of the Pentagon Fraud variable (X) is 5,688 and the significance of t is 0.000, so the conclusion is that H_0 is rejected because $t_{count} > t_{table}$ and the significance of $t < \alpha$. In other words, at a significance level of 5% there is a significant positive influence of the Fraud Pentagon variable on Fraudulent Financial Reporting.

d. Determination Test

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.537 ^a	,288	,279	1.30727

a. Predictors: (Constant), Pentagon Fraud

The magnitude of the influence of the Pentagon Fraud variable on Fraudulent Financial Reporting can be shown by the coefficient of determination with the following formula:

$$KD = R^2 \times 100\% \\ = (0.537)^2 \times 100\% = 28.84\%$$

This shows that the Fraud Pentagon variable has an influence of 28.84 % on the Fraudulent Financial Reporting variable.

3. Hypothesis test

Hypothesis 1:

The hypothesis H_0 is rejected because it is based on the t-count value obtained at 5,688, which means the t-count value for the Pentagon Fraud variable is 6,688 and the significance of t is 0.000 so the conclusion is that H_0 is rejected because $t_{count} > t_{table}$ and the significance of $t < \alpha$. In other words, at a significance level of 5% there is a significant positive influence of the Fraud Pentagon variable on Fraudulent Financial Reporting.

DISCUSSION

The research results show that the fraud pentagon has an influence on fraudulent financial reporting. Based on the results of interviews with respondents in the Timor-Leste ministry, there are still many people who use opportunities to commit financial report fraud, this is due to a lack of supervision from auditors to see several opportunities that irresponsible people will use to commit financial report fraud. . Then, with high work pressure, people will commit fraud, as is done in the Timor-Leste ministry, where when work pressure is too high, it will create opportunities to commit financial report fraud. In addition, pressure from an individual's own economic factors can influence the individual to commit financial statement fraud. Rationalization such as never changing auditor positions can also trigger financial statement fraud

to occur. Then the auditor's ability becomes the main trigger in committing financial report fraud, as is the case in the Ministry of Timor-Leste, by using the auditor's ability to read the state of the financial report, the auditor will use various means to manipulate the financial report so that the financial report cannot be used. Detected by any auditor. Then the leader's arrogance can be a trigger for committing financial report fraud. In the Ministry of Timor-Leste, with a lack of insight in conducting audits, the leader's arrogance can pressure his subordinates to commit financial report fraud just to prioritize personal gain or organizational interests.

In line with research by Indarto & Ghozali (2016), companies often experience pressure from external parties. One of the pressures often experienced by Management Company is the need to obtain additional debt or external funding sources to remain competitive, incl funding research and development or capital expenditure. Companies that have a high debt ratio are motivated to manipulate profits. Companies prefer to commit fraud in financial reporting when they have the opportunity to carry out earnings management so that their performance looks successful in front of shareholders. Managers may manipulate financial statements because of their need to fulfill debt covenants. This shows that the higher the level of debt can increase the possibility of financial statement fraud. According to (Antawirya, Putri, Wirajaya, Suaryana & Suprasto, 2019), it shows that financial collection has a positive positive effect on financial report fraud and the number of audit committee meetings which reflects effectiveness has a negative effect on financial report fraud. The study results also contribute to the pentagon theory of fraud and provide evidence that elements in the pentagon model of fraud can be used to detect financial statement fraud. Tessa & Harto (2016), which proxies the pentagon fraud factor into several elements consisting of financial targets, financial stability, external pressure, institutional ownership, ineffective monitoring, quality of external auditors, change of auditors, change of directors and frequent number of photos of leaders for detect fraudulent financial statements. The research results show that there are three variables that have a significant influence on financial report fraud, namely financial stability, external pressure, and the frequent number of photos of leaders.

CONCLUSION

Based on the results of research, Pentagon fraud has a significant and positive effect on fraudulent financial reporting. Where the level of Pressure, Opportunity, Rationalization, Capability/Competence, Arrogance increases and has an impact on fraudulent financial reporting, this is because the quality of internal auditors in the Timor-Leste ministry has not been tested, and there is no single standard that can be used as a reference in examining financial reports, This causes the level of Pressure, Opportunity, Rationalization, Capability/Competence, Arrogance to increase and has an impact on fraudulent financial reporting.

REFERENCE

- ACFE (Association of Certified Fraud Examiners, Inc). (2016).
- American Institute of Certified Public Accountants (AICPA). (1997). Consideration of Fraud in a Financial Statement Audit. AU Section 316. PCAOB Standards and Related Rules as of December 1997. New York, NY: AICPA.

- Antawiryana, RDEP, Putri, IGAMD, Wirajaya, IGA, Suaryana, IGNA, & Suprasto, HB (2019). Application of fraud pentagon in detecting financial statement fraud. *International research journal of management, IT and social sciences*, 6(5), 73-80.
- Arens, A. A., Elder, R. J., & Beasley, M. S. (2014). *Auditing And Assurance Services: An Integrated Approach* 15th Ed. Pearson.
- Beasley, C.M., Dellva, M.A., Tamura, R.N., Morgenstern, H., Glazer, W.M., Ferguson, K., & Tollefson, G.D. (1999). Randomized double-blind comparison of the incidence of tardive dyskinesia in patients with schizophrenia during long-term treatment with olanzapine or haloperidol. *The British Journal of Psychiatry*, 174(1), 23-30.
- Cressey, D. R. (1953). *Other people's money; a study of the social psychology of embezzlement*.
- Crowe, H. (2011). *Putting the Freud in Fraud: Why the Fraud Triangle Is No Longer Enough*.
- Indarto, SL, & Ghozali, I. (2016). Fraud diamond: Detection analysis on the fraudulent financial reporting. *Risk Governance and Control: Financial Markets and Institutions*, 6(4Continued1), 116–123. <https://doi.org/10.22495/rcgv6i4c1art1>
- Jamie, 2022. Results of February research interviews. Trigonal and Contas
- Lista, 2022 interview results in March
- Tessa, C., & Harto, P. (2016). Financial statement fraud: Testing the Pentagon Fraud Theory in the Financial and Banking Sector in Indonesia. *Journal of National Symposium Accounting XIX* , 1-21
- Sarwoko. 2005. *Basics of Econometrics*. Yogyakarta: Andi Offset
- Skousen, C. J., Smith, K. R., & Wright, C. J. (2009). Detecting and Predicting Financial Statement Fraud: The Effectiveness of The Fraud Triangle and SAS No. 99 in Corporate Governance and Firm Performance. In *Advances in Financial Economics: Corporate Governance and Performance* St edition, JAI Publishing, Emerald Group (Vol. 13, Issue 99). [https://doi.org/https://doi.org/10.1108/S1569-3732\(2009\)0000013005](https://doi.org/https://doi.org/10.1108/S1569-3732(2009)0000013005)
- Tilman. 2022 results of interviews with the Inspectorate General Do Estado. March
- Unodc. (2019). *The Anti-Corruption Commission in Timor-Leste Builds Its Capacities to Investigate Corruption and Financial Crimes*. United Nations. <https://www.unodc.org/roseap/en/what-we-do/anti-corruption/topics/29-The-Anti-Corruption-Commission-In-Timor-Leste-Builds-Its-Capacities-To-Investigate-Corruption-And-Financial-Crimes.html>.