

What Factors Affecting Auditors' Fraud Tendency Perception? Fraud Pentagon Theory Perspective

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Abstract: *This research aims to analyze the influence of the pentagon fraud theory, which consists of pressure, opportunity, rationalization, competence, and arrogance, on auditors' perceptions of fraud tendencies. The sample for this research is 153 auditors who work at the Regional Inspectorate of Central Java Province. This type of research is quantitative research. The data analysis technique uses Partial Least Square (PLS). Data was processed using SmartPLS software version 3.29. The results of this research are that pressure, opportunity and rationalization do not have a significant effect on the auditor's perception of fraud tendencies, while competence and arrogance have a significant effect on the auditor's perception of fraud tendencies. This research contributes to the development of fraud pentagon theory by providing empirical evidence.*

Keywords: *Auditors fraud tendency perception, Fraud, Fraud pentagon theory*

JEL: G28, G38, G40

1. INTRODUCTION

Fraud remains a serious problem plaguing organizations and stakeholders around the world (DeZoort & Harrison, 2018). The Association of Certified Fraud Examiners (ACFE) in 2020 showed that there was a loss of 3.6 billion USD based on examination of 2,504 cases from 125 countries (ACFE, 2020). Asia Pacific, including Indonesia, is in third place with the most cases in the world (198 cases). Based on the 2019 Indonesian Fraud Survey, there were 239 cases of fraud consisting of corruption, misuse of state and company assets/wealth and cases of financial statement fraud (ACFE Indonesia, 2019). The total state losses were more than 873 trillion rupiah.

If we look back, the problem of accounting fraud has existed for a long time and has undermined public trust in the accounting profession. Various fraud scandals have occurred since the last quarter century, including the Enron scandal, Worldcom, Tyco International, Qwest Communications, HealthSouth and others. A 2014 PwC survey stated "Thirty-seven percent of our respondents reported that their organizations had experienced economic crime during the survey period, an increase of 3 percentage points from our 2011 survey". (PwC's Global Economic Crime Survey, 2014). This shows that fraud within client organizations is real and increasing. In Indonesia there are also various cases of fraud, such as the case of PT. Kimia Farma, PT. Indonesian Railways, PT. Nusantara Clothing Industry, PT. Hanson 2 International, Citibank, Garuda Indonesia in 2018, the Jiwasraya Insurance financial report manipulation case and finally the Maybank case in 2020.

Some of these scandals have implicated external auditors as part of the responsibility. Historically, the most famous cases of fraudulent financial reporting and the failure of auditors to prevent them are the Enron and Arthur Andersen scandals (Roszkowska, 2021). Andersen was proven to have collaborated in manipulating the financial reports of Enron and WorldCom to the detriment of many parties, both external and internal to the two giant companies. The end of Andersen's story was his collapse in 2002 and his exit from the top four. In the case of PT Kimia Farma, KAP Hans, Tuanakotta and Mustofa failed to detect an increase in the company's net profit in 2001 which should have only been 99.7 billion rupiah but was reported to be 132 billion rupiah, this was because double sales were recorded in units that were not sampled by accountant (Lukman & Harun, 2018). Another case occurred at Citibank, involving customer funds worth 17 billion rupiah by the relationship manager (RM) due to the absence of regular RM rotation in handling customer funds and the internal auditor's negligence in identifying weaknesses in Citibank's work system (Lukman & Harun, 2018). Another viral fraud case in Indonesia at the beginning of 2019 was the PT case. Garuda Indonesia Tbk reported that the company

made a profit from the 2018 financial year by falsifying revenue recognition, even though the company was actually making a loss (Handoko & Tandean, 2021), and it is suspected that there was a role for external auditors based on the report of the Financial Professional Development Center of the Ministry of Finance (PPPK) (Kemenkeu, 2018).

Crowe (2011) refined the fraud triangle theory previously proposed by Cressey (1953) and the fraud diamond theory by (Wolfe & Hermanson, 2004). Crowe's research produced a new model consisting of five indicator elements, namely pressure, opportunity, rationalization, competence and arrogance. This theory became known as the pentagon fraud theory. This research uses the pentagon fraud theory on the grounds that it is a renewable theory and the fraud indicators described in Crowe's pentagon fraud theory are much more complete than previous theories.

In 2004, Wolfe and Hermanson refined the fraud triangle theory into a fraud diamond by adding one component, namely competence. Competence is defined as an individual's ability and plays an important role in fraud. The success of cheating depends on a person's abilities, which consist of position, intelligence, egoism, persuasion, deception, and stress management (Wolfe & Hermanson, 2004)

The latest theory that digs deeper into the factors that trigger fraud is the fraud pentagon theory. This theory was proposed by Crowe Horwath in 2011. The fraud pentagon theory is an extension of the fraud triangle theory previously proposed by Cressey. This theory adds two other elements of fraud: competence and arrogance. The competencies described in the pentagon fraud theory have the same meaning as the capabilities previously explained in the diamond fraud theory by (Wolfe & Hermanson, 2004).

Kassem dan Higson (2012) argued that pressure/motivation for fraud can be personal, company or work pressure and external pressure. At the individual level, fraud can occur due to financial and non-financial pressures. Financial stress is related to lifestyle and non-financial stress is related to greed and lack of financial discipline (Adebisi, 2013).

2. LITERATURE REVIEW

2.1 The Effect of Pressure on Auditor's Fraud Tendencies

Skousen dan Wright (2009) examines the role of elements of the fraud triangle theory in detecting and predicting fraud cases. Financial need, luxurious lifestyle, greed are factors that support fraudulent behavior in terms of external pressure (Skousen et al., 2009). Apart from external pressure, there is also internal pressure, namely in the form of a workload that is too high to achieve certain targets. Job competition with fellow professionals can cause pressure on the auditor. Concerns that CPA FIRMS will be able to survive in the face of intense competition can also trigger broader pressures. Auditors may also feel pressure from their clients to report false information. This pressure can encourage auditors to collude, collaborate with clients in inappropriate ways, resulting in fraud as happened in the Andersen case.

Donald R. Cressey developed the fraud triangle theory in 1953. This theory was the first theory to explain the elements that cause fraud, and much research has been conducted to confirm this theory. Cressey conducted extensive research to determine what motivates seemingly honest people to commit fraud. The three components of the fraud triangle are pressure, opportunity and rationalization (Kassem & Higson, 2012a).

Perception is the process by which individuals organize and interpret their sensory impressions to understand their environment. Perception is a sensory process that collects stimuli from the real environment, then understands and creates human insight into these stimuli. From the definition above, it can be concluded that cognition is a process that aims to create meaning which begins with receiving stimuli to be used to interpret and understand the world around (Robbins, 2013).

Several researchers have found a significant relationship between stress and the occurrence of fraud. Fitri et al., (2019) found that companies with higher level of fraud more emphasis on financial stability, leverage, and financial targets. Another research conducted by Faradiza, (2019) also stated that pressure had an influence on fraudulent financial reporting in manufacturing companies listed on the IDX for the 2014–2015 period. Said et al., (2017) in his research stated that pressure was not proven to play an important role in increasing the possibility of fraud among bank employees in Malaysia. Therefore, the first hypothesis proposed as follows:

H1: Pressure has a positive effect on external auditors' perceived fraud tendencies.

2.2 The Effect of Opportunity on Auditor's Fraud Tendencies

Opportunities are the lack of controls and governance structures to control the operations and use of corporate assets (Peprah, 2018). The greater the opportunity someone has to cheat, the higher the likelihood they will do so (Utami & Purnamasari, 2021). A person can be motivated to commit fraud by perceived opportunities, such as the opportunity to gain profits from other sources. Internal control weaknesses have been identified as a key mechanism that provides opportunities for fraud. Internal control weaknesses can also be exploited by auditors to commit fraud.

Mintara & Hapsari, (2021) found that opportunities through the proxy of ineffective supervision have a negative effect on the detection of financial statement fraud, but other proxies, namely the nature of the industry, are proven to have a positive effect. Another research also found that (Said et al., 2017) opportunities have a positive effect on fraud. These findings also supported by who found empirical evidence on the influence of opportunities on fraud. The second hypothesis is proposed as follows:

H2: Opportunity has a positive effect on the auditor's perception of fraud tendencies.

2.3 The Effect of Rationalization on Auditor's Fraud Tendencies

Rationalization is the justification given for fraudulent actions with the aim of overcoming competition or making a profit (Peprah, 2018). Rationalization is a reason given by someone to support the acceptance of committing fraud. A fraudster makes excuses to justify their actions, they argue that they only borrowed the organization's money, so that no one was harmed by this action. (Fitri et al., 2019). In this case, the auditor rationalizes the gift from the client as compensation for his services and is not part of an approach or bribe to fulfill the client's wishes. Tolerating some procedures to help clients is also considered rational. A research that investigated the influence of razionalization conducted by Apriliana & Agustina, (2017) found that Changing auditors is not proven to be a factor influencing fraudulent financial reporting. In line with these findings, the research results (Faradiza, 2019) also stated that rationalization had no effect on fraudulent financial reporting. also states that rationalization has no effect on fraudulent financial reporting. It also proves that rationalization is a factor that influences fraud committed by bank employees in Malaysia (Said et al., 2017). In line with the statement, hypothesis three is written as follows:

H3: Rationalization has a positive effect on the perception of auditors' fraud tendencies.

2.4 The Effect of Competence on Auditor's Fraud Tendencies

Competence according to Crowe (2011) is the ability of employees to ignore internal controls, develop concealment strategies and control social situations for their personal gain. At the same time, arrogance is an attitude of ignoring one's rights when internal or company control policies are not implemented (Crowe, 2011).

Competent means a person's attempt to commit fraud to achieve certain goals by ignoring internal controls, developing concealment strategies and controlling social situations for his personal interests. (Kassem & Higson, 2012a). An auditor is a person who really understands the accounting process, including the gaps for carrying out creative accounting. These competencies can be used to take advantage of opportunities to commit fraud. According to (Wolfe & Hermanson, 2004), Competency relates to the skills, knowledge, confidence and position an individual has to commit fraud. Fraud cannot possibly occur if it is not carried out by someone who has the right ability and position to carry out every detail of the fraud.

Several studies have examined the influence of competence on fraud. The results show different evidence. On research (Apriliana & Agustina, 2017), (Peprah, 2018), (Puspitha & Yasa, 2018) The results obtained show that competence has a positive effect on fraudulent financial reporting which is proxied through changes in directors. Meanwhile research (Mintara & Hapsari, 2021) shows that there is a positive but not significant influence between competence and financial statement fraud (Utami & Purnamasari, 2021) reported that there is a positive influence of competence on the tendency of cheating behavior in the academic world. The fourth hypothesis is written as follows:

H4: Competence has a positive effect on the perception of auditors' fraud tendencies.

2.5 The Effect of Pressure on Auditor's Fraud Tendencies

Arrogance is the attitude of a person who expresses that internal controls, company policies and regulations do not apply to him (Utami & Purnamasari, 2021). He felt excluded from applicable procedures, regulations and internal controls. Someone who commits fraud with arrogance is not afraid of the sanctions that will befall him. The arrogance that may arise from auditors is feeling that they are superior in the audit engagement process. It is almost certain that company management respects and is "afraid" of auditors during the audit process. This condition can be exploited by auditors to commit fraud.

Several research was conducted to investigate the relationship between arrogance and fraud tendencies. A study found that arrogance has no impact on fraudulent financial reporting. (Faradiza, 2019). Meanwhile, the research result of Mintara & Hapsari (2021) also shows that the number of CEO photos in the company's annual report which is a proxy for arrogance is not proven to have an effect on fraudulent financial reporting. (Christian et al., 2019) proves that arrogance is a predictive factor in the pentagon fraud theory. However, (Pamungkas et al., 2018) also stated that arrogance has no effect on fraudulent financial reporting. (Puspitha & Yasa, 2018) and (Apriliana & Agustina, 2017) found that arrogance has a positive effect on fraudulent financial reporting. Hypothesis five is proposed as follows:

H5: Arrogance has a positive effect on the perception of auditors' fraud tendencies.

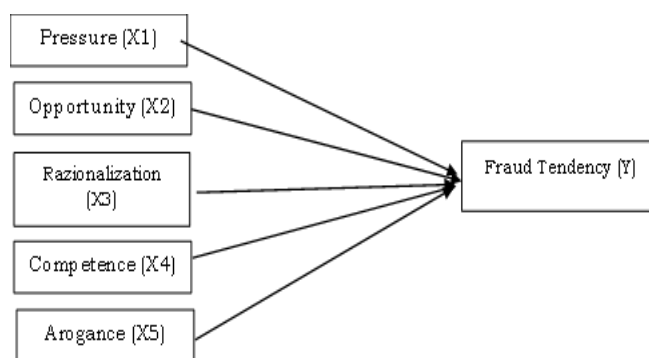


Figure 1. Research Model
Source: Primary Data, 2024

3. METHODS

3.1 Population and Sample

The population in this study were auditors who worked at the Regional Inspectorate of Central Java Province, totaling 257 people. The sampling technique used in this research is the saturated sample method, meaning that all members of the population are sampled. However, the number of auditors who were willing to take part in this research was 153 people.

3.2 Variable Measurement

The variables in this research consist of dependent and independent variables. The dependent variable is Perception of Fraud Tendency which is defined as the auditor's view of issues related to fraud in their professional environment. The questions that measure this variable consist of three questions (Y.1 – Y.3).

The independent variables consist of pressure, opportunity, rationalization, competence, and arrogance. Pressure is defined as time pressure, financial and inter-professional competition, which consists of eight questions (X1.1 – X1.8). The opportunity variable is the opportunity for an auditor to cheat due to a weak monitoring system for assigned auditors. This variable consists of four questions (X2.1 – X2.4). Rationalization is defined as justifying cheating on the grounds that it is reasonable to do so as long as no one is substantially harmed by the act. This variable consists of four questions (X3.1 – X3.4). The questions in the questionnaire to measure the variables of perception of fraud tendencies, pressure, opportunities and rationalization were adopted from research (Said et al., 2017).

Other independent variables, namely competence and arrogance, were measured using a questionnaire instrument from (Utami & Purnamasari, 2021). Competency is the auditor's skills, knowledge, confidence and position to commit fraud, which consists of six questions (X4.1 – X4.6). Arrogance is the attitude of a person who expresses that internal controls, company policies and

regulations do not apply to him. He felt excluded from applicable procedures, regulations and internal controls. This variable is measured with five questions (X5.1 – X5.5). All items use a five-point Likert scale from 1–5. A score of 1 means "strongly disagree" to a score of 5 which means "strongly agree".

3.3 Data Analysis Technique

Data analysis uses Partial Least Square (PLS) analysis, data is processed using SmartPLS software version 3.29. Before testing the hypothesis (inner model), validity and reliability tests (outer model) are first carried out. The decision whether the independent variable has a significant effect or not is determined by the magnitude of the probability value. If the probability value (p-value) or sig. below 5% (0.05) then the independent variable is said to have a significant effect. Conversely, if the probability value (p-value) or sig. above 5% (0.05) then the independent variable is said to have no significant effect (Ghozali & Latan, 2015).

4. RESULTS AND DISCUSSION

4.1 Outer Model Testing

Outer model testing consists of validity and reliability tests or also known as questionnaire feasibility tests. The condition for a valid question item is to have an outer loading value > 0.7, while the condition for a valid variable is to have an Average Variance Extracted (AVE) value > 0.5. A variable is called reliable if it has a Cronbach's Alpha value and composite reliability > 0.7 (Ghozali & Latan, 2015).

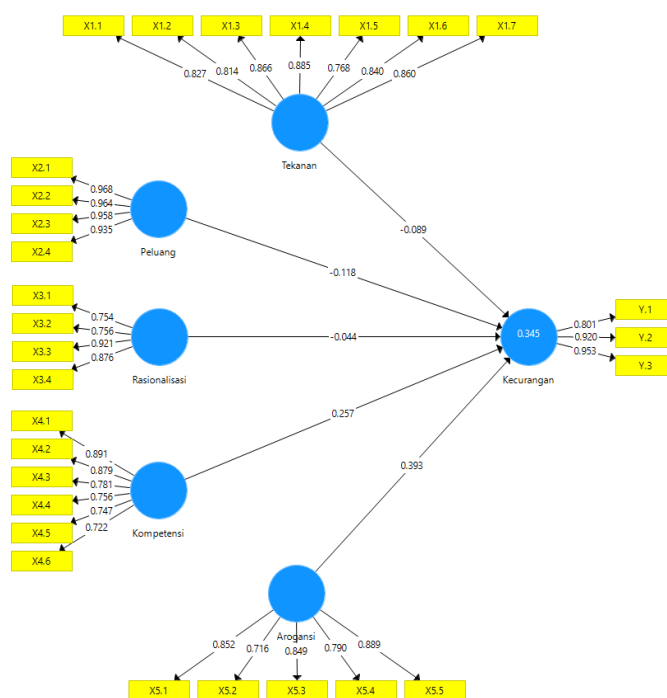


Figure 2. Structure Model
Source: Primary Data, 2024

The validity test results stated that the outer loading value of all question items was > 0.7. This means that all question items are valid. Furthermore, the results of the variable validity test and reliability test are shown in table 1.

Table 1. Reliability Testing Result
Source: Primary Data, 2024

Variables	Cronbach's Alpha	Composite Reliability	Average Variance Extracted (AVE)
Arogance	0.878	0.912	0.675
Fraud	0.871	0.922	0.799

Competency	0.885	0.913	0.638
Opportunity	0.972	0.977	0.915
Rationalization	0.913	0.898	0.689
Pressure	0.930	0.943	0.702

Table 1 presents the Cronbach's Alpha and composite reliability values for all variables > 0.7. This means that all variables are reliable. And the AVE value for all variables is > 0.5, which means that all variables are valid.

Inner Model Testing

Inner model testing consists of the R-Square test, Goodness of Fit and hypothesis testing (t test). The R-Square test results are shown in table 2.

Table 2. R Square Test

Variable	R Square	R Square Adjusted
Fraud	0.345	0.304

Source: Primary Data, 2024

Table 2 presents an R-Square value of 0.345. This means that 34.5% of changes in perceptions of fraud tendencies are influenced by pressure, opportunity, rationalization, competence, and arrogance of auditors, while the remainder (32.1%) is influenced by other variables not examined.

The next test is Goodness of Fit. The model is said to be fit if the Standardized Root Mean Square Residual (SRMR) value is smaller than 0.1. The Goodness of fit test result is presented in the table 3

Table 3. Goodness of Fit Test

	Estimated Model
SRMR	0.083

Source: Primary Data, 2024

The table 3 shows an SRMR value of 0.083 (< 0.1), so it can be said that the model goodness-of-fit test in this research is considered sufficient and hypothesis testing can be carried out. The results of the hypothesis test are shown in the table 4.

Table 4. Hypotheses Testing Result

Variables	Original (O)	Sample T Statistics (O/STDEV)	Values
Arrogance -> Fraud	0.393	3.414	0.001
Competence-> Fraud	0.257	2.530	0.012
Opportunity -> Fraud	-0.118	1.019	0.309
Rationalization-> Fraud	-0.044	0.301	0.763
Pressure -> Fraud	-0.089	0.808	0.420

Source: Primary Data, 2024

Table 5. Variables Average Scores

Variables	Average Score
Fraud	1,61
Pressure	4,11
Opportunity	3,93
Rationalization	3,93
Competence	1,72
Arogance	1,83

Source: Primary Data, 2024

4.2 The Effect of Pressure on Auditor's Fraud Tendencies

Based on the test results, the pressure variable has a p-value of 0.420, this value is greater than 0.05, which means there is no significant influence between pressure and the tendency to commit fraud, so hypothesis 1 is not supported statistically. This finding can be explained by looking at the average respondent's answer to the pressure variable of 4.11. If measured on a Likert scale of 1 to 5, it means that auditors tend to admit that there is pressure in their work. However, pressure in the form of time, funds and competition between professions does not influence auditors' perceptions of committing fraud. Auditors are used to facing various work pressures, but this does not encourage them to commit fraud. These results are in line with research (Said et al., 2017) and not in line with the result of (Faradiza, 2019) and (Fitri et al., 2019).

4.3 The Effect of Opportunity on Auditor's Fraud Tendencies

Based on Table 4 above, the p-value of the probability variable is 0.309 and is greater than 0.05, so hypothesis 2 is not supported. From the average respondent's answer to the question measuring the opportunity variable, a value of 3.93 was obtained (Table 5), it can be said that there is an opportunity to commit fraud, but this does not encourage them to commit fraud. These results are in line with research (Apriliansa & Agustina, 2017) but does not in line with (Faradiza, 2019) and (Fitri et al., 2019).

4.4 The Effect of Rationalization on Auditor's Fraud Tendencies

Testing the third hypothesis is also by looking at the p-value of the rationalization variable in Table 4, the results show 0.763 and are greater than 0.05, so hypothesis 3 is not supported statistically. Rationalization is defined as justifying fraudulent behavior and considering it normal and reasonable to do as long as it does not cause major losses. For example, auditors consider it quite rational when accepting gifts from clients on the grounds that the gift is a sign that they have provided good service and there is no significant loss from receiving the gift. The average respondent's answer was 3.93, which means they tended to respond high to the rationalization variable. It can be said that even though there is a reasonable response regarding cheating, it does not necessarily encourage them to cheat. These results are in line with research (Utami & Purnamasari, 2021) and does not in line with the result of (Fitri et al., 2019) and (Puspitha & Yasa, 2018).

4.5 The Effect of Competence on Auditor's Fraud Tendencies

In Table 4, it can be seen that the p-value of the competency variable is 0.012 and is smaller than 0.05. This result is significant which proves that competency has a positive effect on the perception of auditors' fraud tendencies, so hypothesis 4 is supported. The competencies defined in this research are related to the auditor's skills, knowledge, confidence and position to commit fraud. There is the question of whether it is natural for someone not to feel afraid or worried and be able to control themselves when committing fraud. And also ask their opinion whether a strategy is needed to commit fraud. The average respondent's answer was 1.72, which means that the respondent's answer tended to disagree. This result is significant, the lower the auditor's competency, the lower the tendency to commit fraud, and vice versa, the higher the auditor's competency, the higher the tendency to commit fraud. These results are in line with the findings of (Puspitha & Yasa, 2018) and (Utami & Purnamasari, 2021).

4.6 The Effect of Arogance on Auditor's Fraud Tendencies

Testing hypothesis 5 can be seen from the p-value of the arrogance variable of 0.001 and is smaller than 0.05, so hypothesis 5 is supported. Arrogance is defined as a person's attitude that reveals that internal controls, company policies and regulations do not apply to him. He felt excluded from applicable procedures, regulations and internal controls. An arrogant auditor feels that he is superior and feared enough, which can trigger a tendency to cheat. The higher the auditor's arrogance, the higher their tendency to cheat. These results are in line with the findings of several studies such as (Christian et al., 2019) and (Puspitha & Yasa, 2018).

5. CONCLUSION AND SUGGESTION

5.1 CONCLUSION

This study provides evidence that the five components of the pentagon fraud theory are not

fully proven in predicting auditors' perceptions of fraud tendencies in Indonesia. Pressure, opportunity and rationalization in previous research, namely (Apriliana & Agustina, 2017), (Fitri et al., 2019), and (Pamungkas et al., 2018) proven to have a positive effect on the tendency to cheat apparently cannot be applied to this research. This can be explained because this research examines the pentagon fraud theory in the context of behaviour in the auditor's environment so that the results cannot be compared with previous research which used proxies in financial reports as predictors of fraud. Another finding is that competence and arrogance are proven to influence perceptions of fraud tendencies. Auditors' understanding of creative accounting methods is an indicator of their competence. The high level of auditor arrogance also triggers a tendency for fraud to occur. Auditors often feel superior in audit assignments because in many situations the auditor's arrival is frightening for their clients. This research is not free from limitations, the time for carrying out the survey was relatively short so that there were relatively few respondents who participated. Future research can extend the survey time so that it can reach a larger sample. Second, since Inspectorate belongs to internal auditor of government institution, they might be not free from internal pressure during their duty. Hence, it might drive to the bias results.

5.2 SUGGESTION

Future research can also add other variables that can trigger fraud other than those contained in the pentagon fraud theory considering that as much as 65.5% (remaining R-Square) the influence of other factors outside our model has not been tested yet. Future research can also investigate external auditor to observe the effect of pressure.

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