

Internal Control System between Fraud Asset Management and Local Governance: A Social and Organizational Perspective

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Abstract

This study aims to examine the effects of peer influence and outcome expectancies on fraud in local government asset management. This study is also to analyze moderating effect of the internal control system between peer influence and outcome expectancies on the fraudulent behavior. By utilizing purposive sampling method to obtain data from government units of Palu City and by using PLS with the help of WarpPLS software, the results show that peer influence has a positive effect on fraudulent behavior, while outcome Expectancies have a negative effect on the fraudulent behavior. Moreover, internal control system is able to moderate the influence of peer influence and outcome expectancies against fraudulent behavior. The results would imply that strong internal control system is more likely able to reduce or weaken the influence of peer influence on fraudulent behavior.

Keywords

Fraudulent Behavior, Asset Management, Local Government, Peer Influence, Outcome Expectancies, Internal Control System.

Introduction

Fraud is a form of fraud that is intentionally carried out so that it can cause losses. Fraud usually occurs because of pressure, opportunity and rationalization, where a person may feel pressure to commit fraud because of a need or financial problem. Opportunities to commit fraud are usually triggered by opportunities that cause perpetrators to freely carry out their actions caused by a weak control environment and undisciplined information asymmetry.

Therefore, it is important for local governments to carry out adequate asset management. Regional asset optimization can be done by asset management. Regional asset management is implementing the management of assets based on the basic principles of asset management by following the policy foundations regulated by Laws, Government Regulations, Presidential Decrees, Ministerial Decrees and other Decrees related to regulations/regional asset management (Budisusilo, 2005). Regional assets are all assets owned by the region, either obtained or purchased at the expense of the regional budget (Sholeh & Rochmansjah, 2010). Goods that can move, for example in the form of vehicles such as cars and motorcycles. For immovable goods, for example, office supplies and equipment, such as computers, printers, photocopiers, tables, chairs and so on. Regional Property is used by employees to assist in work and is used to support and succeed in activities or activities held by the government. Employees can use the asset in accordance with applicable rules and regulations, but employees can also commit fraud and abuse the asset provided. When conducted research, it showed that employees and managers who were senior or who worked long enough were committing fraud or abuse (ACFE, 2008).

Perpetrators of fraud are usually carried out by unscrupulous leaders and employees who work in an organization or company where he works, fraud will be more difficult to detect if it is carried out by the leadership or management compared to what is done by employees. In asset management, misuse of assets often occurs, including misuse or theft of assets. This type of fraud is also the type of fraud that occurs most often and is usually carried out by employees or employees who have less influence or authority in the organization.

According to Indonesia Corruption Watch (ICW) from 2014 to 2018, various types of corruption cases such as bribery, abuse of authority, misuse of funds and falsification of data handled by the KPK reached a total of 64 cases spread across several regions in Indonesia. In addition, fraudulent practices in the management of regional assets are still commonly found in local government institutions and agencies. Like the phenomenon that occurred in Donggala Regency, Central Sulawesi Province in 2018, at that time the Department of Highways and Spatial Planning of Central Sulawesi carried out work to replace the torate bridge with a budget ceiling of Rp. 18 billion sourced from the budget (Zamzam, 2019). Another case occurred in Makassar City, South Sulawesi, where the Head of the Regional Financial and Asset Management Agency (BPKAD) of Makassar City, South Sulawesi, Erwin Syafruddin Haija, was suspected of being involved in the alleged corruption case of cutting money for socialization budget services by 30 percent from the activity budget ceiling of Rp. 70.049 billion (Sohuturon, 2018). The phenomenon of fraud that occurs in both the private and public sectors is inseparable from individual behavior. Research on fraudulent behavior by Donald Cressey (1953) with the fraud triangle. However, this research in recent years has received criticism from several researchers because fraudulent behavior is not only caused by individual factors but also by organizational factors, social factors and environmental factors (Wells, 2005; Ramamoorti, 2008; Krambia-Kapardis, 2016; Yusrianti et al., 2020). this study focuses on social factors and the role of organizational factors to reduce fraud in asset management. Social factors in this study related to social learning theory, namely peer influence, fraudulent behavior is influenced by colleagues and outcome expectancies, fraudulent behavior in asset management is influenced by rewards and sanctions. Meanwhile, the organizational factor in this research is opportunity. It means that an organization with a weakness in internal control will likely to have more chance of fraud.

Literature Review and Hypothesis Development

The Influence of Peer Influence on Fraudulent Behavior

Peer influence is an individual's belief or perception of the influence of peers in carrying out an action. Festinger (1954) states that humans seek to seek social environments as cues in making ethical decisions that cause them to be open to being influenced by the behavior of other referents including peers. The influence of peers in attitudes, thoughts and actions of individuals is peer influence (Bristol & Mangleburg, 2005). Based on Social Learning Theory, individuals internalize learned behavior based on exemplary behavior (Bandura, 1971). Unethical peer behavior that is observed positively will affect the unethical behavior of observers (O'Fallon, 2007). Thus, it can be concluded that peer

influence affects individuals in decision making. So, it can be hypothesized that the higher the peer influence, the higher the tendency for fraud to occur in asset management. Based on these thoughts, in this study formulate the following hypothesis:

H1: Peer influence has a positive effect on fraudulent behavior in local government asset management.

The Effect of Outcome Expectancies on Fraudulent Behavior

Outcome expectancies is an individual's perception of the expected results, both positive and negative in taking action. Based on the Social Exchange Theory, individual behavior is a consequence of their thoughts. In an organization the ethical behavior of its members is influenced by the rewards or punishments for that behavior (Trevino, 1986; Wood & Bandura, 1989). It can be concluded that the Outcome expectancies of the rewards or punishments that will be received have an effect on fraud. Thus, the higher the individual's perception of Outcome expectancies, the lower the tendency of individuals to commit fraud in asset management. Based on these thoughts, in this study formulate the following hypothesis:

H2: Outcome expectancies have a positive effect on fraudulent behavior in asset management.

Moderating Effect of Internal Control System

Based on a survey conducted by Association of Certified Fraud Examiners (2016), weak internal control is the main cause of fraud. The same result is also found from the results of the KPMG survey cited in Huefner (2011), which proves that the most significant cause of fraud that occurs in the government is weak internal control. With a good internal control system, organizations can minimize fraud and increase opportunities to detect errors in accounting that are done intentionally or unintentionally (DeFond & Jiambalvo, 1991; Kawedar, 2010; Keong, 2020; Fakhimuddin et al., 2021). In the Fraud Triangle Theory, the perception of opportunity explains that weak internal control provides an opportunity to commit fraudulent actions. Kenyon & Tilton (2012); Dorminey et al. (2012). Thus, if the influence of co-workers on fraud in asset misappropriation is higher without being accompanied by good internal control, the level of fraud in asset management will be higher, on the contrary if internal control runs well, the influence of co-workers will not affect behavior to commit fraud. Based on these thoughts, in this study formulate the following hypothesis:

H3: internal control system is able to moderate the effect of peer influence on fraudulent behavior of local government asset management.

The Role of the Internal Control System in Moderating the Effect of Outcome Expectancies on Fraudulent Behavior

Internal control is an organizational factor which in this study is the perception of opportunity in the Fraud Triangle Theory concept. Summers & Sweeney (1998) state that poor financial conditions indicate weak internal controls that allow fraud to occur. Bell & Carcello (2000) stated that weak internal control and aggressive management attitude tend to lead to fraud. Thus, if behavior is based on outcomes and is supported by good internal control, the rate of fraud in asset misappropriation will be low. Based on these thoughts, in this study formulate the following hypothesis:

H4: Internal Control System is able to moderate the effect of outcome expectancies on fraudulent behavior of local government asset management.

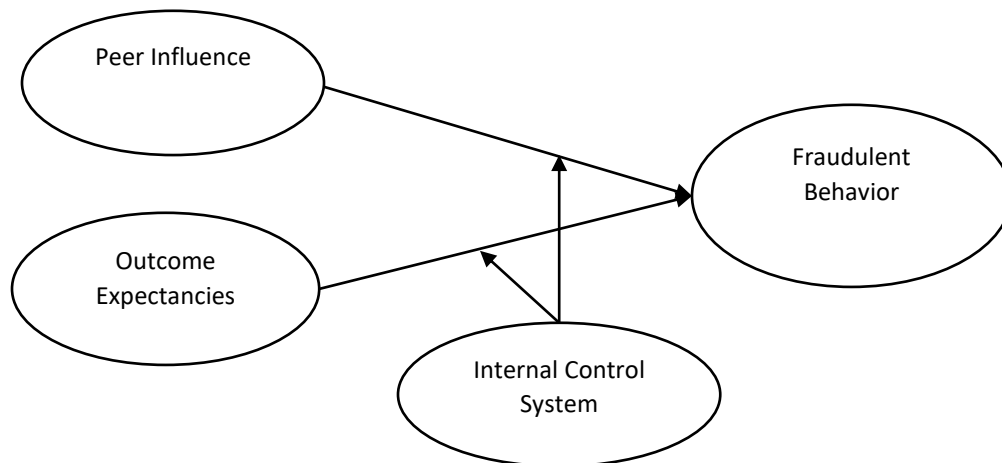


Figure 1 Research Framework

Research Methods

This study was conducted using a survey method, namely research that collects opinions from respondents using a questionnaire related to the managerial performance of local government apparatus in Palu City. Questionnaires will be distributed using email to respondents.

The variable measured in this series of research is fraudulent behavior with misappropriation of regional assets based on the perception of social and organizational factors with the research object of Palu municipal government in Central Sulawesi

Province. This research will distribute the questionnaire electronically via google form to the Regional Property Management Officer of the Central Sulawesi Provincial Government. The data in this study came from primary data using a list of statements (questionnaires) which were distributed directly to each regional government unit. Respondents in this study were all asset managers working within the unit of Central Sulawesi Province. Based on the predetermined sample, there are 117 respondents who will fill out the research questionnaire. Respondents were taken from 39 units where each of them was taken as many as 3 respondents.

Results

Of the 117 copies of the questionnaire distributed, 114 of the returned questionnaires and 3 of the questionnaires did not return because the respondents refused to fill out the questionnaire. Thus, the number of questionnaires that can be processed is as many as 114 copies of the questionnaire can be seen from Table 1.

Table 1 Response Rate

Information	Freq.	Percentage
Questionnaires distributed	117	100%
Non-returning questionnaires	3	2,5%
Questionnaires Returned	114	97,5%
Response rate	114	97,5%

The results of the tests that have been carried out to test several other fit model indicators (parameters) such as: Average path coefficient (APC), Average R-squared (ARS), Average adjusted R-squared (AARS), Average block VIF (AVIF) and Average VIF block (AVIF) is presented in Table 2.

Table 2 Model Fit Indicators

Parameter	Value	Limitation	Conclusion
Average path coefficient (APC)	0.117 P=0.013	p<0.05	Model fit
Average R-squared (ARS)	0.169 P<0.015	p<0.05	Model fit
Average adjusted R-squared (AARS)	0.139 P<0.032	p<0.05	Model fit
Average block VIF (AVIF)	1.228	acceptable if ≤ 5 , ideally ≤ 3.3	Model fit
Average full collinearity VIF (AFVIF)	1,117	acceptable if ≤ 5 , ideally ≤ 3.3	Model fit
Tenenhaus GoF (GoF)	0.321	small ≥ 0.1 , medium ≥ 0.25 , large ≥ 0.36	Model fit

Table 3 showed the Average path coefficient (APC) of 0.117 with p-value of 0.013, Average R-squared (ARS) of 0.169 and p-value of <0.015, Average adjusted R-squared (AARS) of 0.139 and p-value of <0.032, Average block VIF (AVIF) of 1.228, Average full collinearity VIF (AFVIF) of 1,117 and Tenenhaus GoF (GoF) of 0.321. Thus, all parameters are of model fit.

Structural model analysis can be used to test hypotheses. The measurement results of the full structural equation model based on data processing using the WarpPLS software are presented in Figure 2.

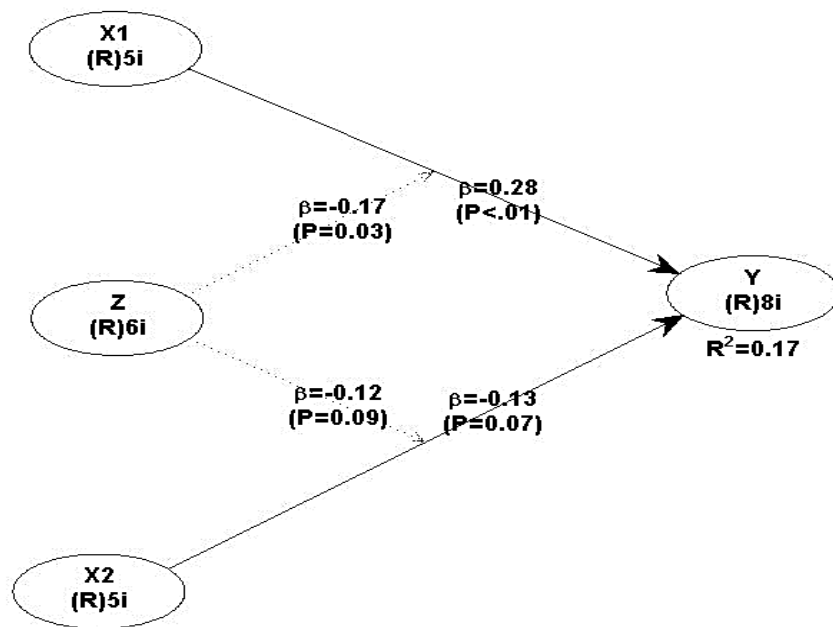


Figure 2 Full Structural Equation Model

Figure 2 indicates that by using a significance level of 0.10. Thus, there is a significant path in the empirical research model (p value generated <0.10).

Table 3 Coefficient

Hypothesis	p-Values	Regression coefficient	Information
H1	<0.01	0.28	Accepted
H2	0.07	-0.13	Accepted
H3	0.03	-0.17	Accepted
H4	0.09	-0.12	Accepted

Discussion

This study found that there was a significant influence of peer influence on the fraudulent behavior. The test results on the parameters between peer influence and fraudulent

behavior as shown in the output of the structural equation model indicate a positive influence between the two variables. The resulting coefficient value in the influence between peer influence on the fraudulent behavior is 0.28 and the resulting p-value of <0.01 is significant at the level of $\alpha = 10\%$. This shows that the hypothesis is accepted and means that peer influence has a positive influence on fraudulent behavior, which means that the higher the Peer Influence, the higher fraudulent behavior of asset management.

The results of this study are in line with several studies related to peer influence which indicate that peer influence affects individuals in carrying out ethical and unethical actions. The results found that that observed unethical peer behavior is more likely to have positive effect on the unethical behavior. This research is in line with that conducted by McCabe & Trevino, (1993), Beams et al. (2003), O'Fallon & Butterfield (2012) with the results of Peer Influence research affecting a person's tendency to abuse assets with the influence of 0.28 and a significance of <0.01 means that the effect is very strong.

The second hypothesis found a significant effect of outcome expectancies had a negative effect on the fraudulent behavior. The test results on the parameters between outcome expectancies and the fraudulent behavior are shown in the output of the structural equation model. The results show a negative effect. This is indicated by the resulting coefficient value of -0.13 and the resulting p-value of 0.07 which is significant at the level of $\alpha = 10\%$. Based on these results prove that the hypothesis is empirically proven and accepted. This means that the higher the outcome expectancies, the lower the tendency for fraud in financial management.

This second hypothesis implies that the thought of being sanctioned from the office and will interfere with future job prospects is a very important indicator of the reduction in the fraudulent behavior in this study as this study was conducted Trevino & Youngblood (1990), Butterfield et al. (1996), Ashkanasy et al. (2006) with the results of their research showing that the making of policy regulations regarding punishment for fraud perpetrators, although the losses due to fraud are not large, this provides a deterrent effect to fraud perpetrators, giving this punishment is also one of the government's efforts to enforce discipline.

The third hypothesis states that the internal control system moderates the effect of peer influence on the fraudulent behavior. The results show a negative effect. This is indicated by the test result coefficient of -0.17 and the resulting p-value of 0.03 which is significant at the level of $\alpha = 10\%$. Based on these results, it proves that the third hypothesis states that the internal control system moderates peer influence and has a negative effect on the

fraudulent behavior. So, the hypothesis is accepted. internal control system is a strong supporting variable that can reduce peer influence on the fraudulent behavior.

The fourth hypothesis states that there is a moderating role of the internal control system in the effect of outcome expectancies on the fraudulent behavior. The test results on the parameters between outcome expectancies and fraudulent behavior with the internal control system as moderating as shown in the output of the structural equation model show that there is a negative effect of the internal control system moderating outcome expectancies on the performance of the fraudulent behavior. With the resulting moderating coefficient of -0.12 and the resulting p-value of 0.09, it is significant at the level of $\alpha < 10\%$.

Conclusion

The analysis concluded that peer influence has a positive effect on fraudulent behavior to be accepted. This means that peer influence can influence fraudulent behavior. Outcome expectancies have a negative effect on fraudulent behavior to be accepted. The second hypothesis is empirically proven. Thus, outcome expectancies have an effect on fraudulent behavior. Internal control system can moderate or weaken the influence of peer influence on fraudulent behavior so that the hypothesis can be accepted. The internal control system can moderate or weaken outcome expectancies against fraudulent behavior so that the hypothesis is supported. This means that the internal control system can moderate outcome expectancies in influencing fraudulent behavior.

Based on the conclusions of the research, future research is recommended. Thus, future research needs to delve deeper into fraudulent behavior. Second, this study is only a tester of the internal control system as a moderator of the influence of peer influence on fraudulent behavior and outcome expectancies on fraudulent behavior.

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