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The Moderation Effect of Islamic Corporate Governance on Fraudulent Financial Statement Detection Using Fraud Hexagon

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Abstract:
Purpose: Given that Islamic corporate governance serves as a moderating variable, this study aims to examine the impact of the hexagon theory on fraudulent financial statements.
Method: This study employed a quantitative methodology and garnered secondary data on Islamic commercial banks in Southeast Asia. Purposive sampling was carried out to collect data from 18 companies during five years (2017–2022), yielding 90 observations. The data analysis method employed Warp-PLS software version 8.0 and partial least square structural equation modeling (PLS-SEM).
Findings: Study results demonstrate that financial stability significantly worsens the performance of fraudulent financial statements. Related party transactions, external auditors, director changes, C.E.O. education, company existence, and political connections did not affect governance, moderate the significant positive influence of financial stability, related party transactions, company existence, and political connections on fraudulent financial statements. Meanwhile, good oversight, external auditors, director changes, and C.E.O. education did not moderate the impact of misleading financial statements.
Originality/Value: This research contributites significantly to the Islamic banking management. The Islamic corporate governance mechanism forms the process and structure of the entity's supervisory, monitoring and advisory functions. The presentation of financial statements is carried out in an accountable and transparent manner based on Sharia principles, which can reduce the practice of financial statement fraud, so stakeholders will be more confident in investing.
Keywords: Fraudulent Financial Statement, Supervisory Effectiveness, Change of Directors, Political Connection, Islamic Corporate Governance
Paper Type: Research Paper

1. Introduction

Financial statements are helpful for external parties, especially investors, to make decisions when investing, so they are used as vital information to measure entity performance. Income and other comprehensive financial statements, statements of financial position, statements of changes in equity, and cash flow activities of a corporation are examples of financial performance statements presented in the Statement of Financial Accounting Standards (PSAK) No. 1 of 2020 regarding the purpose of financial statements. They are helpful for users as a step in economic decisions. Profit figures are used as the central aspect of financial statements, which are indicators of company valuation. This provides opportunities for management as a target for financial statement engineering actions that result in fraud committed by entities. Fraud occurs due to opportunities to take advantage and carry out specific goals on the perpetrator's part. This fraudulent practice is a form of asset irregularities, financial statement fraud and corruption (Stubben & Welch, 2020).

PricewaterhouseCoopers (2018) surveyed ASEAN countries on the percentage of preventive fraud, with the lowest results being in Vietnam, the Philippines, Indonesia, Thailand, Malaysia, and Singapore. The same investigation conducted by the Association of Certified Fraud Examiners (ACFE) (2020) reported that there were cases of fraudulent financial statements in Asia Pacific in third place out of eight parts of the country with 198 cases and an average loss of around U.S. $ 1,988,000. 36 cases occurred in Indonesia making the highest cases and 6 cases found in Thailand.

Informed by the Corruption Perception Index (CPI) 2021 on corruption rate investigations of surveys from 180 countries, the GPA score obtained by Indonesia was 38 from the global average GPA of 43 (Transparency International, 2021). Even though it increased by 1 point from 2020 with a score of 37 and 2019 with a score of 40, the survival score for three consecutive years was still below the global average. According to a survey by Transparency International (2021), based on the Corruption Perception Index (CPI), countries in Asia obtained the most alarming levels of corruption, including the score received by North Korea as much as 16, Cambodia's score was 23, Myanmar's score was 28, Laos' score was 30. Papua New Guinea's score was 31. Transparency International (2022) shows that Southeast Asian countries are mainly below the global average. Two countries that obtained GPAs exceeding the global average were Singapore, with a score of 85, and Malaysia, with a score of 48.

P.T. Bank Maybank Indonesia Tbk committed the banking industry fraud case in Southeast Asia in 2020, namely the loss of customer funds of IDR 22 billion. Maybank is Malaysia's second largest financial services company under the trade name Malayan Banking Berhad and an essential bank in Singapore, Indonesia and the Philippines. In addition, Maybank has a role in developing Islamic banking through Maybank Islamic Bank and insurance from Etiqa's subsidiaries (Sidik, 2020). In 2018, fraud cases were also perpetrated by P.T. Bank Syariah, by distributing fictitious financing of Rp 1.1 trillion. As a result of this fraud, the state as a state-owned enterprise has the potential to suffer losses because, as shareholders, it is 99%, so it must provide additional capital as a reserve (Fauzie & Agustiyanti, 2018). Furthermore, the fraud case occurred in the Acting Main Directorate of Bank West Java and Banten (BJB) in 2017 contained fictitious loans, resulting in the entity's loss of Rp 548 billion. Then, the misuse of customer deposit funds of IDR 20 billion is a case of P.T. Bank Mega Syariah fraud from 2015 to 2021, which has not resulted in a settlement (Anton, 2018).

Vousinas (2018) developed a fraud hexagon theory called the S.C.C.O.R.E. Model: "stimulus, capability, collusion, opportunity, rationalization, and egoism". An additional element of the hexagon fraud theory is collusion. Collusion is a partnership between company management and parties outside the company with specific interests or cooperation between internal employees with dishonest actions. Collusion is an element of fraud committed by an individual or group of employees. Other employees eventually follow it. It develops into a bad culture and makes it normal for the company to be influenced by parties with persuasive personalities. Collusion can be carried out, including the use of one's ability to take the position of others (Kusumosari & Solikhah, 2021).

Internal supervision as one of the units in an entity can prevent the risk of fraud in financial statements. Islamic corporate governance monitors management activities to prevent the risk level of fraudulent financial statements, so the presentation of financial statements and Islamic corporate governance must be accountable and transparent for the business units (Al-Homaidi et al., 2020). Islamic corporate governance is being implemented, and transparent disclosure shows the quality of Islamic banking governance to improve the institution's reputation (Alhammadi et al., 2020).

In the banking industry, the fraud component, including the stimulus with the financial target variable, influences fraudulent financial reports (Kusumosari & Solikhah, 2021; Noble, 2019). Research Octani et al. (2021) suggest financial stability affects fraudulent financial reports. Afiani et al. (2020) recommend that financial stability impacts on fraudulent financial reports, in which there was an effect of pressure on fraudulent financial statements in Indonesia and Malaysia. Meanwhile, financial targets did not affect financial statement fraud (Cahyani & Annisa, 2021; Handoko, 2021; Umar et al., 2020). The opportunity component, which measures monitoring effectiveness, positively affects fraudulent financial reporting (Meidijati & Amin, 2022; Rohmatin et al., 2021). Conversely, previous studies conducted by Handoko (2021) and Octani et al. (2021) the opportunity component did not affect financial statement fraud. An ineffective internal control system in the financial reporting process can result from management activities that dominate and know more about the company's financial statement information, in addition to the lack of compensation control and ineffective performance of the board of directors and audit committee.

The rationalization element in the hexagon fraud theory with the variable auditor turnover had an impact on financial statement fraud (Aviantara, 2021; Meidijati & Amin, 2022; Umar et al., 2020; Utami & Pusparini, 2019). Meanwhile, other research shows that auditor turnover does not significantly impact financial statement fraud (Handoko, 2021; Ratmono et al., 2020). Management and external parties to justify financial statement fraud using the rationalization element. Capability with the proxy of CEO education of companies in Indonesia impacts on fraudulent financial reports (Aviantara, 2021). Meanwhile, the change of directors did not affect financial statement fraud (Handoko, 2021; Utami & Pusparini, 2019). Changing the board of directors is one sign of financial statement fraud. When a director reports that the management of the company is engaging in fraudulent activity, the corporation fires the director, resulting in a shift of directors.

The element of egoism measured by the frequent number of CEOs' pictures gave an impact on detecting financial statement fraud (Beijaard et al., 2004; Utami & Pusparini, 2019). However, research overtaken by Handoko (2021) and Ilham et al. (2022) suggests that CEO narcissism did not affect financial statement fraud. The appearance of the CEO image in the annual report results from the CEO's willingness to be recognized by report users. The frequency of CEO photos is arrogant, considering that the CEO is not included in the internal control assessment. The collusion element, the political connection variable, affects financial statement fraud (Handoko, 2021). Research by Octani et al. (2021) shows that cooperation with government projects had no impact on fraudulent financial reporting. Companies implementing projects from the government get significant funds and can improve the company's image for stakeholders.

Implementing Islamic corporate governance in Islamic banking affects financial statement fraud (Li et al., 2021). Studies conducted by Lidyah (2018) and Ilham et al. (2022) state that Islamic corporate governance affects financial statement fraud in banking in Indonesia. Similar results were presented by Elghuweel et al. (2017), indicating that Islamic corporate governance, as measured by the audit committee, influences corporate earnings management in Oman. Islamic corporate governance had no impact on financial statement fraud (Desiana et al., 2021; Indrati et al., 2021; Mahrani & Soewarno, 2018). The study results by Lassoued et al. (2018) reveal that Islamic corporate governance did not affect corporate earnings management in Morocco. Agency theory and Sharia enterprise theory are the basic concepts in disclosing Islamic corporate governance in Islamic banking. The Islamic corporate governance mechanism forms the process and structure of the entity's supervisory, monitoring and advisory functions. The presentation of financial statements is carried out in an accountable and transparent manner based on Sharia principles, which can reduce the practice of financial statement fraud, so stakeholders will be more confident in investing.

2. Literature Review

2.1 Agency Theory

The agency perspective explains the understanding of the different interests between agents and principals (Jensen & Meckling, 1976). Agency theory assumes that individuals are motivated by self-interest, which can lead to principal and agent conflicts. The focus of shareholders is to improve welfare by getting maximum profit, while management aims to increase investment funds, loans and compensation contracts.

Agency relationships can be a problem between agents and principals. It happens because humans have the nature always to satisfy their interests. Managers, as agents, want significant incentives for their performance in carrying out tasks in the company. At the same time, shareholders, as principals, desire greater returns from capital and relatively quick investments.

Agency theory assumes that individuals are driven by self-interest, resulting in conflicts of interest between principals and agents. Shareholders contract for their welfare by maximizing probabilities, whereas managers have the motivation to maximize the return on investments, loans and compensation contracts. Managers are encouraged to select and apply accounting methods by reporting their performance to obtain shareholder bonuses. It inditaes that there are interests that are not in line between agents and principals, each party is motivated by they want the level of welfare (Hendrastuti & Harahap, 2023).

2.2 Shariah Compliance Theory

Shariah compliance is the Islamic banks' conformity to sharia laws. Sharia compliance reflects a culture of compliance in managing Islamic banking risks and is a component of the risk management framework's application (Widialoka et al., 2016).

Adherence to Sharia principles is essential in Islamic banking, so Sharia advisory or supervision is another important aspect. Moreover, sharia advisory and supervision are part and parcel of sharia compliance. In this context, a Sharia supervisory board is integral to the regulatory framework for Sharia compliance.

The principle of Sharia enterprise theory in Islamic commercial banks will make bank performance healthier because management will comply with the principles set. With the implementation of Islamic values, the bank's daily activities will be carried out based on sharia rules (Anggraini & Suryaputri, 2023). Employees will be treated well, contracts offered to customers will prioritize contracts regulated by sharia, social community activities will be improved, and so on. Vice versa, the failure of Islamic banks to meet the wants and needs of stakeholders will impact the loss of company support and access to the resources they need, which will disrupt the performance of Islamic banks.

2.3 Hypotheses

Agency theory explains the company's financial stability; if financial stability decreases due to the economic influence of the company's operating activities, it will make the potential for management to get pressure and find ways to cover the situation, then carry out fraudulent financial reporting actions (Sawaka & Ramantha, 2020). Financial stability positively affected fraudulent financial reporting. Good financial stability increased the company's image and gives stakeholders a good impression (Meidijati & Amin, 2022; Sawaka & Ramantha, 2020). Nevertheless, if the financial condition improves, investors will consider it when making investment decisions. This causes management to receive increased pressure and be motivated to do fraudulent financial reporting.

H_1: Financial Stability Affects Fraudulent Financial Statement

An inadequate internal supervision system in the financial reporting process can be caused by a lack of compensation control, subpar performance by the board of directors and audit committee, dominating management operations, familiarity with the company's financial statements, and other issues. A board of commissioners' participation can result in more efficient oversight due to the independent commissioners' proportionate involvement in regulating management policies and reducing financial statement fraud.

According to studies by Luthan et al. (2016), Arshad et al. (2012), and Mahrani and Soewarno (2018), insufficient monitoring had a significant impact on the ability to identify financial statement fraud. However, Noble's (2019) research demonstrates that inadequate monitoring did not identify fraud in financial statements. A board of commissioners can provide more optimal supervision because the proportion of independent commissioners has the function of supervising management policies to reduce financial statement fraud.

H_2: Adequate Supervision Affects Fraudulent Financial Statement

Related party sales transactions are complex because of transactions between entities and internal parties, so companies can justify fraudulent actions (Olszewski, 2014). Research by Wang et al. (2019) states that related party transactions increased the opportunity to commit financial statement fraud by violating applicable accounting standards.

H_{3a}: Related Party Transaction Affects Fraudulent Financial Statement

External auditors are of good quality if the company chooses audit services from public accounting firms in the BIG4 category (PWC, Deloitte, Ernst & Young, K.P.M.G.). The use of external audit services from KAP BIG4 is believed to be able to detect, assess and reveal reporting errors in better management (Meidijati & Amin, 2022). Management and external parties justify financial statement fraud actions by using rationalization elements. This can reduce the results of poor auditor conservation, but senior auditors who detect it will identify risks to prevent financial statement fraud. Rohmatin et al. (2021) reveal that external auditor quality negatively affected fraudulent financial reporting. It can reduce the results of poor auditor observations, but senior auditors who concern this will identify risks to prevent financial statement fraud.

H_{3b}: External Auditors Influence Fraudulent Financial Statements

The change of directors is one of the indicators of financial statement fraud. This is due to the existence of a director who knows the actions of the company's management who carried out fraud, and the company issued the director, so there was a change of directors. With the change in directors, the new directors must make adjustments to the environment, culture, and new work so that it becomes a loophole for management to commit fraud in the financial statement.

The findings of change in directors play a role in detecting financial statement fraud, as found in research by Utami & Pusparini (2019) and Ratmono et al. (2020). However, research overtaken by Meidijati and Amin (2022) uncovers that a change in director had no effect in detecting financial statement fraud. With the change in directors, the new directors must adjust their new environment, culture and work so that this becomes a gap for management to commit financial statement fraud.

H_{4a}: Change of Directors Affects Fraudulent Financial Statement

Highly educated, broad-minded leaders can analyze business transactions and are more effective in future policy-making (Suyanto et al., 2022). Mukhibad et al. (2022) point out that a competent CEO can influence management in decision-making. Thus, the higher the CEO's education level, the more excellent the opportunity to commit fraud.

H_{4b}: CEO Education Affects Fraudulent Financial Statement

The condition of a company in increasing its existence is that management can make financial statements redundant (Suyanto et al., 2022). In the company's existence, management's efforts can manipulate financial statements to produce good performance (Meidijati & Amin, 2022).

H_5: The Existence of the Company Affects the Fraudulent Financial Statement

Collusion is an agreement between two or more people for unfavorable purposes, such as deceiving third parties of their rights (Vousinas, 2018). The company carries out projects from the government, gets significant funds and fosters the company's image for stakeholders. Thus, the company will always look for ways to get projects from the government because it has become a government relationship. The more often companies cooperate with the government, the more it will cause the nature of company collusion, which can lead to financial statement fraud.

According to Mukaromah and Budiwitjaksono (2021), working on government projects together can reduce financial statement fraud. The company's participation in government projects increases efforts to secure a large project to demonstrate strong company performance (Ilham et al., 2022). Thus, the company will always look for ways to get projects from the government because it has become a government relation. The more often the company cooperates with the government, the more it will lead to collusion like the company, which can lead to financial statement fraud.

H_6: Political Connection Affects Fraudulent Financial Statements

Agency theory and Sharia enterprise theory are the basic concepts in disclosing Islamic corporate governance in Islamic banking. The process and structure of supervising, monitoring, and advising entities are formed in the mechanism of Islamic Corporate Governance. The presentation of financial statements is carried out in an accountable and transparent manner based on Sharia principles, which can reduce the practice of financial statement fraud so that stakeholders will be more confident in investing (Desiana et al., 2021).

Research by Mukhibad et al. (2021) states that Islamic corporate governance negatively affected preventive fraud. This aligns with Lidyah's (2018) study, which reporting that Islamic corporate governance negatively affected preventive fraud, so it can monitor management actions to minimize fraud.

H_7: Islamic Corporate Governance Moderates the Effect of Fraud Hexagon on Fraudulent Financial Statements

A research model for this topic can be framed in Figure 1 based on the four examined hypotheses:

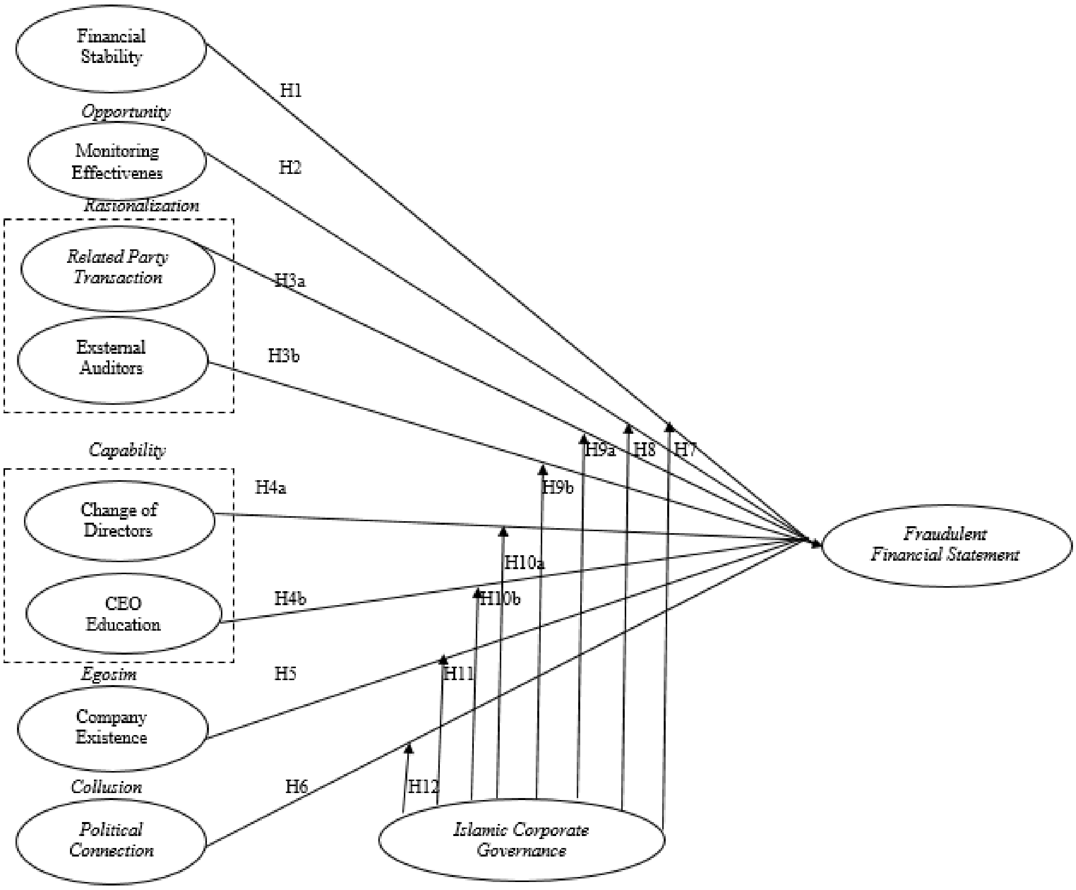

Figure 1. Research Model

3. Research Method

3.1 Research Approach

The correlational research style used in this work has a quantitative methodology. This study aims to examine the impact of the parts of the fraud hexagon theory, such as "stimulus, opportunity, rationalization, capability, egoism and collusion", and Islamic corporate governance on fabricated financial statements of Islamic banking in Southeast Asia.

All Southeast Asian Islamic commercial banks served as the study's sample. Purposive sampling strategies were used to select the sample considering the following criteria:

1) They were Sharia banks in Southeast Asia.
2) From 2017 through 2021, Sharia banks produced annual reports.
3) Sharia banks provided comprehensive annual reports for 2017 through 2021 on the websites of Islamic bank businesses in Singapore, Brunei Darussalam, Thailand, and

the Philippines, Indonesia Stock Exchange (www.idx.co.id), Malaysia Stock Exchange (www.bursamalaysia.com), and Indonesia Stock Exchange.

3.2 Data

Table 1. Research Samples

No	Information	Total
1	Islamic banks operated in Southeast Asia: Indonesia (17), Malaysia (17), Brunei Darussalam (2), Singapore (2), Thailand (1), the Philippines (1)	41
2	Islamic banks did not publish annual reports in 2017-2021	(18)
3	Islamic banks had incomplete annual reports for 2017-2021	(5)
	Total Samples 18 x *5*	**90**

3.2.1 Fraudulent Financial Statement

A fraudulent financial statement manipulates the presentation of financial statements carried out intentionally and not by accounting standards by providing unaccountable information and misleading users in decision-making. Measurement of fraudulent financial statement, i.e. Beneish M-Score Modified (Tarjo & Herawati, 2015):

$$\text{M - Score} = -2{,}634 + 0{,}920\text{DSRI} + 0{,}009\text{GMI} + 0{,}404\ \text{AQI} + 0{,}043\text{SGI} - 2{,}191\text{TATA}$$

The ratio index or modified Beneish M-Score ratio can be calculated as follows:

1) DSRI (Days sales in the receivable index) = $\frac{(\text{Net Receivables}_{t}/\text{Sales}_{t})}{(\text{Net Receivables}_{t-1}/\text{Sales}_{t-1})}$
2) GMI (Gross Margin Index) = $\frac{(\text{Sales}_{t-1}-\text{COGS}_{t-1})/\text{Sales}_{t-1}}{(\text{Sales}_{t}-\text{COGS}_{t-1})/\text{Sales}_{t}}$
3) AQI (Aset Quality Index) = $\frac{(\text{TA t}-(\text{CA t}+\text{PPE t})/\text{TA}_{t}}{(\text{TA t}-1-(\text{CA t}-1+\text{PPE t}-1)/\text{TA}_{t-1}}$
4) SGI (Sales Growth Index) = $\frac{(\text{Sales t}}{-\text{ Sales t}-1)/\text{Sales t}-1 \text{ x } 100}$
5) TATA (Total Accruals to Total Assets) = $\frac{\text{Net Income Continuing Operations t}-\text{Cash Flows from Operation)}}{\text{Total Assets t}}$

3.2.2 Financial Stability

Financial stability provides information on the stability of an entity's financial condition as a benchmark for company performance. Measurement with Sales to Total Asset Ratio (Handoko, 2021). SALTA = revenue / total assets

3.2.3 Monitoring Effectiveness

The audit committee is a party outside the company that has the function of increasing the effectiveness of supervision to prevent fraudulent financial statements (Mukaromah & Budiwitjaksono, 2021). BDOUT = number of audit committees for accounting matters/ number of audit committees

3.2.4 Related Party Transaction

Related party sales transactions are complex because of transactions between entities and internal parties, so companies can justify fraudulent actions (Habib et al., 2017). RPT Sales = number of related-party sales / total sales.

3.2.5 Related Party Transaction

External auditors are the experts at public accounting firms who detect and report the results of audits that have been carried out. External auditor proxies are measured with dummy variables by giving code 1 if the company partners with Big Four KAP and code 0 if the company does not partner with Big Four KAP.

3.2.6 Change of Directors

To improve directors' performance more effectively, the board of directors is replaced with new directors from the preceding time. If there is a change in directors, the measurement of the change in directors using dummy variables yields code 1, and if there is not, it yields code 0.

3.2.7 CEO Education

A capable CEO can place pressure on management to make decisions. A dummy variable with a value of 1 if the CEO has a master's degree or more and 0 if they do not is used to measure the CEO Education variable (Kusumosari & Solikhah, 2021).

3.2.8 Company Existence

The existence of the company is the existence of a sustainable company. Test company existence with dummy variables code 1 if the company establishment is at least ten years and code 0 if the company establishment is less than ten years (Mukaromah & Budiwitjaksono, 2021).

3.2.9 Political Connection

Companies that collaborate with government projects tend to approach fraudulent financial reporting (Octani et al., 2021) by measuring political connection with dummy variables, code 1 if the entity collaborates with government projects and code 0 if the entity does not carry out government project cooperation.

3.2.10 Islamic Corporate Governance

The Sharia business good governance (GGBS) guidelines published by the National Committee on Governance Policy (KNKG) in 2011 contained 25 items, including four items related to the organization and operation of the Sharia advisory board, 11 items related to the directors' structure and operation, and ten items related to sharia business ethics. Islamic corporate governance is measured by dividing the total items by the number of indicators that have been published.

The data analysis technique used the PLS 4.0 Path Analysis test. Latan and Ghozali (2016) define partial least square (PLS) is a robust set of analytical methods, commonly called soft modeling since it eliminates the assumptions of ordinary least square (OLS) regression, such as data must be normally distributed, and there is no multicollinearity problem between exogenous variables.

In this study, all variables were observed that could be measured directly. The PLS-SEM testing method in this study is the evaluation of the structural model (inner model). The structural model is evaluated to predict the relationship between variables by seeing how much variance can be explained and determining the significance of the P-value.

The first step in evaluating the structural model was to assess whether the research model has met the goodness of fit criteria. This assessment was carried out by looking at the value of six indicators, namely average path coefficient (APC), average R-square (ARS), average adjusted R-square (AARS), average variance inflation factor (AVIF), average full collinearity VIF (AFVIF), and Tenenhaus GoF.

The criteria must be considered in assessing model fit. The recommended average path coefficient, average R-square, and average adjusted R-square scores were less than or equal to 0.05 at 5% significance level. Meanwhile, the acceptable average variance inflation factor and average full collinearity VIF scores were less than or equal to 5, especially for models where all variables were single indicators.

The next step of structural model evaluation was to assess how much the model's ability to explain the dependent variable. This stage was done by looking at the coefficient of determination R 2, F two effect size, and Q 2 predictive relevance. The final step in testing was to look at the P-value and path coefficient to determine the significance and direction of the relationship between exogenous variables and endogenous variables.

$$Y = \alpha + \beta_1 SALTA + \beta_2 BDOUT + \beta_3 RPT\ Sales + \beta_4 AE + \beta_5 CEO\ Change + \beta_6 CEO\ Edu + \beta_7 EP + \beta_8 PC + \beta_9 SALTA * ICG + \beta_{10} BDOUT * ICG + \beta_{11} RPT\ Sales * ICG + \beta_{12} AE * ICG + \beta_{13} CEO\ Change * ICG + \beta_{14} CEO\ Edu * ICG + \beta_{15} EP * ICG + \beta_{16} PC * ICG + \varepsilon \quad (1)$$

4 Results and Discussion

4.1 Descriptive Statistics

The descriptive statistical analysis describes research data regarding the distribution and behavior of data collected in Ghozali (2018).

Table 2. Descriptive Statistics

Variable	N	Minimal	Maximal	Mean	SD
Fraudulent Financial Statement	90	-3,750	-1,080	-2,217	0,504
Financial Stability	90	0,006	0,448	0,103	0,077
Monitoring Effectiveness	90	0,333	0,500	0,419	0,062
Related Party Transaction	90	0,016	0,967	-0,357	0,230
External Auditors	90	0	1	-	-
Change of Directors	90	0	1	-	-
C.E.O. Education	90	0	1	-	-
Company Existence	90	0	1	-	-
Political connection	90	0	1	-	-
Islamic Corporate Governance	90	0,530	0,920	0,753	0,106

Table 2 illustrates that the fraudulent financial statement had a minimum value of -.3750, a maximum value of -1.080, an average of -2.217, and a standard deviation of 0.504. Additionally, Islamic corporate governance had a minimum value of 0.530, a maximum value of 0.920, an average value of 0.753, and a standard deviation of 0.106.

4.2 Goodness of Fit

The following are the results of goodness of fit testing on PLS-SEM conducted on research data:

Table 3. Goodness of Fit

Indicator	Value	Sig.	Information	Criteria
APC	0,135	P = 0,047	Accepted	P ≤ 0,05
ARS	0,111	P = 0,007	Accepted	P ≤ 0,05
AARS	-0,083	P = 0,015	Accepted	P ≤ 0,05
AVIF	1,773		Ideal	Ideal ≤ 3,3 Accepted ≤ 5
AFVIF	1,618		Ideal	Ideal ≤ 3,3 Accepted ≤ 5
Tenenhaus GoF	0,334		Medium	≥ 0,1 small ≥ 0,25 medium ≥ 0,36 big

Table 3 demonstrates that the average path coefficient (APC) value was 0.135 with a P-value of 0.047. The average R-squared (ARS) value was 0.111 with a P-value of 0.007. Average adjusted R-square (AARS) value was -0.083 with a P-value of 0.015. All three indicators had fulfilled the criteria of P ≤ 0.05. The average variance inflation factor (AVIF) value of 1.773 has met the ideal criteria of ≤ 3.3. The average full collinearity VIF (AFVIF) value of 1.618 has met the ideal criteria ≤ 3.3. The Tenenhaus GoF value of 0.334, above 0.25, means the model has explanatory strength in the medium category. Thus, all goodness of fit criteria has been met so that the structural model is said to be fit.

4.3 Coefficient Determination Test

The next stage of structural model evaluation is to assess how much the model can explain the dependent variable. This assessment was done by examining the value of R-squared coefficients, Q-squared coefficients and effect size. The test results are shown in Table 4:

Table 4. Coefficient of Determination R-squared, Q-squared

Indicator	Value	Information	Criteria
R-Squared	0,111	Weak	≤ 0,70 strong, ≤ 0,45 medium, ≤ 0,25 weak
Q-squared	0,393	Strong	≥ 0,02 weak, ≥ 0,15 medium, ≥ 0,35 strong $Q^2 > 0$ indicates the model has predictive relevance $Q^2 < 0$ indicates the model lacks predictive relevance

4.4 Hypothesis Test

The evaluation stage of the PLS-SEM structural model is to report the analysis results by looking at the value of the path coefficient and P-value (Latan & Ghozali, 2016). The following figure shows the full structural model of PLS-SEM along with each path's coefficient and P-value.

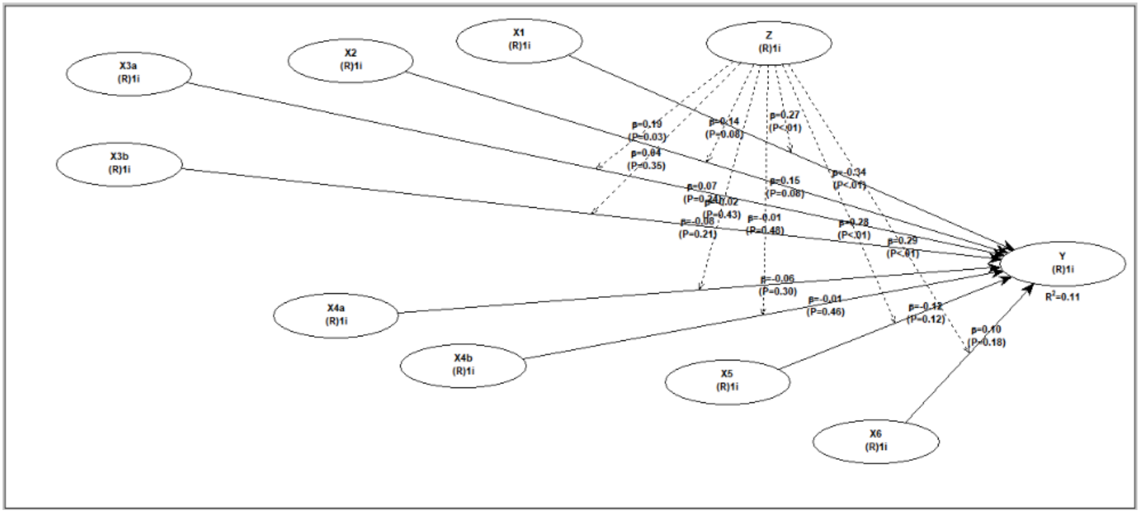

Figure 2. Structural Model of PLS-SEM

Hypothesis testing in this study was based on significance levels of 1% (P-value < 0.01), 5% (P-value < 0.05), and 10% (P-value < 0.10) to accept or reject the hypothesis. The results of hypothesis testing in PLS-SEM is presented in Table 5:

Table 5. Path Coefficient and P-Value

Variables	Path Coefficient	P-value	Information
SALTA → M-Score Modified	-0,343	<0,001	Accepted P < 0,01
BDOUT → M-Score Modified	0,146	0,076	Rejected
RPT Sales → M-Score Modified	0,072	0,242	Rejected
AE → M-Score Modified	-0,083	0,210	Rejected
CEO Change → M-Score Modified	-0,055	0,297	Rejected
CEO Edu→ M-Score Modified	-0,010	0,463	Rejected
EP → M-Score Modified	-0,119	0,122	Rejected
PC→ M-Score Modified	0,095	0,178	Rejected
SALTA*ICG→ M-Score Modified	0,274	0,003	Accepted P < 0,01
BDOUT*ICG → M-Score Modified	0,141	0,083	Rejected
RPT Sales*ICG → M-Score Modified	0,186	0,033	Accepted P < 0,05
AE*ICG → M-Score Modified	0,041	0,347	Rejected
CEO Change*ICG→ M-Score Modified	-0,018	0,432	Rejected
CEO Edu*ICG→ M-Score Modified	-0,006	0,478	Rejected
EP*ICG→ M-Score Modified	0,281	0,002	Accepted P < 0,01
PC*ICG→ M-Score Modified	0,286	0,002	Accepted P < 0,05

4.5 Discussion

4.5.1 Financial Stability on Fraudulent Financial Statement

According to the results of testing Hypothesis 1, the path coefficient for financial stability was -0.343, with a P-value of 0.001, indicating that it is not in line with fraudulent financial statements. According to Hexagon's thesis, pressure is a motive for manipulating financial stability negatively and significantly impacts false financial statements. The company's reputation improves and makes a good impression on stakeholders when its finances are stable. According to agency theory, if financial stability improves as a result of the company's operating activities' economic influence, management potential will decrease pressure and limit fraudulent financial reporting (Sawaka & Ramantha, 2020).

The results of this study indicate that changes in total assets in the company cause the company to commit fraud. Management often gets pressure to show that the company has managed assets well so that the resulting profit is achieved and produces a high return for investors because the amount of total assets affects its attractiveness for investors, creditors, and company owners. However, when total assets decrease, the attractiveness decreases because the company's financial condition is unstable. Therefore, management uses financial statements to cover up unstable financial conditions by committing fraud.

According to studies by Meidijati and Amin (2022) and Sawaka and Ramantha (2020), financial stability reduces the likelihood of misleading financial reporting. According to research, financial stability may affect false financial reporting (Octani et al., 2021). According to Afiani et al. (2020), pressure impacts financial statement fraud in Malaysia and Indonesia. Financial statement fraud is unaffected by the financial target (Cahyani & Annisa, 2021; Handoko, 2021; Umar et al., 2020).

4.5.2 Adequate Supervision of Fraudulent Financial Statements

The results of the Hypothesis 2 test obtained the value of the supervisory effectiveness path coefficient was 0.146 with a P-value of 0.076 so that the effectiveness of supervision did not have a significant effect on fraudulent financial statements. An ineffective internal supervision system in the financial reporting process can result from management activities that dominate and know more information on the company's financial statements, in addition to lack of compensation control, the performance of the board of directors, and the ineffective sharia supervisory board. The audit committee cannot provide more optimal supervision because recruiting audit committee members with an accounting or financial education background in the company is only to meet regulatory requirements, resulting in less-than-optimal roles and functions of the audit committee in conducting company supervision.

The insignificant results of this study indicate the ineffectiveness of the audit committee's control function over financial reports. Audit committee members in the company must refrain from carrying out their duties of monitoring financial reporting. Consequently, the existence of audit committee members has yet to be able to detect fraudulent financial statements. The audit committee's function is to assess the company's performance and monitor management's performance to create an excellent corporate governance company and create a more objective and independent climate.

The research outcomes Handoko (2021) and Octani et al. (2021) have no bearing on financial statement fraud. According to Noble (2019), inadequate monitoring has little impact on the ability to identify fraud in financial statements. While this is happening, studies by Luthan et al. (2016), Arshad et al. (2012), and Mahrani and Soewarno (2018) demonstrate how crucial ineffective monitoring is in spotting financial statement fraud.

4.5.3 Related Party Transaction on Fraudulent Financial Statement

The results of testing Hypothesis 3a obtained the value of the coefficient of the related party transaction path was 0.072 with a P-value of 0.242 so that the related party transaction did not significantly affect fraudulent financial statements. Related-party transactions did not affect fraudulent financial statements because there was a dividing line. Related party sales transactions are complex because of transactions between entities and internal parties, and management still carries out financial reporting based on applicable accounting standards that do not make management commit fraud (Olszewski, 2014). Research by Wang et al. (2019) states that related party transactions increase the opportunity to commit financial statement fraud by violating applicable accounting standards. This is because accounts receivable can be used as a tool to commit fraud in financial statements, such as in uncollectible accounts. Company receivables that have increased from the previous year indicate that the company has poor cash turnover. The company's limited cash can allow managers to commit financial statement fraud. It shows that the higher the receivables in the company, the greater the indication that the company is committing fraudulent financial statements.

4.5.4 External Auditors on Fraudulent Financial Statements

The results of testing Hypothesis 3b obtained the value of the coefficient of the related party transaction path was -0.083 with a P-value of 0.210 so that the external auditor did not significantly affect fraudulent financial statements. External auditors, including KAP Big Four, basically have the same duties and roles in auditing financial statements, whether the financial statements are free from material misstatements caused by fraud or recording errors.

The rationalization element in hexagon fraud theory with external auditor variables did not impact financial statement fraud. This research results agree with that the results of changing auditors do not significantly impact financial statement fraud (Handoko, 2021; Ratmono et al., 2020). Management and external parties justified financial statement fraud actions by using rationalization elements. This can reduce the results of poor auditor conservation, but senior auditors who know about it will identify risks to prevent financial statement fraud. This is not in line with research conducted by Rohmatin et al. (2021), which shows that external auditor quality negatively affects fraudulent financial statements.

4.5.5 Change of Directors on Fraudulent Financial Statement

According to the findings of testing Hypothesis 4a, the change in directors did not significantly affect fraudulent financial statements because the change in directors' path coefficient was -0.055 with a P-value of 0.297. As there is a strategic role to increase commitment and cooperation throughout the organization's ranks to achieve organizational goals efficiently and effectively, the change of directors in the company did not impact on financial statement fraud. The change of directors is a change of leadership in an organization, which is a crucial factor in determining the status and color of the organization. Additionally, the corporation uses the change of directors to replace directors with higher levels of competence and productivity than the prior directors to boost business performance and reduce the likelihood of false financial reporting. Financial statement fraud is unaffected by a director change (Handoko, 2021; Utami & Pusparini, 2019). Nonetheless, according to a study by Utami and Pusparini (2019) and Ratmono et al. (2020), a change in the director can help detect financial statement fraud.

The majority of the companies studied made changes in directors, but this was not executed because there were indications of fraud, but rather for reasons of dissatisfaction with the performance of the current director and making changes to more competent directors. Likewise, directors can be changed because the director's term of office has been completed. The change of directors can also be caused by a company's strategy to reshuffle the new board of directors to improve the company's performance.

4.5.6 CEO Education on Fraudulent Financial Statement

The results of testing Hypothesis 4b obtained the coefficient value of the CEO education path was -0.010 with a P-value of 0.463 so that CEO education did not significantly affect fraudulent financial statements. The results of this study showed that CEO education had a negative and insignificant direction, so the second hypothesis was rejected. The results of the hypothesis test declare that CEO education had no influence on indications of financial statement fraud. The high level of education the CEO possesses could not prove any indication of financial statement fraud. CEOs with educational backgrounds below the master's degree are also competent to manage company activities carefully. This condition is because the CEO's tenure can reinforce the ability to manage company operations.

Rohmatin et al. (2021) and Mukhibad et al. (2022) argue that a competent CEO can influence management's decision-making. Thus, the higher the CEO's education level, the less chance of committing fraud to improve accountability and financial reporting transparency. Research by Rohmatin et al. (2021), Handoko (2021), and Ilham at al. (2022) stated that CEO narcissism had no effect on financial statement fraud. The appearance of the CEO image in the annual report results from the CEO's willingness to be known by report users. It is arrogant to assume that the frequency of CEO photos is not included in the internal control assessment.

4.5.7 The Existence of the Company on the Fraudulent Financial Statement

The results of testing Hypothesis 5 obtained the value of the company's coefficient of existence path was -0.119 with a P-value of 0.122 so that the company's existence did not significantly affect fraudulent financial statements. The condition of a company increasing its existence is that management can commit financial statement fraud (Suyanto et al., 2022). The company's existing defense and management efforts can manipulate financial statements to produce sound financial statement performance (Meidijati & Amin, 2022).

4.5.8 Political Connection on Fraudulent Financial Statements

According to the results of testing Hypothesis 6, political connection did not significantly affect fraudulent financial statements because the path coefficient for political connection was 0.095, with a P-value of 0.178. According to the theory of agency employed as a guide, political ties in this study had a beneficial impact. Management may abuse the benefits and privileges acquired through political connections.

The difference in objectives between agents and principals encourages management to get the maximum profit from their performance. Companies with political connections have the convenience of obtaining loan funds that can bring them into financial distress. This situation gives impetus to management to carry out fraudulent financial statements. In addition, it is also related to adverse selection, which is information known by management and not submitted to the principal. Matangkin et al. (2018) stated that through political connections, companies can get many benefits; one of which is loan funds. However, the large number of loans the company receives will make it more difficult to pay debts and can create financial distress, which can cause pressure to commit fraudulent practices.

4.5.9 Islamic Corporate Governance Moderates the Effect of Financial Stability on Fraudulent Financial Statements

The results of the H_7 test obtained that the coefficient of the variable path of interaction between financial stability and Islamic corporate governance was 0.274 with a significant P-value of 0.003. The results show that Islamic corporate governance moderated the positive influence of financial stability on fraudulent financial statements. Implementing Islamic corporate governance that assists the board of directors and the Sharia supervisory board in ensuring the supervision of financial statements can reduce fraudulent financial statements. Nevertheless, it is pivotal to explain that a company with a stable and sound financial condition is in good condition when implementing Islamic corporate governance to avoid pressure on the management to make fraudulent financial statements.

4.5.10 Islamic Corporate Governance Moderates the Effect of Effective Supervision on Fraudulent Financial Statements

The results of the H_8 test calculated that the coefficient of the variable path of interaction between the effectiveness of supervision and Islamic corporate governance was 0.141 with a P-value of 0.083, which was not significant. The results show that Islamic corporate governance did not moderate the effect of supervisory effectiveness on fraudulent financial statements. The ratio of the audit committee to the field of accounting expertise in banking subsector companies was higher due to meeting regulatory requirements. Therefore, an elected audit committee did not guarantee more effective internal control practices and Islamic corporate governance. The audit committee could only minimize the possibility of fraud because it did not have shares in the company so that it carried out its supervisory function more independently. This implies that an entity with a number of external audit committees may influence profit management practices because the actions taken, including supervision, are independent.

4.5.11 Islamic Corporate Governance Moderates the effect Related Party Transactions on Fraudulent Financial Statements

According to the H_{9a} test results, there was an interaction between related party transactions and Islamic corporate governance with a coefficient of 0.186 and a significant P-value of 0.033. The results demonstrate that Islamic corporate governance limited related party transactions' beneficial effects on fraudulent financial statements. A perspective known as rationalization evaluates the fairness of unethical behavior, including fraudulent financial statements. Although the adoption of Islamic corporate governance may aid in the reduction of fraudulent financial statements, management still justifies the manipulation of financial accounts by considering transactions with linked parties to be internal.

4.5.12 Islamic Corporate Governance Moderates the Effect of External Auditors on Fraudulent Financial Statements

According to the H_{9b} test results, there was no significance between external auditors and Islamic corporate governance, as indicated by the coefficient of the variable route of interaction being 0.041 and a P-value of 0.347. The research results demonstrate that Islamic company governance did not affect external auditors' ability to detect fraudulent financial statements. Financial statement fraud was unaffected by a company's audit by one of the Big Four public accounting firms. The majority of the organizations under study changed their auditors during the research period, but they did not conduct to hide the audit trail left by earlier auditors who discovered fraud in the company; instead, they did so in response to an external auditor's appraisal of their performance. Nonetheless, the corporation has previously found the auditor's performance wanting.

4.5.13 Islamic Corporate Governance Moderates the Effect Change of Directors on Fraudulent Financial Statements

According to the H_{10a} test results, there was no significance between the effect of changing directors and Islamic corporate governance because the coefficient of the variable interaction route was -0.018, with a P-value of 0.432. The results demonstrate that Islamic corporate governance did not affect how fraudulent financial statements were affected by a change in directors. Most of the corporations under investigation changed their board of directors, but not because there was evidence of fraud; instead, they did it because they were unsatisfied with the performance of the directors who were in place at the time and wanted to replace them with more capable individuals.

The concerned director's term of office has expired, and a change of directors may be made. Another reason for a change in directors could be a corporate plan to shuffle the new board of directors to boost performance. This allows the recently appointed directors to adjust and become familiar with the entire organization. Therefore, others may utilize this to conduct fraud. Using Islamic corporate governance will lessen the use of false financial statements. In order to prevent Islamic corporate governance from limiting changes in directors to false financial statements, the company replaces directors as needed to improve company performance.

4.5.14 Islamic Corporate Governance Moderates the Effect of CEO Education on Fraudulent Financial Statements

According to the H_{10b} test results, there was no statistical significance between CEO education and Islamic corporate governance, with an interaction coefficient of -0.006 and a P-value of 0.478. The study results demonstrate that Islamic corporate governance did not affect reducing the impact of CEO training on fraudulent financial statements. A manager's capability to commit fraud in the course of the business's daily operations.

The chosen educational path may be relevant to the ability to produce fraudulent financial statements. The level of education is independent of management's decision to falsify financial statements. Fraud is anticipated to decrease as a result of Islamic corporate governance being used in the supervisory function. To produce financial statements that are fair, transparent, accountable, and relevant to the principles and objectives of Islamic corporate governance, management and directors must receive CEO education along a high education pathway.

4.5.15 Islamic Corporate Governance Moderates the Effect of the Existence of the Company on Fraudulent Financial Statements

The H_{11} test yielded a coefficient of 0.281 with a significant P-value of 0.002 for the variable interaction route between the company's presence and Islamic corporate governance. The study results indicate that Islamic corporate governance limited the beneficial impact of corporate presence on fraudulent financial reporting. Management's ability to falsify financial statements is a requirement for a company to grow (Suyanto et al., 2022). Fraud is anticipated to decrease due to Islamic corporate governance used in the supervisory function. Due to the company's long history and the large number of stakeholders that support Islamic general banking, management can alter financial statements to achieve positive financial statement performance (Meidijati & Amin, 2022).

4.5.16 Islamic Corporate Governance Moderates the Effect of Political Connection on Fraudulent Financial Statements

The H_{12} test yielded a coefficient of 0.286 with a significant P-value of 0.002 for the variable interaction route between political ties and Islamic corporate governance. The study results reveal that Islamic business governance limited the beneficial impact of political ties on false financial statements. The audit committee can monitor the firm's performance and relationships with the government, mainly when the company works with them, so that the audit committee's support for fraudulent financial statement initiatives with the government is reduced. The implication of this research result is to help company principals consider the application of policies in fraudulent financial statements in terms of fraud hexagons and effective internal control by implementing Islamic corporate governance.

5 Conclusion

The present study promotes that financial stability had a significant negative effect on fraudulent financial statements. The effectiveness of supervision, related party transactions, external auditors, changes of directors, CEO education, company existence, and political connection did not affect fraudulent financial statements. Meanwhile, Islamic corporate governance moderated the significant positive influence of financial stability, related party transactions, corporate existence and political connection on fraudulent financial statements. Islamic corporate governance did not moderate the effect of adequate supervision, external auditors, change of directors, or CEO education on fraudulent financial statements.

This study limits the focus on the Islamic banking industry, which results in several fraud hexagon indicators that are not significant in preventing fraudulent financial statements. In response to this, this study recommends further researchers can investigate more diverse variables on other industrial fields, such as manufacturing, and expand the region coverage. The proxies in this study used several dummy variables for external auditors, changes in directors and CEO education, with the results having no significant effect, so further studies are suggested to employ other measurements with a ratio scale for more accurate results. Other studies can use a proxy for fraudulent financial statements F-Score.

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