

The Effect of Diamond Fraud on Indications of Financial Statement Fraud in Manufacturing Companies

*Diamond Fraud on
Financial Statement
Fraud*

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ABSTRACT

Financial statement fraud remains a critical issue in the manufacturing sector, where complex operations and managerial discretion create opportunities for manipulation, highlighting the need to examine the roles of pressure, opportunity, rationalization, and capability as outlined in the fraud diamond framework. This research investigates the influence of the fraud diamond elements on the occurrence of financial statement fraud. Fraudulent financial reporting continues to pose a critical challenge for corporations, as inaccuracies reduce the reliability and usefulness of information in the decision-making process. Recognizing the underlying drivers of such fraud is therefore essential. The study employs a quantitative method and utilizes secondary data derived from annual reports. The research population comprises manufacturing firms listed on the Indonesia Stock Exchange between 2021 and 2023. Through purposive sampling, 39 firms were selected as the sample. Data analysis was conducted using logistic regression with the aid of EViews version 13. The findings reveal that rationalization and capability exert a significant influence on financial statement fraud, whereas pressure and opportunity show no significant effect. These results contribute empirical insights into the dominant determinants of financial reporting fraud and highlight implications for strengthening corporate governance and fraud detection practices in the Indonesian manufacturing industry.

Keywords: *Capability, Diamond Fraud, Financial Reporting Fraud, Opportunity, Pressure, Rationalization.*

ABSTRAK

Kecurangan laporan keuangan tetap menjadi isu krusial di sektor manufaktur, di mana operasi yang kompleks dan kebijakan manajerial membuka peluang untuk manipulasi, sehingga menekankan pentingnya menelaah peran tekanan, peluang, rasionalisasi, dan kapabilitas sebagaimana dijelaskan dalam kerangka fraud diamond. Penelitian ini mengkaji pengaruh elemen-elemen fraud diamond terhadap terjadinya kecurangan laporan keuangan. Pelaporan keuangan yang manipulatif terus menjadi tantangan serius bagi perusahaan, karena ketidakakuratan informasi mengurangi keandalan dan kegunaannya dalam proses pengambilan keputusan. Oleh karena itu, memahami faktor-faktor yang menjadi pendorong kecurangan tersebut sangat penting.

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Penelitian ini menggunakan metode kuantitatif dengan memanfaatkan data sekunder dari laporan tahunan. Populasi penelitian terdiri dari perusahaan manufaktur yang terdaftar di Bursa Efek Indonesia pada periode 2021–2023. Melalui purposive sampling, sebanyak 39 perusahaan dipilih sebagai sampel. Analisis data dilakukan menggunakan regresi logistik dengan bantuan EViews versi 13. Hasil penelitian menunjukkan bahwa rasionalisasi dan kapabilitas memiliki pengaruh signifikan terhadap kecurangan laporan keuangan, sedangkan tekanan dan peluang tidak menunjukkan pengaruh signifikan. Temuan ini memberikan wawasan empiris mengenai faktor dominan penyebab kecurangan pelaporan keuangan serta menyoroti implikasi bagi penguatan tata kelola perusahaan dan praktik deteksi kecurangan di industri manufaktur Indonesia.

Kata kunci: *Kemampuan, Diamond Fraud, Penipuan Pelaporan Keuangan, Peluang, Tekanan, Rasionalisasi.*

INTRODUCTION

Financial statements serve as the main channel through which a company communicates its financial information to stakeholders, including creditors, investors, regulators, and the public. These statements provide critical data that support informed and rational economic decision-making. Prepared in accordance with PSAK Number 1, financial statements present an entity's financial position, operational performance, and cash flows, helping users evaluate management accountability and estimate the company's potential future cash flows.

However, commonly accepted accounting rules are not always followed while preparing financial accounts. Financial statement fraud, which is the intentional and deceptive presentation of facts with the goal of achieving personal gains or the interests of particular parties, is one of the issues that frequently arises (Zack, 2012). This fraud can be carried out through data falsification, transaction manipulation, or the loss of important information. Even though financial statement fraud only makes up 10% of all fraud cases, the damages it produces are far more than those caused by other forms of fraud, according to the Association of Certified Fraud Examiners. Cases of financial statement fraud are common in Indonesia as well as throughout the world. One example is the corruption case of the procurement of village standby cars in Bojonegoro Regency in 2024 involving two employees of an automotive company, with a state loss value of more than IDR 5 billion. Another case occurred in 2021, where an electronics company director was named as a suspect for allegedly embezzling vouchers worth IDR 10 billion. This phenomenon indicates that the firm's internal control is not optimal and that fraudulent practices are still difficult to detect, necessitating a robust approach to understanding it.

To explain the causes of fraud, the fraud triangle theory was proposed, which consists of three main elements, namely pressure, opportunity, and rationalization (Cressey, 1953). Wolfe and Hermanson (2004) Then, they developed this theory into a fraud diamond by adding a fourth element, namely capability, which shows that individuals who have greater ability, access, and authority tend to have a higher potential to commit fraud. Fraud diamond is a theoretical framework used in contemporary research to identify and analyze the factors that cause financial report fraud. Some studies have found that the diamond fraud element has a significant effect on fraud practices (Abdullahi & Mansor, 2018; Wanjiru & Ndegwa, 2020). While other studies state the opposite (Ratmono & Frendy, 2022). This inconsistency encourages the need to retest the theory by considering different research sectors and periods.

Financial statement fraud in the manufacturing sector poses unique challenges due to the complexity of production processes, inventory valuation, and cost allocation, which offer opportunities for manipulation. Compared to other sectors, manufacturing companies often engage in long-term projects and transactions that may not be immediately transparent, thereby increasing the risk of misstatements going undetected (Shodiq et al., 2025). Furthermore, management may falsify financial data to satisfy

internal performance benchmarks or stakeholder expectations as a result of performance demands in competitive industrial environments.

In this context, evaluating the role of the fraud diamond elements becomes increasingly relevant, particularly in industries where managerial discretion and technical capability are high (Utami et al., 2021; Avortri & Agbanyo, 2021). By focusing on manufacturing companies listed on the IDX, this research provides a focused investigation into how internal and external pressures, access to opportunities, rationalization strategies, and individual capabilities interact to influence fraudulent behavior. Understanding these relationships not only helps improve fraud detection mechanisms but also strengthens corporate governance practices, especially in sectors that play a crucial role in national economic development.

This research aims to analyze how the elements of the fraud diamond pressure affect financial statement fraud in manufacturing companies listed on the Indonesia Stock Exchange (IDX) during 2021–2023. The manufacturing sector was chosen due to its diverse characteristics, relatively high transparency in information disclosure, and substantial role in the national economy. The findings are expected to advance accounting knowledge and provide a practical reference for detecting and preventing fraud within corporate environments.

LITERATURE REVIEW & HYPOTHESIS DEVELOPMENT

Agency Theory and Fraud Diamond Theory

According to agency theory, the principal (capital owner) and the agent (management) have a contractual arrangement whereby the principal assigns decision-making authority to the agent (Jensen & Meckling, 2019). In practice, conflicts of interest arise because each party has different goals. performance-based bonuses, which can trigger acts of manipulation of financial statements (Mitchell & Meacham, 2011). Eisenhardt (1989) added that there are three basic human traits in agency theory, namely self-interest (humans tend to be selfish), bounded rationality (humans have limitations in thinking and acting rationally), and risk aversion (tendency to avoid risks). These three traits are the basis for understanding the emergence of managerial opportunistic actions.

By adding capability to the preexisting components of pressure, opportunity, and rationalization, the Diamond Theory expands on Wolfe and Hermanson's (2004) Fraud Triangle. Pressure, often stemming from financial instability or target demands, can drive managers toward manipulation, measured here by changes in total assets (Bishop et al., 2017). Opportunity arises from weak oversight, such as low board independence, which is proxied using the BLOUT ratio (Rahman et al., 2021). Rationalization reflects efforts to justify fraudulent acts and is indicated by changes in external auditors, signaling attempts to avoid detection (Sealy & Simon, 2025). Finally, capability emphasizes the power and skill of individuals in key positions to exploit weaknesses and conceal fraud, proxied in this study through changes in directors (Zahra et al., 2007; Goode & Lacey, 2022).

Theoretical Foundation of Financial Statement Fraud

Fraud is a deliberate act to gain personal or group gain by deviating from the rules of law or ethics. According to the Association of Certified Fraud Examiners (ACFE), fraud in organizations is divided into three main categories, namely corruption, which is a form of abuse of power for personal gain that violates the authority of office. Asset abuse, which includes theft or embezzlement of company assets by individuals in the organization (Pavlović & Paunović, 2019). Financial statement fraud involves the presentation of misleading financial data through inflated income, burden reduction, or concealment of liabilities (Tomak & Yilmaz, 2025). The main motive is to display the image of a financially sound company in order to attract investors or maintain stock prices (Young, 2020).

The purposeful publication of information that misrepresents the company's true financial situation in order to deceive users of financial accounts is known as financial statement fraud (Abimanyu, 2022). The F-Score model, which was created by Dechow et al. (2011) and has two primary components, accrual quality and financial performance, which were used to detect fraud. F-Score identifies companies that show indications of accounting manipulation by comparing accruals and operating cash flows and observing financial performance that deviates from the industry average.

The Determinants of Financial Statement Fraud

Pressure is a state that incites people or business executives to falsify financial figures. Numerous things, including monetary requirements, the drive to meet goals, lifestyle choices, and unstable businesses, can cause this strain. Management is frequently urged to falsify financial figures in order to project an impression of stability when the company's financial situation is disturbed. This is consistent with a study by Manurung and Hadian (2013) that demonstrates the beneficial impact of pressure on financial report fraud. Weak internal control systems within the organization, like inadequate monitoring, give rise to opportunities (Daud & Patandean, 2025). There will be more opportunities to falsify financial statements if supervision is not functioning properly. According to a study by Putro and Puspawati (2023), there is a substantial likelihood that fraud will be committed since the offender believes that their acts won't be readily discovered.

The process by which people morally defend the dishonest things they have done is known as rationalization. For a variety of reasons, including saving the business or pursuing a genuine personal interest, people who commit fraud frequently believe that their actions are appropriate. Research by Siddiq et al. in (Jayanti, 2021) proves that rationalization affects an individual's tendency to cheat. Capability deals with an individual's ability, power, or position that allows them to commit fraudulent acts undetected. One of the indicators of capability is the change of directors, which can open a gap for new perpetrators to commit fraud. Capability has been proven to influence fraudulent actions in financial statements (Fortuna, 2022)

H1: Pressure has a positive and significant effect on financial statement fraud.

H2: Opportunity has a positive and significant effect on financial statement fraud.

H3: Rationalization has a positive and significant effect on financial statement fraud.

H4: Capability has a positive and significant effect on financial statement fraud.

H5: Pressure, opportunity, rationalization, and capability simultaneously have a significant effect on financial statement fraud.

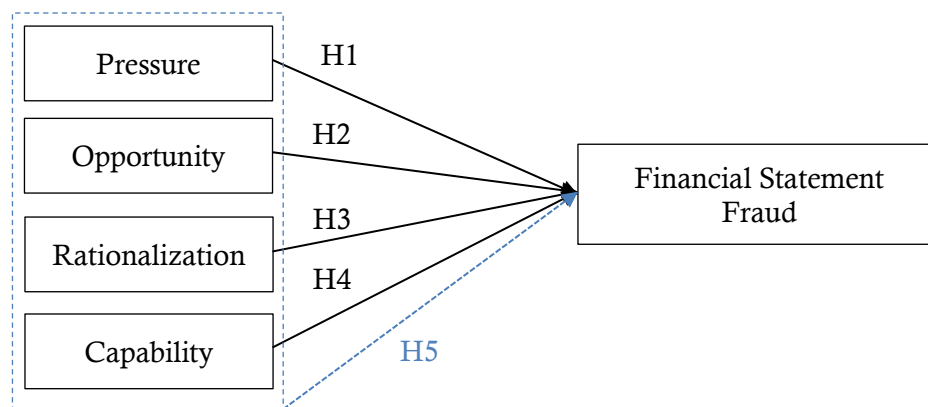


Figure 1. Research Framework

Looking at Figure 1, this research is based on the Diamond Theory of fraud. This theory says that fraudulent financial reporting happens because of four main reasons:

pressure, opportunity, rationalization, and capability. Pressure comes from things like financial problems or pressure to meet goals, which makes management more likely to act unethically. Opportunity happens when there's not enough oversight or weak internal controls, making it easier to manipulate financial statements. Rationalization is when people convince themselves that their actions are justified or necessary. Capability refers to individuals in powerful positions who have the skills and authority to take advantage of weaknesses and hide bad behavior. All four of these factors work together, and each has a strong positive effect on the chance of financial statement fraud happening.

RESEARCH METHODS

This study used a quantitative method, relying on numerical data to represent the research variables and answer the study's questions. The purpose of the study was to examine how the independent factors that make up the fraud diamond's components relate to the dependent variable, financial statement fraud. Manufacturing firms that were listed between 2013 and 2016 on the Indonesia Stock Exchange (IDX) were the study's primary focus. Purposive sampling, which finds respondents according to predefined criteria, was used to choose the samples. Through purposive sampling, 39 firms were selected as the sample.

In this study, the measurement of pressure (X1) is proxied using the ratio of changes in total assets, calculated by comparing asset growth between two consecutive periods. Opportunity (X2) is measured through the Board Lack of Independence (BLOU) ratio, which reflects the proportion of non-independent commissioners to the total board, indicating the effectiveness of monitoring mechanisms. Rationalization (X3) is assessed using a nominal variable, where a value of 1 is assigned if the company changes its external auditor and 0 if no change occurs, capturing management's tendency to justify fraudulent behavior. Capability (X4) is also measured with a nominal variable, assigning a value of 1 if there is a change in the board of directors and 0 otherwise, reflecting the potential for individuals in strategic positions to manipulate systems. Finally, financial statement fraud (Y) is identified using the F-score, which combines accrual quality and financial performance to detect irregularities in reporting.

Using E-Views version 13, logistic regression was used to analyze the data. Eviews 13 provided comprehensive analysis results and facilitated quick and precise data computations. Techniques from logistic regression analysis were applied in this investigation. Data analysis procedures are a methodology whereby, following the collection of data, research will be conducted that yields informational findings that may be utilized as study.

RESULTS

The research looked at some key factors that might be linked to financial statement fraud, such as pressure, opportunity, rationalization, and capability. The table shows how many observations there were (N), along with the lowest and highest values, the average, and how much the values varied for each of these factors. This gives a general idea of how each factor is spread out and how much they differ.

Table 1. Descriptive statistical results

Variable	N	Minimum	Maximum	Mean	Std. Deviation
Financial statement fraud	39	-0.380000	1.230000	0.000256	0.208552
Pressure	39	-0.280000	1.250000	0.053333	0.174470
Opportunity	39	0.200000	0.750000	0.409402	0.114450
Rationalization	39	0.000000	1.000000	0.213675	0.411663
Capability	39	0.000000	1.000000	0.393162	0.490553

Looking at Table 1, there are differences in how these factors are measured. Financial statement fraud is measured using the F-score. The lowest score was -0.38, which was recorded by PT Polychem Indonesia Tbk in 2022, showing the least amount of fraud. The highest score was 1.23, seen in PT Dharma Polimetal Tbk when it first went public in

2021, meaning the most fraud was detected. The average F-score was 0.000256, with a standard deviation of 0.208552. For the pressure variable, measured by CHANGE, the lowest value was -0.28, found in PT Tifico Fiber Indonesia Tbk in 2023, and the highest was 1.25, also from PT Dharma Polimetal Tbk in 2021. The average CHANGE was 0.053333 with a standard deviation of 0.174470. Opportunity is measured by BLOUT, which had a minimum of 0.20 (PT Polychem Indonesia Tbk) and a maximum of 0.75 (PT Indospring Tbk). The average BLOUT was 0.409402 with a standard deviation of 0.114450. Rationalization, measured as a dummy variable, had values between 0 and 1, with an average of 0.213675 and a standard deviation of 0.411663. The change of directors' variable, also a dummy variable, had values between 0 and 1. Its average was 0.393162, with a standard deviation of 0.490553.

Table 2. Model and Goodness of Fit Test Result

Test	Statistic	Value
Test Overall Model Fit	LR Statistics	38.34036
	Prob (LR Statistics)	0.00000
Goodness of Fit Test Results	H-L Statistics	3.3564
	Prob. Chi-Sq (8)	0.9100

Table 2 shows that the LR statistic exceeds the F table value at the 5% significance level, with Prob (LR Statistic) = 0.00000 < 0.05. Thus, H0 is rejected, indicating that the logistic regression model is statistically significant and that the independent variables jointly affect the dependent variable. The Hosmer-Lemeshow test yields a significance of 0.9100 (>0.05), suggesting no significant difference between observed and predicted values. This confirms that the model has strong predictive accuracy and is appropriate for the data.

Table 3. R Square (Nagelkerke R Square) Test Results

Test	Value
Step	1
McFadden R-Squared	0.9100

Table 3 shows that the McFadden R-squared for the logistics regression test's determination coefficient test was 0.495486 (49.5%). This suggests that the variation of the variables of pressure, opportunity, rationalization, and capability may account for 49.5% of the variable of financial statement fraud. The McFadden R-squared result of 49.5% for this investigation was arguably good. Because a number between 20% and 40% implies that the model being employed is excellent, according to the McFadden R-squared determination coefficient test in the Eviews application.

Table 4. Results of Classification Matrix Test

Test	Estimated Equation			Constant Probability		
	Dep=0	Dep=1	Total	Dep=0	Dep=1	Total
P(Dep=1) <=c	100	5	105	105	12	117
P(Dep=1) <=c	5	7	12	0	0	0
Total	105	12	117	105	12	117
Correct	100	7	107	105	0	105
% Correct	95.24	58.33	91.45	100.00	0.00	89.74
% Incorrect	4.76	41.67	8.55	0.00	100.00	10.26
Total Gain*	-476	58.33	1.71			
Per cent Gain**	ON	58.33	16.67			

Table 4 shows that the entire result of the percentage value of correct prediction accuracy in the estimated equation column is 91.45%. This indicates that the model's accuracy in forecasting financial statement fraud in this study is 91.45%.

Table 5. F Test Results

Test	Value
Step	1
Prob (LR Statistics)	0.00000

Based on Table 5, the Probability Likelihood Ratio Statistic (LR statistic) is 0.000000 < 0.05. Thus, the alternative hypothesis (H5) is accepted. The logistic regression model is deemed viable for use in this investigation since it indicates that independent variables significantly impact dependent variables. These findings demonstrate that the variance of the bound variables can be explained by the free variables taken together.

Table 6. Results of the t-test

Variable	Coefficient	Std. Error	t-Statistics	Prob.
Financial Statement Fraud	-4.089984	1.850688	-2.20998	0.271
Pressure	3.158143	1.711456	1.845404	0.0650
Opportunity	5.751544	4.376636	1.314147	0.1888
Rationalization	4.444862	1.160875	3.828888	0.0001
Capability	2.749329	0.986597	2.786679	0.0053

Table 6 shows that the pressure variable (X1) has a positive coefficient of 3.158143 with a p-value of 0.0650, exceeding $\alpha = 0.05$, indicating it does not significantly affect financial statement fraud (H1 rejected). Similarly, opportunity (X2) has a positive coefficient of 5.751544 and a p-value of 0.1888, also above 0.05, suggesting no significant effect (H2 rejected). In contrast, rationalization (X3) has a coefficient of 4.444862 with a p-value of 0.0001, and capability (X4) has a coefficient of 2.749329 with a p-value of 0.0053, both below 0.05, confirming that they significantly influence financial statement fraud (H3 and H4 accepted).

DISCUSSION

The results show that the pressure variable has a positive coefficient of 3.158143, but the significance level is 0.0650, which is higher than $\alpha = 0.05$. This means that even though pressure and financial statement fraud seem to be linked, the connection is not strong enough to be considered statistically significant. The first hypothesis is thus unsupported. These results imply that financial statement fraud in manufacturing organizations in 2021 and 2023 may not be primarily caused by external demands or financial performance expectations. There could be several reasons for this lack of significance. One possibility is that these companies have strong internal control systems or good corporate governance, which prevent pressure from directly leading to fraud. Also, some companies might use risk management approaches that help manage pressure without needing to manipulate financial statements (Celestin, 2015; Cohen et al., 2017).

The opportunity variable has a positive coefficient of 5.751544 with a significance value of 0.1888, which is also above $\alpha = 0.05$. This implies that while financial statement fraud and opportunity are related, this relationship is not strong enough to be statistically significant. Therefore, the second hypothesis is also not supported. This suggests that even if there are opportunities, such as weak internal controls or management influence, they may not be the main drivers of fraud in manufacturing companies during the study period. This can be explained by companies being more aware of the importance of strong internal controls and monitoring systems, especially after new accounting and financial reporting rules were introduced (Abbas & Iqbal, 2012). Additionally, a lot of businesses regularly perform both internal and external audits, which lowers the possibility of financial statement fraud. In other words, although opportunity is a fundamental component of the fraud diamond theory, it does not always serve as the primary catalyst for fraud in practice if businesses have effective control mechanisms.

Below $\alpha = 0.05$, the rationalization variable shows a positive coefficient of 4.444862 at a significance level of 0.0001. This confirms the third hypothesis by demonstrating that financial statement fraud is greatly reduced for this reason. This study supports the notion that the likelihood of financial statement fraud significantly rises when people or management can morally or rationally defend their dishonest behavior. Rationalization can take various forms, such as the assumption that fraudulent actions are carried out for the sake of the company's survival or that all parties are doing the same thing. In this context, weak organizational culture and ethical values can reinforce such tendencies. Therefore, companies need to build strong integrity and moral values in the workplace, including regular ethics training (Kancharla & Dadhlich, 2021; Pratama et al., 2024; Nurcahya et al., 2025). This finding is consistent with the fraud diamond theory emphasising the importance of rationalisation factors in driving fraudulent behaviour (Faradiza, 2019; Handayani et al., 2021).

The results indicate that the capability variable has a positive coefficient of 2.749329 with a significance level of 0.0053, which is below $\alpha = 0.05$. As a result, the fourth hypothesis is accepted, showing that capacity significantly reduces financial statement fraud. The research highlights that those in positions of competence, power, and strategic placement within an organization are more likely to engage in and cover up fraudulent activity (Lamawitak & Goo, 2021). In line with both agency and stakeholder theories, individuals with high capability must be subject to strong checks and balances to ensure that their power is exercised responsibly and in the best interest of all stakeholders. Capability allows individuals to access important information, influence decision-making processes, and cover up traces of manipulation (Baz et al., 2016; Arel et al., 2023). High management or technical skills without sufficient oversight might raise the risk of fraud in sophisticated manufacturing organizations. Therefore, it is crucial for businesses to assess the integrity of people in vital positions in addition to their ability. The implementation of checks and balances principles and strict separation of functions is a crucial step to prevent the misuse of capabilities that lead to fraud (Dimitrijevic et al., 2015; Musyoki, 2023).

CONCLUSION

Pressure does not significantly influence the occurrence of financial statement fraud, indicating that various forms of pressure, such as financial obligations, work demands, lifestyle expectations, or personal habits, do not automatically trigger fraudulent behavior in reporting. Similarly, opportunity does not have a significant effect on financial statement fraud. This suggests that a strong and independent board of commissioners enhances management oversight, effectively limiting or preventing management from acting solely in pursuit of personal interests. Rationalization has a significant effect on the occurrence of financial statement fraud. When something unusual happens, the company tends to change the KAP because the company does not want unnatural things to be known to the public. Companies that have bad intentions or motives will certainly seek justification in their own way and even ignore the public interest when the information presented by the company is not true or misleading. The incidence of financial statement fraud is influenced by capability. After a director change, the organization must adjust to the new culture, which lowers performance effectiveness and opens the door for fraud.

This study demonstrates that financial statement fraud is largely driven by capability and rationalization, whereas opportunity and pressure do not directly affect financial statement fraud, most likely as a result of robust governance and control systems. The findings imply that companies must prioritize building an ethical culture, integrity, and effective oversight alongside technical controls, with particular attention to the competence and trustworthiness of individuals in key positions. Theoretically, the results support the fraud diamond framework by highlighting the critical role of rationalization and capability, while practically, they emphasize the importance of ethics training, checks and balances, and cultural reinforcement. This study is limited by its focus on manufacturing companies during 2021–2023, which may not fully capture variations in

fraud behavior across other sectors or periods where different regulatory pressures, governance quality, and ethical cultures exist. Future research should extend the model by exploring other sectors, incorporating factors such as corporate culture or whistleblowing systems, and applying longitudinal approaches to capture changes in fraud drivers over time.

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