

Analysis of Diamond Fraud and Individual Morality on Village Fund Fraud

Sufiati^{1*}, Eva Marin Sambo², Rahman Pura³

^{1,2,3}Sekolah Tinggi Ilmu Ekonomi Makassar Bongaya, Makassar, Indonesia

**Corresponding author: Sufiati*

Corresponding email: yufhie_stiem@yahoo.co.id

ARTICLE INFO

Article history:

Received 17 May 2024

Revised 01 June 2024

Accepted 13 June 2024

Available Online 30 June 2024

Keywords:

Corruption, Fraud Diamond, Individual Morality, Village Fund Fraud

Cite as:

Sufiati, S., Sambo, E. M., & Pura, R. (2024). Analysis of Diamond Fraud and Individual Morality on Village Fund Fraud. *Economics, Business, Accounting & Society Review*, 3(2), 82–91.

<https://doi.org/10.55980/ebasr.v3i2.136>

ABSTRACT

This study investigates the key drivers of village fund fraud, expanding on the established fraud diamond model. Conducted in the Patallasang sub-district of Gowa Regency, the research surveyed 51 village government officials to analyze the influence of pressure, opportunity, rationalization, capabilities, and individual morality on fraudulent activities related to village funds. The results reveal that pressure, opportunity, and rationalization have significant positive effects on village fund fraud, while capabilities and individual morality exert significant negative influences. Individual morality emerges as the most dominant factor in determining the occurrence of village fund fraud. This study contributes to the theoretical development of the fraud diamond framework by incorporating individual morality as a critical causal element in understanding fraud within the village fund context. The findings of this study hold important implications for policymakers and local government authorities tasked with mitigating fraud and ensuring the effective utilization of village funds. By addressing the multifaceted drivers identified, targeted interventions can be designed to strengthen governance, promote ethical decision-making, and safeguard the integrity of village-level financial management.

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1. Introduction

Corruption in Indonesia has reached alarming levels, with a troubling trend of escalating cases and staggering financial losses for the state. Data from Indonesia Corruption Watch (ICW) paints a concerning picture - the number of corruption cases has steadily risen from 444 in 2020 to 533 in 2021 and 579 in 2022. Correspondingly, the number of suspects has surged from 857 in 2020 to 1,173 in 2021 and 1,396 in 2022. The financial impact on the state's coffers has been equally staggering, with losses skyrocketing from Rp 18,615 billion in 2020 to Rp 29,438 billion in 2021 and a staggering Rp 47,747 billion in 2022 (Anandya & Easter, 2023).

Village funds are a source of village development (Purba et al., 2022), contained in the Village Revenue and Expenditure Budget (Ginting et al., 2024). The findings from the Corruption Mapping by sector indicate that the village fund sector ranks among the highest in terms of corruption prevalence when compared to other sectors. Poor governance and failure to prevent and detect fraud are the main problems in the internal control of village funds (Putri et al., 2024). The management of village funds in Indonesia has not been immune to corruption, prompting the government to explore alternative approaches (Kasim et al., 2023). Corruption prevention is undertaken through

a multifaceted approach, which encompasses conducting investigations, prosecuting offenders, and ensuring the execution of court decisions, as well as forming government safeguarding teams and providing supervisory oversight (Rahman et al., 2024). Corruption of village funds is caused by the weak supervisory function of the authorized body as a result of complex power dynamics (Sugiharti et al., 2021). The results of the mapping conducted by Indonesia Corruption Watch (ICW) over the last three years are presented in the table below.

Table 1 Corruption Mapping By Sector (Village Fund Sector)

Year	Number of cases	Rank of Corruption
2020	129	Rank 1 from 10 sectors
2021	154	Rank 1 from 40 sectors
2022	155	Rank 1 from 21 sectors

Source : ICW (2023)

According to the findings of the Anti-Corruption Committee (ACC) of Sulawesi, 11 districts in South Sulawesi were identified as the locations with the highest prevalence of corruption involving village financial funds throughout the year 2022. Particularly, Gowa Regency was reported to have the highest number of corruption cases, with 6 (six) such incidents documented during the period under review.

Corruption is one of the primary fraud schemes, with the two other prevalent types being asset misappropriation and financial statement fraud. Corruption is a form of fraud that requires strong internal control and oversight to detect and address this problem (Kassem, 2024). Corruption and fraud are significant problems that threaten an organization's finances (Amponsah et al., 2022). Fraud, corruption, and governance inefficiencies are widespread in developing countries (Said et al., 2020). Fraud, defined as an intentional act of deception carried out by one or more individuals generally for financial gain, has become a subject of significant discourse and public attention. Decision support systems help detect companies that are potentially involved in fraud cases (Velasco et al., 2021).

It is an inherent component of criminal behavior and carries consequences not only for the perpetrator but also for other uninvolved employees or family members. Criminal sanctions are still imposed on corruption perpetrators, even though there is an order to terminate the investigation due to the lack of strong evidence (Poernomo et al., 2024). Financial sanctions are imposed on corrupt perpetrators with the aim of creating a deterrent effect (Amrani et al., 2023).

Indonesia's anti-corruption laws are unclear and incomplete in regulating the accountability of transnational corruption perpetrators, which poses obstacles in prosecuting foreign corporations. In contrast, the US International Corrupt Practices Act (FCPA) has criminalized foreign corporations either as a holding company or branch that has a working relationship with the corporation or someone involved in corruption in their country, allowing law enforcers and courts to prosecute their accountability and decide on their conviction. The article concludes that in amending Indonesia's anti-corruption law, it is necessary to criminalize corporate subjects that are holding companies or associated with them abroad, which are involved in corruption detrimental to state finances and the private sector. Fraud activities have an impact, directly and indirectly, on the company's revenue and reputation (Yaqoub et al., 2023). The individual-level impact of fraudulent actions includes the loss of trust and reputational damage, while the organizational-level impact manifests as financial losses, asset depletion, and investor distrust (Alfarago et al., 2023). Given the multifaceted impact of fraud on both individuals and organizations, it is essential to analyze the factors that motivate individuals to engage in such illicit activities.

There are four factors propelling people to commit fraud: pressure, opportunity, rationalization and capability. Previous study reveals that implementing the government's internal control system and regional management information systems, with the spiritual quotient (SQ) as a moderating factor, can prevent fraud in Indonesian local governments and confirm fraud diamond theory (Abdullah et al., 2023). Financial statement fraud affects the reliability of financial statements and increases stakeholder decision-making risks (Yarana, 2023). Opportunity gives access to fraud, pressure and rationalization attract people commit the act of fraud, but the person must have the capability to comprehend the opportunity and abuse it for fraud (Wolfe & Hermanson, 2004). The existence of fraudulent activities can be assessed through various fraud models, including the fraud triangle, fraud diamond, and ABC model, which highlight the importance of

factors such as pressure, opportunity, rationalization, and integrity in understanding why people commit fraud (Saluja et al., 2022).

Apart from the fraud diamond aspect which encourages people to commit fraud, individual morality may also result in the fraud to occur. Moral development can influence individual's ethical behaviors (Shahzad et al., 2023). At the pre-conventional stage individuals undertake an action due to be afraid of existing laws/regulations. On the conventional stage they will base their actions on the approval of friends and family and also on the norms applied in society. On the post-conventional stage individuals base their actions by taking into account the interests of others and on universal laws.

Information asymmetry and organizational commitment significantly increase the accounting fraud, while individual morality significantly reduces the accounting fraud. Information asymmetry between parties in an agency relationship can lead to earnings management practices and fraud (Flayyih & Khiari, 2023). The low morale encourages the fraud activity that ultimately damage and even destroy an organization (Houdek, 2020). This study aims to examine and analyze the effect of fraud diamond aspects (pressure, opportunity, rationalization and capability) and individual morality on village fund management fraud.

Village Fun Fraud

Implementation of Law Number 6 of 2014 concerning Villages has given villages the authority and freedom to manage their government and finances independently. Villages are given adequate authority and financial resources to be able to manage their potential to bolster village development. To realize the village development, Government has allocated a fairly large village fund for village development. However, many village government officials abuse the village funds.

Fraud is an act of deception performed intentionally by one or more individuals, generally for financial gain. It is a dishonest act or deviation that is carried out intentionally with the aim of taking money (assets or other resources of an organization/company) through deception or cheating which results in losses for the organization/other people and/or benefits the perpetrator. Association of Certified Fraud Examiners/ACFE (2022) categorizes three types of fraud; (a) financial statement fraud (b) corruption (c) asset misappropriation. Local government financial statements play a crucial role in conveying accountability to the people, and an audit of these statements by an independent auditor serves as a mechanism to ensure the credibility and legitimacy of government financial management (Mainingrum et al., 2023). The financial statement of village government institutions plays a crucial role in ensuring accountability. But the current practice, accountability mechanism is imperfect, particularly in terms of reporting and disclosure, making it difficult for the public to access information (Nurul Fauzi et al., 2023). The misappropriation mode generally carried out by village government officials on village funds which generally occurs, including: (a) using the village funds for personal interests, (b) diverting funds to other programs, (c) including new activities previously unplanned, (d) manipulating reports on the use of village funds, (f) village fund is used to cover PBB deposits, (g) village fund allocation discomplying with provisions, (h) village heads did not allocate funds for community activities that should be financed by village funds.

Fraud diamond

Along with the world development, the cause of fraud to occur is also undergoing development. Wolfe & Hermanson (2004) developed fraud diamond model from Donald R. Cressey's model, namely the fraud triangle. Their research incorporated the three constituent elements of the fraud triangle, and additionally, they introduced a fourth factor, specifically the capability (or capacity) factor. According to this framework, opportunity provides the means for fraudulent activities to occur, while pressure and incentives, as well as rationalization, serve as attractants that motivate individuals to engage in fraudulent behavior. However, it is also essential to recognize that individuals must possess the capability to recognize and capitalize on these opportunities in order to successfully execute fraudulent acts. Fraud cannot be committed if the potential perpetrators have no skills or capability to do it (Maulidi, 2020). Many frauds in a large amount were undertaken without the right people and the right skills (Shonhadji & Maulidi, 2021).

Fraud diamond discusses four causes of fraud, namely pressure, opportunities, rationalization and the capabilities of the perpetrators. The fraud diamond model is depicted by the following figure.

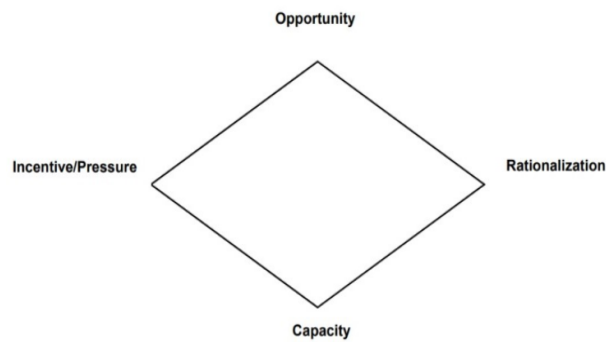


Figure 1 *Fraud Diamond*

Pressure

Every perpetrator of fraud always undergoes pressure which some may involves financial needs, although there are also non-financial pressures in form of frustration with work which can motivate the fraud to occur. Pressure always leads to unethical behavior and every fraud perpetrator encounters several types of pressure to carry out unethical behavior. That pressure to commit fraud can be divided into personal pressure, work pressure, external pressure, and each of these pressures is due to financial and non-financial factors.

H1: Pressure has a significant positive effect on village fund fraud

Opportunity

Individual does not only decide to commit fraud but choose when and where the fraud will be committed. They always try to avoid the possibility to be caught. Perpetrators take the opportunity to commit fraud if the fraud they commit has a small risk of being detected. Opportunities become attractive to perpetrators if there is little possibility of being caught. This opportunity occurs when internal control conditions are weak. AICPA – SAS 99 (2021) stated the opportunities the fraudulent acts be committed in company; (a) Certain characteristics or conditions that can increase vulnerability to fraud, (b) ineffective management, (c) complex and unstable organizational structure, and (d) inadequate internal control that can increase vulnerability to fraud.

H2: Opportunity has a significant positive effect on village fund fraud

Rationalization

The conditions when fraud occurs is that those involved in a fraud activity can rationalize their fraudulent actions. Rationalization is an important factor in fraud occurrence in which the Perpetrators seek justification for his behavior. Rationalization encourages people to commit fraud because they are under stress so that they consider the action is natural or just an ordinary action (Achmad et al. 2022). AICPA – SAS 99 (2021) explains the characteristics of fraud perpetrators who rationalize their actions; (a) ignoring the need to reduce risk, (b) ignoring internal control, (c) dissatisfaction with the entity, and, (d) tolerance for minor fraud.

H3: Rationalization has a significant positive effect on village fund fraud

Capability

Fraud perpetrator is someone who understands and be able to explore internal control weaknesses and uses position, function or access to gain large profits. Many fraud activities especially on financial reporting in billions of dollars would not have occurred if the perpetrators have no ability to carry it out. There are many cases of fraud in large amounts without the right people and the right abilities. Opportunities open access to fraud, pressure and rationalization pull people towards fraud, but the person must have the ability to understand the opportunities and take advantage of them.

Several important characteristics of fraud perpetrators who have capability to commit fraud, namely: (a) position or function in an organization that can provide individuals to create opportunities for fraud that other people do not have, (b) the perpetrators of fraud activity are capable enough to understand and exploit weaknesses in the control system, (c) the perpetrators

are convinced with a high self-confidence that their actions will not be detected, (d) the perpetrator of fraud has persuasive abilities to affect people to commit or hide the fraud they have committed, (e) the fraud perpetrator can convince and successfully lie effectively and consistently to avoid detection from auditors, investors and other parties, (f) the fraud perpetrator can successfully deal with stress well.

H4: Capability has a significant positive effect on village fund fraud

Individual Morality

Moral development theory is used to explain individual morality aspects in influencing fraud behavior. Moral development theory was developed by Kohlberg in 1963. Morals develop through three levels, namely: (a) pre-conventional level; oriented to legal compliance and personal interests, (b) conventional level; individuals will base their actions on approval from friends and family as well as norms applied in society, (c) post-conventional level; Individuals base their actions by paying attention to the interests of others, awareness of the rights of others and the principles of universal justice.

Individual morality is a good attitude and behavior individuals perform without asking for rewards of what they have done possesses. Individual morality is behavior or attitude where individuals undertake something that leads to positive or good things based on sincerity without asking for reciprocation. The higher a person's level of moral reasoning, the greater the possibility of doing the 'right thing'. The higher the individual's moral level, the more the individual tries to avoid unethical behavior and so as not to harm many parties. Low morale encourages acts of fraud and can ultimately damage and even destroy the organization. Morality is an important element that causes fraud. Low morality tends to commit fraud.

H5: Individual morality has a significant negative effect on village fund fraud

Conceptual Framework

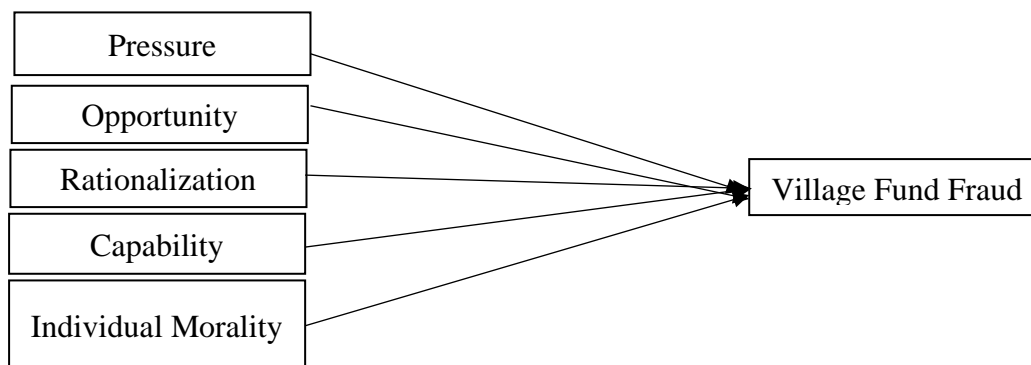


Figure 1 Conceptual Framework

2. Methods

This type of research is survey research, namely describing the past and present beliefs, opinions, attitudes and behavior from a large population by studying the samples drawn from the population and using questionnaires and interviews as data collection methods with the aim of generalizing the sample to the population. The population were all village officials in 8 village governments in Patalasang District, Gowa Regency, South Sulawesi Province. The sampling technique was purposive sampling, with criteria that village officials held positions as village head, village secretary, 3 heads of affairs and 3 heads of sections. Hence, the number of samples and respondents was 64 village officials. This type of qualitative data is quantified by giving a score to each item of the respondent's answer. The primary data sources and data collection techniques use questionnaires. There were 64 questionnaires distributed, but only 52 questionnaires were returned and processed.

The research variables are village fund fraud (Y) measured by using 3 indicators developed by ACFE (2022), the pressure variable (X1) measured by using 2 indicators, opportunity (X2) measured

by using 4 indicators, rationalization (X3) uses 4 indicators, capability (X4) uses 5 indicators and individual morality (X5) uses 3 indicators.

To answer the problem and test the research hypothesis, multiple regression analysis is used with the following regression equation:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \varepsilon$$

Where :

- Y = Village Fund Fraud
- X₁ = Pressure
- X₂ = Opportunity
- X₃ = Rationalization
- X₄ = Capability
- X₅ = Individual Morality
- α = intercept coefficient (constant), namely the value Y if the value of all variables is zero (0)
- β₁₋₈ = Regression Coefficient
- ε = error term (residual) factors affecting auditor performance outside the variables observed

3. Results

To test the effect of pressure, opportunity, rationalization, capability and individual morality on village fund fraud variable, multiple regression analysis was used. The results of the hypothesis test are presented in the table below.

Table 2 Hypothesis Test

Model	coefficient	t-calculation	Prob.	Notes
Constanta (α)	32.451	6.176	.000	-
Pressure (X1)	.639	2.970	.005	Ha ₁ : Accepted
Opportunity (X2)	.321	2.202	.033	Ha ₂ : Accepted
Rationalisation (X3)	.337	-1.470	.028	Ha ₃ : Accepted
Capability (X4)	-.258	-2.166	.036	Ha ₄ : Rejected
Individual Morality (X5)	-.393	-3.523	.001	Ha ₅ : Accepted

a. Dependent Variable: Village Fund Fraud (Y)
 Source: Data processed in 2023 using SPSS 27

4. Discussion

The effect of of pressure on village fund fraud

The results of the data analysis presented in the regression coefficient table (table 2) show that the regression coefficient value for the pressure variable has a positive sign of 0.639 with a probability value of 0.005 which is smaller than 0.05. So the first hypothesis (H1) is accepted. The results of this analysis show that pressure has a significant positive effect on village fund fraud. The higher the pressure felt, the higher the village fund fraud. A person of under pressure to fulfill the life's needs, while the financial condition is not supportive will be motivated to commit fraud. The results of this study are in line with research conducted by Kazimean et al. (2019) that pressure has a significant effect on fraud by asset abuse. Research by Avortri & Agbanyo (2020) also denotes that fraud activity in the Ghanaian banking sector is motivated by pressure to commit fraud.

The effect of opportunity on village fund fraud

The data in table 2 shows that the regression coefficient value for the opportunity variable has a positive sign of 0.321 with a probability value of 0.033 smaller than 0.05. So, the second hypothesis (H2) is accepted. It means that opportunity has a significant positive effect on village fund fraud. The greater the opportunity, the greater the increase in village fund fraud. Crimes in form of misappropriation of village funds are not only caused by the intention to carry out such actions, but can also be caused by opportunities to commit fraud. The more access opened corruption, the more opportunities to carry out village funds fraud. The results of this research support research conducted by Kazimean et al. (2019) that opportunity has a significant effect on asset abuse fraud. Research by Avortri & Agbanyo (2020) also shows that fraud activity in the Ghanaian banking sector is motivated by the opportunity to commit fraud.

Crimes in the form of misappropriation of village funds are not only due to intention, but can be caused by opportunities or opportunities that make them commit fraud. The more gaps that open holes for corruption, the more opportunities there are for misappropriation of village funds. The results of this research support research conducted by Kazimean et al. (2019) shows that opportunity has a significant effect on asset misappropriation fraud. And research by Avortri & Agbanyo (2020) shows that fraud activity in the Ghanaian banking sector is motivated by the opportunity to commit fraud.

The effect of rationalization on village fund fraud

The regression coefficient for the rationalization variable has a positive sign of 0.337 with a probability value of 0.028 smaller than 0.05. So, the third hypothesis (H3) is accepted. The results of this analysis show that rationalization has a significant positive effect on village fund fraud. The higher the fraud perpetrators justify their actions; the more village fund fraud will increase. Fraudsters try to find excuses when committing fraud, so that they feel calm and not afraid when committing fraud. Rationalization is the cause of why organizations fail to address other negative behaviors (Shepherd & Button, 2019). Rationalization in fraud involves a complex cognitive process that enables individuals to justify their fraudulent behavior (Yang & Chen, 2023). Rationalization in fraud involves not only individual self-justification, but also the collective elaboration of rationalizations among insiders and their associates to legitimize and conceal fraudulent activities (Ilieva, 2024). Rationalization in fraud can be measured using a valid and reliable tool, is a crucial aspect of understanding and preventing fraud in this industry (Waters & Wright, 2024).

The effect of capability on village fund fraud

The results of calculating the regression coefficient of the effect of capabilities on village fund fraud show that the coefficient value is negative at 0.258 with the significant probability value is 0.036, which is smaller than 0.05. So the fourth hypothesis (H4) is rejected. Therefore, the results of the analysis show that capability has a significant negative effect on village fund fraud. The higher the capability of the fraud perpetrator, the lower the village fund fraud will be. A person with high knowledge, skills and good attitude will raise awareness to perform his best to improve his performance, and not take actions harmful for the organization. Capabilities, as a component of the fraud triangle, play a significant role in enabling individual to engage in rule-breaking behavior (Arend, 2024). The results of this study also confirm previous research that enhanced information and communication technology (ICT) capabilities can significantly reduce supply chain fraud within small and medium-sized enterprises (SMEs) in Ghana (Abdul Mumin et al., 2024).

The Effect of individual morality on village fund fraud

The regression coefficient of the effect of individual morality on village fund fraud has a negative sign of 0.393 with a significant probability value of 0.001 which is smaller than 0.05. This analysis shows that individual morality has a significant negative effect on village fund fraud. The better the morale of village officials, the lower the village fund budget. Moral is a factor greatly affecting village fund fraud when compared to the other four factors. This can be seen from the results of statistical analysis showing that individual morality has a more significant effect (probability value 0.001) compared to pressure (0.005), opportunity (0.033), rationalization (0.028) and morality (0.033). It depicts that when a person has good morals, his greed will be directed towards positive things, not committing fraud. He will not commit fraud even if there is an opportunity to do so, realizing that fraud is a bad act that can harm himself, his family, and other people

5. Conclusion

This study provides compelling evidence that pressure, opportunity, and rationalization are significant predictors of village fund fraud, while capability and individual morality have a negative impact on fraudulent behavior. Morality is the most dominant factor influencing village fund fraud. These findings have important implications for the prevention and detection of fraud in village fund management, highlighting the need for effective measures to mitigate pressure and opportunity, and to promote a culture of ethical behavior and moral responsibility. By understanding the complex interplay of factors that contribute to fraud, village officials and policymakers can take targeted steps to reduce the incidence of fraud and promote transparency and accountability in village fund management. Ultimately, this research underscores the importance of a multifaceted approach to fraud prevention, one that addresses the root causes of fraudulent behavior and

promotes a culture of integrity and ethical conduct. The research is only limited to data was collected only in one sub-district area and the fraud model developed was only a fraud diamond. Therefore, it is recommended for future researchers to explore these other factors for further research. These other factors include aspects of the pentagon and hexagon fraud models.

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