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## PREVENTION OF ACCOUNTING FRAUD THROUGH INTERNAL CONTROL SYSTEMS: A LITERATURE REVIEW

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### ABSTRACT

This study analyses articles or journals related to internal control's role in preventing accounting fraud. Accountant transparency is a very important aspect in the world of accounting. The method used in this research is a narrative literature review method from several previous studies related to internal control and accounting fraud. The sources used were 13 articles found through Google Scholar using certain keywords. The findings from this study indicate that internal control has a very significant role in preventing accounting fraud practices in various organizational sectors. Implementation of internal control is carried out through the application of adequate authority, responsibility, and supervision.

**Keywords:** Internal Control, Accounting Fraud, Literature Review

### INTRODUCTION

Accountant Transparency is a very important aspect in the world of accounting. In the era of globalization, where technological developments are rapid, the need for honest, reliable, and transparent information is becoming increasingly important. Accountants play a very important role in providing information regarding financial reports that are accurate and usable to stakeholders such as investors, creditors, and the government in a trusted manner. With accountant transparency, decision-makers can understand the financial performance of an entity well and take appropriate steps based on available information. Therefore, the practice of transparency of information provided to the public about company performance and financial reports is very important and will have a positive impact on the organization, principals (stakeholders) (Sagala, 2020)

Accounting fraud is a form of fraud on financial statements that someone intentionally carries out to seek profit for himself and harm other parties (Thorik, 2022). Accounting fraud in financial statements will result in information created and presented as unreliable, with invalid content, and not following the provisions for writing financial reports. Accounting fraud can be found through audits, so auditor independence is needed to support audit quality, as expected. According to (Ardhani et al., 2019), when the auditor upholds high independence, the results of the audit that has been carried out will be in line with the high independence of the auditor. In addition, the audit committee also supports how the quality of financial reports are produced; when the Audit Committee fulfills its role and carries out its authority and responsibilities actively and well, it will produce good and quality financial reports as well (Lestari & Oktaviana, 2020). Good auditor quality will affect the quality of the company, one of which is Corporate Social Responsibility. According to (Handayati et al., 2022), the existence of a qualified auditor will improve the CSR quality disclosure of the company.

Fraud can occur due to many things, such as pressure to achieve high financial targets or investor expectations, which can later encourage an individual or organization to commit accounting fraud (Hidayati et al., 2022). Nevertheless, accounting fraud is generally done because of an opportunity. When there is a lack of oversight and internal control within an organization, there are very large opportunities for individuals to commit accounting fraud.

Preventing fraudulent acts should be the initial effort to minimize the emergence of accounting fraud. The search for fraudulent acts usually arises after the prevention of

financial fraud has failed to achieve its objectives. Prevention of fraudulent acts in accounting is necessary to prevent losses that can even lead to bankruptcy caused by fraud (Primadhany & Puspaningsih, 2018). The application of SPI within an organization will assist companies in maintaining company assets and examining the accuracy and reliability of accounting information. The purpose of SPI itself is that the company can carry out all its activities so that it is following the company's goals.

## LITERATURE REVIEW

### Internal Control

According to Government Regulation No. 60 of 2008, Internal Control is "an integral process of actions in activities carried out continuously by leaders and all employees to provide adequate assurance regarding the achievement of organisational objectives through effective and efficient activities, reliable financial reporting, safeguarding state assets, and compliance with laws and regulations." Meanwhile, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) defines internal control as "a process carried out by the board of directors, management, and individuals within the organisation to provide adequate assurance regarding the achievement of objectives related to operational effectiveness and efficiency, reliable financial reporting, and compliance with applicable laws and regulations."

In general, the objectives of internal control are to ensure that an organisation achieves its established goals effectively and efficiently. According to Mulyadi (2016), the objectives of the internal control system are as follows: It safeguards the organisation's assets from theft, misuse, or damage due to accidents. It is checking the accuracy and reliability of accounting data to serve as a basis for decision-making. It is preventing unnecessary actions and waste in business activities to promote efficiency. Encouraging compliance with management policies.

### Accounting Fraud

According to Hall (2010), fraud is a deliberate misrepresentation of information or deception involving false reporting of company assets or manipulation of financial data to benefit those manipulating the information. Fraud can also be defined as the intentional presentation of false material facts that are believed and acted upon by the victim, resulting in harm to the victim.

According to the American Institute of Certified Public Accountants (AICPA), accounting fraud is an intentional act to manipulate financial data, evade tax payments, or provide false information to obtain personal gain or benefit others. Meanwhile, according to Mardiasmo (2018), accounting fraud is intentional actions that violate accounting principles and policies to influence financial information, making financial reports appear favourable or evading taxes unlawfully.

From the above definitions, it can be understood that the definitions of fraud and accounting fraud are broad and can be categorised into several types. According to the Financial Supervisory Agency (2022), elements of fraud include 1) misrepresentation; 2) material facts; 3) intention or recklessness; 4) with purpose; 5) the misrepresentation harms someone; 6) causing losses; 7) benefiting the perpetrator or other parties associated with the perpetrator.

## METHODS

This research uses the narrative literature review method from several previous studies related to internal control and accounting fraud. This method aims to review and summarise previously published articles, avoid duplication of research, and look for gaps in the sources obtained (Baumeister & Leary, 1997). The research begins with determining the topic, searching journal literature, selecting literature, and processing data to conclude.

Furthermore, article collection was carried out by manual search through Google Scholar. The selection of keywords to look for in the article submission process included: "fraud", "internal control system", and "accounting fraud". This study uses Indonesian-language articles published in the last five years (2018-2023). The number of initial articles found was 54, then filtered for title and relevance of the abstract to a total of 34, filtered again according to the results and discussion to 12 articles.

**Table 1.** List of articles used in the literature review

No	Writer	Title	Year
1	Yanti & Purnamawati	Analysis of Internal Control and Efforts to Prevent Accounting Fraud in the Hospitality Sector	2020
2	Fatimah & Pramudyastuti	Analysis of the Role of Internal Audit in Preventing and Detecting Accounting Fraud Tendencies (Fraud)	2022
3	Khoiriyah & Asyik	The Impact of Locus Of Control On Individual Morality And Internal Control Against Accounting Fraud Tendencies	2019
4	Paranoan et al.	Internal Control Effectiveness, Job Satisfaction and Accounting Fraud Tendencies	2018
5	Azmi et al.	Factors Affecting the Tendency of Accounting Fraud at Pekanbaru City Hospital	2021
6	Aswad et al.	Factors Influencing Trends Accounting Fraud With Control Effectiveness Internal As Moderating Variable (Study on Private Oil Palm Plantation Companies in Riau Province)	2018
7	Fernando & Sitorus	Internal Audit, Quality Control, Asymmetry Information, Dysfunctional Behavior of Accounting Staff and Its Impact on Accounting Fraud	2020
8	Cendani	The Influence of Individual Morality And Control Internal Against Fraud Tendencies Accounting at Bappeda Makassar City (Case Study of SKPD Makassar City)	2020
9	Muna & Haris	The Effect of Internal Control and Information Asymmetry on the Tendency of Accounting Fraud	2018
10	Dasuki & Yudawati	The Influence of Internal Control, Appropriateness of Compensation, and Compliance with Accounting Rules on Accounting Fraud Tendencies (Study on SKPD Majalengka Regency)	2022
11	Yuliani	Influence of Unethical Behavior, Internal Control and Organizational Culture Against the Tendency of Accounting Fraud	2018
12	Gustina	The Influence of Internal Control Systems and Compliance with Accounting Rules Against the Tendency of Accounting Fraud at SKPD Indragiri Hulu Regency	2018

Source: Author Analysis, 2023

## RESULTS

### **Relationship of Internal Control to Accounting Fraud**

Internal control is a process carried out by the principals of an organisation, including the board of directors, management and other individuals, to ensure the achievement of various important objectives, such as reliability in the preparation of financial reports, compliance with applicable laws, and achieving a level of operational effectiveness and efficiency that is optimal. This process is designed and structured to assure users of the organisation's success in achieving those goals.

The results of a review of 12 articles which are a source of literature in this study where these articles examine various accounting sectors, from the private sector to the public sector, show that the Internal Control System has a relationship with the potential for accounting fraud. This means that the better the quality of an entity's Internal Control System, the less fraud can occur. According to (Cendani, 2020), someone who has no internal control is more likely to commit accounting fraud than someone who gets an element of internal control and obeys it. Where the better the quality of internal control in an organisation, the lower the possibility for someone to commit accounting fraud. That is, with high internal control carried out by an organisation on the individuals in it, it will minimise the tendency of accounting fraud in terms of things done by the organisation. On the other hand, if a company has poor internal control quality, the possibility of accounting fraud will be higher.

### **Prevention of Public Sector Accounting Fraud**

Prevention is the first step that an organisation must take to minimise the occurrence of accounting fraud. Fraud is different from error and must be distinguished. Errors can be defined as "Unintentional Mistakes" or unintentional errors. Unintentional mistakes or unintentional errors in accounting can be caused by individual negligence or human error in preparing financial statements not accompanied by an intention to make mistakes. Fraud can occur because individuals have the opportunity to commit fraud or intentional mistakes. However, these frauds can be prevented or controlled by the organisation by applying the rules that apply and are implemented into effective internal controls.

An important element of internal control activities that can minimise fraud is the application of authority and responsibility. Implementing these elements no one can authorise, and only certain individuals can do it. Oversight of internal control also plays an important role in preventing and detecting accounting fraud. Effective controls will help an organisation prevent fraud by ensuring consistent segregation of duties, authorisation of transactions, and monitoring. Good oversight can also create a sense of trust with external stakeholders such as investors or creditors by ensuring that the financial information compiled is accurate, complete and reliable.

Strong factors affecting internal control consist of several basic components. The first factor is a sense of responsibility from the management of an organisation that creates precise control with stakeholders who have integrity. A sense of responsibility from the management of an organisation is a key factor affecting control. Internal. When management is aware of the importance of internal control and feels responsible for implementing it, they will create clear and effective controls. Integrity is an important characteristic that must be possessed by stakeholders in an organisation. High-integrity leaders will promote a culture based on moral, ethical, and compliance principles. They will set a good example and demonstrate their commitment to good internal control practices. Responsible management will design and implement appropriate policies and procedures to ensure effective internal control. They will set clear goals, allocate adequate resources, and ensure that responsibility and authority are properly distributed in the organisation.

Second, organisations can identify the risks and solutions to overcome risks in the business. Organisations that are effective in internal control can identify risks that might affect their business. Risk identification involves recognising and understanding potential

threats or events that may interfere with achieving organisational goals or cause harm. Risk identification usually involves thoroughly analysing the organisation's internal and external environment. Factors such as regulatory changes, technological developments, market competition, and financial and operational risks are evaluated systematically. Organisations may also conduct stakeholder interviews, conduct surveys or market studies, Third, the organisation has good communication and information skills in conveying relevant information to related internal and external parties. Good communication and information skills are vital to an organisation's internal control. Organisations that are effective in internal control must be able to convey relevant information to relevant internal and external parties.

Fourth, the organisation can monitor activities regularly to ensure that the controls that have been implemented are running as they should (Hidayati et al., 2022). The organisation shall have mechanisms designed to monitor the implementation of day-to-day activities. This involves regular monitoring of relevant business processes, transactions and operational activities. Organisations need to conduct periodic evaluations to assess the effectiveness of the controls that have been implemented. This can be done through an internal audit process or systematic testing of compliance with policies and procedures. By monitoring activities regularly, organisations can identify and address problems as they arise immediately, prevent the spread of risks, and ensure the effectiveness of internal controls. Consistent monitoring and continuous evaluation help organisations improve performance and achieve set goals.

### **DISCUSSION**

The Internal Control System has many factors, including a healthy control environment. This can create a corporate culture that upholds integrity, ethics and transparency. With a healthy control environment in an organisation, individuals within it tend to comply with established policies and procedures and report any indications of fraud they encounter. In other matters, establishing clear and firm policies and Standard Operating Procedure is also important in preventing accounting fraud. These policies and procedures must include segregation of duties, determination of authority and responsibility, verification that certain individuals can only carry out, and intense monitoring and evaluation. To prevent accounting fraud, attention to effective supervision and control is important. The group in charge of internal control needs to be active in ensuring the implementation and success of internal control.

### **CONCLUSION**

Based on the research results obtained, it can be concluded that the implementation of internal controls that have been going well in an organisation has a positive effect on how effective the prevention of accounting fraud is. However, on the contrary, if the implementation of these controls is less effective, then what will happen is a high tendency of accounting fraud within the organisation. The application of authority, awareness of responsibility, and supervision are important elements in internal control in minimising the occurrence of accounting fraud tendencies, and these elements can produce good internal control. The five basic components can help improve internal control in preventing and minimising accounting fraud. With these components, internal control can be more effective.

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