

Application of Internal Control in Reducing Accounting Chance

Aldila Dinanti Lina Rifda Naufalin Pretisila Kartika Putri

Faculty of Economics and Business, Jenderal Soedirman University, Purwokerto, Indonesia 53122

* E-mail of the corresponding author: aldiladinanti88@gmail.com

Abstract

This study aims to analyze the effect of internal control on the tendency of accounting fraud conducted on SME Kurnia. This research is a qualitative descriptive research that is paying attention to a fact and perform analysis on the results of observation. Methods of data collection are semi structured interviews, owners and employees as research subjects. The data collected are primary data of interview result and some accounting process notes as well as secondary data in the form of journals and supporting books. The result of the research shows that internal control influences the tendency of accounting fraud. The higher the internal control will be able to reduce the tendency of accounting fraud, and vice versa. Internal controls such as leadership, effectiveness and efficiency of operations, segregation of duties, recording periodically conducted, and supervision.

Keywords: internal control, accounting fraud

1. Introduction

Micro Small and Medium Enterprises (SMEs) is one element that plays an important role in improving the economy of Indonesia therefore the Government gives great attention to the development of MSMEs. One of the main challenges faced by MSMEs is related to the accuracy of internal control. Good internal control is a key factor that can lead to the success or failure of SMEs. Although many other factors that affect UMKM, but problems in MSMEs usually arise due to failure to control their business. Practical methods in internal control of SMEs one of them by applying the accounting well. Thus, accounting makes MSMEs can obtain various financial information that is important in running their business. Financial information that MSMEs can obtain include company performance information, tax calculation information, company's fund position information, owner's capital change information, income and cash disbursement information (Elisabeth, 2012)

Sufficient accounting on MSMEs can meet the requirements in the filing of credit in the form of financial statements, evaluating performance, knowing the financial position and calculate the tax. (Warsono, 2010). Financial problems related to MSMEs are slightly different from large-scale enterprises. In large-scale business generally use accrual method in accounting recording, whereas at UMKM generally use cash-based method which recognize income and expense when cash received or issued.

Cheating in accounting has gained much public attention as the dynamics that center the attention of business people in the world. Even in Indonesia, accounting cheating has become a habit from year to year. Cheating is a deliberate form of fraud that can result in losses. According to Wilopo (2006), in general, accounting fraud is related to corruption. In corruption, the common practice is to manipulate the recording, omission of documents, and mark-ups that are detrimental to the state's finances or economies. Trends indicate an indication of an action that leads to fraud or fraud.

Fraud refers to a misrepresentation of a fact done by a party to another party in order to deceive and make the other party believe in the fact that it is harmful to them. The fraud is generally done with three schemes, namely: (1) fraudulent financial statements, in which assets or revenues are presented higher or lower than actual, (2) corruption, which consists of bribery, extortion, illegal gifts, and conflicts of interest, (3) misappropriation of assets, either company assets in cash or other forms of assets (Hall, 2009).

To handle the problem of accounting fraud, monitoring is required, to obtain a good monitoring result, effective internal control (Wilopo, 2006) is required. Good internal controls allow management to be ready for rapid economic change, competition, shifting customer demand and restructuring for future progress (Ruslan, 2009) in Hermiyetti (2007). If a company's internal control is weak then the likelihood of errors and fraud is greater. Conversely, if the internal control is strong, then the possibility of fraud may be minimized. The effectiveness of internal control has a great influence in preventing the tendency of accounting fraud, with the existence of internal control, the check will happen automatically to one's work by others.

Effective internal controls will help protect the company's assets, ensure reliable financial and managerial

reporting, improve compliance with prevailing rules and regulations, and reduce the risk of losses, irregularities and violations (Susanto, 2008). Internal control is crucial to protecting the entity against human weakness and to reduce the possibility of errors and actions that are inconsistent with the rules (Wilopo, 2006).

Judging from the facts that exist, the researchers will conduct research that aims to find out how internal controls can affect the tendency of accounting cheating on SMEs Kurnia.

2. Literature Review

2.1 Internal control

According to PP. 8 Year 2006 internal control is a process influenced by management created to provide adequate confidence in the achievement of effectiveness, efficiency, compliance with applicable laws and regulations, and reliability of the presentation of financial statements. Meanwhile, according to COSO (1992) in Hermiyetti (2008), internal control is representative of all activities within the organization that must be implemented, where the process undertaken by the board of commissioners is intended to provide reasonable assurance about achieving the objectives of effective and efficient operational control, financial statements, and compliance with applicable law. Strong internal control will be able to reduce the level of the tendency of accounting fraud, if internal control is weak then the tendency of accounting cheating will be large.

Coram et al. (2008) explains that organizations that have an internal audit function will be better able to detect accounting fraud. Hogan et al. (2008) discusses the role of auditors in reducing the opportunity factor in accounting fraud. According Bastian (2006), accounting control is part of the internal control system, including organizational structure, methods, and measures that are coordinated primarily to maintain the wealth of the organization and check the accuracy and reliability of accounting data.

Three internal control objectives according to Mulyadi (2002) are:

1. Reliability of financial information.

Managers are responsible for preparing financial statements for investors, creditors, and other users. Management has a legal and professional responsibility to allow that information to be reasonably prepared.

2. Compliance with applicable laws and regulations.

Control within an organization is intended to encourage effective and efficient use of its resources, including personnel to optimize management objectives.

3. Effectiveness and efficiency of operation

Companies should be able to improve the effectiveness and efficiency of the company's operations, where the operations of the company does not conflict with the provisions of applicable laws and regulations.

Internal controls include five categories that are designed and implemented by management to provide assurance that the objectives of management control will be met, internal control components according to Arens (2008) are:

1. Control Environment

It consists of actions, policies and procedures that reflect the attitudes of top management, directors, and owners of an entity concerning internal control and the importance of components for the entities.

2. Risk Assessment

Identify management and risk analysis relevant to the preparation of financial statements that are in accordance with generally accepted principles.

3. Control Activities

Policies and procedures are made to provide confidence that the instructions made by management are implemented. Control activities include the following:

- a. Performance reviewers are activities that include performance analysis, for example, through comparison of actual results with budget, and past period data.
- b. Task separators include assigning responsibility for authorizing transactions, executing transactions, recording transactions, and maintaining assets to different employees.

- c. Application controls are applied to each SIA application (e.g., order entry and accounts payable)
 - d. General control is general control related to many applications.
4. Information and Communication
- The information system is relevant to the purpose of financial statements covering the accounting system.
5. Monitoring
- The process of quality performance assessment of the internal control structure over time.

Internal control is a representative of the overall activities within the organization that must be implemented to provide reasonable assurance about achieving the objectives of effective and efficient operational control, financial report reliability, and legal compliance (Single 2011: 3). Good internal controls allow management to be ready to face changes and global competition appropriately for future progress.

Internal controls according to AICPA (American Institute of Certified Public Accountants, 2007) are the plan of organization, and all of the coordinate methods and measures adopted within a business, to safe guard its assets, check the reliability of its accounting data, promote operational efficiency, and encourage adherence to prescribed managerial policies.

Internal control by COSO (The Committee of Sponsoring Organizations of the Treadway Commission's) is broadly defined as a process, effected by an entity's board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

1. Effectiveness and efficiency of operations.
2. Reliability of financial reporting.
3. Compliance with applicable laws and regulations.

2.2 Accounting Fraud

Indonesian Institute of Accountants (IAI, 2001), explains the accounting fraud as follows:

1. Misstatements arising from fraud in financial reporting are misstatements or deliberate deletion of amounts or disclosures in financial statements to override reports of users of financial statements.
2. Misstatements arising from undue treatment of assets (often referred to as misuse or embezzlement) relate to the theft of an entity's assets resulting in a financial statement not being presented in accordance with generally accepted accounting principles in Indonesia.

Singleton (2010) defines fraud as a crime, in which fraud is a general term that encompasses a variety of human ingenuity in which one individual takes advantage of another through a false picture. Then, cheating is a mistake, where fraud is a deliberate act in giving a report of the wrong material facts, so someone is wrong in making decisions because they consider the facts to be true. There are two types of crimes, namely:

1. Cheating as a crime. Cheating is a general term that covers the various human shrewdness in which one individual takes advantage of another through the wrong picture.
2. Cheating as a mistake. Fraud is a deliberate act of giving a report of the wrong material facts, so that one is wrong in making decisions because they consider the facts to be true.

Sawyer et al. (2006) mentions cheating is a series of unlawful and illegal acts that are deliberately committed to cheat, cheating committed by individuals or organizations to earn money. The Association of Certified Fraud Examiners (ACFE) groups fraud in three groups:

1. Financial statement fraud (fraud), which is an action performed by an official or executive of a company or government agency to cover the actual financial condition by performing financial engineering in the presentation of its financial statements to gain profit.
2. Misuse of assets (asset misappropriation), ie misappropriation / theft of assets or property of the company or other party. It is the easiest form of fraud to detect because it is measurable / calculated (defined value).
3. Corruption, this type of fraud is the most difficult to detect because it involves cooperation with other parties. This type of fraud is most prevalent in developing countries where law enforcement is weak and lack of awareness of good governance so that the integrity factor is questionable. Forms of

corruption can be misuse of authority / conflict of interest, bribery, illegal gratuities, and economic extortion.

Bologna's fraud perspective (2013) from an accounting and auditing point of view, cheating is a misrepresentation of material facts in the general ledger or financial statements. Wrong statements may be directed to outside parties of the organization such as shareholders or creditors, or to the organization itself by covering or obscuring embezzlement, incompetence, improper application of funds or theft or improper use of organizational assets by officers, employees and agents. Fraud may also be directed to the organization by outside parties, for example, salespersons, suppliers, contractors, consultants and customers, by excessive billing, billing, material substitution of lower quality, false statements about the quality and value of purchased goods, or the amount of customer credit.

3. METHODS

The research used descriptive qualitative approach. Qualitative research is a research used to analyze data by way of describing or describing the data that has been collected as it is without intending to make conclusions that apply to the public or generalization (Sugiyono, 2005). Researchers want to know how internal control affects the tendency of accounting fraud. The object of this study is SME Kurnia and the subject of research are owners and employees. Researchers collect data with semi-structured interview techniques, namely finding problems of control and accounting cheating more openly.

The data collected in the form of primary and secondary data. Primary data obtained through semi-structured interviews in the form of summary of interviews and some notes made in the accounting process such as proof of transactions, accounts receivable accounts payable, daily reports and some monthly reports. While the secondary data in the form of previous research journals, supporting books, and other resources needed in making this article.

4. RESULTS

4.1 Profile of SME Kurnia

SME Kurnia is located on Jl Gunung Slamet VIII No.9 Purwosari Indah Housing Purwokerto. SME Kurnia produces its own drinking water packing gallon which is named "SPIRIT" and "GRACE". Drinking water production is sold to various places to eat and shops around Purwokerto and Purbalingga. In addition to selling its drinking water, SME Kurnia also became a distributor of drinking water with other brands in the form of glass, bottle, or gallon packaging. In addition to drinking water, SME Kurnia also sell LPG gas with various sizes of 5.5kg, 12kg, and 50kg are sold to various places. Places to eat, cafes, shops, and hospitals are already many who are customers of SMEs Kurnia.

At first SME Kurnia only run by the owner with the help of 2 employees. Over time, his business is growing and now has 10 employees. All employees have different duties and responsibilities. The employee's duties are set alternately at any time except for the administration and finances held by the owner

4.2 Internal control

The owner uses the rolling method or exchanging roles and assignments every few time with the intention that his employees can do all the work and backup other employees who were not able to work at that time. However there are some disadvantages and advantages in using the Rolling method. advantages that are felt by the owner is when there are conditions where the employee is unable to attend the business activities will continue to run as usual. While the weakness is the employee will be able to see opportunities to commit acts of fraud over time. On the application of rolling method it can be said that the owners apply flexibility in work that has not been poured in the Standard Operational Procedure (SOP) officially.

The flexibility that the owner applies to his employees also applies to himself. This is evidenced by the existence of the dual role of the owner of the owner who doubles as an employee of the finance and marketing department. Less effective splitting of tasks has an impact on less than optimal performance. Owners have full power to organize their employees. But the employee can provide his or her critics and suggestions to the owner about the circumstances in the field, this input can be used by the owner to make better field policy and create new innovations of marketing and service.

In addition to employee control, the control on the accounting side is also fully owned by the owner. This control is due to frequent conflicts of interest between employees when previously the accounting and finance section held by an employee. This is considered ineffective by the owner due to interfere with the performance of the field caused by personal affairs. Then the owner takes full control of the accounting and finance department. The finance department is closely related to the sale because the sales results are the initial data for the finance department. After the employee gives a daily sales recap, the finance section checks the records with the money given. The finance department rarely makes even monthly or even yearly sales recaps as well as simple financial statements due to lack of time. This is caused by the concurrent owner in the sales department.

Based on the results, this study shows that the problems that occur in SMEs Kurnia caused by the lack of effective internal controls that can lead to fraud. The same study conducted by (Komang, 2015) found that the effectiveness of internal controls had a significant negative effect on the tendency of accounting fraud. Thus, the higher the effectiveness level of internal control will be able to decrease the tendency of accounting fraud. The results of this study are consistent with the theory stated by Tuanakotta (2007: 100) in Friskila (2010), from the form of illegal asset fraud (asset misappropriation) or the theft of loot form known from the beginning of human civilization. Effective internal controls will help protect the company's assets, ensure reliable financial and managerial reporting, improve compliance with prevailing rules and regulations, and reduce the risk of losses, irregularities and violations (Susanto, 2008). Internal control is crucial to protecting the entity against human weakness and to reduce the possibility of errors and actions that are inconsistent with the rules (Wilopo, 2006).

5. CONCLUSIONS, LIMITATIONS AND SUGGESTIONS

The results of this study show that internal control affects the tendency of accounting cheating on SMEs Kurnia. Influential internal control elements are management style, effectiveness and efficiency of operation, task separation, periodic recording, and supervision. High internal control will decrease the tendency to commit accounting fraud. The lack of effective internal controls such as the management style of the owner in leading SME Kurnia and the division of employee duties so that no double role needs to be fixed. The absence of periodic recording to supervise SME Kurnia. Effective and efficient internal controls need to be done to prevent the tendency to commit accounting fraud and can improve business performance.

Limitations of the research is only done in one SME, then the results of this study can not be generalized. It is expected that further research can add research objects and reproduce samples so that the results of his research can be generalized.

References

- Adelin, Vani. 2013. Pengaruh Pengendalian Internal, Ketaatan Aturan Akuntansi, dan Perilaku Tidak Etis terhadap Kecenderungan Kecurangan Akuntansi (Studi Empiris pada BUMN di Kota Padang).
- Arens, Alfin A.Randal J Elder dan Mark S.Beasley. 2008. Auditing & Assurance Services An Integral Approach. 14th Edition. Pearson Prentice Hall.
- Ayu, Lestari Komang, dkk. 2015. Pengaruh Pengendalian Internal dan Budaya Etis Organisasi terhadap Kecenderungan Kecurangan (Fraud) pada Koperasi Simpan Pinjam di Kecamatan Buleleng.
- Gusti. 2014. Pengaruh Moralitas Individu dan Pengendalian Internal pada Kecurangan Akuntansi (Studi Eksperimen pada Pemerintah Daerah Provinsi Bali).
- Mulia, M Krishna. 2017. Pengaruh Moralitas Individu dan Pengendalian Internal terhadap Kecurangan (Sebuah Studi Eksperimental).
- Puspasari, Novita dan Eko Suwardi. Pengaruh Moralitas Individu dan Pengendalian Internal Terhadap Kecenderungan Kecurangan Akuntansi: Studi Eksperimen Pada Konteks Pemerintah Daerah.
- Romadhon, dan Elfan. 2017. Pengaruh Sistem Pengendalian Internal, Sistem Kompensasi, Moralitas Individu, dan Asimetri Informasi terhadap Kecenderungan Kecurangan Akuntansi (Studi Empiris pada Koperasi di Kabupaten Wonosobo).
- Thoyibatun, Siti. 2009. Faktor-faktor yang Berpengaruh terhadap Perilaku Tidak Etis dan Kecenderungan Kecurangan Akuntansi serta Akibatnya Terhadap Kinerja Organisasi. Jurnal Ekonomi dan Keuangan ISSN 1411-0393.
- Undang-Undang Republik Indonesia No. 20 Tahun 2008 tentang Usaha Mikro, Kecil, dan Menengah