



## THE ROLE OF INTERNAL CONTROL TO MINIMIZE THE FRAUD CAUSED BY ORGANIZATIONAL JUSTICE

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### Abstract

Many companies often encounter with accounting fraud. The fraud may be performed by either internal or external party. One's motivations to commit fraud are varied; one of them is the sense of fairness. An individual who perceives being treated unfairly tends to undertake actions that are against the organisation's goals. In order to prevent this matter to occur, an effective internal control system is required to minimize the possibility of fraud being committed which will negatively impact the company. This research is intended to discover the influence of organizational justice towards fraud, with internal control as the moderator. 83 respondents will be applied as the sample of this research. The method that will be applied to analyse this data is moderated regression analysis. The result of this research indicates that internal control is influencing the organizational justice towards fraud.

**Keywords:** organizational justice, internal control, fraud

### Introduction

Many companies often encounter with accounting fraud. The fraud may be performed by either internal or external party. According to Dewi (2017), accounting manipulation within the business normally involves company's internal party. The fraud that is committed by the company's internal party is the most difficult fraud to be avoided. The fraud can be committed by either the management or by the company's employees



themselves. If there is a goal's bias amongst the individuals and the company, the fraud is highly likely to occur. The impact of the accounting fraud will lead to the decreation of the management accountability dan will result in the increment of the monitoring cost towards the management as proposed by the shareholder. Sofia (2014) stated that the fraud is intentionally performed to utilize the company's resources for personal interests by manipulating data.

According to Fachrunisa (2015), the one's motivation to commit fraud is relatively varied. One of the theories that explains in regards to one's motivation to commit fraud is the fraud triangle theory which consists of three components namely, pressure, opportunity, dan rationalization (Arens et al, 2008). The pressure perceived by an employee can be from the urgent needs for living, lack of income, unwell-paid, and lack of fairness within the job. The one that has been treated fairly by the company will show loyalty dan well job performance. The assessment towards the fairness within an organisation has an impact on the one's behaviour and reaction (Hwei dan Santosa, 2012). Puspitadewi and Irwandi (2012) explained that if the fairness within the organisation is not well executed, the number of the employees commit the fraud will be increased.

The concept of the organisational fairness consists of three forms of fairness, namely distributional fairness, procedural fairness, and interactional fairness (Bakshi dan Ekta, 2009). In general, the employees will evaluate towards the fairness in three classification conditions as follows, the income obtained from the organisation (distributional fairness), formal policy or achievement process that is allocated (procedural fairness), and the treatment that is taken by the decision maker amongst the personnels within the organisation (organisational fairness). The perception in regards to the distributional, procedural, and interactional fairness can be interrelated with various outcomes of a certain occupation, such as an event execution, a group's behaviour, and work attitude. Organisation fairness is a condition



that leads individuals to have a conviction that they are treated fairly or unfairly by the organisation. The individual that perceives being treated unfairly will emerge a disappointment which leads to undertake actions that against the organisation's goals.

Puspitadewi and Irwandi (2012) stated that when an employee perceives that the fairness in the organization does not meet and there is a stimulus as well as an opportunity to commit fraud, committed fraud is rationally the right thing to perform. To avoid it occurs, internal control is required. According to Committee Sponsoring Organization (COSO), internal control is a process that is influenced by the board of directors, management and other personnels which is formulated to provide assurance in relation to the achievement of the performance target in terms of effectivity and efficiency operational, financial report reliability, and fulfilment of the law provision that can be applied and regulated. An internal control system has a potential to prevent fraud and error through a control on the process of financial and organisational report as well as to ensure the law fulfilment and the validity of the regulations.

Internal control system consists of the policy and proccure that are designed to provide a feasible assurance to the management that the company reaches its goal. COSO stated that there are components interrelated to each other in internal control system which are control environment, risk assessment control activities information dan communication monitoring. The effective internal control can minimize the possibility of fraud that can harm the company. Risk management strategy can be applied to reduce the risk of fraud by creating a strong internal control environment (Hernawan, 2010). Pristiyanti (2012) explained that an organisation which has a low internal control system tends to increase the opportunity of fraud within the organisation. A low internal control system and a low employee's conformity can trigger the fraud.



Based on the discussed background, it can be concluded that the problems of the research are as follows:

- 1) Does the organisation fairness have an effect towards fraud?
- 2) Does internal control system improve the influence of the organisational fairness towards fraud?

The hypothesis proposed in this research are as follows:

H<sub>1</sub>: Organisational fairness affects negatively towards fraud.

H<sub>2</sub>: Internal control system improves the influence of the organisational fairness towards fraud.

## Discussion

The fraud is committed to gain personal interest or to inflict a loss of the other party. Dewi (2016) stated that the fraud can be related to individual factors namely, greed and need. There are two ways to commit fraud which are as follows, the fraud within financial report and the fraud within non-financial report. The fraud within the financial report is based on misstatement, either overstatement or understatement, which is providing asset or revenue overstatements or providing asset or revenue understatements. On the other hand, the fraud within non-financial report is based on non-financial bias statements. The report is created to manipulate the genuine condition.

The misstatement fraud on the financial report can potentially inflict a financial loss for the investors and creditors. The misstatement fraud can be divided into following categories (Herman, 2013):

- a. Timing difference (improper treatment of sales), is the financial report fraud committed by recording the transaction time incorrectly. It can be either too early or too late from the exact transaction time.



- b. Fictitious revenues, is the financial report fraud by creating fictive revenue.
- c. Concealed liabilities and expenses, is the financial report fraud committed by concealing the company's expenses which makes the report is favourable.
- d. Improper disclosure, is the financial report fraud committed by improperly disclosing the report with an attempt to conceal the frauds occurred in the company which makes the report reader unaware towards the genuine condition in the company.
- e. Improper asset valuation, is the financial report fraud committed by disregarding the the accounting principles with an attempt to increase the revenue while reducing expenses or liabilities.

According to (2014) and Udayani (2017), there are three conditions that trigger the one to commit fraud which is known as "fraud triagle", namely:

a. Pressure

Pressure is one of the factors that triggers a person to commit fraud. For example, a pressure due to debt or a pressure to have a higher position in a company. The employees will potentially undertake illegal or unethical actions to obtain better position and escape from pressure.

b. Opportunity

The fraud can be occurred if there is an opportunity in the company, mainly in a company which does not have proper internal control. By having proper internal control, the fraud can be minimalised or even be removed.

c. Rationalization (rasional)

The ones who commit fraud assume that the fraud they did as a normal matter. They claim that they only take a few of the



company's asset or revenue which will not cause a loss to the company.

Organisational justice is the employees' perception in regards to how they are treated fairly by the company compared to what they have performed or they have obtained (Azhariman, 2014). Bakshi and Ekta (2009) explained that organisational fraud consists of distributional fairness, procedural fairness, and interaksional fairness.

a. Distributional Fairness

The the employee will perceives this fairness if the income or benefit is in line with the income or benefit obtained by the other employees. Haryani and Hidayah (2013) stated that one of the fairness definition of distributing rewards is based on merit or equity norm. The employees which performed excellently or productive are given major rewards.

b. Procedural Fairness

The quintessence of the procedural fairness is the attention towards the employees which how the procedure can be well executed (Hwei and Santosa, 2012). Haryani and Hidayah (2013) proclaimed that there are two models that explains procedural fairness, namely self-interest model dan group-value model.

1) Self-Interest Model

This model is based on egocentric principle that is experienced by the employees towards the situation caused by the will to control or to influence the valid procedures in the company. The intention is to obtain maximum results for personal interests.

2) Group-Value Model

This model is based on the uncomfot feeling towards the work environment due to an employee feels that his or her personal interest is under the threat.



### c. Interactional Fairness

Interactional fairness is focus on social sensitivity, such as when the superior treats the employees with respect and dignity (Al-Zu'bi, 2010). This fairness perception is focusing on the stage which the employees are correctly informed in regards to the main company's decision towards the employee incumbency (Cheng et al., 2011). According to Herman (2013), interactional fairness is divided into three aspects as follows:

#### 1) Reward

The better the management treat the employees, the fairer the interaction will be.

#### 2) Neutrality

Neutrality can be obtained if the decision making principles are based on objectivity and have a high-level of validity with the use of fact instead of opinion.

#### 3) Trust

The trust is put to the other people to reach the future expectation.

According to PP. 60 Tahun 2008, the Internal Control System is an integral process of actions and activities undertaken continuously by the leadership and all employees to provide reasonable assurance on the achievement of organizational goals through effective activities, reliability of financial reporting, security of state assets, and compliance with legislation. The way that management uses to streamline internal control activities is to review employee performance, perform information processing, perform physical control, and perform task separation.

This research was conducted by distributing questionnaires to 93 people as permanent employees of PT Bank Pembangunan Daerah (BPD) Bali in Mangupura. This study used multiple linear regression analysis, and before the analysis, first tested the research instrument and the classical assumption test.



Testing of research instrument included test of validity and reliability test to know that the questionnaires used in this research were valid and reliable. Validity test in this research used product moment correlation. Instrument is valid if the correlation coefficient ( $r$ )  $\geq 0,3$  and if ( $r$ )  $< 0,3$  is invalid. The results of validity test showed all items of questionnaire statement in this research is valid. Measurement of reliability in this study used the formula of coefficient Alpha Cronchbach. The instrument is said to be reliable when  $r_i > 0.6$ , not reliable if  $r_i < 0.6$ . Reliability test shows that the instrument used in this research is reliable.

The classical assumption test in this study includes normality test and heterokedastisity test.

**Table 1**  
**The Result of Classic Assumption Test**

Keterangan	Indikator	
Normality Test	Asymp. Sig. (2-tailed)	0,200
Heteroskedasticity Test	Sig. X <sub>1</sub>	0,071
	Sig. X <sub>2</sub>	0,792

The results of the Kolmogorov Smirnov normality test in Table 1 show that the Sig (2-Tailed) value is 0.200. It shows that the value of Sig (2-Tailed)  $0,200 >$  from Level of Significant (0,05), so it can be concluded that the analyzed residual is normally distributed. The result of heteroscedasticity test with Glejser test in Table 1 shows that the residual absolute value or X1 significance value is 0.071 and the significance value of X2 is 0.792. The value of significance of each variable is above the value of  $\alpha$  (0.05), so it can be concluded that the model does not have heteroscedasticity problem. From the results of data analysis in Table 1 it can be concluded that this study has met both types of classical assumption test.



Multiple regression analysis (moderated regression analysis) is an analysis used to determine the effect of organizational justice on fraud moderated by internal control.

Using the SPSS program, the results of the research in Table 2 are obtained.

**Table 2**  
**The Result of Multiple Linear Regression Analysis**  
**Coefficients<sup>a</sup>**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	57.145	16.512		3.461	.001
Organizational Justice	-4.737	2.009	-2.493	-2.358	.021
Internal Control	-.710	.526	-.841	-1.351	.180
Organizational Justice* Internal Control	.143	.064	2.838	2.245	.027

a. Dependent Variable: Fraud

Based on the table 2, The formula of Multiple Linear Regression Analysis as follows:

$$Y = 57,145 - 4,737X_1 - 0,710X_2 + 0,143 X_1X_2 + e$$

The first hypothesis testing was conducted to determine the effect of organizational justice on fraud. The test results in Table 2 show the significance value (Sig.t) coefficient X1 that is organizational justice of 0.021 smaller than  $\alpha = (0.05)$ , with negative regression coefficient. This means that organizational justice negatively affects fraud, so H1 is accepted. Employees who



feel they have received justice from their organizations will tend to avoid cheating, because they have more loyalty to the company. Conversely, employees who think that they get injustice in the organization will tend to be fraudulent in order to obtain justice for them. The results of this study in accordance with the results of research of Setiawan, et al (2015) states that organizational justice has a negative and significant effect on fraud.

The second hypothesis test was conducted to find out the internal control ability in moderating the effect of organizational justice on fraud. The test results in Table 2 show the significance value (Sig.t) coefficient of 0.027 is smaller than  $\alpha = (0.05)$ , meaning that internal control is able to moderate the effect of organizational justice on fraud, so that H2 is accepted. An organization with good internal control will be able to detect fraud within the organization. Cheating can be done by employees within the organization who feel that they are being treated unfairly within the organization. Such perceived injustice will encourage employees to commit fraud. But with good internal control in an organization, the cheating will be able to be detected and can be avoided. The role of organizational justice in reducing fraud will increase as companies have good internal control. Well-managed internal control within an organization will create a fair atmosphere for every layer of employees, so employees feel satisfied and comfortable working, and will not be motivated to commit accounting fraud. Puspitadewi and Irwandi (2012) stated that employee motivation to commit fraud, mostly occurs when there are two impulses, namely the low perceptions of organizational justice perceived, and the opportunity to commit fraud. In addition, in situations where organizational justice perceptions are low will lead to high employee fraud, and if the quality of the company's internal controls is also bad in the situation, employee chances of fraud increase



## CLOSING

### Conclusion

Based on the results of data analysis has been done, it can be submitted conclusion of research results as follows:

- a. Organizational justice negatively affects fraud with a significance value of 0.021. This means that the higher the higher the fairness that employees gain in their organization then cheating will be avoided.
- b. Internal control moderates the effect of organizational justice on fraud with a significance value of 0.027.

### Suggestion

Suggestions that can be submitted for the next research is the next research can use other variables, such as leadership style, employee integrity, individual morality, and others. This research is also expected to give implication for organization to give fair behavior for every employee so that employees intention to do fraud can be avoided. The organization is also expected to have good internal controls in order to avoid the occurrence of fraud that can be done by employees.

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