Risk Management for Mitigation of "Corruption" Fraud Risk: Profiling Techniques

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Abstract

Risk management provides signs for key areas in the company that contain risks. Risk management manages and profiles risk classification so that the company is more responsive in preventing fraud or fraud risk. Corruption is a form of fraud risk that causes the most losses to the state. Corruption that occurs in various private, government and state-owned organizations can be minimized by understanding the risk classification profile and profiling techniques. This study uses a descriptive method with secondary data from the 2016-2020 Association of Certified Fraud Examiner (ACFE) survey report. The author concludes that the fraud prevention process with a risk management approach is one of the strategies in an effort to prevent fraud by using profiling techniques.

Keywords: *Risk Management, Corruption, Profiling*.

A. Introduction

In the Asia Pacific region including Indonesia, the Report to the Nations(2018) issued by the Association of Certified Fraud Examiner (ACFE) shows that there have been cases of corruption with a percentage of 51%. This figure covers various types of acts of corruption, small to the largest scale. The Association of Certified Fraud Examiner (ACFE) investigations show that corruption is the largest fraud case that occurs in the Asia Pacific region. According to Umar (2016), since 1999 corruption has been classified as a crime that has an impact on various aspects of life, thus requiring strong handling and commitment. Corruption can lead to reduced budget allocations for services to the poor in the regions; budget for education services; budget for infrastructure development, budget for health services, as well as budgets related to various community interests (Hadi, 2010).

Every day we will face uncertainty both individually and organizationally. All these uncertainties which we later refer to as risk. Risks that are not managed properly can lead to deviations from normal conditions. A company with good and strong internal control if it is not accompanied by the commitment and integrity of human resources in the company, there is a great chance of being exposed to the risk of fraud. Karyono (2013) states that in every organizational activity there will always be uncertainty that is identical to risk, so management must be responsible for managing risks that have great opportunities to be faced in the future. Risk management in business organizations is an important thing to do.

According to the Association of Certified Fraud Examiners (ACFE) in the Fraud Examiners Manual (2016), fraud is defined as relating to the benefits obtained by someone through bad ways and violating regulations such as deception, dishonesty and harm to other parties. ACFE: Report To the Nations on Occupational Fraud and Abuse (2016), describes the forms of fraud in business organizations in 3 (three) major groups, namely corruption, misappropriation of assets and fraud in financial statements. Corruption can be broken down into: (a) conflicts of interest, namely personal and organizational interests; (b) bribe, namely the act of giving a sum of money, goods or in kind to obtain something; (c) unofficial levies, namely payments outside the official rules or rates; and (d) extortion, which is forcing a person or organization to do something such as paying a sum of money to acquire a project.Misappropriation of assets can consist of (a) misappropriation of cash such as cash theft, unauthorized disbursement of cash, intentional errors in recording cash, while misappropriation of inventories and other assets such as theft of inventories, (b) intentional errors in recording inventories. Fraud in financial statements consists of (a) understatement of assets or income and (b) intentional overstatement of assets or income.

Corruption can occur in several government agencies, private companies or state-owned enterprises. The involvement of companies in corrupt practices and embezzlement of state assets are some examples of fraud that occurs in Indonesia. Several corruption cases in Indonesia are the Century Bank, the Hambalang case, the head of the regional government is involved in corruption such as the Nganjuk Regent, the Kutai Kartanegara Regent and most recently the alleged corruption of the North Penajam Paser Regent in 2021. Strategies and designs are needed for each organization or company to prevent fraud in accordance with the characteristics of each organization. Research by Spira, Laura F., Page, Michael, 2003 concluded that fraud can be mitigated by implementing the framework of organizational governance, risk management, accountability, audit and internal control. The risk management applied by companies in Indonesia is ISO 31000:2009 referring to The Committee of Sponsoring Organizations (COSO). Based on ISO 31000:2009 risk management is presented in more detail, easy to apply, closer to practice and can be applied to all industries, both small and large. Meanwhile, The Committee of Sponsoring Organizations (COSO) approach is more theoretical, complex and more suitable for large organizations.

ISO 31000:2009 explains the benefits of risk management for business organizations, namely: creating a competitive advantage, streamlining decision-making processes, anticipating losses, providing added value to the company, encouraging better organizational governance and helping organizations identify and take advantage of strategic opportunities. Boiral, Olivier (2012) concluded that ISO 31000:2009 on risk management is a standard and can be applied effectively, integrated with practices, experiences and certain goals that the organization wants to achieve. Because for the purpose of mitigating fraud, the design and risk management framework need to be developed, including identifying anti-fraud principles, mapping anti-fraud principles to risk management designs.

The fraud prevention method by profiling is carried out by recognizing and studying the behavior and characteristics of potential fraud perpetrators who are trusted to safeguard assets. Profiling means collecting various pieces of information and data or intelligence related to criminal acts or criminals. The information collected is then formulated into a profile that can be used to model potential fraud perpetrators in the future. This method is part of an effective anti-fraud management program. Profiling is used to fight occupational fraud, behavioral signs to watch out for, motivations and opportunities as indicators of fraud behavior, and to profile individual behavior and characteristics of a fraud perpetrator. Companies can obtain and collect pieces of information, the process of building a fraud profile, and the role of personnel department in the employee recruitment process helps the profiling process. Profiling in the pre-employment stage is aimed at minimizing the possibility of talent with low integrity.

B. Research Methods

This study uses a descriptive method by providing an overview of who the perpetrators of fraud are from a demographic review. The analysis uses data from the Association of Certified Fraud Examiners (ACFE) which produces the Indonesian Fraud Survey (SFI). ACFE Chapter Indonesia compiles the Indonesia Fraud Survey (Indonesian: SFI) based on the guidelines from ACFE Global. SFI is expected to provide awareness to the organization on the occurrence of fraud risk.

C. Results and Discussion

Fraud is a deliberate act by one or more individuals in management or those charged with governance, employees and third parties involving the use of deception to obtain an unfair or unlawful advantage (SA 240, 2013). According to SAS No. 99 financial statement fraud can be carried out as follows: (1). Manipulation, falsification, or alteration of accounting records, supporting documents of the prepared financial statements. (2). Intentional mistake or omission in information that is significant to the financial statements. (3). Deliberately abuse the principles relating to the amount, clarification, manner of presentation, or disclosure.

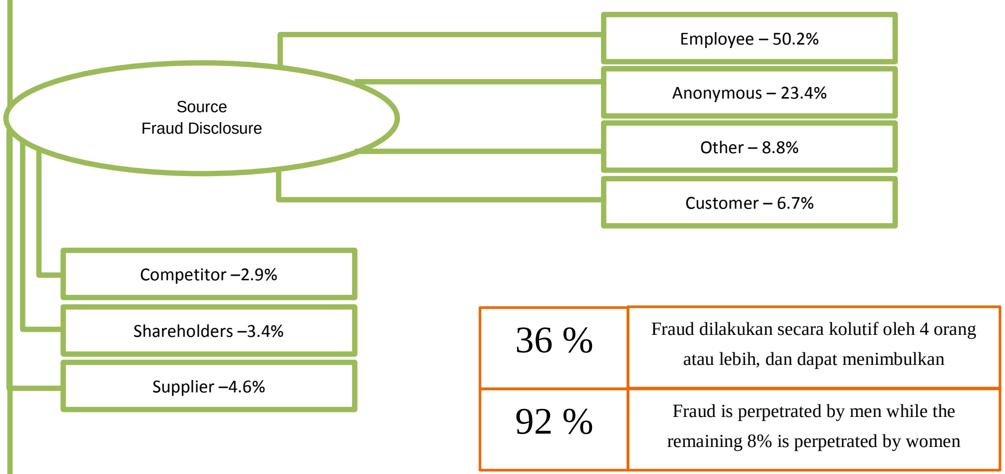
Corrupt behavior (fraud) is basically a sociological phenomenon that has economic and political implications. Robert K. Merton (1967) put forward his theory that corruption is a human behavior caused by social pressure, thus causing a violation of norms. Every social system has a goal and humans try to achieve it through agreed means. Achsin (2010) revealed that investigative audit assignments require the auditor to make extra efforts, namely the auditor must go into the depth of the problem. The hypothetical construction of crime becomes the main radar in searching, finding and collecting evidence to uncover cases of fraud or corruption.

The definition of a criminal act of corruption is based on Article 2 Paragraph (1) of Law Number 31 of 1999 concerning Eradication of Criminal Acts of Corruption in conjunction with Law Number 20 of 2001 concerning Amendments to Law Number 31 of 1999 concerning Eradication of Criminal Acts of Corruption (UU Tipikor) which later underwent another change in the Decision of the Constitutional Court Number 25/PUU-XIV/2016 are:

"Everyone who unlawfully commits an act of enriching himself or another person or a corporation that is detrimental to state finances or the state economy, shall be sentenced to life imprisonment or a minimum imprisonment of 4 (four) years and a maximum of 20 (twenty) years and a fine of at least Rp. 200,000,000.00 (two hundred million rupiah) and a maximum of Rp. 1,000,000,000.00 (one billion rupiah)."

The definition of a criminal act of corruption from Article 2 Paragraph 1 of the Corruption Law, there are 3 (three) elements, namely against the law, to enrich oneself, and loss to the state. These three elements must be interconnected and can be proven to exist. The types of corruption crimes are divided into 7 (seven) groups as referred to in Article 2 to Article 12C of the Anti-Corruption Law, namely: (1) Corruption Crimes that are detrimental to state finances (Article 2 and Article 3); (2) Corruption in the form of bribery (Article 5 paragraph (1) letters a and b, Article 13, Article 5 paragraph (2), Article 12 letters a and b, Article 11, Article 6 paragraph (1) letter a and b, Article 6 paragraph (2), Article 12 letter c and letter d; (3) Corruption crime in the form of embezzlement in office (Article 8, Article 9, Article 10 letter a, letter b and letter c); (4) Corruption in the form of extortion (Article 12 letter e, letter f and letter g); (5) Corruption crime in the form of cheating (Article 7 paragraph (1) letter a, letter b, letter c and letter d, Article 7 paragraph (2), Article 12 letter h; (6) Corruption crime in the form of conflict of interest in procurement (Article 12 letter i); (7) Corruption crime in the form of gratification (Article 12 B in conjunction with Article 12 C). The following is a picture of fraud that occurred in Indonesia during the range of 2020.

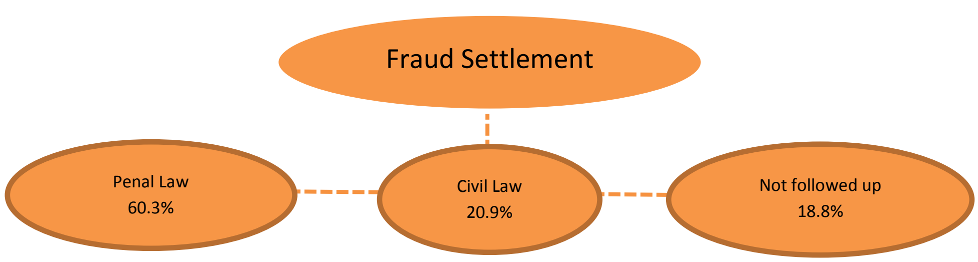
Figure 1: Data processed by ACFE, 2020.



Position of Fraud Perpetrator			
Employee 31.8%	Owner 29.4%	Manager 23.4%	Other 15.1%
The biggest fraud value is committed by the owner with a range between IDR 500 million – more than IDR 10 billion			

Fraud Perpetrators by Working Period
< 1 year = 16 cases 1 -5 years = 54 cases 6 – 10 years = 90 cases Lebih dari 10 years = 82 cases

Punishment VS Prosecution		
Lower than demand 58.2%	According to demands 32.6%	Freed 9.2%



The results of a survey conducted by the ACFE Indonesia Chapter on 239 respondents showed that the most common fraud in Indonesia was corruption with a percentage of 64.4% or chosen by 154 respondents. The next type of fraud is Misuse of State and Company Assets/Wealth with a percentage of 28.9% or chosen by 69 respondents, while Financial Report Fraud is 6.7% or chosen by 16 respondents. The positions of the perpetrators of fraud are 31.8% employees, 29.4 owners, 23.4% managers and 1% others. Fraud is usually carried out in groups of about four (4) people with a percentage of 36%. Fraud perpetrators are 92% male and eight(8)% female. Fraud perpetrators have varying tenures of less than 1 year with 16 cases and the highest is having a tenure of more than ten years (10) with a total of eighty-two cases (82). Then the settlement of fraud cases is in the aspect of criminal law by 60.2% of all cases, civil law by 20.9% and not being followed up by 18.8 %.

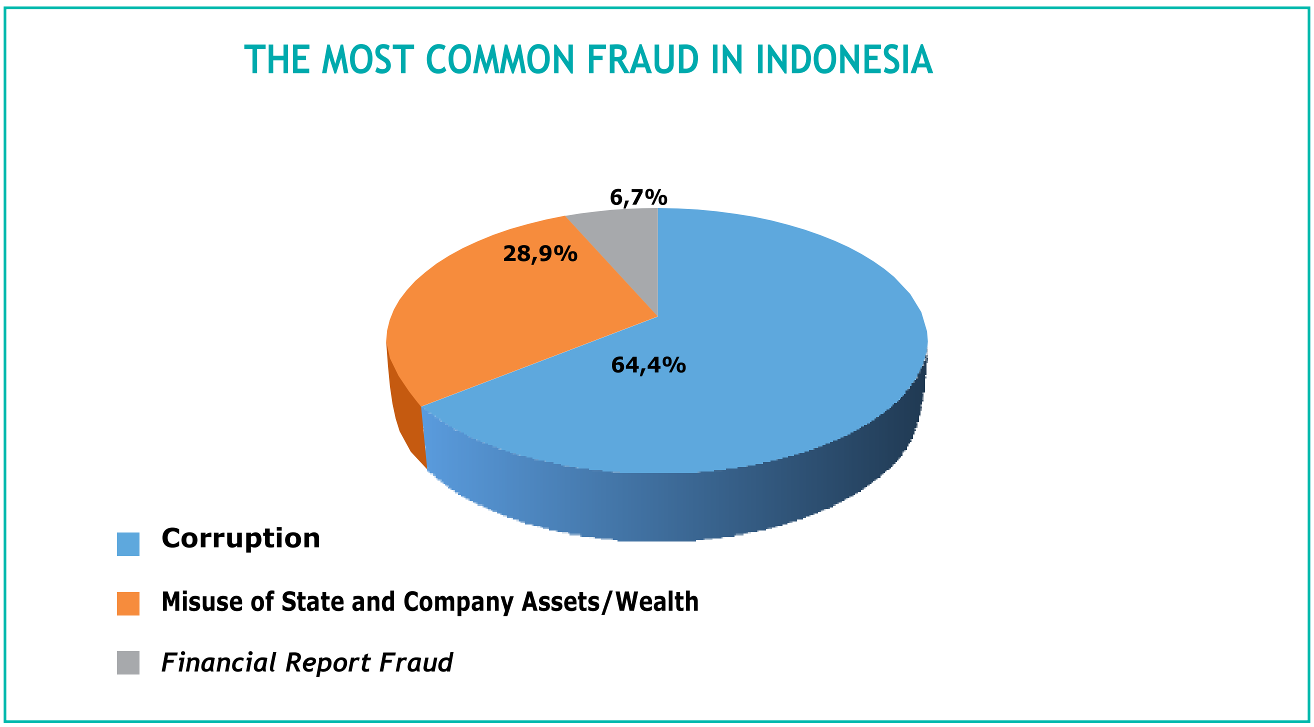


Figure 2: The most common fraud in Indonesia

The results of the ACFE survey show that the most detrimental fraud in Indonesia is corruption. Sequentially as many as 167 respondents or 69.9% stated that corruption is the most detrimental fraud act in Indonesia. The next order as many as 50 respondents or 20.9% stated that the Misuse of State & Company Assets/Wealth caused losses. While the third as many as 22 respondents or 9.2% stated that financial statement fraud caused losses.

The results of this survey show that the largest proportion of fraud perpetrators in Indonesia is 36-45 years old, which is 42%, followed by the 46-55 years age group, which is 32%. This condition indicates that most of the perpetrators of fraud are from the mature and productive age group, which on average have entered the middle manager level and above. Meanwhile, the lowest age group is the age group <26 years and >66 years, each with a percentage of 1%. Fraud in the form of corruption is the most for losses below Rp. 10 million. Fraud in the form of corruption, financial statement fraud and asset misappropriation, the majority of cases are under Rp. 10 million, but the frequency of occurrence with total losses is below Rp. 10 million at most. On the other hand, there are the fewest incidents in corruption cases but the biggest loss is above Rp. 10 billion. The following table presents the value of losses caused by fraud (cheating).

Table 1: Value of Losses due to Fraud

VALUE OF LOSS	Corruption	Fraud Financial statements	Misuse of State and Company Assets/Wealth
Rp. ≤10 Million	48.1%	67.4%	63.6%
Rp.10 Million - 50 Million	4.2%	2.9%	3.3%
Rp.50 Million - 100 Million	8.4%	5.4%	8.8%
Rp.100 Million - 500 Million	11.7%	6.7%	9.6%
Rp.500 Million - 1 Billion	10.9%	6.7%	2.9%
Rp.1 Billion - 5 Billion	5.9%	3.8%	3.8%
Rp.5Billion-10Billion	5.4%	2.1%	3.4%
Rp. >10 Billion	5.4%	5.0%	4.6%

Source: ACFE Data, 2020

The fraud prevention process with a risk management approach is one of the strategies that can be taken as an action to prevent fraud. This approach requires commitment and responsibility from all members of the organization from the top management level to the implementing staff. The fraud risk management framework starts with mapping the potential sources of the fraud originating. Sources of fraud risk can come from (1) audit results issues, namely based on previous audit results which indicated fraud, (2) cases of fraud and violations of regulations that have occurred, and schemes that have the potential to occur in the organization. The next step after mapping the potential sources of fraud is to identify the risks that may occur. The risk identification process is mapped according to the fraud area in the organization and the schemes carried out. The fraud risk identification process will produce a risk register.

The next stage is an assessment of the risks contained in the risk list. The assessment involves aspects of the occurrence and impact of the fraud risk on the organization. Fraud risk assessment formula by multiplying the occurrence and impact to form a score for each risk. These risk scores are then mapped to form a risk map with areas from the lowest to the highest risk. The process of identifying fraud risk and producing this risk map can be accomplished by means of data reviews, focus group discussions (FGD), feedback from the parties concerned or a combination of these procedures. Meanwhile, the involvement of organizational members in the preparation of fraud risk management is comprehensive, participatory and independent.

Fraud risk management framework, starting from mapping the potential sources of fraud originating. These sources can come from (1) audit results issues, namely based on the results of previous audits that indicated fraud, (2) cases of fraud and violations of regulations that have occurred, and potential fraud schemes can be sourced from issues of audit results that have the potential to indicate fraud, cases of fraud or compliance violations that have occurred and the schemes used in fraud cases consist of: (1) fraud by management, namely potential fraud committed by organizational management, (2) fraud by employees, namely potential fraud committed by employees, (3) fraud by parties outside the organization, namely potential fraud committed by parties outside the organization. Hery (2015) states that every member of the organization is a risk owner. So that this area of fraud involves frauds originating from management, employees and parties outside the organization.

Risk management will produce a risk map that describes the potential fraud risk in the organization in areas from very low to very high. Areas with a risk score of 1 – 4 indicate very low risk to low risk. Areas with a risk score of 5 – 9 indicate moderate risk to high risk. Meanwhile, areas with a risk score of 10-25 indicate a very high risk. Mapping this fraud risk serves to determine the priority scale and control aspects that need to be followed up immediately. The most important thing is in a very high area so that it does not have a very large impact on the organization or company.

Profiling the Fraudster as a process to identify the characteristics of a fraud perpetrator (corruption) and when a fraud will occur. Based on this, employee profiling is carried out at the pre-employment stage, employment stage and post-employment stage. Profiling at the pre-employment stage is intended to minimize the possibility of recruiting talent with low commitment and integrity. Steps that can be taken through background check. In order to prevent fraud, the institution must develop anti-fraud awareness, identify vulnerabilities and employee profiling (know your employee). Profiling is important to be applied before an employee is accepted into the company through the process of identifying/recognizing the characteristics of people who have been successful and the characteristics of fraud perpetrators as well as identifying factors that support the success of human resources who do not commit fraudulent acts. The results of the profiling are followed up with the preparation of pre-employee screening procedures. The application of this model is expected to be able to produce human resources with integrity and quality and form a work culture. The profiling process should be carried out in an integrated manner through clear systems and methods related to performance, remuneration and work standards.

D. Conclusion

Corruption cases are a form of fraud or deception that causes the most losses, carried out in groups. Fraud is revealed mostly because of the number of bank accounts owned. Disclosure patterns must be followed and traced from behavior, accounts, to habits.

Disclosure of cases requires disguises in order to know the patterns and the paths leading to evidence of corruption. Investigative activities cannot be carried out instantly and quickly, but require a long time.

The strategy to prevent fraud is a demand for business organizations to protect the sustainability of their business. The fraud prevention process with a risk management approach is one of the strategies that can be taken as an action to prevent fraud. This approach requires commitment and responsibility from all members of the organization from the top management level to the implementing staff. The absence of commitment from the organization will make the implementation of this prevention strategy fail.

Profiling technique is a search for characteristic information from fraud perpetrators in the form of corruption starting from the pre-employment stage, employment stage and post-employment stage. Profiling techniques require examples from leaders or superiors to form a conducive work culture so as to create accountability, transparency of performance appraisals and rewards for employees. This will reduce the motivation of the perpetrators of corruption to commit fraud (corruption).

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