

THE EFFECT OF SHARIA COMPLIANCE, LEVERAGE, AND CORPORATE GOVERNANCE MECHANISMS ON FINANCIAL STATEMENT FRAUD WITH INFORMATION TRANSPARENCY AS A MODERATING VARIABLE

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ABSTRACT

This study examines the influence of Sharia compliance, leverage, and corporate governance mechanisms on financial statement fraud among firms listed in the Jakarta Islamic Index (JII), with information transparency as a moderating variable. The research adopts a quantitative, causal-associative design using 150 firm-year observations from 2020–2024. Sharia compliance and transparency were measured through the Islamic Social Reporting (ISR) Index, while financial statement fraud was detected using the Beneish M-Score model. Data were analyzed using multiple regression and Moderated Regression Analysis (MRA) with SPSS software. The results indicate that Sharia compliance and corporate governance significantly reduce the likelihood of financial statement fraud, whereas leverage shows no significant effect. Transparency does not statistically moderate the relationships among the main variables, suggesting that disclosure quality in Islamic firms remains largely procedural rather than substantive. The findings extend the Fraud Pentagon Theory by integrating ethical and spiritual dimensions within the Islamic financial reporting context. Practically, the study highlights the need for regulators such as the Financial Services Authority (OJK) and the National Sharia Board (DSN-MUI) to strengthen Sharia-based disclosure frameworks and promote ethical governance practices. This research contributes to the literature on Islamic corporate governance by providing empirical evidence that moral and spiritual compliance serve as effective deterrents to fraudulent financial reporting.

Key words: Financial statement fraud; Sharia compliance; Leverage; Corporate governance; Transparency.

INTRODUCTION

Financial statement fraud remains a serious threat to the integrity of the global financial system. The Association of Certified Fraud Examiners (ACFE, 2024) reports that global losses from fraud amount to billions of dollars annually, with a substantial share arising from financial statement manipulation that is often difficult to detect. Such practices not only violate ethical standards but also weaken investor trust, disrupt capital markets, and damage corporate governance credibility.

In Islamic finance, financial statement fraud carries a deeper moral implication. It is regarded not only as a legal violation but also as a breach of the ethical foundations of the Islamic economic system. The Qur'an, particularly Surah Al-Mā'idah verse 2, prohibits cooperation in sinful and unjust acts, underscoring the moral gravity of fraudulent behavior. Nevertheless, a paradox persists: companies listed in the Jakarta Islamic Index (JII), despite meeting Sharia criteria, are not immune to fraud. Prior studies indicate that elements of the Fraud Pentagon Theory—pressure, opportunity, rationalization, capability, and arrogance—remain relevant predictors, while transparency levels among Islamic firms vary significantly and may allow fraud risk to reach considerable levels.

Although previous research has explored fraud determinants using the Fraud Triangle and Fraud Pentagon frameworks, most studies emphasize internal factors such as leverage and governance, with limited attention to the moderating role of transparency and information quality. Empirical findings also differ across countries, suggesting contextual influences. Additionally, Islamic Social Reporting disclosure remains relatively low, indicating that transparency has not yet become deeply embedded in organizational culture. This gap highlights the need to re-examine the Fraud Pentagon within Indonesia's Islamic capital market by integrating Sharia compliance, governance, leverage, and transparency. The present study contributes theoretically by extending the Fraud Pentagon into a value-based financial context and by positioning transparency as a moderating variable to better explain how ethical and accountability mechanisms can reduce financial statement fraud.

METHOD

This study employs a quantitative approach with a causal-associative design. The quantitative approach was chosen because it allows for the measurement of relationships among variables in numerical form, enabling the results to be statistically tested and generalized to a broader population (Creswell & Creswell, 2018). The causal-associative design is used to analyze cause-and-effect relationships between Sharia compliance, leverage, and corporate governance on financial statement fraud, with information transparency and quality serving as moderating variables. Data analysis in this study was conducted using Moderated Regression Analysis (MRA) to examine both direct effects and interaction effects among variables. MRA was chosen because it efficiently

identifies interaction effects in regression models with moderate sample sizes (Aiken & West, 1991). Before forming the interaction terms, all independent and moderating variables were mean-centered to minimize multicollinearity risk. Classical assumption tests (normality, multicollinearity, and heteroscedasticity) were conducted prior to regression to ensure model validity. Data processing was performed with the assistance of SPSS software. This causal-associative design was chosen because it allows the testing of both direct and interaction effects statistically, making it suitable for studies involving moderating variables such as information transparency. Similar approaches have been used in prior fraud-related research (e.g., Shodiq et al., 2025; Rahman Siddiq & Sutopo, 2024). Compared to hierarchical regression or PLS-SEM, MRA was preferred because it directly estimates interaction effects in a single regression model and is more efficient for medium-sized samples (Hair et al., 2022). This approach maintains parsimony while preserving statistical power.

The population of this research includes all companies listed in the Jakarta Islamic Index (JII) during the 2020–2024 period. The total of 150 firm-year observations consists of approximately 30 JII firms observed over a five-year period (2020–2024). The 2020–2024 period was selected because it reflects the post-pandemic adjustment era and the implementation of new Sharia reporting policies. The total of 150 firm-year observations is considered adequate for multivariate and moderation analysis, following the guideline of Hair et al. (2022), which suggests that samples above 100 are sufficient for robust statistical testing. The selection of JII companies was based on the consideration that firms in this index have fulfilled Sharia investment principles, making them relevant subjects for examining Sharia compliance and good governance aspects. The sampling technique applied was purposive sampling, which involves selecting samples based on specific criteria aligned with the research objectives.

This study uses secondary data obtained from the official websites of the Indonesia Stock Exchange (IDX) and the respective companies. The primary data sources include audited financial statements, annual reports, and Islamic Social Reporting (ISR) disclosures. The financial statements were used to measure leverage levels and detect potential fraud using the Beneish M-Score model, while the annual reports were analyzed to assess corporate governance mechanisms. The Beneish M-Score model, originally developed to detect accrual-based earnings manipulation, remains relevant in the context of Sharia-compliant firms because it captures deviations arising from managerial discretion over accruals without violating Sharia accounting standards (Miharsi et al., 2024). Thus, it is an effective early warning indicator for fraudulent reporting even in Islamic financial contexts. Meanwhile, the level of transparency was measured based on the number of ISR disclosure items reported by each company.

Variable	Operational Definition	Measurement/Formula	Number of Items	Reference
Financial Statement Fraud	Likelihood of fraudulent reporting	Beneish M-Score	8 indicators	Beneish (1999)
Sharia Compliance	Level of adherence to Islamic principles	Islamic Social Reporting (ISR) Index	5 categories (environment, zakat, society, employees, halal products)	Putra et al. (2020)
Corporate Governance	Mechanisms ensuring ethical management	Board independence, audit committee, managerial ownership	3 indicators	Mutmmainah & Mahmudah (2024)
Information Transparency	Extent of ISR disclosure in annual reports. transparency refers to both the quality and accessibility of disclosed information, including completeness, comparability, and timeliness.	ISR disclosure ratio. Measured through ISR disclosure ratio complemented with timeliness and cross-company comparability dimensions.	1 composite measure	Shodiq et al. (2025)

All data used in this study were sourced from publicly available, audited financial statements officially published by the Indonesia Stock Exchange (IDX). This study did not involve any personal or confidential data and was conducted in compliance with academic research ethics and integrity standards.

RESULTS AND DISCUSSION

The normality test results show an Asymp. Sig. (2-tailed) value of 0.200, which is higher than the significance level of 0.05. This indicates that the null hypothesis (H_0) is accepted, meaning the residuals are normally distributed. Therefore, the data used in this study meet the normality assumption.

The multicollinearity test results indicate that Sharia Compliance (X1), Leverage (X2), and Corporate Governance (X3) each have tolerance values above 0.10 and VIF values below 10. Specifically, the tolerance values range from 0.923 to 0.930, while the VIF values range from 1.075 to 1.084. Since all variables meet the required criteria (Tolerance > 0.10 and VIF < 10), it can be concluded that there is no multicollinearity issue in this regression model.

The heteroscedasticity test was performed using a scatterplot of ZPRED (standardized predicted values) against SRESID (standardized residuals). The plot shows that the data points are randomly distributed above and below the zero line without forming any clear pattern, such as waves or funnel shapes. This indicates that heteroscedasticity is not present, meaning the residual variance is constant and the model satisfies the homoscedasticity assumption.

The regression equation obtained is:

$$\text{Financial Statement Fraud (Y)} = 9.088 - 1.751X1 + 1.884X2 - 1.450X3 + e.$$

The t-test results show that Sharia Compliance (X1) has a negative and significant effect on financial statement fraud (sig. 0.003 < 0.05), indicating that higher compliance reduces the likelihood of fraud; therefore, H1 is accepted. Leverage (X2) has a significance value of 0.399 (> 0.05), meaning it does not significantly affect financial statement fraud, so H2 is rejected. Meanwhile, Corporate Governance (X3) has a negative and significant effect (sig. 0.014 < 0.05), suggesting that stronger governance lowers fraud risk; thus, H3 is accepted.

Table 1. Uji F (Simultan)

Model	Sum of Squares	df	Mean Square	F	Sig
Regression	196,347	3	65,449	9,871	.000 ^b
Residual	288,801	44	6,564		
Total	485,149	47			

Source: SPSS Output Results (Processed Data, 2025)

Based on Table 1, the calculated F-value is 9.871 with a significance level of 0.000. Since the significance value (0.000) is lower than $\alpha = 0.05$, the null hypothesis (H_0) is rejected simultaneously. This indicates that the variables Sharia Compliance (X1), Leverage (X2), and Corporate Governance (X3) jointly and significantly influence Financial Statement Fraud (Y).

The regression model, which includes Sharia Compliance (X1), Leverage (X2), Corporate Governance (X3), and their interactions with Transparency (M), is statistically significant (F = 7.502; p < 0.001). This indicates that all variables jointly explain variations in Financial Statement Fraud (Y).

The model produces an R^2 value of 0.523 and an Adjusted R^2 of 0.454, meaning that approximately 45–52% of the variation in financial statement fraud can be explained by the variables included in the model. The remaining variation is influenced by other factors not examined in this study.

Table 2. Uji Moderated Regression Analysis (MRA)

Model	Unstandardized Coeffisients		Standardized Coeffisien	t	Sig	Collinearity Statistic	
	B	Std. Error	Beta			Tolerance	VIF
(Constant)	-4.612	4.221		-1.093	0.281		
Kepatuhan Syariah (X1)	47.119	38.274	1.324	1.231	0.225	0.010	99.469
Leverage (X2)	-25.062	15.119	-9.290	-1.658	0.105	0.000	2701.352
Corporate Covernance (X3)	10.294	16.506	0.264	0.624	0.536	0.065	15.414
Kepatuhan Syariah (X1) x Transparansi (M)	-70.415	52.347	-1.360	-1.345	0.186	0.011	87.936
Leverage (X2) x Transparansi (M)	32.380	18.821	9.854	1.720	0.093	0.000	2821.950
Corporate Governance (X3) x Transparansi (M)	-6.868	21.575	-0.198	-0.752	0.752	0.030	33.109

Source: SPSS Output Results (Processed Data, 2025)

Based on table 2, the results indicate that the interaction between Sharia Compliance and Transparency (X1 x M) has a negative coefficient of -70.415, suggesting that transparency may potentially strengthen the

fraud-prevention effect of Sharia compliance. However, with a significance level of $p = 0.186$, which is greater than 0.05, the effect is not statistically significant. This implies that transparency has not been empirically proven to moderate the influence of Sharia compliance on financial statement fraud.

The interaction between Leverage and Transparency ($X_2 \times M$) has a positive coefficient of 32.380 with a significance value of 0.093. Although it does not meet the 0.05 threshold, it approaches the 0.10 level, indicating a weak or marginal moderating effect. This suggests that transparency may slightly influence how leverage relates to financial statement fraud, but the statistical evidence remains limited. In contrast, the interaction between Corporate Governance and Transparency ($X_3 \times M$) shows a negative coefficient of -6.868 with a significance value of 0.752, indicating that transparency does not moderate the relationship between corporate governance and fraud.

Overall, the findings show that Sharia compliance and corporate governance significantly reduce financial statement fraud, while leverage has no significant effect. Transparency has not been empirically proven to moderate these relationships. Theoretically, these results extend the Fraud Pentagon Theory into the context of Islamic finance, suggesting that Sharia principles help mitigate fraud drivers such as pressure, opportunity, rationalization, capability, and arrogance by embedding ethical and spiritual values. From a policy perspective, regulators such as Otoritas Jasa Keuangan, Bursa Efek Indonesia, and Dewan Syariah Nasional Majelis Ulama Indonesia can strengthen value-based reporting systems, emphasizing integrity and internal control rather than focusing solely on financial pressure.

In practice, firms—particularly those listed in the Jakarta Islamic Index—should integrate Sharia compliance into organizational culture and enhance governance mechanisms, including audit committees and internal controls, to ensure substantive transparency. These findings align with prior studies highlighting the role of Sharia adherence and governance in fraud prevention, although they differ from research in other regulatory contexts. The insignificance of transparency as a moderator suggests that disclosure practices, including Islamic Social Reporting, have not yet functioned effectively as behavioral control tools due to their largely administrative nature.

CONCLUSION

This study provides empirical evidence that the integrity of financial reporting among companies listed in the Jakarta Islamic Index (JII) is largely determined by the level of Sharia compliance, the degree of financial pressure reflected in leverage, and the effectiveness of corporate governance. The analysis reveals that Sharia compliance has a significant negative effect on the likelihood of fraudulent financial reporting, indicating that the higher a firm's adherence to Islamic principles, the lower its tendency to engage in financial manipulation. Conversely, high leverage reflects financial pressure that could potentially increase the likelihood of manipulation, although its effect was not statistically significant. Meanwhile, corporate governance was found to have a negative influence on the risk of fraud, yet its effectiveness appears to be moderated by the relative homogeneity of governance practices among Sharia-compliant issuers.

Regarding the moderating variable, transparency and information disclosure quality were not statistically proven to moderate the relationship between the independent variables and fraud risk. However, the direction of the coefficients suggests that higher levels of transparency tend to reduce the potential for financial statement manipulation. Hence, this study strengthens the Fraud Pentagon Theory within the context of Islamic economics, extending its scope through the integration of Islamic Corporate Governance (ICG) values and information transparency principles. This emphasizes that fraud prevention is not solely dependent on formal mechanisms, but also on the strength of moral, ethical, and spiritual values embedded within the organization.

Practically, the findings provide important implications for regulatory bodies such as the Financial Services Authority (OJK) and the National Sharia Board (DSN-MUI) to enhance Sharia-based information disclosure regulations, improve the quality of internal supervision, and promote a value-driven culture of transparency in Islamic financial institutions. For Islamic firms, the results highlight the importance of maintaining debt ratios within Sharia-compliant limits, strengthening internal audit and governance committees, and improving Islamic Social Reporting (ISR) disclosures to enhance public accountability.

Overall, this study contributes to the development of a conceptual model of Sharia accounting grounded in transparency and ethical values, which is expected to serve as a foundation for future research aimed at reinforcing fraud prevention within Islamic-based entities. For future studies, it is recommended to extend the observation period, apply more robust analytical techniques such as re-estimated MRA with mean-centering and robust standard errors, incorporate additional control variables and alternative fraud measures (e.g., F-Score or Dechow model), and broaden the temporal and sample scope to strengthen generalizability.

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