

International Conference on Accounting Studies (ICAS) 2016
15-18 August 2016, Langkawi, Kedah, Malaysia

Factors Minimizing Propensity to Create Budgetary Slack: Empirical Evidence in Indonesia

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Abstract

Budgetary slack is an example of dysfunctional behavior as a result of the participative budgeting process. Budgetary slack is the behavior of making underestimated revenue and overestimated cost. The purpose of budgetary slack is to make budget target easier to achieve and also to make the performance looks good. This research is conducted to prove the factors that empirically can minimize budgetary slack occurrence. This research wants to prove the influence of budgetary control and ethical work climate on budgetary slack and also want to prove the procedural justice perception as a mediating variable. Data used in this research is primary data which are collected using a survey through questionnaires to persons who have structural position in several private universities in Indonesia. Respondents were selected purposively to the lecturers and staffs with minimum of one year experience in structural position and actively involved in the budgeting process. Eighty-eight questionnaires were accepted and used. The analysis technique used in this study is path analysis. This research reveals that the effectiveness of budgetary control through the mediation of procedural justice perception will minimize the propensity to create budgetary slack. This research also found the effectiveness of budgetary control and ethical work climate has positive influence on procedural justice perception. This research has no evidence to prove the negative influence on effectiveness of budgetary control and ethical work climate toward propensity to create budgetary slack. Procedural justice perception has no influence on propensity to create budgetary slack. The mediating effect of procedural justice perception on the influence of ethical work climate towards propensity to create budgetary slack could not be proved. The outcome of this research is employees need to be controlled in budgeting process with good procedural justice perception of subordinates to top management.

Keywords: Budgetary slack, budgetary control, ethical work climate, procedural justice perception

1. INTRODUCTION

Budgeting is most effective when lower-level managers actively participate and meaningfully engage in the budgeting process. Participation requires “honest” communication about the business from subordinates and lower-level managers to their bosses. At that times, subordinates may try to build the budgetary slack (Horngren et al., 2015). One approach to dealing with budgetary slack is to build control during the budgeting process. The optimum level of budgetary control will give more information to managers. Based on this information, managers will have the ability to detect the dysfunctional behavior such as budgetary slack (Callahan and Waymire, 2007). Another approach to reducing budgetary slack is for managers to involve themselves regularly in understanding what their subordinates are doing. A manager’s involvement should take the form of providing support, challenging in a motivational way the assumptions and perceptions subordinates make, and enhancing

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mutual learning about the operations. Regular interaction with their subordinates allows managers to become knowledgeable about the operations and diminishes the ability of subordinates to create slack in their budgets (Horngren et al., 2015).

Most research concerning positive budgetary behavior of managers and or subordinates has generally focused on the motivational role of participative budgeting and its influence on job performance (Argyris 1952; Brownell 1981, 1982, 1983; Frucot & Shearon 1991; Kren 1992; Chow et al. 1991, 1994, 1996, 1999, Lina 2003, Leach-López 2007, Indarto & Ayu 2011, Venkatesh & Blaskovich 2012, Lina & Stella 2013, Soleha, et al. 2013, Rani 2013, Giri 2014, & Lina 2015). The dysfunctional behavior of budgeting process which is called budgetary slack is this research focus. This study is replication of research by Özer and Yilmaz (2011). There has been a lack of research about budgetary control, ethical work climate, perception of procedural justice, and budgetary slack especially in educational industries. This research focus on budgeting process in private university as an institution where persons involve in budgeting process mostly are lecturers who are familiar with theoretical concept. Private universities in Indonesia are self-funded institution that do not receive any fund from government. Thus, the budgeting process should be prepared thoroughly.

This research was conducted to prove empirical evidence of dysfunctional behavior in preparing budget which is called budgetary slack in industry, particularly in private university. The following are the research problem statements. 1). Does effectiveness of budgetary control have negative influence on the propensity to create budgetary slack? 2). Does ethical work climate have negative influence on the propensity to create budgetary slack? 3). Does effectiveness of budgetary control have positive influence on the perception of procedural justice? 4). Does ethical work climate have positive influence on the perception of procedural justice? 5). Does perception of procedural justice have negative influence on the propensity to create budgetary slack? 6). Does effectiveness of budgetary control have negative influence on the propensity to create budgetary slack through the mediation of procedural justice perception? 7). Does ethical work climate have negative influence on the propensity to create budgetary slack through the mediation of procedural justice perception?

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

2.1. Effectiveness of Budgetary Control, Procedural Justice Perception, and Propensity to Create Budgetary Slack

Lau (1999) found that more information improves the ability of managers to detect slack and accounting control system would reduce the budgetary slack. The effectiveness of budgetary control would affect the managers' propensity to create budgetary slack in two ways. First, if managers perceive that budgetary control is effective, they will reduce or give up their propensity to create budgetary slack. Because the managers know that if they create budgetary slack, it will be detected. Secondly, thanks to effective budgetary control, budgetary slack may be detected. So, budgetary slack creation could be prevented (Özer and Yilmaz, 2011). Özer and Yilmaz (2011) proved that effectiveness of budgetary control has negative impact on managers' propensity to create budgetary slack. Özer and Yilmaz (2011) proved that perception of procedural justice has partial mediation effect between effectiveness of budgetary control and propensity to create budgetary slack.

H₁ Effectiveness of budgetary control has negative influence on the propensity to create budgetary slack.

H_{1a} Effectiveness of budgetary control has negative influence on the propensity to create budgetary slack through the mediation of procedural justice perception.

2.2. Ethical Work Climate, Procedural Justice Perception, and Propensity to Create Budgetary Slack

Luft (1997) stated that organization could prevent self-interested behavior such as budgetary slack by creating ethical work climate. This ethical work climate should be accepted by all employees. Study by Özer and Yilmaz (2011) reveals that ethical work climate has negative impact on managers' propensity to create budgetary slack. So, it could be inferred that formation or improvement of ethical work climate would reduce managers' propensity to create budgetary slack. Özer and Yilmaz (2011) proved that perception of procedural justice has partial mediation effect between ethical work climate and propensity to create budgetary slack.

H₂ Ethical work climate has negative influence on the propensity to create budgetary slack.

H_{2a} Ethical work climate has negative influence on the propensity to create budgetary slack through the mediation of procedural justice perception.

2.3. Effectiveness of Budgetary Control and Perception of Procedural Justice

Niehoff and Moorman (1993) found that justice perception of employees positively affected by budgetary control. Effective budgetary control in organization includes procedure can strengthens the employees' perception of procedural justice (Luft, 1997). Budgetary control and ethical work climate affect managers' perception of procedural justice (Özer and Yılmaz, 2011).

H₃ Effectiveness of budgetary control has positive influence on the perception of procedural justice.

2.4. Ethical Work Climate and Perception of Procedural Justice

Unfairness situation will increase when organization doesn't have ethical climate (Buckley et al., 2001). Lau and Wong (2009) proved that principle climate such as rules and procedures positively influence the procedural justice of organization's member. Özer and Yılmaz (2011) also found that ethical work climate affect managers' perception of procedural justice.

H₄ Ethical work climate has positive influence on the perception of procedural justice.

2.5. Perception of Procedural Justice and Propensity to Create Budgetary Slack

Managers will care about themselves and they will look for personal benefits and try to enhance their performance which leads them to create slack (Staley & Magner, 2007). Research by Özer and Yılmaz (2011) found the higher managers' perception of procedural justice, the less propensity to create budgetary slack.

H₅ Perception of procedural justice has negative influence on the propensity to create budgetary slack

2.6. Research Model

The following is the research model.

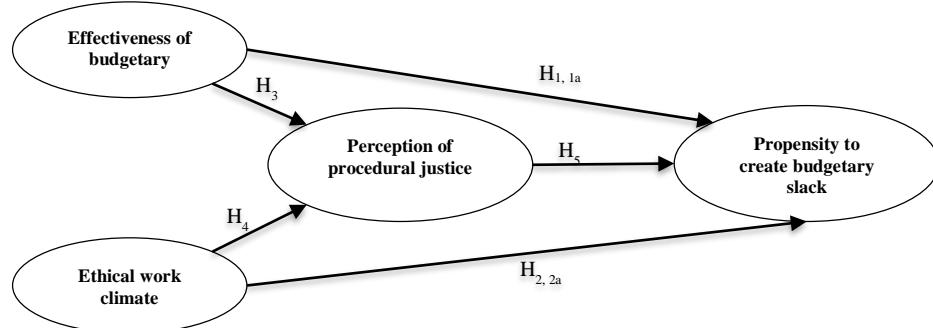


Figure 2.1. Research Model

3. RESEARCH METHOD

3.1. Operational Variables

This research has two independent variables which are effectiveness of budgetary control and ethical work climate. Effectiveness of budgetary control was measured using 5 items on 5-point likert scale developed by Ozer & Yılmaz (2011). These items measured the control process on budget allocation. The instrument to measure ethical work climate was from the ethical work climate scale of Schwepler, Ferrell and Ingram (1997). This scale is based on the scale developed by Quails and Puto (1989). The instrument consists of 5 items on 5-point likert scale. Items used describe whether the organizations apply good ethical conduct. Propensity to create budgetary slack is dependent variable. This variable was measured by instrument adapted from Onsi (1973). The instrument consists of 3 items on 5-point likert scale. This instrument measures the tendency to create slack in budgeting process. Perception of procedural justice is intervening variable. The measurement of this variable used instrument was adapted from Niehoff and Moorman (1993). Each respondent was asked to rate the perception of 7 questions using 5-likert scale. These items represent the perception of employee whether the superiors' decisions are taking prudently and align with the certain project.

3.2. Research Data

The data collected are primary data. Data collection is done by sending a questionnaire to the respondent. Purposive sampling method is used to select the respondent with the following criteria: At least one year of experience as a structural official in private university and actively involved in the budgeting process. Questionnaires was distributed to the respondents through direct delivery or by sending via email. Here is presented a summary of the questionnaires were distributed and used in this study.

Table 3.1 Questionnaire Summary

Description	Amount
Distributed questionnaire	110
Accepted and used questionnaire (80%)	88

The following is respondent demographic description.

Table 3.2 Respondent Demographic Description

Demographic	Amount
Number of Respondent	88
Gender	
Male	41 (46.60%)
Female	47 (53.41%)
Age	
Mean	41.45
Interval	27-55
Median	41
Deviation Standard	7.08
Education Level	
Undergraduate Degree	12 (13.64%)
Master Degree	61 (69.32%)
Doctoral Degree	15 (17.05%)
Period in Structural Position (in Year)	
Mean	4.94
Interval	1-16
Median	4
Deviation Standard	3.22

Age interval of respondents are 27 – 55. Respondents consist of 41 male (46.60%) and 47 female (53.41%). Most of the respondents have master degree education level (69.32%). On average, all respondents have been in structural position for 4.94 years.

4. RESULTS AND DISCUSSION

4.1. Data Quality Test

4.1.1. Validity Test and Reliability Test

Table 4.1. Validity Test and Reliability Test

Variable	Validity Test		Reliability Test		
	Correlation Range	r table	Results	Cronbach's Alpha	Result
Effectiveness of budgetary control	0.660 - 0.800	0.21	Valid	0.774	Reliable
Ethical work climate	0.715 - 0.902	0.21	Valid	0.869	Reliable
Propensity to create budgetary slack	0.451 - 0.481	0.21	Valid	0.853	Reliable
Procedural justice perception	0.357 - 0.809	0.21	Valid	0.555	Quite Reliable

Construct validity test was done through pearson correlation test. Through this test, r count was obtained. This r count will compare to r table at a significance level of 5% and a degree of freedom = $n - 2 = 88 - 2 = 86$. n represent the number of respondents. Table above shown that correlation range of all statements are greater than r table. It means that all statements are valid. Based on the cronbach's alpha, all statements are reliable. It means that respondents' responses of each statement are consistent.

4.2. Hypothesis Test

Table 4.2. Hypothesis Test

Hypothesis	Unstandardized Coefficients	Sig.	R	R Square/ Adjusted R Square	Explanation
H ₁ : Budgetary Control ---> Slack	-0.296	0.201	0.152	0.000	H ₁ not supported
H ₂ : Work Climate ---> Slack	0.174	0.332	0.152	0.000	H ₂ not supported
H ₃ : Budgetary Control ---> Perception	0.336	0.000	0.498	0.230	H ₃ supported
H ₄ : Work Climate ---> Perception	0.171	0.018	0.498	0.230	H ₄ supported
H ₅ : Perception ---> Slack	-0.336	0.154	0.153	0.023	H ₅ not supported
				Standardized Beta	Explanation
Budgetary Control ---> Perception		0.364		Direct Effect	
Perception ---> Slack		-0.153		Direct Effect	
Budgetary Control ---> Slack		-0.146		Direct Effect	
H _{1a} : Budgetary Control ---> Perception ---> Slack		-0.056		Indirect Effect	H _{1a} supported
				Standardized Beta	Explanation
Work Climate ---> Perception		0.240		Direct Effect	
Perception ---> Slack		-0.153		Direct Effect	
Work Climate ---> Slack		0.111		Direct Effect	
H _{2a} : Work Climate ---> Perception ---> Slack		-0.037		Indirect Effect	H _{2a} not supported

This research uses path analysis using SPSS software to test the hypothesis. According to table above, this research cannot support the first hypothesis. Budgetary control effectiveness has no influence on propensity to create budgetary slack. It means all the system and procedure in preparing budget is just a tool that will not be followed unless there is a good role model shown by top management. This research can prove the mediating effect of procedural justice perception on the influence of budgetary control effectiveness towards propensity to create budgetary slack. It means H_{1a} has been supported. Good system and procedure in preparing budget needs to be emphasized by good daily activity shown by top management. This good role model will then minimize the propensity to create budgetary slack.

This research cannot support second hypothesis. Ethical work climate has no influence on propensity to create budgetary slack. It means moral atmosphere is not enough to prevent budgetary slack occurrence. This research also cannot support H_{2a}. It means this research fails to prove the mediating effect of procedural justice perception on the influence of ethical work climate towards propensity to create budgetary slack. The moral atmosphere of the work environment and the level of ethics practiced within a company are not influence factors to minimize the propensity to create budgetary slack.

This research support the third hypothesis which is effectiveness of budgetary control has positive influence on procedural justice perception. It means the clear and sound procedure in budgetary control process that comes from top management will emerge employees' good perception of fair procedural justice. Fourth hypothesis state that ethical work climate has positive influence on procedural justice perception. This hypothesis has been proved through the result of t test. Ethical work climate refers to the moral atmosphere of the work environment and the level of ethics practiced within a company. Good ethical work climate that build by top management will be seen by subordinates within the company and finally will impact on procedural justice perception.

This research cannot support fifth hypothesis. It means propensity to create budgetary slack is not driven by perception of subordinates to top management.

5. CONCLUSIONS

The followings are the research contribution. Effectiveness of budgetary control is the systems and procedures that developed by superior while procedural justice perception is the perception of employee whether the superiors' decisions are taking prudently and align with the certain project. The combination of these two factors was proved could minimize the propensity to create budgetary slack. This result also contribute to the management accounting literature.

The implication of this study is budgetary control effectiveness solely cannot directly minimize the propensity to create budgetary slack. Top management need to build good perception of subordinates with good systems and procedures in budgeting process in order to minimize the propensity to create budgetary slack. The limitation of this research is the fact that the distribution of the questionnaires was not throughout Indonesia yet. Further research should concern to distribute the questionnaires to as many as private universities throughout Indonesia.

ACKNOWLEDGEMENTS

This research was funded by University of Pelita Harapan through research scheme at Business School No: 001/ORP/IV/2016.

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