



THE EFFECT OF BUDGETARY PARTICIPATION ON BUDGETARY SLACK USING BUDGETARY ETHICAL COMPLIANCE AS THE MEDIATING AND MODERATING VARIABLE

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ABSTRACT

This study aims to empirically analyze the relationship between budgetary participation and budgetary slack using budgetary ethical compliance as the mediating and moderating variable. Data were collected through survey method involving heads of work regional unit, secretaries, heads of planning division, heads of equipment division, heads of program development section and head of equipment section in North Maluku province as participants. The respondents were 185 in total. SPSS AMOS 20 version was used to test the hypotheses. The results show that first, budgetary participation has negative effect on budgetary slack. Second, budgetary participation has significant positive effect on budgetary ethical compliance. Third, budgetary ethical compliance significantly, negatively affects budgetary slack. The variable of budgetary ethical compliance was the mediator of the relationship between budgetary participation and budgetary slack. Moderating variables (interactions of budgetary participation and budgetary ethical compliance) have negative and insignificant estimated coefficient value.

Key words: budgetary participation, budgetary ethical compliance, budgetary slack.

Cite this Article: Asrudin Hormati, Rudy Laduna, Suriyana AR. Mahdi, Suleman H. A. Kahar, The Effect of Budgetary Participation on Budgetary Slack Using Budgetary Ethical Compliance as the Mediating and Moderating Variable. *International Journal of Civil Engineering and Technology*, 8(8), 2017, pp. 1081–1092
<http://www.iaeme.com/IJCIET/issues.asp?JType=IJCIET&VType=8&IType=8>

1. INTRODUCTION

Budgeting is categorized as a statement regarding the performance estimation to be achieved in a certain period of financial concern. In public sector organizations such as local authorities, budgeting is a relatively complicated process. Different from private sectors in which budgeting is confidential, budgeting in public sectors must be disclosed for criticism and advice. This budgeting is an accountability instrument for the management and

implementation of programs financed by public funds (Mardiasmo, 2002). Budgeting of public sector relates to the process of determining the allocation of funds for each program and activity in monetary units. Budgeting phase in public sector becomes exceedingly important because ineffective budgetary will lead to a failure at planning. In summary, budgeting is a managerial plan for action to facilitate the achievement of organizational objectives.

Among problems concerning local finances, the basic change of local government budget (*Anggaran Pendapatan dan Belanja Daerah/APBD*) becomes the focus of attention. This emphasis relates to greater demand for the accountability and transparency of budgetary management by considering the principle of fairness and propriety. The paradigm shift of local budgeting is performed to generate local budget reflecting the interest and expectation of local community on financial management economically, efficiently, and effectively.

In public sector, especially the government, budgeting is a relatively complicated process, and it includes political content. In line with the authority established by the Indonesian central government for municipalities and regencies to regulate the domestic affairs, local government officials, especially the echelons are involved in determining the direction and policy of local development, including budget formulation. The participation in budgeting is a process of shared decision-making by the public sector as an accountability instrument for the management and implementation of programs financed by public funds. The budget of public sector relates to the process of determining the allocation of funds for each program and activity in monetary units. Budgeting phase in public sector becomes exceedingly important because ineffective budgetary will lead to a failure at planning (Mardiasmo 2002).

Budgeting involves human relationships thus developing human behavior, positively and negatively. Positive behavior includes an increase in the performance of managers motivated by the budget used as the basis for the performance assessment, while negative behavior includes the emergence of the notion that budget is frequently seen as a tool of managerial pressure. Intermediate and lower level managers experience the pressure when the highest management tries to improve the efficiency by obtaining more output from existing input level (or lower). Consequently, the managers tend to create slack in budgetary in order to increase the possibilities to meet or exceed performance standard.

Previous studies reveal that the level of budgetary slack is influenced by several factors including the subordinate role or participation in formulating a budget. The studies show inconsistent results. Onsi (1973), Cammann (1976), Merchant (1985), Dunk (1993) Kren (2003), Maiga (2005), Maiga and Jacobs (2008) Husain (2011), Kahar et al. (2016), Husain (2014) find that budgetary participation reduces the amount of budgetary slack. On the other hand, Yuwono (1998), Lukka (1988), Young (1985), Basri (2010) Djasuli and Fadila (2011), and Jaya and Rahardjo (2013) prevail the different findings. In addition, Collins (1978) and Vemy et al. (2011) find that budgetary participation and budgetary slack have an insignificant relationship. The difference of the results is caused by diverse mediating or moderating variables. Therefore, this study aims to examine the effect of budgetary participation on budgetary slack using budgetary ethical compliance as the mediating and/or moderating variable.

This study attempts to propose a valuable determinant regarding the budgetary ethical compliance and budgetary slack. Budgetary ethical compliance is based on theories of institutional culture of organization and ethics. This new concept is expected to play a role in addressing the gap. The new concept has not been used in preceding studies. The results of this study are expected to be used as a reference in the field of behavioral accounting

discussing the role of budgetary ethical compliance in mediating and moderating budgetary participation and budgetary slack more comprehensively. Budgetary ethical compliance is generated from the institutional theory, organizational culture theory, and ethical theory. This compliance is potentially bridging the controversy of study concerning budgetary participation and budgetary slack.

2. LITERATURE REVIEW AND HYPOTHESES

Institutional theory refers to the process of public budgeting with two main conceptions. First, budgeting process is a very technical issue including demanding economic calculations, efficiency, and accountability. Rooting from this concept, budgeting managers use the authority on various programs. Second, budgeting process emphasizes the importance of institutions, individual ethics, formal rules, capability to negotiate over budgetary priorities, and the outcomes. This concept allows the public budgeting process involving many parties, focusing on utility maximizing the determined program; positioning shared benefits as the main objectives; and orienting the responsibilities of the public budgeting process. These concepts were fundamentally different in the terms of orientation. The first concept emphasizes on the effectiveness and efficiency of the process, while the others focus on the role as a political tool. If public budgeting is considered as a management process, it becomes a rationale to make effective decisions.

In the institutional theory framework, the use of expenditure standard analysis by local government will minimize the absorption of local government expenditure; promote logical unit cost establishment and allocation for each work unit; and succeed in efficient continuous achievement. To achieve effective and efficient local budgetary implementation, the budgetary formulation process is essential to determine the legitimacy of the inclusive local budgeting cycle (Ling, 2008).

Carpenter and Feroz (2001) state that internally, subordinates will comply with existing regulations, tending to perform properly in determining the budget. Subordinate's behavior can also be reflected in the reasonable amount of the budget in which the disclosure of the information supports the performance. Meanwhile, Covaleski et al. (2003) argue that the employee involvement in the budget formulation has a positive influence on ethical compliance. It means that the higher the participation, the higher the level of ethical compliance is likely to be. Smith and Bertozzi (1998) prevail that in the process of public budgeting individual ethics will be influenced. This means that the higher the subordinates participation level in the budgeting process, the higher the individual ethics. Subramaniam and Ashkanasy (2001), and Ajibolade and Akinniyi (2013) conclude that organizational ethics positively affects budgetary participation in public sector organizations.

This study tries to explain how the budgeting process builds a behavior as a guide in evaluating the performance based on the accounting numbers in the budget. Institutional theory explains the development of organization by the established rules as a guide to create customs and norms in the organization. Budget is regarded as organizational guidelines including the rules creating the customs to be followed in the organization (Ajibolade & Akinniyi, 2013). Moreover, Valentine et al. (2015) find a significant positive effect of ethical professional standards on organizational ethical values and organizational ethical values on budgetary orientation.

This study aims to complement the preceding studies by using the basic framework of institutional theory. This study intends to develop and test the relationship between variables in public sectors in Indonesia. Therefore, the participation involves direct interaction between

superiors and subordinates in determining the budget acceptable to both parties. The effectiveness of budgetary participation depends on the actions of superiors and subordinates in participation. In addition, Ozer and Yilmaz (2011) use the perception of procedural justice as a mediation of the relationship between the effectiveness of budgetary control and ethical work climate and the creation of budgetary slack. The results show negative significant effects on the relationship.

This study uses the budgetary ethical compliance as the mediating variable of the relationship between budgetary participation and budgetary slack. Budgetary slack occurs when individuals realize that the performance will be assessed based on the budget. This situation motivates individuals to perform optimally in formulating the budget.

H1: The budgetary participation of public sector officials negatively influences the budgetary slack.

H2: The budgetary participation positively influences the budgetary ethical compliance.

H3: The budgetary ethical compliance negatively influences budgetary slack.

H4: Budgetary ethical compliance can be a mediating variable of the relationship between budgetary participation and budgetary slack.

H5: Budgetary ethical compliance can be a moderating variable of the relationship between budgetary participation and budgetary slack.

3. RESEARCH METHOD

3.1. Population, Sample, and Data Source

This study was conducted in government organizations in North Maluku province. The population was the regional work units throughout North Maluku. The study was conducted for 3 months starting from June until August 2016. The sample of this study was the officials including the head of regional work units, secretary, head of planning division, head of equipment division, program development section, and head of equipment section, involved in the formulation of work and budget plan of 41 regional work units.

The sample was selected through purposive sampling, by which several consideration and criteria were used. The consideration was that the selected respondents were officials having an important role in budgetary formulation and utilization. Moreover, the respondents had accurate information on the operational budget in each unit. The sample of this study was 246 respondents consisting of officials participating in budgetary formulation and utilization.

Following the data collection, it was found that one regional work unit did not return the questionnaire (Liaison Office in Jakarta with 6 questionnaires); and among the returned questionnaires, 27 were invalid; 6 were incomplete, and 10 were not filled in accordance with the criteria of serving-period. Invalid questionnaires were not included in the subsequent data analysis. The total sample used in this study was 203 respondents with the effective respond rate 82.52%. After analyzing the data, 18 outlier data questionnaires were found. Therefore, only 185 respondents were legitimate for further analysis.

The respondents consisted of 141 male (76.2%) and 44 female (23.68%) including 31 heads of regional work units (16.8%), 30 secretaries (16.2%), 35 heads of planning division (18.9%), 35 heads of program development section (18.9%), 25 heads of equipment division (14.5%) and 29 head of equipment section (15.7%). Regarding the education level, the respondents consisted of 92 undergraduates (49.7%), 90 postgraduates (48.6%), and 3 doctoral graduates (1.6%).

3.2. Variable Measurement

This study used budgetary participation as an independent variable, budgetary slack as a dependent variable and job satisfaction as mediating and moderating variable. These variables were measured using questionnaires adopted from previous related research.

Budgetary participation is the level of involvement and influence of individuals in the budget formulation process. To measure this variable, the instrument consisting six question items developed by Milani (1975) was used. This instrument had high validity rate and had been used in several previous studies. Using this instrument, the respondents were asked to answer six questions on a scale of 1 to 7. Scale 7 showed the highest level of participation, while 1 scale showed the lowest level of participation.

Budgetary slack is the gap between the amount of the proposed budget with the pre-eminent estimated amount of the organizations. The instrument developed by Dunk (1993) was used to measure budgetary slack. The instrument consisted of six questions using a scale 1 to 7. Scale 7 showed the highest level of budgetary slack, while 1 scale showed the lowest level of budgetary slack.

The core idea of institutional theory is the establishment of an organization by the pressure of institutional surroundings leading to institutionalization. Abernethy and Chua (1996) developed three constructs in institutional area including regulative, normative, and cognitive. Regulative construct highlights rules and sanctions; normative pillar contains evaluative dimension and obligations; while cognitive construct involves the shared conception understanding meaning. Each construct provides different reasons in terms of legitimacy, either based on penal sanctions, moral, or culture. Therefore, it is not humans determining institution, but institution affecting human behavior based on rules and norms (Burgstaler & Sundem, 1989). In summary, budgetary ethical compliance is an interpersonal appropriate normative behavior within an organization using norms, values, culture, compliance, and authentic legitimacy as the guide for individuals in social structure or organization.

Budgetary ethical compliance was measured using five items instrument developed by (Hoogh & Hartog, 2008). Likert scale ranging from 1 (strongly disagree) to 7 (strongly agree) was used. This instrument was formerly used by Brown and Trevino (2006) reporting that the composite reliability of this instrument was 0.72.

4. RESULTS

4.1. Factor Analysis

The results of the factor analysis showed that the level of data reliability was good. The minimum consistency value of reliability testing is 0.60 (Ghozali, 2013). The results mean that the question items measuring budgetary participation construct, budgetary ethical compliance, and budgetary slack, are reliable.

Using Maximum Likelihood as the estimation model, the number of samples required a minimum of 100 and a maximum of 200 (Ghozali, 2013). Prior to further testing, the indicators that failed to meet the criteria were studied. The study showed that while those indicators are excluded from the measurement model, the remaining indicators were able to measure each construct (Hair et al. 2010).

Table 1 Factor Loadings (N = 185)

Factors and Scales	Factor 1	Factor 2	Factor 3
BP (Cronbach α : 0.824)			
BP 2	0.637		
BP 3	0.714		
BP 4	0.734		
BP 5	0.792		
BEC (Cronbach α : 0.825)			
BEC1		0.770	
BEC2		0.760	
BEC3		0.754	
BEC4		0.754	
BS = Budgetary Slack (Cronbach α : 0.861)			
BS2			0.693
BS3			0.723
BS4			0.750
BS5			0.849
BS6			0.720

Note: * $p < .05$, ** $p > .05$. BP = Budgetary Participation; BS = Budgetary Slack; BEC = Budgetary Ethical Compliance.

Table 1 showed that each construct or variable has Cronbach alpha value above 0.60, meaning that the interval consistency of the variables of budgetary participation, budgetary ethical compliance, and budgetary slack were reliable.

An indicator is considered valid if the loading factor value is above 0.5 towards intended constructs. Table 1 showed that the loading factor value less than 0.5 was indicator BP1 and BP6 of budgetary participation construct, and indicator BEC5 of budgetary ethical compliance construct. Budgetary slack construct had three negative questions—BS1, BS3, and BS6, while the answers of question BS3 and BS6 were reversed prior to analysis because BS1 had loading factor value below 0.5.

4.2. Correlation Analysis

Correlation analysis was conducted to observe the relationship among variables. The correlation matrix in Table 2 showed that there was a relatively strong positive correlation between budgetary participation and budgetary ethical compliance with correlation coefficient of 0.295 and it is significant. In addition, there was a negative relationship between budgetary participation and budgetary slack with correlation coefficient 0.291 and it is significant.

Table 2 Mean, Standard Deviation, Correlation Coefficients

Variables	Means	Standard Deviation	Min.	Max.	BP	BEC	BS
BP	31.56	4.993	1	7			
BEC	28.52	3.858	1	7	0.295*		
BS	23.61	2.042	1	7	-0.312*	0.291*	

Note: * $p < .05$, ** $p > .05$. BP = Budgetary Participation; BS = Budgetary Slack; BEC = Budgetary Ethical Compliance.

4.3. Assessment of Fit Indices

Based on the results of the feasibility test of Goodness-of-Fit indices as shown in Table 3 below for all criteria using Chi-square, the probability, TLI, CFI, GFI, AGFI, CMINDF, and RMSEA had high-quality values.

Table 3 The Goodness-of-Fit Statistics

Goodness of-Fit Indices	Suggested Value	Value	Result
Chi-Square	expected to be small	64.858	Fit
Probability	≥ 0.05	0.377	Fit
GFI	≥ 0.90	0.996	Fit
AGFI	≥ 0.90	0.997	Fit
TLI	≥ 0.90	0.950	Fit
CFI	≥ 0.90	0.929	Fit
CMINDF	≥ 2.00	1.046	Fit
RMSEA	≥ 0.08	0.016	Fit

4.4. Hypothesis Testing

Based on the hypothesis testing using model fit of AMOS 20.0, regression weights were obtained. According to Ghozali (2013), regression weights provide a description of unstandardized and standardized coefficient value for ordinary least square of regression equation. The value of the critical ratio is equal to the value of ordinary least square regression, while P is equal to the probability of significance.

Table 4 Regression Weights

Hypothesis			β	S.E.	C.R.	<i>p</i>
BP	\Rightarrow	BS	-0.282	0.082	-3.457	0.000*
BP	\Rightarrow	BEC	0.253	0.083	3.057	0.002*
BEC	\Rightarrow	BS	-0.247	0.086	-2.875	0.004*
BP	\Rightarrow BEC	\Rightarrow BS	-0.217	0.081	-2.677	0.007*
Moderating	\Rightarrow	BS	-0.001	0.001	-0.515	0.607**

Note: * $p < .05$, ** $p > .05$. BP = Budgetary Participation; BS = Budgetary Slack; BEC = Budgetary Ethical Compliance.

The analysis as shown in table 4 revealed the relationship between budgetary participation and budgetary slack ($\beta = -0.282$, CR = -3.457, $p = 0.000$). Thus, hypothesis one stating the negative significant relationship of the budgetary participation and the budgetary slack was accepted. The subsequent analysis revealed that budgetary participation had a positive effect on budgetary ethical compliance. It was shown that budgetary participation is likely to increase budgetary ethical compliance, indicated by the value of $\beta = 0.253$, SE = 0.083, CR = 3.057, $p = 0.002$. This meant that the second hypothesis was accepted. The analysis later revealed that hypothesis three stating budgetary ethical compliance negatively affects budgetary slack was accepted. This was indicated by the value of $\beta = -0.247$, SE = 0.086, CR = 2.875, $p = 0.008$, meaning that budgetary ethical compliance was likely to reduce budgetary slack.

The testing procedure of job satisfaction as a mediator variable of the relationship between budgetary participation and budgetary slack was first, estimating the direct effect of budgetary participation on budgetary slack, and second, estimating the indirect effect simultaneously using SEM (Baron and Kenny, 1986). Therefore, the model of the testing was budgetary participation \Rightarrow budgetary ethical compliance \Rightarrow budgetary slack.

The results showed that the coefficient of the direct effect of budgetary participation on budgetary slack was -0.282 and significant, while indirect effect coefficient was -0.611 and significant. This meant that budgetary ethical compliance was partially capable in mediating the relationship between budgetary participation and budgetary slack. In other words, budgetary ethical compliance was not the only mediator in this relationship (Baron & Kenny 1986; Hair et al., 2010; Kock, 2011). The results supported hypothesis four stating that budgetary ethical compliance as a partial mediator variable indirectly affects the budgetary slack.

Moderated hypothesis testing was conducted using moderated regression analysis (MRA) estimated using SEM (Kock, 2010, 2011). Table 4 showed that the coefficient of the interaction between budgetary participation and budgetary ethical compliance was not significant with $p = 0.607$. Finally, the results indicated that the last hypothesis stating that budgetary ethical compliance as a moderator of the relationship between budgetary participation and budgetary slack was not accepted. Thus, in this study, the compliance of work ethic was a quasi-moderator (Ikhsan & Ane 2007).

5. CONCLUSIONS

This study examines the budgetary ethical compliance as the mediating and moderating variable of the relationship between budgetary participation and budgetary slack in North Maluku province. The analysis of the direct relationship shows that the slack can possibly decrease. This means that the higher the subordinates' involvement in budgetary formulation, the budgetary slack can possibly be reduced. These results are consistent with the research conducted by Husain (2011, 2014).

This study reveals that budgetary ethical compliance is capable in mediating the relationship between budgetary participation and budgetary slack, in the budgeting formulation process of local government in North Maluku province. However, this variable is not a moderating variable. Therefore, future studies should examine job satisfaction variable as an independent variable.

Budgetary ethical compliance in the research is proposed as a new concept used to bridge the research gap of budgetary participation and budgetary slack. This compliance is a situation or character of an individual in the organization's activities oriented towards objectives. Empirically, compelling evidence is found regarding the mediating role of budgetary ethical compliance in bridging the gap. Budgetary ethical compliance refers to the belief that if an individual behaves ethically, they are likely to enjoy the success of the organization. The findings are consistent with the institutional theory based on the assumption that the rationale requires ethical values for effective decision policy.

The findings of this study support the budgetary ethical compliance from the perspective of agency theory explaining the phenomenon occurred when superiors delegate a power to subordinates to perform a task or authority in making decisions. Therefore, if subordinates involved in the budgeting formulation have specific information on local conditions, they are likely to provide information to facilitate the organization.

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