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**THE INFLUENCE OF PARTICIPATIVE BUDGETING ON BUDGETARY SLACK
(WITH LOCAL CULTURE AND CORPORATE GOVERNANCE AS THE MODERATORS:
AN EMPIRICAL STUDY ON RURAL BANKS (BPRS) IN BALI**

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ABSTRACT

This research is aimed at revealing the moderation of good corporate governance and Tri Hita Karana as a local culture on the relation of participative budgeting towards budgetary slack. The research population is the rural banks in Bali province. The data are analyzed by using Moderated Regression Analysis. The results provide empirical evidence suggesting that corporate governance can moderate the relationship of participative budgeting towards budgetary slack, whereas the Tri Hita Karana culture shows no evidence of influence that can moderate the relationship of participative budgeting and budgetary slack.

KEY WORDS

Corporate governance, Tri Hita Karana, local culture, budgeting, budgetary slack.

Budget is an important tool that can be used by the management to control the company operations and to ensure the chosen strategies can be used to achieve the company's goal (Triana *et al.* 2012). Budget can also assist managers to be more responsible because budget is the means to communicate the plans, to allocate resources, to set the goals, and to function as the guidance in an organization (Garrison & Noreen in Bradshaw *et al.* 2007). Budget is an element of a management controlling system which functions as the planning and controlling tool which enables managers to implement the organization activities more effectively and efficiently (Schiff & Lewin 1970).

Participative budgeting is a process of composing a budget which involves individuals who have influences on the budget target. This process involves many parties from the top-level management to the lower-level management. The participative budgeting may result in certain individual behavior, e.g. improvement in performance because of the rewards given by the company when the budget target has been achieved. The participation of managers and their subordinates in setting up the budget is significantly needed. Each member of an organization who involves in budget determination process might tend to create a biased or lower budget, depending on their behavior, because by making a low budget their performance might look better. This kind of behavior in determining budget can create budgetary slack; moreover, some experts, among others, Lyne 1995; Walker & Choudhury 1987, state that it is 'common' for budgetary slack to exist in a budget which is composed participatively.

Budgetary slack is a variance between the planned budget and its realization. During the process of setting up a budget, lower-level managers often lower their abilities or performance by displaying the allocation for resource needs at a much higher number than the actual ones by overestimating the expenses or underestimating the incomes (Kren, 2003). Due to this budgetary slack, the accuracy of the information shown in the budget is doubtful.

Several researches testing the relationship between the subordinates' participation and the budgetary slack had already been done with inconsistent results. The research by Lowe & Shaw 1968; Young 1985; Lukka 1988; Falikhatun 2007; Kartika 2010; Widyaningsih 2011;

and Pello 2014; show that participative budgeting has a positive influence towards the budgetary slack. The same research suggests that the individuals involved in the budgeting process might tend to bring their own interests into the budget. When this happens, these people create budgetary slack indirectly. On the other hand, some research by Camman 1976; Merchant 1985; Chow *et al* 1988; Dunk 1993; Supanto 2010; and Apriyandi 2011; show that the participation in determining a budget can reduce the budgetary slack (i.e. has a negative influence).

The existing contrast found in that research above can be settled by applying the contingency approach which allows other variables to act as the moderating or intervening factors and influence the relationships between the participative budgeting and the budgetary slack. *Good corporate governance* (GCG) applied in a company contains 5 essential principles which must be applied in running a company, namely transparency, accountability, responsibility, independency, and fairness. The application of GCG in participative budgeting might reduce its influence on the budgetary slack. Similarly, the influence of participative budgeting on budgetary slack can also be reduced by applying the *Tri Hita Karana* culture (THK), as a local wisdom which believes in the harmony of nature, human, and God.

This current research is conducted in rural banks (*Bank Perkreditan Rakyat*; hereafter, BPRs) located in Bali province. BPR is different from other types of banks because BPR is oriented to rural society in Indonesia including Bali. The development of BPRs has a quite significant impact in Indonesian economic improvement as perceived by Indonesian government. This is mainly due to the orientation of BPR towards improving the Micro, Small and Medium Enterprises (hereafter, UMKM) by channeling credit or loans. Each bank, including BPR, needs to manage their business effectively and efficiently to win the competition in the competitive business environment. Therefore, budget planning is crucial for BPR to support their operations. This research focuses on three questions: whether or not participative budgeting influence budgetary slack of BPRs in Bali province?; whether or not the application of *Corporate Governance* can create influences on the relationship of participative budgeting towards budgetary slack of BPRs in Bali?; and, whether or not *Tri Hita Karana* culture can create influences on the relationship of participative budgeting towards budgetary slack of BPRs in Bali?

The objective of this current research is to recognize the influence of participative budgeting on the budgetary slack of BPRs in Bali by focusing on the influences of *Corporate Governance* and *Tri Hita Karana* culture on their relationship.

This current research is significant because the Micro, Small and Medium Enterprises (UMKM), especially in Bali, rely heavily on BPRs to carry out their business. BPRs help UMKM by providing the capital. BPR performance is considered good when one of the indicators in the budget planning is the lack of significant budgetary slack.

The implication of this research can be used as one of the considerations in banking world, namely suggesting BPRs to create an effective and efficient budget by applying GCG and THK culture appropriately.

LITERARY REVIEW

Agency Theory and Contingency Approach. Within the budgetary slack practices, the agency theory is the conflict of interests between principals and agents which happens when each party tries to achieve their intended goals. In the process of formulating the budget for a company, participative managers tend to provide information which is different from the actual resources that they should have had in order to attain rewards. Contingency theory is based on the assumption that organization management can observe and resolve certain situations which are currently faced by the company, and each situation must be analyzed separately.

Previous research shows inconsistent results with regards to the relationship between participative budgeting and budgetary slack. Some researchers, such as Merchant 1985; Dunk 1993; Supanto 2010; and Apriyandi 2011; argue that participative budgeting can reduce the tendency to create budgetary slack. This happens because the subordinates can

provide their own private information with regard to the future prospect; consequently, the planned budget becomes more accurate.

On the other hand, other research done by Young 1985; Falikhatun 2007; Kartika 2010; Widyaningsih 2011; and Pello 2014; gain empirical evidence showing that participative budgeting can, in fact, cause the participating managers to create budgetary slack during the budget planning. Due to the inconsistency, it is deemed necessary to use other approaches to look at the relationship between those two variables.

Several researchers from the management accounting field conduct research by applying the contingency approach in order to see the relations between contextual variables and the design of a management accounting system; furthermore, it can be used to evaluate the effectiveness of the relationship between two variables (for example, the relationship between participative budgeting and budgetary slack) by using certain moderating variables. This current research uses the *Corporate Governance* and the *Tri Hita Karana* culture as the moderating variables for the relationship between participative budgeting and budgetary slack.

The influence of Participative Budgeting on Budgetary Slack. Hansen & Mowen 2012, states that budget is the main component of planning, i.e. the financial planning for the future, because budget contains the objectives and the activities which enable the company to achieve the objectives. In budgeting, there are two main elements, namely how the budget is formulated and how the budget is implemented as the company's plan.

Participative budgeting needs contribution from each member of an organization because it is believed that the subordinates might have more understanding of the situation in their respective departments. Participation in determining a budget is an effective way in creating the standards and alignment of objectives from each responsibility-center with the overall objectives of the company (Siegel & Marconi 1989).

The fact that participation is an effective way to align the objective of the responsibility-centers with the overall objective of the organization makes participative budgeting have an important function in motivating the subordinates by giving them targets to achieve the goals. By undertaking the participation process, the management can provide information based on the resources they have on hand; consequently, the owners of the company can make the right decisions in order to achieve the company's goals (Ikhsan and Ishak 2005). Nevertheless, participation in budget determination has a flaw, namely it can create budgetary slack.

Budgetary slack is the act of the subordinates who understate their capabilities or productive capabilities in the budget proposal (Young 1985). Thus, budgetary slack is the variance resulting from the difference between the budget estimation and its realization. The subordinates create the budgetary slack by overstating the planned costs and understating the expected revenues. This is caused by the subordinates who tend to compose a budget which is easy to realize, i.e. by loosening the budget.

The participation of the subordinates in composing a budget gives them the freedom to determine the targets they want to achieve for their own interests and not for the interests of the organization or institutions. This is confirmed by a research done by Djasuli 2011, in which it is stated that participative budgeting has a positive influence towards budgetary slack.

According to Lau & Eggleton 2003, subordinates have a higher motivation to create budgetary slack in the proses of participative budgeting because they have more information than their superiors, and the subordinates are also responsible for achieving the targeted budget. Thus, the subordinates might tend to overstate their needs and to understate their productivity in the budget that they compose in order to achieve the budget (Widanaputra & Mimba 2014). This statement is in line with a research by Ramdeen 2006, which states that the higher the level of participative budgeting is, the higher the number of the resulting budgetary slack will be.

H₁: Participative budgeting influences budgetary slack.

The Influence of Corporate Governance towards the Relationship of Participative Budgeting and Budgetary Slack. In brief, good corporate governance is a concept of

governing a healthy company which is expected as the means to ensure the stockholders and creditors can regain their investments (Khairandy & Malik, 2007: 60). GCG consists of five principles (usually abbreviated to TARIF), i.e. transparency, accountability, responsibility, independency, and fairness. Thus, the objectives of GCG is to maximize the values of the company and the stockholders by developing the transparency, accountability, and responsibility; in addition, another GCG's objective is also to establish the governance system which encourages and promotes creativity and progressive entrepreneurship.

GCG can be considered as a compulsory concept to be applied in every organization because GCG can contribute to public welfare, and it is also supported by the philosophical assumption behind the birth of GCG. CG is a mechanism which manage the governance of a company to be better. GCG's function is to help protecting the rights of the stakeholders. The application of GCG and its five principles can minimize the self-interested behavior of the people who compose the budget.

H₂: *Corporate Governance* influences the relationship of participative budgeting and budgetary slack.

The Influence of Tri Hita Karana Culture towards the Relationship of Participative Budgeting and Budgetary Slack. *Tri Hita Karana* is considered as a culture which is believed and has become the fundamental part in the life of Balinese people. Hofstede, a writer in cultural organization, admits the importance of culture to management. *Tri Hita Karana* is a local wisdom of Balinese people containing the virtues which can become their guidance to live in every aspect of life.

The virtues found in THK culture contains the suggestion that THK is relevant to be used as the guidance for personal life and businesses because THK culture reflects a harmony of three aspects: the harmony between human and their creator, the harmony between human and nature, and the harmony amongst human themselves. These three aspects can influence the behavior of an agent or the management. The THK culture can strengthen the influence of participative budgeting which has the nature of reducing the budgetary slack; conversely, the THK culture can weaken the influence of participative budgeting which has the nature of increasing the budgetary slack.

H₃: The *Tri Hita Karana* culture can influence the relationship of participative budgeting and budgetary slack.

METHODS OF RESEARCH

This current research studies the rural banks (BPRs) located in Bali province. The objects of research are participative budgeting, good corporate governance, *Tri Hita Karana* culture, and budgetary slack found in those BPRs.

The data are analyzed by using the *Moderated Regression Analysis* (MRA). MRA test is a multiple linear regression application in which its regression equation contains the interaction of multiplication of two or more independent variables.

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 (X_1 \cdot X_2) + \beta_5 (X_1 \cdot X_3) + e \quad (1)$$

Where:

Y = budgetary slack;

α = constant;

X₁ = participative budgeting;

X₂ = GCG;

X₃ = THK culture;

$\beta_1 \beta_2 \beta_3$ = regression coefficients;

e = standard error.

The hypotheses of this present research can be tested by measuring the coefficient of determination value, F-test, and t-test (Ghozali, 2013:97-99).

- The coefficient of determination is one of the main tools to measure the alignment of the regression line with the data distribution. The coefficient of determination on linear

regression is often interpreted as the ability value of all the independent variables to interpret the variance of the dependent variables. The coefficient of determination used in this research is the value of R^2 for hypothesis 1 and the value of the Adjusted R^2 for hypothesis 2.

- F-test model. The F-test is used to test whether or not all independent variables which are put in the model have the joint influences on the dependent variables. The criteria for decision-making are set by comparing the score of F value with that of F table. H_0 is rejected if F value > F table ($\alpha = 0,05$), and H_0 is accepted if F value \leq F table ($\alpha = 0,05$).
- t-test. t-test is conducted to test individually the degree of influence which a particular independent has on the interpretation of dependent variables. The criteria for decision-making are set by comparing the statistic score of t value with that of t table. H_0 is rejected if t value > t table ($\alpha = 0,05$), and H_0 is accepted if t value \leq t table ($\alpha = 0,05$).

The variables analyzed in this research are participative budgeting, budgetary slack, and two moderating variables: GCG and THK culture.

The operational definition in this research is as follows:

- Participative budgeting is defined as the participation of the managers of responsibility-centers in the matters related to the budgeting process (Govindarajan, 1986). To measure the participation of a manager or subordinate in the budgeting process, an instrument developed by Kartika (2010) is used. It consists of 6 items of questions with a five-point Likert scale for each item.
- Budgetary slack is a variance resulting from the difference between the reported budget and its actual estimation (Anthony & Govindarajan, 1998). It is aimed at making the targets easier to achieve by the subordinates. The items used in the measurement of the budgetary slack refer to the list of questions used by Kartika (2010). There 6 question items with a five-point Likert scale.
- *Corporate Governance* (CG) is a principle underlying a good governance of a company by considering the interests of the stakeholders which consist of village leaders, the government, the management, and public. The measurement of CG variable uses the group of values or index attained from the application of CG principles obtained from the questionnaire distribution containing CG indicators and using Likert scale.
- Local culture is the manifestation of Balinese people cultural value by adopting the *Tri Hita Karana* concept and its indicators, namely the relations between human and human, human and nature, and human and God. The measurement uses Likert scale, and the data are taken from questionnaires.

This current research makes use of qualitative and quantitative data. The qualitative data are the names of BPRs which are registered in Bali province, whereas the quantitative data are the scores of the answers given by the respondent on the five-point Likert scale ranging from strongly disagree to strongly agree. The primary data are obtained from the survey method by using questionnaires distributed to the respondents.

The population of this research is a number of directors and staff who participated in the budgeting in 137 BPRs in Bali (Source: <http://www.bi.go.id>). This current research also uses the purposive sampling methods with two criteria: 1) the BPR asset is worth Rp. 60.000.000.000,- minimum; 2) the respondents have been in their positions/section for two years minimum. The two-year period is chosen with an assumption that the respondents should have had the experiences of composing a budget and might have had the necessary professional certification. Prior the analysis, the data collection instruments have been tested by using the validity and reliability tests, and continued with the classical assumption test.

RESULTS AND DISCUSSION

This research is conducted to reveal the influence of GCG and the THK culture on the relations between participative budgeting and budgetary slack. The number of samples is 35

BPRs in Bali. Three questionnaires are given for each BPR. They are to be completed by the managing director, and two heads of departments who are professionally certified. These people are chosen because they are responsible for the budgeting process. Initially, the respondents are 105 people who composed the budget and who have been professionally certified. From 105 respondents, 19 are declared unusable with 3 of them did not return the questionnaires and the other 16 did not meet the criterion of professional certification. Consequently, there are 86 respondents used in this research. The data are collected from the questionnaires which are distributed directly to the 35 BPRs. The detailed description about the distributed questionnaires, the returned questionnaires, and the questionnaires given to each BPR is made afterward.

The instruments used in this research are tested by using the validity test and reliability test with a sample of 30 respondents. The validity test uses the correlation coefficient between the scores in which the related indicators should be valid when the correlation indicates positive relationship and valued at $> 0,3$.

The result of the validity test shows the correlation coefficient (r) on the entire variables is bigger than $0,3$ with a significance smaller than $0,05$. The result of the reliability test shows that all variables have their *Cronbach's Alpha* scores which are bigger than $0,7$. Based on the result of data processing, it can be interpreted that the instruments used in this research have fulfilled the requirements to be used.

The results of the *Moderated Regression Analysis* test (MRA) are as follows:

Table 1 – The Results of *Moderated Regression Analysis*

Variable	Unstandardized Coefficients		Standardized Coefficients	T	Sig
	B	Std. Error	Beta		
(Constant)	58,218	20,158		2,888	0,005
Participative budgeting (X1)	-2,2932	1,128	-2,527	-2,599	0,011
CG (X2)	-0,663	0,215	-1,814	-3,077	0,003
THK (X3)	0,228	0,321	0,412	0,710	0,480
X1*X2	0,039	0,011	3,851	3,474	0,001
X1*X3	-0,00000	0,0173	0,000	0,000	1,000
F	17.468				
Sig. F	0,000				
R Square	0,522				
Adjusted R Square	0,492				

Based on Table 7 above, the regression equation is as follows:

$$Y = 58,218 - 2,2932X_1 - 0,663X_2 + 0,228X_3 + 0,039(X_1 * X_2) - 0,000(X_1 * X_3)$$

Where:

Y = Budgetary slack;

A = Constant;

β_{1-5} = Regression coefficient;

X1 = Participative budgeting;

X2 = Good corporate governance;

X3 = *Tri Hita Karana* culture;

X1 * X2 = Interaction between participative budgeting and good corporate governance;

X1 * X3 = Interaction between participative budgeting and *Tri Hita Karana* culture.

The results of the analyses on the *Moderated Regression Analysis* (MRA) test by observing the goodness of fit and by looking at the model appropriateness test (the F-test), coefficient of determination (Adjusted R^2), and hypothesis test (t-test) are as follows:

- The result of the model appropriateness test (the F-test). The F-test is used to test whether or not the independent variables used in this research have an influence on the dependent variables simultaneously. Based on the F-test result, it is recognized that the regression model has F_{valued} at 17,468 with a significance of $0,000 < \alpha < 0,05$.

Thus, the tested model in this research has met the goodness of fit test, and the hypothesis testing can be continued.

- Coefficient of determination (*Adjusted R²*). The coefficient of determination describes how far the independent variables in the model are able to explain the variability in the dependent variables (Ghozali, 2016). The indicator of the coefficient of determination in the *Adjusted R²*. The value of the *Adjusted R²* is 0,492 which means 49 percent of the variation changes of the dependent variables found in the budgetary slack can be explained by the participative budgeting variables which are moderated by CG and THK culture. Meanwhile, the other 51 percent is influenced by other variables which are not included in the research model.
- Hypothesis testing (T-test). For the first hypothesis, the coefficient value of the participative budgeting is -2,2932 with a significance level at $0,000 < 0,05$ which means that if the participative budgeting increases by one percent, then the budgetary slack can decrease by 2,29 percent with an assumption that the other variables remain constant. Thus, it can be stated that the participative variables in budgeting process has a negative and significant influence on the budgetary slack variable.

The second hypothesis (H_2) states that CG moderates the influence of participative budgeting towards budgetary slack. The MRA analysis shows the interaction coefficient between the participative budgeting and CG is at 0,039 with a significance level at $0,001 < 0,05$ which means that CG intensify the influence of the participative budgeting which lower the budgetary slack significantly. As a result, the second hypothesis can be accepted.

The third hypothesis (H_3) states that the THK culture can moderate the influence of participative budgeting towards the budgetary slack. The MRA analysis shows the interaction coefficient between participative budgeting and THK culture is at -0,000004 with a significance level at $1,000 > 0,05$. This means the THK culture shows no influence on the relationship of participative budgeting which can reduce the budgetary slack. Thus, the third hypothesis is rejected.

RESULTS AND DISCUSSION

The agency theory concept explains that the executives (agents) will apply the principle of prudence in determining the budget targets for income and cost efficiently and effectively. Based on the results of analyses above, the t-test shows a negative and significance direction. Accordingly, the first hypothesis stating that participative budgeting influences the budgetary slack can be accepted.

From the results, it can also be inferred that the higher the level of participation from the subordinated in the budgeting process of BPRs in Bali, then the lower the level of budgetary slack will be. The participation of subordinates in budgeting process gives them opportunities to create the budget targets. The results of this research is in line with those of Camman (1976), Merchant (1985), Chow *et al* (1988), Dunk (1993), Supanto (2010), and Apriyandi (2011) which show that participation in budgeting process can reduce budgetary slack.s

GCG is a mechanism which manage the company's governance to be better. GCG can assume the role of a protector of the rights of the stakeholders. By applying the GCG and its principles, namely transparency, accountability, responsibility, independency, and fairness, then the self-centered behaviors of the people who prepare the budget can be minimized.

The results of the interaction test between the participative budgeting and GCG also indicates positive and significance results. Thus, it can be stated that CG can influence the relationship of participative budgeting towards budgetary slack. The results also show that the application of GCG can intensify the behavior of the participative budgeting which can reduce the budgetary slack of the BPRs in Bali. In other words, the higher the application of CG is, the higher the level of tendency will be for the participating managers to reduce the budgetary slack.

In this research, the THK culture is not proven to show influences on the relationship between participative budgeting and budgetary slack. This is because the THK culture is only applied at the surface level. The THK culture has not been able to be measured physically yet because it is merely a perception.

CONCLUSION

Based on the data analysis and discussion above, some conclusions can be drawn as follows:

- The participative budgeting has a negative influence towards the budgetary slack. This means that the higher the participation during the budgeting process in BPRs in Bali, the lower the budgetary slack will be.
- Good Corporate Governance (GCG) can influence the relationship between participative budgeting and budgetary slack. A better application of GCG by BPR management in Bali can reduce the budgetary slack which can be incurred during the participative budgeting process.
- The THK culture does not influence the participative budgeting process and budgetary slack.

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