

ORGANIZATIONAL ETHICAL BEHAVIOR AND CONTROL MECHANISMS IN THE BUDGET PERFORMANCE OF LOCAL GOVERNMENT IN INDONESIA

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ABSTRACT

This study aims to examine the effect of budget participation variable on managerial performance with budget ethics compliance and budget emphasis as moderating variables. This study uses a survey method with questionnaires distributed to 30 regional work units in the Local Government of Ternate City, Maluku, Indonesia. A total of 180 questionnaires were distributed to managers involved in budgeting. In the further data tabulation, only 163 questionnaires were declared eligible to be tested at further stage. Data analysis used is simple linear regression and Moderated Regression Analysis (MRA). The results showed that budgetary participation had a significant influence on managerial performance. In their role as moderating variables, the budget ethics compliance and budget emphasis are empirically able to function as moderating in the effect of budgetary participation on managerial performance. Some theoretical and managerial implications are also presented as a follow-up to the results of the study.

Keywords: Budget Participation, Budget Ethics Compliance, Budget Emphasis, Managerial Performance.

INTRODUCTION

The public sector budget is an instrument of accountability for the management and implementation of programs financed with public money (Lubis 2010; Din, 2017). Budget in public sector organizations is a fairly complicated stage, containing high socio-political nuances (Laupe et al., 2018; Isgiyarta & Yulianto, 2018). One aspect that is the main consideration in the budget is the participation of stakeholders in the planning and implementation process (Kurniawan, 2017). Erez et al. (1985), Kahar et al. (2016) reveal that if employees were involved in budgeting, the performance of employees in realizing the budget could increase. Gul et al. (1995) found that budgetary participation in performance would have a positive effect on organizations which authority was decentralized. Acceptance of goals and increasing employee commitment in setting goals will improve employee performance. Moreover, there are also needs to control mechanisms in budgeting being used as a process of monitoring, evaluating, and providing feedback (Ouchi, 1978; Hakim, 2017). Ouchi (1978) further argues that there are two types of organizational control and behavioral control, involving superiors observing their subordinates in their behavioral activities and results control. The supervisor will observe after the effects of behavior as the output of a productive process. Jermias and Setiawan (2008) show the results control is right to use when the tasks to be carried out are very complex and unstructured. In general the control system moderates the relationship between budget

participation and performance (Jermias and Setiawan, 2008). Specifically, the results show that budget participation has a positive relationship with performance on high job complexity by using outcome controls rather than using behavioral control.

The problems of budgeting process along with its control mechanisms in governmental bodies are relevant to be studied for the development of management accounting, because the budgeting in the public sector has long been considered less efficient and effective both in planning and implementation (Mulyawan, 2018; Wirawan, 2018). Accordingly, this study attempts to examine the influence of procedural factors in budgeting and control mechanisms on managerial performance. Procedural factors here will refer to the behavior factors and the willingness of managers to involve subordinates in the budgeting process. The variables used as proxies are budget participation. The second factor refers to the control mechanism represented by the emphasis of the budget and compliance with budget ethics. In such formulation, both control mechanism factors from budget emphasis and ethical compliance are modeled to have an influence on the relationship between budget participation and managerial performance. This study empirically offers novelty in the context of how budget control mechanisms can be involved in participatory budgeting procedures and processes and how the role of compliance with budget ethics and budget emphasis in moderating the relationship of budget participation, and managerial performance. The main objective of this research is to build a theoretical model to explain the role of compliance with budget and budget emphasis in the relationship of budget participation, and managerial performance, to conduct an empirical model testing. Conceptually, this test is also insightful because the formulated model is synthesized from institutional theory, organizational culture and ethical theory at once. The review of the literature was carried out according to the systematic review process defined by Seuring et al. (2012) and Cerchione et al. (2018) that are well-known in the field of literature reviews to provide a conceptual framework. The results of this study are expected to contribute to the development of studies in the field of management accounting and public sector management.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Ramdeen et al. (2007) stated that budget pressures in performance evaluation can encourage budgetary slack. The main reason for lower-level managers creating slack in their budgets is to create opportunities for them to increase the rewards they will get. Awards received by lower level managers based on the achievement of the budget will create budgetary slack during the participation process (Chow et al. 1988). According to Baiman (1991), participating subordinates will be encouraged to help their superiors by providing information they have so that the budget is more accurate. According to him, subordinates who have specific information about local conditions will report the information to their superiors. Individuals who have a high commitment will prioritize the interests of the organization and try to make the organization more productive and profitable. Ramdeen et al. (2007) assume that lower level managers try to do slack in their budgets if information asymmetry and budget pressures are high. However, Chow et al. (1988) explained that if high budget pressures and information asymmetry are low, agents will have the desire to develop slack, but do not provide security guarantees for their budget. Lower level managers who expect to benefit through their budgetary slack must increase their participation in the budget preparation process (Lukka, 1988). If participation is low, the opportunity for lower managers to create slack in their members will be very small by ignoring the presentation of budget compliance and budget emphasis. Based on the relationship between variables, the hypothesis is formulated as follows:

H1: Budget participation has a positive effect on financial performance.

H2: Budget ethical compliance moderates the relationship between budget participation and managerial performance.

H3: Budget emphasis moderates the relationship between budget participation and managerial performance.

RESEARCH METHOD

The sample selection method used in this research is the purposive sampling method. The population in this study was the Regional Work Unit in the Regional Government of Ternate City which amounted to 42 Regional Work Units, but in this study, only 30 Regional Work Units involve. The Regional Work Unit is a unit of equipment for the government as a budget user. The selection of regional work units is carried out on the grounds that this institution is a government work unit, this means that the institution uses and reports the realization of the budget or as the executor of the budget from the regional government (Regional Regulation No. 11 of 2009). In measuring the Managerial Performance (MP), this study used eight question items, namely planning, investigating, coordinating, evaluating, supervising, staffing, negotiating, and representing. Budget Participation (BP) is measured by 6 question items developed by Milani (1975), and Covaleski et al. (2003). Budget Emphasis (BE) is measured by the instrument adopted from Hopwood (1972), Otley and Fakiolas (2000). Budget Ethics Compliance (EC) is measured using 5 (five) instrument items developed by (De Hoogh and Den Hartog 2008). All items are measured by a 7-point Likert scale with a range of 1 (strongly disagree) to 7 (strongly agree). This study uses multiple linear regression statistical methods for testing the *hypothesis 1*, while for the *second and third hypotheses*, the testing uses the interaction regression or Moderated Regression Analysis (MRA).

RESULTS

Descriptive Statistics

The study was conducted by distributing 180 questionnaires with the questionnaire level of 96.11% (173 questionnaires). After removing 10 incomplete questionnaires, 163 questionnaires were processed further. In terms of gender, the majority of respondents (79.1%) were men, under the age of 30 as many as 126 people (77.3%), most of whom had graduated from master education level (98 people or 60.1%).

Validity and Reliability Testing

Construct	KMO and Bartlett's Test	Coefficient
Budget Participation	0.732	0.851
Budget Ethics Compliance	0.787	0.746
Budget Emphasis	0.874	0.882
Managerial Performance	0.749	0.851

Reliability testing is used to determine the extent to which a measuring device can be trusted or reliable and remains consistent if done twice or more in the same group with the same measuring instrument. Cronbach Alpha test is used to test the reliability of each variable

questionnaire. If the Cronbach Alpha value gets closer to 1, it indicates that the higher the internal consistency is the reliability. In summary, the results of the reliability test are shown in Table 1. The reliability test results show that all reliability coefficient values are greater than 0.5, so all items are declared reliable.

Multicollinearity Testing

The normality test is analyzed by looking the value of the One-Sample probability of Kolmogorov-Smirnov Test alpha greater than 5% (0.05). The results of the Kolmogorov-Smirnov One-sample (KSO) Probability Test were 0.146, and $0.105 > 0.05$, meaning that the data was normally distributed. Multicollinearity test is used to determine whether there is a correlation between independent variables with each other, with the indicators of Tolerance Value > 0.10 and Variance Inflation Factor (VIF) < 10 . The analysis results in Table 2 show that all independent variables do not have multicollinearity problems.

Variable	Tolerance	VIF	Interpretation
Budget Participation	0.893	1.120	Multicollinearity free
Budget Ethics Compliance	0.951	1.051	Multicollinearity free
Moderation 1 (BP*EC)	0.912	1.096	Multicollinearity free
Budget Emphasis	0.952	1.050	Multicollinearity free
Moderation 2 (BP*BE)	0.905	1.105	Multicollinearity free

Hypothesis Testing

For analyzing the degree the model is capable of explaining the variability, the coefficient of determination or the value of R-square is used. Statistical testing results show that the coefficient of determination shown from the R-Square value is 0.148. This means that 14.8% of the dependent variable is managerial performance can be explained by two independent variables namely budget participation, while the remaining 85.2% managerial performance is explained by variables or other causes outside the model.

Variable	Coefficient	t_{count}	Significance level
Constant	4.761		
Budget Participation	0.275	5.281	0.000
R	0.348		
R^2	0.148 ^a		
F-Statistic	27.889		0.000
a. Dependent variable: Managerial performance			

Furthermore, the results show that the positive effect of budget participation on managerial performance is fully proven. The results of regression analysis show that there is a positive influence of budget participation on managerial performance with a significance level below 0.05, which is equal to 0.000. This shows that *hypothesis 1* is accepted, meaning that budget participation has a positive influence on managerial performance.

Variable	Coefficient	t-count	Significance level
Constant	1.961	-	-
Budget Participation	0.124	2.335	0.021
Budget Ethics Compliance	0.423	5.584	0.000
Moderation 1 (BP*EC)	0.028	2.155	0.033
R	0.561	-	-
R ²	0.315	-	-
F. Statistic	24.341	-	0.000
Constant	1.876	-	-
Budget Participation	0.117	2.257	0.031
Budget Emphasis	0.449	6.197	0.018
Moderation 2 (BP*BE)	0.026	1.994	0.048
R	0.577	-	-
R ²	0.333	-	-
F Statistic	26.449	-	0.000

Hypothesis 2 examined the interaction of Budget Participation and Ethical Compliance (BP*EC) to Managerial Performance. In testing *hypothesis 2*, the results reveal that there is a moderating effect of budget emphasis the relationship between budget participation and managerial performance. Statistical results show the coefficient of determination is 0.315, which means that the budget emphasis variable affects managerial performance with variations in changes of 0.167%. In the next test, the interaction testing of budget participation with budget emphasis is carried out, with the test results showing the coefficient of determination to be 31.5%. This means that the budget emphasis together with budget participation is likely able to influence managerial performance.

To obtain the result whether the budget emphasis variable is capable of acting as a moderating variable, it is necessary to pay attention to the equations (1), and (2). Both of these equations are different, namely $\beta_2 \neq 0$ and $\beta_3 \neq 0$. Based on these results, it can be obtained that the variable of budget ethics compliance is pure moderator variables.

Hypothesis 3 analyzes the interaction of budget participation and budget emphasis (BP*BE) on managerial performance. The test results show that the calculated F-value is 26.449 with a significant F of 0.000. Because the F-count value < 0.05 , the multiple linear regression model is feasible to be used to examine the effect of interaction variables of budget participation and budget emphasis on managerial performance. Statistical t-test is done by comparing the results of significance with $\alpha = 0.05$. The level of significance on the one-sided t-test is 0.000 with a positive parameter estimation value of 0.275. Thus, budget participation has a significant positive effect on managerial performance, with a significance value smaller than 0.05. Thus, the *Hypothesis 1* in this study was accepted. Moreover, the value of the one-sided t-test significance level for the budget emphasis interaction variable influences the relationship between budget participation to managerial performance by $0.006 < 0.05$ and the parameter estimation value is positive at 0.026. Thus, budget emphasis has a significant effect in the relationship between budget participation on managerial performance. Thus, the *hypothesis 3* is accepted. In general, the results of the study indicate that if the participation of management and subordinates in the budget preparation will be able to increase managerial performance. These results can be concluded that the budget emphasis variable is a pure moderator variable and is considered capable empirically in bridging the relationship between budget participation on managerial performance.

CONCLUSION

The results of this study indicate that budgetary participation has a significant effect on the performance of local government officials. Moreover, the variable of budget emphasis and ethical compliance are empirically proven to be moderating variables capable of influencing the relationship between budget participation on managerial performance. Based on the results of this study, it is important for each government unit to pay more attention to the role of, and participation of employees in the budgeting process. The greater the level of employee participation in budget preparation will likely increase the employee's performance. The results of this study also contribute to strengthening contingency agency theory where employees given the opportunity to determine budget targets by their superiors will better understand and know the targets. Thus, they will achieve the goals by improving their performance. This study also provides empirical evidence that ethics compliance and budget emphasis reinforces the influence of budget participation with the performance of local government officials.

Theoretically, the results are expected to be useful for the development of similar studies and become a reference in assessing the civil servant work performance as a measure of apparatus performance. Managerially, the practical implication taken from the results of this study is that the leadership of the government work unit in the local government of Ternate City should be able to further increase budget participation by increasing the involvement of all lines of structural officials in the budget preparation process. Public sector officials must understand what factors can motivate them in an effort to increase budget participation with better performance goals. One of the efforts that can be done is by implementing a real reward and punishment system. The limitations of this study lies on its lack consideration of characteristics of budget objectives, namely clarity of budget objectives, budget feedback, budget evaluation, budget goal difficulties as predictors of performance. Hence, subsequent research can add those predictors in examining the performance of local government apparatus.

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