JOURNAL OF APPLIED MANAGERIAL ACCOUNTING
Vol. {7}, No. {2}, {2023}, {274-280}
ISSN: {2548-9917} (online version)

Article History
Received {October, 2023}
Accepted {October, 2023}

Budget Communication, Final Authority, And Negotiation On Budgetary Proposal : An Experimental Study

Maulidah Fitria[1)], Muhammad Syam Kusufi[2)*], and Achdiar Redy Setiawan[2)]
[1]Accounting Department, Politeknik Masamy Internasional, Banyuwangi, East Java, Indonesia
[2]Accounting Department, Economics and Business, Universitas Trunojoyo Madura, East Java, Indonesia
Email : syam.kusufi@trunojoyo.ac.id

ABSTRACT

This study aims to investigate the relation between budget communication, final authority and negotiation on budget setting which analyzed by Agency Theory. This research used 2x3 between subject experimental design of budget communications and final authority treatments. The results of this study show that less slack is created when budget proposal requires a factual assertion, but it's not when manager not requires factual assertion. Meanwhile, in final authority condition, manager creates budget slack more when they have final authority than owner's authority. This study show an evidence that there is no significant interaction between budget communication and final authority in creating budget slack. Additionally, this study finds that negotiation can influence manager's performance although it's measured by budget slack or output of production. Negotiation can reduce budget slack. The performance test (which is measured by ability of manager to make product) show that as a whole is not have difference significantly. Meanwhile, for budget slack show that slack in No Factual Assertion treatment is higher than Factual Assertion treatment.

Keywords: *Participative Budgeting, Budget Communication, Final Authority, Negotiation, Budget Slack, Manager's Performance.*

ABSTRAK

Penelitian ini bertujuan untuk mengivestigasi hubungan antara komunikasi anggaran, otoritas final dan negosiasi pada penyusunan anggaran yang dianalisis dengan menggunakan Teori Keagenan. Penelitian ini menggunakan 2x2 antar subyek desain eksperimental dengan perlakuan komunikasi anggaran dan otoritas final. Hasil dari studi ini menunjukkan bahwa kesenjangan anggaran lebih kecil ketika proposal anggaran disajikan dengan pemeriksaan faktual, namun demikian sebaliknya ketika manajer tidak mensyaratkan adanya pemeriksaan faktual. Sedangkan, pada kondisi otoritas final, manajer akan menciptakan kesenjangan anggaran lebih besar ketika mereka diberikan kewengan otorisasi final dibandingkan jika otoritas finalnya berada pada pemilik. Studi ini menunjukkan bukti bahwa tidak ada hubungan yang signifikan antara komunikasi anggaran dan otoritas final dalam menciptakan kesenjangan anggaran. Ditambah lagi, studi ini menemukan bahwa negosiasi dapat mempengaruhi kinerja manajer meskipun keduanya diukur dengan kesenjangan anggaran atau output produksi. Negosiasi dapat mengurangi kesenjangan anggaran. Uji Performance (yang diukur dengan kemampuan untuk membuat produk) menunjukkan bahwa secara keseluruhan tidak beda signifikan. Sedangkan, untuk kesenjangan anggaran menunjukkan bahwa kesenjangan yang dihasilkan dari tidak ada perlakukan Pemeriksaan Faktual lebih besar dibandingkan dengan yang ada perlakukan Pemeriksaan Faktual.

Kata-kata Kunci: *Penganggaran Partisipasi, Komunikasi Anggaran, Otoritas Final, Negosiasi, Kesenjangan Anggaran, Kinerja Manajer.*

*Corresponding author. E-mail: syam.kusufi@trunojoyo.ac.id

1. INTRODUCTION

Participative budgeting have some benefits which is good to organizaton, one of them is to improve manager's creativity, responsibility, and reach larger goal congruence (Hansen and Mowen, 2009). Besides giving good benefits, the existence of participative budgeting also trigger some problems in budgeting. One of the problems is give opportunity to managers to make diffuseness of budget (Slack). Manager oftentimes submit budget which include slack, that is underestimation of capability production or overestimation at the expense and resource on budget proposal (Dunk and Nouri, 1998). Besides of them, manager can play budgeting games in the effort for the manipulation of goals and information utilize to reach bonus as high as possible. (Komalasari et al, 2003)

In agency theory, the existence of budget participation can decrease information asymmetry between principal and agent so that can improve "honesty" on managerial reporting (Evans *et al* 2001; Rankin *et al* 2008 and Church *et al* 2012). Manager as nearest party with resources, have information which is more than principal (Usman et al, 2012)[1] and unhappily not all manager can communicate their privat information honestly.

There are two parties who will take choice in budget setting. They are manager who will act as agent and owner who will act as supervisor and party. For that, important to know categorically who is have the power to take decision. On the other side, participative budgeting is a negotiaton process between manager and owner (Fisher *et al*, 2000; Komalasari et al. 2003). Owner have a valuable opportunity to get private information from manager. So, at the same time participative budgeting not only give opportunity to owner but also give opportunity for manajer to make budget slack during budgeting to increase the resource allocation (Gallani *et al*, 2015). Most of related studies of budget participation (Waller *et al*, 1998; Rankin *et al*, 2008; Church *et al*, 2012; Gallani *et al*, 2015), set budget *unilaterally.* Though in practice, the process of budget setting in most organization is using pass-through process between superior and subordinat. This process is called "negotiation".

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

2.1. Setting and Incentives

This research provide manager with private information about their own performance capability (from pre-test and training). The dyads set production budget by either (1) a unilateral decision of one party or (2) a process of negotiation between two parties. Our unilateral budget-setting conditions include budgets established by manager and budgets established by owner which have been examined in previous research. Besides it, in negotiation conditions, one party proposes a budget and the other party either agrees to the budget or makes a counter offer. In budgeting process, subject in conflict condition. To creat conflict in this experiment with the following compensation contracts which suitable from previous research in Fisher et al 2000.

2.2. Hypothesis

This study used base assumption in agency theory which expressing that a manager has "private" information about area which is becoming manager or agent responsibility (Baiman, 1990). By using agency framework, participation on budget-setting is enable low manager (subordinat) to explain their private information.

Dunk and Nouri (1988) in their review study on budgetary slack, argue that one of the causes of the slack is asymmetry information. The asymmetry information is a condition where one party has more information than the other superior (Usman et al, 2012). Under ideal conditions, the subordinate have more information than superior. However, in practice, companies implemented the participation of the budget that would allow superior to get private information which it's held by the subordinate (Hansen and Mowen, 2009).

Thus, there will be a transfer information from subordinate to superior, it's called the communication. The communication may be generate a reliable or bias information is depends on how the subordinate frame the the budgeting process. Rankin et al (2008) provide evidence that the budget which provides a factual assertion, create lower slack than doesn't require factual assertion in their budget communication.

H1(a) : When managers have final authority in budget setting, slack will be less when budgeting requires a factual assertion than when it does not requires a factual assertion.

In budget-setting, whether superior or subordinate has the final authority also has an influence on the framing of the subordinates. As has been mentioned in the framework of agency theory, which assumes that the manager and owner have different preferences in the achievement of their objectives. For that, when manager or owner has a power to issue a decision, then it will affect the mindset and attitude of each party.

H1(b) : When budgeting does not require a factual assertion, slack will be less when owners have final authority over budget approval than when managers have final authority.

H1(c) : The decrease in slack associated with budgets requiring a factual assertion will be less when owners have final authority over budget approval than when managers have final authority.

Previous studies related to budget participation have a lot of support for the allegations stating that the budget participation positive effect on the budget slack with or without the moderating variables (Waller et al, 1998; Rankin et al, 2008; Church et al, 2012; and Gallani et al 2015). These studies defined condition that the budget set unilaterally by manager or owner. When the superior has the final authority to set final budget, the tendency is subordinate does not approve the budget at a superior level unless they are confident to achieve it.

H2 : The amount of budget negotiations when the managers make the initial offer is lower than when the owner who made the initial offer.

Knowingly or not, the superior know that the subordinate has the economic incentive to do anything that is not useful (disutility) than helpful behavior (utility) in the work activity (Fessler, 2003). This study focused on the slack caused by the deliberate underestimation of revenues and production capabilities to accomplish the task budgeted (Dunk and Nouri, 1998). The process of setting the budget used is negotiationed and determined unilaterally by one party (Owner or Manager). The research hypothesis related to the final budget is as follows:

H3(a) : When owners have final authority, the budget which set by negotiation is lower than when owners unilaterally set the budget.

H3(b) : When managers have final authority, the budget which is set by negotiation is higher than when managers set it unilaterally.

When owner set a budget unilaterally (non-negotiation), they do not have the opportunity to obtain information from managers on their performance capabilities. This is reflected in the phenomenon that budgets tend to be set on a subordinate's performance capabilities, so that commitments subordinate to the budget is low. The direct impact of the decline in organizational commitment is the decline of budgetary slack and subordinate performance than when the budget is set through negotiations.

H4(a) : Slack when the owners have final authority in negotiations is smaller than when budget set in non negotiation.

H4(b) : The manager's performance is higher when the owner has the final authority in negotiations than when managers set budget in non-negotiation.

Viewed from the perspective of the agency, this information asymmetry motivate subordinates to provide misleading information (bias) of their production capabilities.

H5 : There are differences in the amount of the budget gap created by a manager in a state of no factual assertion, and the conditions there are factual assertion.

3. EXPERIMENTAL DESIGN

3.1. Subjects and Experimental Task

Subjects for the budgeting experiment were 138 undergraduate student in Acconting of Trunojoyo Madura University who have done or enrolled in management accounting, and they were divided in eight treatrments based on class availability. Participants act as manager and owner who separated in different class. Those conditions were (1) Manager unilaterally set budget, (2) Owner unilaterally set budget (3) a negotiation process where owner have final authority (4) a negotiation process where manager manager have final authority. The research design for this study is adapted from setting that used in several study in budgetting and negotiation (Rankin et al, 2008 and Fisher et al, 2000). But, for budget-task this study is adapted from Nugrahani and Sugiri (2004)

3.2. Measured

FORECAST is the manager's performance estimate of the item they could correctly made in four minutes. Subjects made this estimate after production training session. BID and COUNTER are the initial budget proposal and the initial counteroffer, respectively made in the negotiation process. BID is first offer about production target in four-minutes which is made by parties who have final authority. COUNTER is counteroffer from parties who got first counter. FINAL BUDGET is the last target which is setting by unilateral or final decision about target in four-minutes. BUDGET SLACK is measured as FORECAST minus BUDGET. PERFORM is the number of plane items manager correctly made in the work session.

4. RESULTS

4.1. Effect of Budget Communication

H1(a) predict that when manager holds authority over the budget, slack will be less when communication requires a factual assertion than when communication does not requires a factual assertion. Mean slack in the Manager's Authority/No Factual Assertion treatment is (-3.6) and (-0.3) in the Manager's Authority/Factual Assertion treatment. The null hypothesis of equal mean slack under both forms of budget communication treatments is rejected in favor of less slack in the Manager Authority/Factual Assertion treatment ($t= 6.325$ and $p = 0.000$). It means that the hypothesis 1(a) is supported.

4.2. Effect of Budget Approval Authority

H1(b) maintains that when budget communication does not require a factual assertion, slack will be less in owner has final authority treatments than when the manager has final authority. The independent t-test results showed that mean slack in Manager's Authority/No Factual Assertion is (-3.6) but only (-0.909) in the Owner Authority/No Factual Assertion treatment. It means that budgetary slack differ significantly between two budget communication conditions ($t= 5.358$, $p <0.000$). This results showed that when Owner has final authority over budget was less then when manager has final authority. This finding supports H1(b).

4.3. Interaction between Budget Authority and Budget Communication

Hypothesis 1(c) predicts that the decrease in slack associated with budgets requiring a factual assertion will be less when owners have final authority over budget approval than when managers have final authority. In manager authority treatments, slack decrease from (-3.6) when communication does not require a factual assertion and (-0.3) when a factual assertion is required.

Conversely, in the owner authority treatments, slack decrease from (-0.09) when no factual assertion and (3.25) when factual assertion. The results of an ANOVA analysis, indicate an insignificant interaction between Final Authority and Budget Communication ($t= 0.001$, $p <0.979$) although the results showed that main effect either Final Authority or Budget Communication have a significant effect to budgetary slack (FA : $t= 20.872$, $p<0.000$) , BC : $t= 18.472$, $p<0.000$). Therefore, the null hypothesis of no difference is rejected in favor of a greater difference in the Manager Authority treatments ($t= 2.4$, $p<0.029$). This finding does not support H1(b) altough it is consistent with the idea that formal authority has a crowding effect on the intrinsic motivation to behave honestly.

4.4. Effect of Budget Authority in Negotiation

Hypothesis 2 predicts that the amount of the final budget when the manager makes the initial offer is lower than when the Owner who made the initial offer. In this study, researchers conditioned the party who has the final authority are parties to the initial offer. The independent t-test results showed that there are significant differences between the manager's budget and the owner's budget in negotiation treatments either in No Factual Assertion or Factual Assertion. In factual assertion conditions ($t= 2.002$, $p<0.061$) and No Factual Assertion ($t= 2.212$, $p<0.040$). This results gave an evidence that mean owner's budget was greater than manager's budget. This finding supports H2.

4.5. The Effect of Negotiation in Budget Final

Hypothesis 3a states that budgets set through a negotistion process where owners have final authority will be lower than budgets set unilaterally by owners. Comparing owner's initial budget negotiation proposals to the budgets owners set unilaterally provides evidence that BUDGET is 6.6 when owners unilaterally set it, and BID is 8.8 when owners make the initial budget proposal and have final authority in factual assertion conditions. This difference is not significant ($t= 1.730$, $p < 0.118$) and in No Factual Assertion treatments there is not significant differences between BID and BUDGET ($t= 2.236$, $p < 0.05$). Thus, H3(b) predict that budgets set through a negotistion process where managers have final authority will be greater than budgets set unilaterally by managers. The independent t-test results showed that there are significant differences between BID and BUDGET either in No Factual Assertion or Factual Assertion. In factual assertion treatments ($t= -3.515$, $p<0.007$) and No Factual Assertion ($t= -2.882$, $p<0.018$).

In the other several test of this hypothesis showed that final budget had significantly differ between two budget-setting conditions. First, when owner have final authority, in factual assertion conditions ($t= -1.678$, $p<0.111$) and No Factual Assertion ($t= -3.648$, $p< 0.002$). Second, when manager have final authority, in factual assertion ($t= -1.852$, $p< 0.08$) and No Factual Assertion ($t= 2.973$, $p< 0.008$). Generally, this findings support H3(a) and H3(b).

4.6. The Effect of Negotiation in Performance

Hypothesis 4(a) predict that when owners have final authority, negotiations slack is smaller than when budget set unilaterally (non negotiation). The results of independent t-test showed that slack in negotiation did not significantly differ with slack non negotiation only on the factual assertion treatment ($t= 1.730$, $p<0.118$). That results support Hypothesis 4(a).

Hypothesis 4(b) predicts that manager's performance when owner has the final authority in negotiations is higher than when managers set budget unilaterally. The t-test results showed that the performance did not significantly differ between two budget-setting conditions or for all treatments. First, when manager has final authority: (1) Factual Assertion ($t= -0.986$, $p< 0.343$) and (2) No Factual Assertion ($t= -1.455$, $p< 0.163$). Second, when owner has final authority; Factual Assertion ($t= -0.825$, $p< 0.335$) and No Factual Assertion ($t= 2.209$, $p< 0.043$). These results do not support the hypothesis 4(b).

4.7. Budgetary Slack on Budget Communications

Based on hypothesis test analysis, it is known that it is basically the performance of managers have significant differences when manipulation of the communications budget. The results show that the value of F table 8.873 with a significance of 0.000 (far below 0.05). It can be concluded that the hypothesis 5a supported and significantly supporting research Fisher et al (2000) and Komalasari et al (2003).

5. CONCLUSION

The results of this study, first this study provides evidence that less slack is created in budget proposal requires a factual assertion, but it's not when manager does not requires factual assertion. Support for this hypothesis would provide evidence that honesty serves as an intrinsic control on slack creation (Rankin et al, 2008). Meanwhile, in final authority condition, manager creates budget slack more when they have final authority than owner's authority. this result is consistent with the results from Rankin et al (2008) and Fisher et al (2000) who found formal controls such as the superiors imposing their final authority over budget negotiations reduce the subordinate's willingness to put effort into a productive task. Additionally, this study show an evidence that there is no significant interaction between budget communication and final authority in creating budget slack.

Second, this study finds that negotiation can influence manager's performance although it's measured by budget slack or output of production. This results suggest that when evaluating different budget-setting processes, companies should not base their decisions solely on budgetary slack because slack is only one economic consequence of budget setting process (Fisher et al, 2000). Third, this study also finds that the performance did not significantly differ between negotiation groups and non negotiation groups.

6. REFERENCES

Hansen, Don R., and *Mowen,* Maryanne. (*2009*). *Akuntansi Manajerial,* Buku 1 (Ed. Ke-8.). Jakarta: Salemba Empat.

Dunk, A., & *Nouri*, H. (*1998*). Antecedents of budgetary slack: A literature review and synthesis. *Journal of Accounting Literature*, 17, *72–96.*

Komalasari, P.T., J.R. Joesoef, & M, Nashih. (2003). Pengaruh Negosiasi dan Asimetri Informasi terhadap Budget Outcomes: Sebuah Eksperimen. *Proceeding, Symposium Nasional Akuntansi VI. Surabaya* (16-17 Oktober). Hlm. 994 – 1007.

Evans, J. H., III, Hannan, R. L., Krishnan, R., & Moser, D. V. (2001). Honesty in managerial reporting. *The Accounting Review*, 76 (4), 537-559.

Church, B. K., Hannan, R. L., & Kuang, X. (2012). Shared interest and honesty in budget reporting. *Accounting, Organizations and Society*, 37 (3), 155-167

Rankin, F., S. Schwartz., and R. Young. (2008). The Effects of Honesty and Superior Authority on Budget Proposals. *The Accounting Review*, 83 (4): 1083-1099.

Fisher, J.G., Frederickson, J.R. and Peffer, S.A. (2000). Budgeting: an experimental investigation of the effects of negotiation. *The Accounting Review*, 75, 93–114.

Usman, E., & Paranoan, S. (2013). Anggaran Partisipatif dalam Menunjang Kinerja Aparatur Pemerintah Daerah. *Jurnal Akuntansi Multiparadigma*, 4 (1), 1–164.

Gallani, S., Krishnan., R., Marinich E.J., and Shields M.D. (2019). Budgeting, Psychological Contracts, and Budgetary Misreporting. Management Science, INFORMS, vol. 67(6), pages 2924-2945, June

Waller, W.S. (1988). Slack in participative budgeting: The joint effect of a truth-inducing pay scheme and risk preferences. Accounting, Organizations and Society, 13 (1), 87-98.

Baiman, Stanley, 1990. Agency research in managerial accounting: A second look. Accounting, Organizations and Society., 15 (4), 341-371.

Fessler, N.J. (2003). Experimental Evidence on the Links among Monetary Incentives, Task Attractiveness, and Task Performance. Journal of Management Accounting Research. 15 (1). 161-176.

Nugrahani, T.S., and Sugiri, Slamet. (2004). Pengaruh Reputasi, Etika, dan Self Esteem Pada Budgeting Slack SNA Proceeding VII, 399-419.