

## **CHAPTER 1**

### **INTRODUCTION**

#### **1.1 Study Background**

The management process of a government institution is started by composing a budget. Operationally, a local government budget is composed by executive who will then ask for approval from the legislative member (i.e. known as Dewan Perwakilan Rakyat Daerah / DPRD). According to Law No. 32 of 2004 concerning Regional Government and Law No. 33 of 2004 concerning Financial Balance between the Central and Regional Governments has changed the accountability or accountability of the regional government from vertical accountability (to the central government) to horizontal accountability (to the public through the DPRD), therefore local governments are required to be able to manage their regional finances well and with accountability, so that they can be accountable to the community. In the process of managing government finances, the budget is one of the important problems. Through the budget, it will be known how much the ability of the government to carry out various government affairs that are its authority. In local government, that budget is shaped of The Regional Budget (i.e. known as anggaran pendapatan dan belanja daerah or APBD) is used as a tool to determine the amount of income and expenditure, to help in development planning and decision making, and the basis for authorizing future expenditure. The budget is also used as a

standard measurement for performance evaluation and coordination tools for all activities in the work unit. Ferawati (2015) with regional autonomy, more regional authority big to manage and manage the household itself is expected to be able to provide flexibility to the regions to develop their regions through efforts that can increase the active participation of the society.

Regional Financial Management consists of all activities that include planning, implementation, administration, reporting, accountability, and regional financial supervision. In its implementation, the government has established Minister of Home Affairs Regulation (i.e. known as Permendagri) Number 59 of 2007 as a guideline in implementing, administering and reporting finance of APBD including accounting policies. Based on Permendagri Number 59 of 2007 Article 265 paragraphs (1), each Work Unit Regional Devices (SKPD) must compile and report accountability periodic implementation of APBD. One of the regional autonomy policies for dealing with budgets is budgeting with participatory methods, i.e. by involving each SKPD to submit a budget, preparing the budget and implementing budgeting (Husain, 2011).

According to Mardiasmo (2009), the government budget is a political document/contract between the government and the DPRD for the future. In agency theory, the government can be formulated as an agent and the community in this case represented by the DPRD is interpreted as principal. The relationship between agents and principals is expected to

facilitate the budget monitoring process so that dysfunctional behaviors do not occur, because the budget in government is a manifestation of development to achieve public welfare. Anthony and Govindarajan (2007) also stated that budget is a very important tool in planning and effective short-term controlling in an organization.

Budget is a plan that is written containing activities in the organization, which are expressed in a quantitative way and are used in units of money in a certain period (Purmita and Adi Erawati, 2014). Whereas according to Harefa (2008) in Pello (2014), the budget is a management tool used to communicate all management plans in an organization, allocate resources and coordinate activities. Because this budget will later become a guideline in carrying out activities, this budget must be prepared as well as possible so that all activities can be carried out properly.

Budget is not only important for private companies but also important in implementing government programs. The budget is a statement about the estimated performance to be achieved during a certain period of time expressed in financial measures. In public sector organizations, budgeting is a political process. In the private sector, budget is part of a company secret that is closed to the public, on the contrary in the public sector, the budget must be informed to the public to be criticized, discussed and given input. The public sector budget is an instrument of accountability

for managing public funds and implementing programs financed by public money (Mardiasmo, 2009).

According to Priyetno (2018), budgetary slack is an action where an agent estimates lower income and higher costs than the actual target can be achieved when given the opportunity to choose work standards so that they can improve their performance.

Many researchers have conducted research on factors that can lead to budget slack. Putra et al. (2015) found that there was a significant and positive effect of Budget Participation on the Budget Slack, Asymmetry Information had a significant and positive influence on the Budget Slack and Budget Emphasis had a significant and positive influence on the Budget Slack. While in the study of Aprianti et al. (2014) it is found that there was a positive and significant influence of budgetary participation on the budget slack. There is a positive and significant interaction effect between the emphasis of the budget on the relationship between budget participation and the budget slack. There is a negative and significant interaction effect between organizational commitment on the relationship between budget participation and the budget slack.

Starting with this condition, the public sector began to implement a budgeting system that could overcome the budgetary slack problem, namely the budget for participation, where employers must be involved in budgeting, budget approval and also following the results of budget

implementation so that realistic budgets were created, because without participation active from superiors, then subordinates tend to set a budget that is easily achieved by doing budgetary slack. Therefore, much subordinate participation in the budgeting process will provide greater opportunities for subordinates to carry out budgetary slack and vice versa when subordinate participation is little, subordinate expectations for budgetary slack are also low. Then there is a need to limit participation, of subordinates in preparing the budget according to proportional or predetermined plans and strategies so as to reduce the emergence of budgetary slack.

Based on agency theory, determining the income target in budgeting has a tendency to be budgeted lower than the maximum capability that should be achieved. This is done so that the budget target will be easily achieved which can be seen in the achievement of budget realization, which tends to be greater than the target. Unlike income, spending has a tendency to be budgeted higher than it should be. So that the realization of spending will be lower than the budget. This tendency is an indication of the occurrence of budgetary slack (Irfan, Santoso, & Effendi, 2016). The Regional Government Work Unit (i.e. known as Satuan Kerja Perangkat Daerah or SKPD) of the City government and Seluma district in Bengkulu, indications of budgetary slack can be seen from the performance reports of government agencies (i.e. known as Laporan Kinerja Instansi Pemerintah or LKIP) in the form of budget realization reports (i.e. known as Laporan

Realisasi Anggaran or LRA) in each SKPD through the Bengkulu Province website. For example, some LRAs from SKPD whose reports are published through the website indicate the occurrence of budgetary slack. It can be seen from the realization of revenues that exceed the budget, and the realization of expenses that are lower than the budget. The following is a summary of the LRA from the transportation office published on the website of the Bengkulu City Government.

**Table 1.1**

**LRA Summary of Transportation of Service of Bengkulu City**

No	Budget details	Regional Revenue and Expenditure Budget	Budget Realization	%
1	Income	Rp 16.169.314.000,00	Rp 22. 313.317.339,00	138
2	Indirect Expenditures	Rp. 8.201.860.339,00	Rp 7.199.444.520,000	87,8
3	Direct Expenditures	Rp 14.111.457.000,00	Rp 10.001.241.000,000	70.9

Source: <https://ppid.bengkuluprov.go.id>

Based on the table above, it can be seen that transportation agency revenues are realized at 138% which exceeds the budgeted target. While expenditure is intended for personnel expenditure and expenditure on goods and services, either direct or indirect expenditure is realized below the budgeted target. The tendency to reduce income and increase this burden is an indication of budgetary slack.

Participation in budgeting will give the agent an opportunity to determine how the budget will be arranged in accordance with the budget target in the section or each division. Agents participate in the budgeting process because of they have sufficient information to predict the future so their involvement is expected to reduce the tendency of individuals to do a budget slack. But on the other hand, participation in budgeting can provide an opportunity for agents to determine the budget plan where this condition can be used negatively so it can actually create slack in the budget (Husain, 2011).

One condition that can cause a budget slack is the existence of information asymmetry, meaning that if a lower or middle manager provides biased information to top managers in the budgeting process, it will affect the occurrence of budget slack. In the study of Putra et al. (2015), it is stated that one of the causes of the emergence of a budget slack is asymmetry information towards organization. The more biased information provided by lower and middle managers to top managers will affect the ability of top managers in determining the budget so that it can lead to budget slack.

A good budget is a budget that is not too low and not too high. The ideal budget is a budget that is challenging but achievable, so that progress will always occur in community development. Another factor that is considered to be the trigger for the emergence of budgetary slack is the budget emphasis. This might happen if the performance evaluation of

subordinates is largely determined by the budget that has been prepared, then subordinates will try to improve their performance by making a budget that is easy to achieve in this case by doing budgetary slack. It can cause subordinates tend to loosen the budget arranged so that the budget is easily achieved (Kusniawati and Lahaya, 2017). The emphasis of this budget in regional government is one of the factors that enable the budget slack to occur. Because if the burden of the area is too high while the income is just ordinary then the possibility of the slack becomes very high.

Organizational commitment shows a strong belief and support for the values and goals to be achieved by the organization. Managers who have a high level of organizational commitment will have a positive outlook and try to do their best for the sake of the organization (Luthans, 2015). With the existence of high commitment, the possibility of a budget slack can be avoided. Contrarily, individuals with low commitment will attach importance to themselves or their groups. If the individual does not have the desire to make the organization a better direction, so the possibility of a budget slack in budgeting will be greater.

Based on the previous research, this study is a replication of the research of Putra et al. (2015) by adding variable organizational commitment as a moderating variable referring to the study of Aprianti et al. (2014). It is consistent with the opinion of Falikhatun (2007), which states that differences in research results can be resolved through a contingency approach. The contingency approach allows other variables



act as moderating variables that influence the relationship of participation in budgeting.

Based on the description, the researcher in this study took the title “The effect of Budget Participation and Budget Emphasis on Budget Slack with Organizational Commitment as a Moderating Variable in Local Government Agencies”. The researcher conducted a study on Regional Work Unit (SKPD) of Bengkulu City and Seluma Districts as the executive who are actively involved in budgeting from planning to reporting. In addition, the researcher wanted to know the factors that cause budgetary slack more deeply at SKPD Bengkulu City Government in connection with the background described.

## **1.2 Research Problems**

1. Does the budget participation have any effect on the creation of budgetary slack?
2. Does the budget emphasis have any effect on the creation of budgetary slack?
3. Does the organizational commitment weaken the relationship between budget participation and budgetary slack?
4. Does the organizational commitment weaken the relationship between budget emphasis and budgetary slack?

### **1.3 Research Objectives**

1. To investigate and analyze the effect of budget participation on the emergence of budgetary slack
2. To investigate and analyze the effect of budget emphasis on the emergence of budgetary slack
3. To investigate and analyze the effect of organization commitment in weakening the relationship between budget participation to the budgetary slack
4. To investigate and analyze the effect of organization commitment in weakening the relationship between budget emphasis to the budgetary slack

### **1.4 Benefit of the Research**

1. The result of this study is expected to be used as a consideration of the management in the government to achieve an effective budget and provide input in government activity planning activities.
2. To give contribution for the development of managerial accounting, specifically about the relationship of budget slack toward participative budgeting, budget emphasis, and organization commitment.
3. To give practical contribution for the management of the company to make policy about the budget.