



# The impact of participation in strategic planning on managers' creation of budgetary slack: The mediating role of autonomous motivation and affective organisational commitment

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## ABSTRACT

This study investigates the impact of participative strategic planning on managers' creation of budgetary slack. Specifically, we draw on self-determination and organisational commitment theory to examine whether and how the degree of managerial participation in strategic planning relates to the creation of budgetary slack. The hypotheses are empirically tested with survey data obtained from 247 managers in a cross-section of West-European organisations. The results from a structural equation model, with controls for budget participation and slack detection, suggest that increased participation in strategic planning leads to lower budgetary slack creation through the suggested path of heightened affective organisational commitment. In addition, the results indicate that budget participation decreases the creation of budgetary slack through the mediating effect of autonomous budget motivation, suggesting that both elements of the organisational planning process are related to the creation of budgetary slack. Our study contributes to the growing research exploring the interface between accounting and strategy by recognizing the importance of participative strategic planning for understanding managers' creation of budgetary slack.

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## 1. Introduction

Budgetary slack, defined as the deliberate incorporation of excess resources in the budget that make the budget easier to attain (Merchant, 1985), is one of the most investigated budgeting outcomes. Not only does evidence indicate that there is considerable budgetary slack in organisations (e.g. Merchant, 1985; Schoute and Wiersma, 2007), it also remains one of the primary controversial, unsolved issues in budgetary control. There is a considerable literature that discusses possible antecedents of budgetary slack (for an overview, see Derfuss, 2012; Dunk and Nouri, 1998). The majority of this prior literature investigated the effect of budget participation (BP) on the creation of budgetary slack. These empirical studies, however, have resulted in contradictory findings. BP seems a necessary but not sufficient explanation for budgetary slack creation,

which establishes a need to identify and test the effect of additional explanatory variables (Webb, 2001).

This study focuses on managers' *participation in strategic planning* (PSP) as an additional explanation for the creation of budgetary slack. The identification of PSP as a possible antecedent of budgetary slack creation is based on the fact that the budget is an indistinguishable part of an organisation's planning process (e.g. Covaleski et al., 2003; Hansen et al., 2003; Merchant and Van der Stede, 2011). This planning process not only includes budgeting but also strategic planning (e.g. Frezatti et al., 2011). Focus in extant research on a manager's immediate budget setting and BP has neglected the possible effect of strategic planning on budgetary slack creation. This omission may be significant as it may, at least partially, explain the inconsistencies in the research findings concerning the effect of BP on managers' budgetary slack creation. This research aims to extend prior research's focus by studying the effect of strategic planning on budgetary slack creation, over and beyond BP's effect in order to capture the whole planning process and as such further our understanding of the antecedents of budgetary slack creation. In particular, as recent work on strategic manage-

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ment (e.g. Floyd and Wooldridge, 2000; Kaplan and Norton, 2001) suggests that strategy should be planned in a *participative* way, this study aims to clarify whether and how PSP relates to the creation of budgetary slack.

As understanding managerial behaviour requires insights from both psychology-based and economic-based theories, we follow Covaleski et al.'s (2003) suggestion and adopt a psychology-based management accounting research approach. More specifically, we use insights from organisational commitment and self-determination theory (SDT) to broaden our understanding of whether and how PSP relates to budgetary slack. To test our hypotheses, we conducted a survey which was completed by 247 managers from a cross-section of West-European organisations.

The contribution of this paper to management accounting research is threefold. First, our study results contribute to the budgetary slack literature by demonstrating that PSP reduces the amount of budgetary slack created through enhanced affective organisational commitment, after controlling for the effect of BP and slack detection. As such, we deepen our understanding of the factors that drive budgetary slack. Second, we show that BP also decreases the creation of budgetary slack through heightened autonomous budget motivation. Taken together, in order to understand the creation of budgetary slack in a specific situation, we should take into account both the level of BP and PSP. Both elements are part of an organisation's planning process and are related to budgetary slack creation, albeit through a different path. Third, our study extends the line of research on the interface between accounting and strategy (Dent, 1990; Langfield-Smith, 1997) by focusing on the relationship between the level of PSP and the creation of budgetary slack. Surprisingly, few management accounting research has been published on PSP despite it being of interest in the academic and professional literature in recent years (Kaplan and Norton, 2008; Wooldridge et al., 2008). In addition to the contributions to management accounting research, this study also has the potential to inform the practice of management accounting. In particular, our results demonstrate the importance of personal variables such as affective organisational commitment and autonomous motivation to understand managers' budgeting behaviour. Indeed, it are not the formal management control systems in itself but it are their effects on these personal variables that are primordial to understand managers' budgetary slack creation. Moreover, our study gives practitioners an understanding of how budgeting and strategy may interact. Specifically, we show that the way managers are involved in the strategy process determines their budgetary slack creation. When trying to influence subordinate managers' budgeting behaviour, top management should hence take a holistic approach and consider both elements of the planning process.

The remainder of this study is organised as follows. Section 2 provides the theoretical background of the constructs used in our research model and develops the hypotheses. Section 3 describes our research method, and Section 4 presents the results of the analysis of our survey data. In Section 5, we summarise the conclusions of our research, discuss the limitations, and suggest some fruitful directions for future research.

## 2. Theoretical background and hypothesis development

### 2.1. Managers' creation of budgetary slack

The traditional concern is that managers have an incentive to create budgetary slack by withholding or misrepresenting their private information in an attempt to control for resources, to achieve personal aspirations, or in order to maximise the expected rewards dependent upon budget attainment (Dunk, 1993; Nouri, 1994).

Consequently, a manager's budget demand not necessarily reflects real organisational necessities (Hopwood, 1974).<sup>1</sup>

The majority of slack-related studies have focused on BP as the main explanation for the creation of budgetary slack (e.g. Merchant, 1985; Nouri and Parker, 1996; Onsi, 1973). BP refers to "a process in which the subordinate is involved in, and has influence over, the determination of his budget" (Anthony and Govindarajan, 2007; p. 380). There is, however, little consistent evidence on the effect of BP on the creation of budgetary slack. While some studies report that the relationship is negative (Dunk, 1993; Merchant, 1985; Onsi, 1973), others report a positive relationship (Lowe and Shaw, 1968; Lukka, 1988) or an insignificant one (Collins, 1978).

These mixed results have led to the use of other approaches such as agency models (e.g. Young, 1985) and the use of contingency factors to predict the creation of budgetary slack (for an overview, see Derfuss, 2012; Dunk and Nouri, 1998). Although these approaches have helped gain insight into the creation of budgetary slack, much remains unexplained, establishing the need to identify and test the effect of additional explanatory variables (Webb, 2001; Yuen, 2004). Such an additional explanation suggested by prior budgeting research is the organisation's strategy (e.g. Merchant and Manzoni, 1989; Van der Stede, 2000, 2001) as research increasingly acknowledges both budgeting and strategy as parts of the organisational planning process (e.g. Cadez and Guilding, 2008; Frezatti et al., 2011). Whereas prior empirical studies incorporating strategy in budgetary slack research have focused on the effect of generic strategies<sup>2</sup> (Derfuss, 2012; Van der Stede, 2000, 2001), we focus on the effect of PSP.

### 2.2. Participation in strategic planning and its relationship with budgetary slack

Strategy, defined as 'the determination of the basic long-term goals and objectives of an enterprise, and the adoption of courses of action [...] necessary for carrying out these goals' (Chandler, 1962; p. 13) was traditionally treated as a dichotomy: strategy planning was the sole responsibility of top management and strategy implementation the task of all other managerial levels (e.g. Ansoff, 1965; Anthony, 1965). This traditional division of work was challenged as environmental uncertainty increased in recent decades: we have observed a shift in focus in the strategic management literature from top management to other managerial levels in the organisation. We may even say that there is currently a widespread feeling that top management is no longer in a position to make strategic decisions on its own. Recent work on strategic management (e.g. Floyd and Wooldridge, 2000; Kaplan and Norton, 2001, 2008) therefore suggests that in today's business environment, strategy should be planned in a *participative* way.

Although there is strong theoretical and empirical support for a positive relationship between PSP and organisational performance (Bourgeois and Brodwin, 1984; Wooldridge and Floyd, 1990), prior literature is less clear on the potential impact of PSP on budgetary slack. First, PSP can be argued to decrease budgetary slack creation. One of the main reasons why managers create slack is to protect themselves and the organisation's core from uncertainty (Cyert and March, 1963). PSP can lower the uncertainty experienced (and,

<sup>1</sup> We recognize that the creation of budgetary slack in itself is not undesirable *per se* (e.g. Davila and Wouters, 2005; Marginson and Ogden, 2005; Van der Stede, 2000) and that it is only detrimental to the organisation to the extent that it results in the expropriation of resources (Church et al., 2012). Judging the (un) desirability of budgetary slack, however, goes beyond the scope of this paper.

<sup>2</sup> We use the phrase "generic strategies" to refer to Porter's distinction between three types of strategies: low cost, differentiation, and focus. In particular, "generic" reflects the choices companies make regarding both the type of competitive advantage (low cost or differentiation) and the scope (narrow or industry-wide focus).

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