

**Organizational, cultural and religious factors of
budgetary slack creation: Empirical evidence from
Malaysia**

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Our study examined the determinants of propensity for slack creation from three perspectives: organizational, cultural and religious perspectives. From the organizational perspective, we examined three variables; budget emphasis, participation and the availability of a slack detection system. From the cultural perspective, we used Hofstede's national cultural value of "Individualism" to examine budget slack creation. Finally, given that budget slack creation is an ethical issue, we examined if religion and religiosity affect slack creation. Data was collected using a questionnaire survey and personal interviews. We sent questionnaires to 91 managers of a Malaysian based Korean company. Information from the company's annual report were also obtained. The results of the study revealed that budgetary participation and the emphasis on meeting budget targets influence budgetary slack creation. However, we found no evidence to support that national culture (Individualism), the presence of a slack detection system, and religion influence a manager's propensity to create slack. Possible reasons for the findings are also discussed.

Field of Research: Accounting (Managerial Accounting)

1. Introduction

Budgetary slack is the difference between the stated budgets and an honest budgetary prediction (Young, 1985; Waller, 1988; Chow et al., 1996; Douglas and Wier, 2000). Lukka (1988) describes budgetary slack as 'budgetary biases', or an overestimate of the costs and underestimates of the income. This view upholds that managers create slack to protect themselves against unforeseen contingencies and improve the probability that budget targets will be met (Stede, 2000).

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Organizational behaviorists regard slack creation as a defensive, tactical response to deceptive behavior (Bourgeois, 1981). Economists argue that slack creation leads to inefficiency and wastage of resources (Williamson, 1964), while advocates of agency theory associate slack creation with the self-interest behavior (Cyert and March, 1963). Prior studies have reported that slack creation results in the misallocation of firms' resources, biased performance evaluations and low efforts by managers (Lowe and Shaw, 1968; Kren and Liao, 1988; Dunk and Nouri, 1998). However, Stede (2000) reported that the existence of slack influences firms' competitive strategy and past performance. Similarly, Davila and Wouters (2004) argue that slack is necessary as to prevent managers from engaging in other dysfunctional behavior, such as having a short-term orientation. Accordingly, the plausible explanation on the existence of budgetary slack is somewhat questionable. However, its detrimental consequences on organizational goals are evident if the slack is created to fulfill an individual's interest.

Objectives of the Study

Our study examines the propensity for slack creation of a large Malaysian based Korean company from three different perspectives: the organizational, cultural and religious perspectives. Specifically, our study investigates how budgetary emphasis, budgetary participation, availability of slack detection, individualism and religion influence the creation of budgetary slack. Our study is significant for several reasons. First, we reexamine the issue of budgetary slack by incorporating all the variables adopted in prior studies to the sample in Malaysia. Secondly, we explore both quantitative and qualitative data. Thirdly, prior studies examining the determinants of budget slack creation have not investigated religion as a variable that may affect budgetary behaviour.

Sulaiman (1998) notes that religion exerts a profound influence on many aspects of human life and personality. Accordingly, a person's religious affiliation may influence the manner in which accounting is practised. Thus, by including religion as a variable, we are investigating the multiple sources of accountability pressures experienced by managers when setting budgets. Hence, the focus on religion and its impact on budget slack creation will contribute to the literature on culture's influence on management accounting practices.

The remainder of the paper is structured as follows. Section 2 discusses the literature review and the formulation of the hypotheses of interest. Section 3 explicates the research methodology while section 4 presents the results and discussions. Section 5 concludes with the limitations of the study and suggestions for future research.

2. Literature Review and Hypotheses Development

Budgetary slack creation may be influenced by the administrative organizational settings including budget emphasis, budget participation, availability of detection, and the degree of predictability in the organization (Merchant, 1985; Lal et al., 1996). Other variables that may also influence slack creation are more towards behavioral and ethical perspectives such as individual's moral philosophy (Douglas and Wier, 2000), ethical ideology (Stevens, 2002; Fisher et al. 2002) and managers' reputation (Webb, 2002). Additionally, culture is also another important variable that may explain the creation of slack (Ueno and Sekaran, 1992; Chow et al., 1996; Tsui, 2001).

Budget emphasis

Stede (2000) defines a rigid budgetary control style or budget emphasis as one that is heavily dependent on budgetary information as a tool to evaluate employees' performances. Accordingly, managers are held fully accountable for their performance as measured by the budget. As such, their compensation scheme and career prospects may be affected if they are unable to meet the budget targets (Merchant and Manzoni, 1989). From this perspective, one can expect that the propensity to create budgetary slack increases with the rigid budgetary control style (e.g. Merchant, 1985; Lal et al., 1996; Walker and Johnson, 1999).

However, organizational economists argue that the purpose of rigid budgetary control is to increase the likelihood of detecting dysfunctional behaviors (Stede, 2000). As a result, managers' propensity to create slack should reduce with the increased emphasis placed on the budgets (Dunk 1993; Stede 2000; Linn et al., 2001; Webb, 2002). Thus, the tendency of managers to create slack in the budgets can be reduced with a rigid budgetary control system. On the basis of the above, the null hypothesis is stated as follows:

H₀₁ Budgetary emphasis does not influence the propensity of managers to create budgetary slack

Budgetary participation

Walker and Johnson (1999) and Douglas and Wier (2000) reported that participative budgeting is viewed as an opportunity for slack creation. In these cases, managers build in slack as they participated in the budget setting process because of their desire to achieve some compensations linked to the budgetary goals. However, other researchers (e.g. Onsi (1973), Cammann (1976), Lal et al. (1996)) advocate that budgetary participation on its own does not result in the propensity to create slack. In fact, the manager's need to build slack in the

budgeting process is reduced if he/she is allowed to participate (Merchant, 1985; Dunk, 1993; Lal et al. 1996; Fisher et al. 2000). Hence, other researchers explained the inconsistent results by investigating the moderating and intervening factors of budgetary participation and budgetary slack. These include organizational uncertainty (Lal et al. 1996), information asymmetry (Dunk and Perera, 1997), organizational commitment (Nouri and Parker, 1996), managers' concern on their reputations (Webb, 2002) and ethical ideology (Douglas and Wier, 2000). Accordingly, the second hypothesis, stated in the null form, is as follows:

H₀₂ Budgetary participation does not influence the propensity of managers to create budgetary slack

Detection availability

Prior studies have found substantial evidence that the existence of a slack detection system reduces the propensity of managers to create budgetary slack (Merchant, 1985; Lal et al., 1996; Walker and Johnson, 1999). For example, Walker and Johnson (1999) found that subordinates' intentions to build slack were unsuccessful primarily because the superiors were able to detect a 'sudden increase' in the sales forecasts (after the budgets were linked to the compensation scheme). Slack was detected by comparing the current year's submitted budget forecast with the previous year's data. Thus, the tendency to build slack in the budget forecasts diminishes with sophisticated data analysis tools and the general availability of information. Accordingly, it is hypothesized that:

H₀₃ Detection availability does not influence the propensity of managers to create budgetary slack

National Culture: Individualism

Prior studies have provided mixed results on the influence of national culture on budgetary behavior. For example, Goddard (1997) and Lau and Tan (1998) did not support the contention that national culture affects the behavior of managers. They argue that factors such as globalization, internationalization and education levels reduce the cultural effects on managers' behaviors, particularly in the context of budgeting. Chow et al. (1996) and Tsui (2001), on the other hand, found substantial evidence of the impact of national culture on managers' behavior and performances.

In the context of budgetary slack, Ueno and Wu (1993) and Chow et al. (1996) limited the scope of their studies to one aspect of Hofstede's national culture, individualism. They reported that US managers are more likely to engage in

dysfunctional behaviors than the Japanese managers because of their high individualism tendencies. Individualism level was also reported to be associated with the slack creation (Ueno and Sekaran 1992). Accordingly, the following null hypothesis is formulated:

H₀₄ Manager's individualism level does not influence the propensity of managers to create budgetary slack

Islam and religiosity

Islam strongly prohibits slack creation which is intentionally built in to serve an individual interest as it is against the accountability, responsibility and justice concepts indicated in several verses in the Qur'an. The assumptions of the self-interested manager underlying agency theory clearly violates the concept of justice in Islam. The manager is seen to be abusing the trust that God has placed in him as a vicegerent. Transcendent accountability is particularly important in Islam. As opposed to other religions, in Islam, religious and business matters are not regarded as existing in separate compartments. Further, every material achievement is an outward expression designed to achieve a spiritual objective that eventually gives meaning to existence (Sulayman, 1993). Rodinson (1974) describes this attitude as follows,

(the) Koranic faith is also something more than intellectual conviction and assent to the truths revealed by the Prophet. This conviction gives rise to an attitude that commits the whole man. Faith brings peace to the soul, releases one from fear....., gives patience, endurance, resignation to the insults and ill-treatment suffered in God's cause, humility and the will to risk all for God and carry out good works (p83).

Self-interest in an Islamic framework denotes a freedom that is coupled with responsibility. Islam regards self-interest on the same plane as collective interest. Thus, an individual must be sensitive to the consequences of the exercise of his own rights (Naqvi, 1994) so that when individual freedom is coupled with responsibility, self interest is kept in check. Given this, one would expect Muslim managers to have a lesser propensity to create budgetary slack than a non-Muslim manager.

On the basis of the above, it is contended that a manager's religious affiliation influences the extent slack is created. Accordingly, the following hypothesis, stated in the null, is formulated:

H₀₅: There is no relationship between a manager's religious affiliation and the propensity to create budgetary slack.

The issue of whether an individual professing a particular faith religiously follows the teachings of that faith is clearly of import to the preceding discussion. A

person may profess to be Muslim but may not be committed to Islam. Prior research examining the relationship between religiosity and ethical behaviour tends to find little evidence of an effect. Smith, Wheeler and Diener (1975) for example, find no differences between religious and non-religious persons regarding dishonesty. Similarly, Hegarty and Sims (1978, 1979) found no relationship between a person's religious commitment and ethical business practices (Weaver and Agle, 2002). Additionally, Kennedy and Lawton (1998) found no support for the contention that highly religious students engage in less unethical behavior than their less religious counterparts. However, Agle and Van Buren (1999) reported a small positive association between religious beliefs and attitudes toward statements of corporate social responsibility (Weaver and Agle, 2002).

The negative results of the studies in the preceding discussion, according to Weaver and Agle (2002), may be due to the relationship between religion and ethical behavior being dependent upon the issues measured and the measures of religiosity used. They argue that there are two potential factors that can help explain the results: *religious identity salience* and *religious motivational intention*. Religious identity salience refers to the extent religion determines one's self-identity. The larger the role religion plays in influencing one's identity and behavior, the more difficult for other factors to diminish the influence of religion on that person. On the other hand, religious motivational orientation represents the motivation that explains an individual's reasons for practicing a particular religion. This could either be *intrinsic* or *extrinsic*. An intrinsically oriented person treats religious beliefs and practices as ends in themselves. For such a person, there is no hidden objective to practice the teachings of a religion. An extrinsically oriented person, on the other hand, practices the teachings of religion as a means to an end. For instance, an individual who goes to church to satisfy social needs, to foster valuable connections in a community or to achieve some other benefits is extrinsically motivated (Weaver and Agle, 2002).

The foregoing concepts present some parallel to Geertz's (1968) suggestion regarding the distinction between the 'scope' and 'force' of religion. The former refers to the range of social contexts within which religious considerations are regarded, while the latter relates to the thoroughness with which such a pattern is internalized in the personalities of the individuals who adopt it. In the present context, one would expect less dysfunctional behavior amongst managers who are intrinsically motivated or where the 'force' of religion is strong. Since an individual's commitment to a religion (i.e. religiosity) may influence the individual's behavior in performing certain actions, the following hypothesis focuses on whether the religious commitment of Muslim managers influence their propensity to create budgetary slack.

H_{05a}: There is no relationship between religiosity and the propensity to create slack amongst Muslim managers.

3. Research Methodology

Sample

The study is restricted to a single organization to control for the variation effects caused by differences in practices across organizations. According to Otley and Pollanen (2000), the specific setting may increase understanding of the manner in which the variables interact and subsequently the results may form the basis for a more general study. Data was collected from the managers of the largest Malaysian based Korean company which has factories in several states in Malaysia. The case company has a total of four business divisions and ninety-one departmental managers.

The instrument

Budgetary slack is measured using a five-item likert scaled instrument. The questions are replicated from Stede's (2000) and Dunk's (1993) studies. A factor analysis on the five items did not load on a single factor. Consequently, items with a loading of less than 0.5 were eliminated and this left a two-item measure for budgetary slack with a cronbach alpha of 0.55.

Budgetary emphasis was measured using six questions developed by Hopwood (1972) and adopted by Dunk (1993) and Stede (2000). The items measure the supervisor's evaluation style when the budget is used as a primary performance evaluation tool. This measure gives a relatively high cronbach alpha of 0.89.

The measure for budgetary participation is adopted from Milani (1975)'s studies for its extensive replication in the literature (e.g. Otley and Polanen (2000), Tsui (2001), Dunk (1993)). The cronbach alpha for budgetary participation in the current study is 0.87.

Slack detection measures the extent to which employees perceive the existence of a slack detection system in the organization. Three questions were used to determine the availability of slack detection. The first was whether the managers were held responsible for any variance in the budget. The second question asked the respondents whether they perceived the submission of a reliable budget was important. The last question asked respondents if there exist a system that could detect slack creation in their organization. The cronbach alpha of 0.81 was obtained.

Individualism was measured using five statements taken from Oudenhoven's (2001) study. Each respondent was asked to select one of the five statements with which they agree most. Each statement provides an ascending level of individualistic behaviors.

For religion, respondents were asked to choose the religious group they belong to from a list provided. Religiosity is generally more difficult to measure. As such, we discriminate the data by only assessing Muslims on their religiosity level. The first measure of religiosity asked Muslim managers if they regard working as a form of religious duty (*ibadah*). The second aspect of religiosity asked respondents if they perceived their code of ethics to be derived from *Qur'an* and *Sunnah* (the two primary sources of knowledge in Islamic teachings). The more the managers perceive that religion guides their ethical code of conduct, the less slack is expected to be built into the budgets. The last three items focus on aspects of Islam that every Muslim regards as forbidden activities (*haram*) such as gambling, alcohol consumption and interest (*riba*).

Other data

In order to provide a “rich” data source from which to make our conclusions, we also conducted interviews with the managers. Additionally, materials relevant to the objective of the study such as the President’s speech, brochures and information from the web site were also used.

4. Results and Discussion

Response rate

Out of 91 departmental managers, 64 participated in the survey. This gives the overall response rate of 70%. One respondent’s questionnaire was not used because the responses were of a ‘straight-line pattern’. The majority of the managers are male (74.6%), aged above 30 years (90.5%) and have a university degree or a professional qualification (84.1%). Twenty-six managers are Muslims, 20 Buddhists, 3 Christians, 5 Hindus and 9 ‘free thinkers’. In terms of ethnic composition, 26 are Malays, 35 Chinese and 3 Indians. A summary of the demographics are presented in Table I.

Descriptive Statistics

Table II presents the means of the various variables. The overall mean for budget slack is 4.08, thus indicating that slack is likely to exist in the sample studied. The sample reports relatively high degree of budgetary participation, budgetary emphasis and slack detection. As expected, the average individualism score is low for the entire sample. This is consistent with prior studies that reported Asian managers to be less individualistic and prefer more collective decision-making (Tsui, 2000). We next computed the mean for budget slack for each group (Muslims and non-Muslims). We found very little difference in the means (see Table III). Thus, it appears a Muslim manager perceives slack in a similar manner to that of a non-Muslim.

Hypotheses testing

We examined the extent to which budgetary slack is influenced by budgetary participation, budgetary emphasis, slack detection, individualism, religious affiliation and religiosity. Hypotheses 1 to 4 were tested using a simple linear regression analysis since we are interested in the causal relationship. Hypothesis 5 was conducted using a t-test since the data was categorical. Table IV presents the results. Only budgetary participation and budgetary emphasis positively and significantly influence the propensity of managers to create budgetary slack. Accordingly, hypotheses 1 and 2 were rejected. We found no support to suggest that slack detection, culture (i.e. individualism), religion and religiosity influence a manager's propensity to create slack. Thus, we fail to reject hypotheses 3, 4, 5 and 5a.

We further conducted personal interviews and extracted information from the financial reports to support the statistical findings. From the interviews, we found that managers were allowed to adjust their budgets upwards or downward to suit their particular circumstance. Additionally, as long as the managers can provide a reasonable explanation for the existence of any variance, the top management was not very concerned with the failure to achieve the specified goals. This is indicated in the president's speech in the year 2000.

“ From now on, there will be no punishment for budget control errors, missed opportunities, or failure to achieve set goals”

(Lee, 2000, p. 49)

In another paragraph, it is noted that:

“ It is my philosophy that supervisors should use primarily rewards to train employees. There is no need for punishment; our role as supervisors is to help those who do well to do even better without fear of reprisal”.

(Lee, 2000, p. 49)

From the president's speech, one gathers that the achievement of any budget targets would mean a reward whilst not achieving the set targets does not incur the wrath of top management. As such, managers incorporate the slack in their budgets in order not to lose any benefits associated with achieving budget targets. This may explain, to some extent, the significant positive relationship between budgetary emphasis and budgetary slack.

The results of this study appear to suggest that slack would still be incorporated in the budgets regardless of the availability of a slack detection system. The reason for this may be related to the preceding discussion (a reward if targets are achieved and no punishment if targets are not achieved). Further given the environmental uncertainties facing the company, the managers did not feel that

budgetary slack was dysfunctional, or detrimental to the organization. The same reason can also explain the significant positive association between budgetary participation and slack creation. That is, slack is incorporated in the budgets to cushion for uncertainties, and this is possible when the managers are allowed to participate in the budget setting process. However, on the basis of the following statements made by President of the company, we may conclude that the participative budgetary style in this company is, to some extent, working positively for the company. The following extracts from the president's speech also provide further support for the practice of collective decision-making in the organization:

"Everyone (in this company) must be able to honestly voice their opinions and complaints and supervisors must be able to listen. It is important to give and accept constructive criticisms if the organization and the individuals are to develop."

"When having a discussion, one should not hold back one's opinion because others in the room may be more senior. Until a final decision is made, there is no right or wrong. Everyone should be able to express his/her opinions and be listened to with an open mind. However, once a final decision is made everyone should adhere to that decision."

(Lee, 2000; pp. 45-47)

On the basis of the above statements, it is not surprising that we found budgetary participation to be relatively high in the company (see Table II). However, our results appear to be inconsistent with the findings of Tsui (2001), who reported that Asian managers were uncomfortable with participative decision-making.

As for national culture (or individualism, to be more specific), our results found no association between managers' individualism levels with budgetary slack. This is, perhaps, due to the effect of organizational culture. Organizational culture may reduce the effect of national culture on budgetary behavior.

One interesting aspect that requires further elaboration pertains to the insignificant influence of religion on budgetary behavior of Muslim managers. Several reasons are plausible. First, it could be due to the existence of intervening variables, such as the intention to create slack and the consequences of slack creation that were not measured in this study. Another plausible reason could be due to the capitalistic tendencies of managers, whatever their religious persuasion. The materialist philosophy is, perhaps, so firmly embedded in the Muslim mind that although Islam may have an effect on how an individual behaves, economic and social pressures exercise a dominating influence over attitudes prevailing in commercial life (Rodinson 1974). Rodinson (1974) observes that,

'among the merchants of Genoa or Venice in the middle ages, the shipowners and bankers of Amsterdam during the Renaissance, the pioneer industrialist of the Industrial Revolution in eighteenth century Britain, the financial magnates of the imperialist era, and the American businessmen of today, we find the same feverish chase after profit, the same quasi-ascetic dedication of their lives to this pursuit' (p217).

Geertz's (1968) distinction between religiousness and religious-mindedness may provide a further explanation for the results of our study. Religiousness is not merely knowing the truth, but embodying and living it. Religious-mindedness, on the other hand, offers reasons for one's beliefs. Hence, if these two concepts are related to the results that have emerged from this study it might be concluded that the Muslim respondents illustrate a religious-minded disposition as opposed to a religious disposition.

Finally, the results of this study are consistent with the 'liberal' theory of social change and development. According to this theory, all societies under the influence of modern science and technology will eventually become urban in their demographic distribution, industrial in their economies, democratic in their political structures and secular in their thoughts, values and culture (Mehmet, 1990)ⁱ.

5. Conclusion

In summary, we highlight three points to answer the objectives of the study. First, our survey findings revealed that to a certain extent, organizational setting determines the propensity of managers to create budgetary slack. Secondly, we failed to demonstrate statistically the influence of national culture (individualism) on slack creation. However, this by no means rejected the importance of culture in describing the managers' budgetary behavior. The *qualitative* information that we derived warrants plausible explanation on the cultural perspectives of budgetary slack. We reported that budgetary participation was relatively high amongst the managers and the top management lays a strong emphasis on the importance of corporation and team work in budget preparation. This finding is contradicted to Tsui(2001)'s studies who reported Asian managers were uncomfortable with budgetary participation as it does not suit with their culture. Lastly, the contention that religiosity could restrain a Muslim from engaging in a dysfunctional behavior like slack creation was not supported in this study.

The study has several limitations including the measures used, reliance on respondents' perceptions, the non-random sample and its size, all of which make the results non-generalizable. Nevertheless, the results raise several questions that would be the subject of future research. For example, what is the intention behind budgetary slack creation? What are the consequences resulting from incorporating slack in the budgets? Is slack incorporated in budgets for personal

or organizational purposes? Most important of all, perhaps, is whether the business conduct in a broader context, is as uninfluenced by the culture and religion as it appears to be in this study of the creation of budget slack.

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Table I: Demographic information of the respondents

Category	Description	N	%
Gender	Male	47	74.6
	Female	16	25.4
Age Group	<30	6	9.5
	30-40	51	81.0
	41-50	5	7.9
	51-60	1	1.6
Academic Qualification	Degree	48	76.2
	Professional Qualification	5	7.9
	Diploma	10	15.9
Religion	Islam	26	41.3
	Buddhism	20	31.7
	Christianity	3	4.8
	Hinduism	5	7.9
	Free thinker	9	14.3
Ethnic Group	Malay	26	41.3
	Chinese	31	49.2
	Indian	6	9.5

Table II: Descriptive Statistics

Description	N	Mean	Std Devn	Theoretical range		Actual range	
				Minimum	Maximum	Minimum	Maximum
Budgetary Slack	63	4.08	1.38	1	7	1.00	7.00
Budgetary Emphasis	63	4.08	1.38	1	7	1.00	7.00
Budgetary participation	63	4.27	1.19	1	7	1.67	6.20
Slack detection	63	5.53	1.35	1	7	1.33	7.00
Individualism	63	2.00	0.71	1	5	1.00	4.00

Table III: Descriptive statistics

Budgetary Slack	Description	N	Med	Mean	Std Devn	Actual range	
						Minimum	Maximum
	Muslims	26	4.55	4.63	1.25	2.4	7
	Non-Muslims	37	4.80	4.62	1.13	2.4	7

Table IV: Hypotheses testing

<i>Correlation of propensity to create budgetary slack with</i>		<i>R²</i>	<i>p- value</i>	<i>Significance of association</i>
Hypothesis 1	Budgetary Emphasis	0.067	<0.05*	Significant
Hypothesis 2	Budgetary Participation	0.203	<0.000*	Significant
Hypothesis 3	Slack Detection	0.047	0.06	Insignificant
Hypothesis 4	Individualism	0.016	0.781	Insignificant
Hypothesis 5	Religious Affiliation			
	Muslims vs. non Muslims	n.a.	0.944	Insignificant
Hypothesis 5a	Religiosity (Muslims)	-0.059	0.26	Insignificant
Note: *one tailed significance				

End Notes

- i Secularism refers to the eradication of religion as an institution in human society and erosion of man's faith in the divine and the transcendental (Haq, 1986).