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PERFORMANCE EVALUATION: THE EFFECT ON THE PROPENSITY TO CREATE BUDGETARY SLACK

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ABSTRACT

This study used Monte Carlo simulation to analyze two previous studies. Noun's examination of organizational commitment and job involvement's association with budgetary slack, and Mia and Chenhall's (1994) study on the association of broadscope managerial accounting systems on superior's evaluation of managers in uncertain and certain environments were the studies that were examined. Regression analysis was used to examine the link between these two models.

INTRODUCTION

Performance evaluations are prevalent in most of today's business settings. Evaluations are usually completed by a superior, and the results are generally shared with the subordinate. When this information is shared with subordinated it is considered to be feedback. If the evaluation is positive then the feedback could be considered praise from the superior by the manager. Locke et al. (1981) found that praise could motivate a manager to perform better. If budget preparation is part of the managers duties, then it would seem that the manager would be motivated to prepare a better budget (less budget slack).

The current study uses simulation to analyze several relationships between managers in differing environments and their propensity to create budgetary slack. Specifically we will examine these managerial characteristics: job involvement, organizational commitment, performance evaluation and the use of broadscope managerial accounting systems (MAS). The results do not confirm that there is a relationship between superiors' evaluation of managers and those managers' propensity to create budgetary slack; however, it does confirm a direct link between broad scope MAS and managers' propensity to create budgetary slack.

Broad Scope Managerial Accounting Systems

MAS has evolved to include traditionally non-financial data focusing on functional areas and predictive information to enable managers to make more informed decisions (Mia and Chenhall 1994). This additional non-financial data, which is referred to as broad scope, has been shown by several

researchers (Hayes, 1977, Larker 1981, Gordon and Narayanan, 1984) to be significant in aiding decision making by managers.

Budgetary Slack

Young (1985) defined budgetary slack as how much managers "intentionally build excess requirements for resources into the budget, or knowingly understate productive capability." Onsi (1973) found that 80 percent of managers admitted to bargaining for budgetary slack, and he assumed that no operating budget had zero slack in any year. While slack may be present in most budgets it is not necessarily in the best interest of the company. It may be beneficial to reduce slack because budget slack may result in a decrease of control or distortion of information used in decision making (Govindarajan).

RESULTS

When the two complete models were tested there was no evidence of a significant relationship between managerial effectiveness and the propensity to create budgetary slack. When no relationship was found, the model was examined for multicollinearity by examining the variance inflation factors. Significant levels of multicollinearity were found in job involvement, organizational commitment, and the interaction term. Each of these had variance inflation factors (VIF) of well over ten. The use of broad scope MAS did not show any multicollinearity. The new model supported a direct relationship between broad scope MAS and the propensity to create budgetary slack; however this relationship was positive instead of inverse as would seem intuitive.

CONCLUSIONS

This study found no support for a significant relationship between performance evaluation and the propensity to create budgetary slack. This is possibly due to confounding of the variables. The study did find a relationship between the use of broad scope MAS and the propensity to create budgetary slack. This relationship is, however, positive. As tested, the model shows that as the use of broad scope MAS

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increases, the propensity to create budgetary slack also increases. The direction of this relationship appears counter intuitive. Information overload may have a significant role in this relationship. When managers obtain additional broad scope information, portions of the information may be irrelevant and therefore cause more confusion.

Managers who use broad scope MAS may attempt to micro-manage the budget, and in doing so are more apt to participate in the budget process. Young (1985) found that subordinates who participated in the budget process built slack into their budgets. Therefore, the results of this study may support the findings of Young's previous study. We believe that further research should be done to examine the relationship between broad scope MAS and the propensity to create budgetary slack.

REFERENCES

References are available upon request.