The impact of compensation system on employee performance: The Islamic perspectives

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Abstract

Compensation system is very vital for organizational development especially in terms of employee's performance. This study intends to determine the impact of compensation system on employee performance from Islamic perspectives. Primary data was collected and SmartPLS 3 version was used for the analysis. The study respondents comprise of senior and junior staff of Health Services Management Board and Specialist Hospital Sokoto, Nigeria. Survey questionnaire was administered to 400 employees through simple random sampling and only 254 were used. The study found that there is significant relationship between compensation system and employee's performance. This study is intended to benefit the level managers of various organizations in ensuring the existence of efficient compensation system based on Islamic values and the rules of the organization for the betterment of employees' performance. This research is significant as it complements the existing literature on Islamic perspective linking the impact of compensation system to employees' performance. While this paper sets the stage, there is however, the need for future research on other variables that enhances the employee performance in the organization.

Key words: Compensation, Employee performance, Islam.

1. Introduction

Employee performance is defined as how the employees fulfil their job duties and executes their required tasks, this refers to the effectiveness, quality, and efficiency of their output (Ciner, 2019). In an organizational context, task performance is a contractual understanding between a manager and employee to accomplish an assigned task (Pradhan & Jena, 2017). Employees are valuable assets that must be maintained by companies or organizations because they are the spearhead of the production process. Thus, employees' motivation is crucial in order to maintain the good relationship in the organization and also get the required output in accordance with the operational standards of the company (Paais & Pattiruhu, 2020). The most integral part of the relationships between organizations and their employees are the Compensation systems (Bloom, 2004). Employee compensation comprises all forms of pay going to employees and arising from their employment. It has two main components, direct financial payments (wages, salaries, incentives, commissions, and bonuses) and indirect financial payments (financial benefits like employer-paid insurance and vacations) (Dessler, 2020). Malik (2018) maintained that compensation can be in transactional or relational form and can be further

provided in monetary and non-monetary reward forms. Transactional elements typically comprise direct and indirect forms of monetary and non-monetary rewards. Relational rewards on the other hand focus on intangibles such as provision of learning opportunities, employee and peer recognition, offering employment security, providing challenging learning tasks and work opportunities among others. This latter aspect of design focuses on factors that appeal certain individuals intrinsically. However, the aforementioned categories of compensation were absent in most of the public and private organizations. Salary which is the most important aspects of compensation is one of the challenges faced by employees in many organizations. While some workers were under paid, some were denied complete payment for some month. Apart from the salary, some incentives supposed to be given to the employees for extra time were also denied. Some workers were even left without promotion for decades in some organizations while security and health care facilities were very rare to be seen. In fact, the faceoff between the labour unions and the authorities on salary issues has become an annual event.

Islam has a solution to all the aforementioned problems as it affects every aspect of human's life (Attahiru, 2022). Using the Islamic perspectives, this study sets to examine the impact of compensation system on employee performance. It aims to benefit those in authority especially the human resource managers in tackling the challenges of compensation in their organizations. This study is significant as it differs from previous studies in the following: The root of the study is from the primary sources of Islamic law, which are the Al-Quran and Hadiths of the Holy Prophet Muhammad (PBUH). This makes it different from the

previous studies that were based on western literature. Similarly, most of the previous studies used the first-generation software such as SPSS in their analysis, while this study uses the new generation SmartPLS software for the analysis and that ensures the reliability of the results. This study is also likely to be useful to the policy-makers and regulators in the organization as they can come up with very important programmes that may lead to the application of Islamic perspectives compensation system for efficient attainment of employees' performance in the organization as well as safeguard other responsibilities given to them by Allah (S.W.T) and their condition of service.

2. Literature Review
2.1 Employee performance
Employee performance is a measurement of how well or how poorly an employee conducts their required job duties and how promptly they meet their deadlines or requirements (Periyasamy, 2021). The employee performance also is seen as the value added on the existing effort of the employee in terms of quantity, quality, efficiency and effectiveness. Whereas related to behaviour can be categorized according to the level of loyalty in contributing to the increase in value added (Saban, Basalamah, Gani, & Rahman, 2020). Aflah, Suharnomo, Ud and Mursid (2021) perceived employee performance as the results of employee's work performance assessed from quality and quantity based on work standards set by the company. Haryono and Yogyakarta (2021) said that employee performance will be excellent if he has high skills and has a better future expectation. But Walumbwa et al. (2011) asserted that performance is influenced by three factors: First, individual factor that consists of capabilities and expertise, background, and demographics, Second, psychological factors that consist of perception, attitude,

personality, learning and motivation and finally, organizational factor that consists of resources, leadership, rewards, structure and job design. Nevertheless, Islam as a religion covers every aspect of human's life including human resources management, therefore, it emphasised the determination of employee's performance through justice, fairness, accountability and responsibility in his organizational life (Uddin, 2019) Rokhman (2016)opined that ethics based on religious norms affects the good performance, thus, when a person has a close relationship with Allah, his attitude, behaviour and performance will be based on the Shariah rule.

2.2 Compensation System

Grimsley (2022) defines compensation system as the sum total of all monetary and non-monetary benefits provided to employees in exchange for their willingness to work. Compensating the employees is very vital in business organization because they are the most important factors of production. Therefore, running a business without employees will not be an easy task to any organization (Attahiru, 2021b). Compensation according to Grimsley (2022) can be broken down into three general categories: Direct financial compensation that involves cash such as wages, salaries, commission and performance payments. Indirect financial compensation that has financial value but no cash payment is involved, such as paid time off, health insurance, life insurance, disability insurance, stock options plans and services provided to employees. The last is non-financial compensation that has economic value, but it involves the satisfaction an employee receives from the work environment. According to Lai (2011) an effective compensation system design has enormous influence to the organizational development by revealing external competitiveness, internal equity and

individual equity. External competitiveness attracts talent, and internal equity helps companies to retain talent by ensuring that employees and colleagues making the same contributions obtain the same compensation. Individual equity allows employees to feel that their potential is fully rewarded; thus, they are encouraged.

2.3 Compensation System in Islam

Islam puts certain conditions and restrictions to ensure a good working relationship and prevent the chances of bitterness between employer and employees (Haron, Musa, & Shaarani, 2013). Also, Islam emphasised that ensuring the welfare and betterment of employees through compensation is a religious obligation on the employer. Workers should be provided brotherly treatment, fair compensation, suitable work, good working condition (Attahiru, 2021a), The Prophet (PBUH) highlighted the importance of compensating the employees in the Hadith of Sahihul Bukhari (2359):

"Those are your brothers who are around you [workers under you], Allah has placed them under you. So, if anyone of you has someone under him, he should feed him out of what he himself eats, clothe him like what he himself puts on, and let him not put so much burden on him that he is not able to bear, [and if that be the case], then lend your help to him"

Compensation to employees is the teachings of Islam. Allah says: *"Do good to parents, kinsfolk, orphans, those in need, neighbours who are near, neighbours who are strangers, the companion by your side, the way-farer (you meet) and those whom your right hands possess..."* (A-Qur'an, 4: 36-37). Those whom your right hands posses' denote the workers (Arshadul, 2018).

An-Nabhani and Tahrir (2008) asserted that, employing a worker connotes delivering a benefit by the employee to the employer and delivering property from the employer to the employee. It is thus described as a contract to provide a benefit in return for compensation. Askari, Iqbal and Mirakhor (2015) opined that Islam has justifiably makes it an obligation for workers to perform the tasks that they have contracted to the best of their abilities, and at the same time demands that the return for every individual's work must be commensurate with his or her productivity. An-Nabhani and Tahrir (2008) highlighted that, at the point of recruitment, *Shari'ah* made provision for defining the work of employee in terms of the type, duration, wage and effort, hence, the wage received by the employee in return for his execution of the work is the property he accrued as a result of the effort he spent.

Arshadul (2018) argued that employees must be treated with dignity and respect; fairly and humanely as it is a religious duty in Islam, failure to treat them well will lead to punishment in hell fire on the day of Judgement. The Messenger (PBUH) said: "He upon whom his brother has a right, be it of the nature of money or honour, let him compensate for it before he is made to compensate for it on a day when there will be neither dinar nor dirham to deal with. Instead, if he has a good deed in his account it will be taken away from him and given to the person he had wronged. And if he has no good deeds in his account, sins of the other person will be taken from him and added to his account"(Sahih Al-Bukhari, 1997).

2.4 Conceptual Framework

This section discusses the conceptual framework of this study which is developed under the Islamic approach. Figure 1 shows the research model indicating employee performance as dependent variable and compensation system as independent variable. The bases of the study are the Holy Al-Qur'an and Hadith of Prophet Muhammad (PBUH) being the primary sources of *Shari'ah* law.
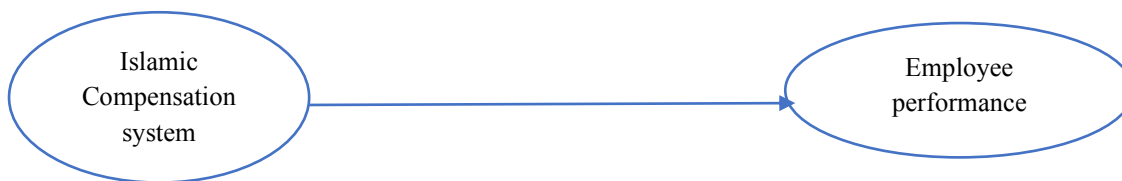

Fig. 1: Conceptual framework

2.5 Employee performance and Compensation in Islam

The impact of performance and compensation in the concept of Islamic management has been mentioned Al-Qur'an (9:105); *"And say, "Do [as you will], for Allah will see your deeds, and [so, will] His Messenger and the believers. And you will be returned to the Knower of the unseen and the witnessed, and He will inform you of what you used to do"*. This verse gives the view that every piece of work must be carried out with a view to achieving performance and job satisfaction, as Allah is witnessing all what is happening within the organization and beyond. Among the major aspects enhancing the performance of employees in an organization is the philosophy of *Ihsan* which is observed as the spiritual

and practical aspect of work (Ali, 2010). Ihsan refers to excellence which comprises goodness and generosity in any interaction and conducts, be it at a personal or at the organizational level. Prophet Muhammad (PBUH) said:*"Verily Allah has enjoined excellence (Ihsan) with regard to everything"*(Sahih Muslim:1955). Ihsan closely shapes the interaction between the individuals, groups and the organizations. It encompasses mercy, justice, goodness, forgiveness, tolerance, and attentiveness at individual and organisational levels. These aspects are well articulated in the Allah's saying: *"But do good; for Allah loveth those who do good"* (Al-Qur'an, 2:195)

Therefore, the criterion should not be selfishness, but the goodness of the individuals and the organisation, for such goodness is pleasing to Allah (Ali, 2016). Hence, human considerations at the workplace take priority on matters related to treatment of employees, justice, and equality in hiring and promotion (Ali, 2010). Thus, as part of *Ihsan,* the organization should maintain excellence, generosity and goodness to the employees so as to enhance their performance and attract reward of the hereafter from Allah the Most generous.

Islamic concept of compensation system is one of the best approaches in performance achievement as it comprises the reward and punishment of this world and the hereafter. This is contained in Al-Quran (18: 87-88): *"As for one who wrongs, we will punish him. Then he will be returned to his Lord, and He will punish him with a terrible punishment. But as for one who believes and does righteousness, he will have a reward of the best, and we will speak to him from our command with ease.""*.

Hashim (2014) said, a good Muslim would always keep running his responsibilities according to the rules of God because he believes that any work done in this world will be shown on the day of judgement (hereafter) and will be accurately taken into account in the presence of God. Al-Qur'an (21:47) also decrees:*"We shall set up scales of justice for the Day of Judgment, so that not a soul will be dealt with unjustly in the least, and if there be (no more than) the weight of a mustard seed, We will bring it (to account): and enough are We to take account"*.

Islam also encourages the timely payment of workers salary without unnecessary delay Prophet Muhammad (PBUH) says: *"Give the wages of employee before his sweat dry"* (Ibn Majah, Hadith no. 2468). Prophet (PBUH) further emphasised: *"Delay in paying debts by a wealthy man is Injustice"* (Sahih Al-Bukhari 2287; Muslim 1564)

Payment of salaries and wages to employees should also be as agreed. Unlawful deduction is not permissible in Islam. Allah Said: *"Do not withhold from the people the things that are their due"* (Qur'an,7:85). Prophet said, *"Allah (SWT) will be an opponent to anyone who employs a labourer and takes full work from him but does not pay him for his labour."* (Sahih Al-Bukhari: 2270)

Sheikh Abdullahi Bn Fodio highlighted that a good leader must have an information pertaining his workers salary, he should pay them what is due to them according to the level of their work at the appropriate time Luwa (2013). Workers that exhibit morality in their work should be considered suitable for additional responsibilities and promotion because of the impact of their action to the organisation and the society. They should be rewarded and encouraged to report any unethical behaviour within the organisation. Similarly, those who unethically violate the rules should be accordingly punished as indicated by Holy

Al-Qur'an: *"As for one who wrongs, we will punish him. Then he will be returned to his Lord, and He will punish him with a terrible punishment. But as for one who believes and does righteousness, he will have a reward of the best, and we will speak to him from our command with ease.".* (Al-Qur'an, 18: 87-88).

H_1: *Compensation system will significantly influence employee performance*

3. Methodology

The sample of this study comprises of senior and junior staff of Health Services Management Board and Specialist Hospital Sokoto, Nigeria. This study uses cross sectional research design. Survey questionnaire was administered to 400 employees through simple random sampling and only 254 were used as indicated in Table 1. To improve the response rate, the questionnaires were delivered to the respondents by hand and collected by hand on a scheduled pick-up date. PLS-SEM 3.0 was used for data analysis. This study classified responses according to a five-point Likert scale ranging from 1 (strongly disagree) to (strongly agree). Partial least square structural equation model (PLS-SEM) method was used and found suitable by this study because, the research model entails considerable complexity regarding the type of relationships in hypotheses (Hair, Hult, Ringle, & Sarstedt, 2017). This study also uses latent variables' scores in the consequent analysis for predictive purposes.

Table 1**:** *Demographic Profile of the Total Sample*

Characteristics	Frequency	Percentage%
Gender		
Male	161	63.4
Female	93	36.6
Marital Status		
Married	150	59.1
Single	78	30.7
Divorced	26	10.2
Age		
18-29	52	20.5
30-39	87	34.3
40-49	81	31.9
50-59	34	13.4

Category

Senior staff	172	67.7
Junior staff	82	32.3
Educational level		
Informal Education	29	11.4
Diploma/NCE	73	28.7
Degree/HND	109	42.9
Postgraduate Degree	43	16.9

4. Results

The PLS model analysis covers two stages: (1) assessment of reliability and validity of measurement model and (2) evaluation of structural model.

4.1 Measurement model

The reflective measurement model assesses model's reliability and validity which involves indicators item loading, composite reliability, convergent validity and discriminant validity. Convergent validity is the level to which items accurately represent the intended latent construct and certainly correlate with other measures of the similar latent construct is evaluated by examining the AVE of each latent construct, as recommended by Hair *et al*. (2014). To achieve adequate convergent validity, the rule of thumb indicates that only items with loadings between 0.40 and above, and items with Average Variance Extracted (AVE) of 0.50 and above should be retained as suggested by Hair *et al*. (2017) and Chin (1998). Also, Bagozzi and Yi (1988) and (Hair, Ringle and Sarstedt (2011) recommended that the composite reliability coefficient should be at least 0.70 or more.
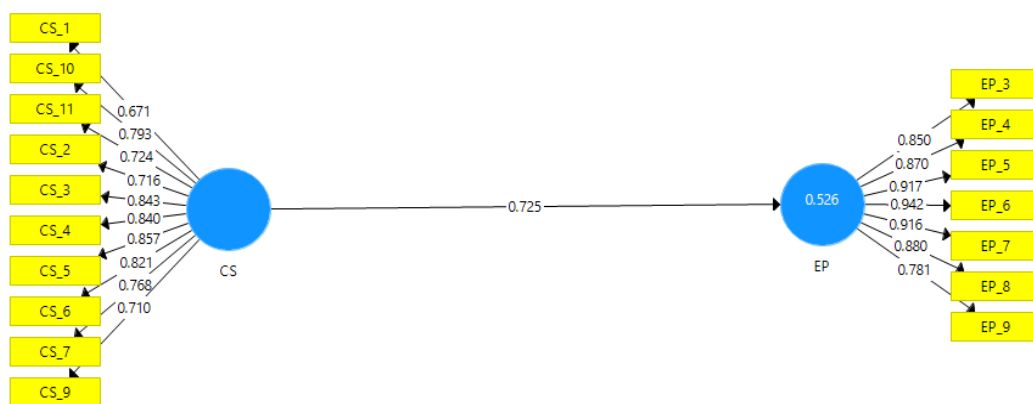

Figure 2: *Measurement model*

Result shows that all the requirements were met in assessing measurement model. Firstly, reflective individual items are reliable, because all standardised loadings are above 0.6 as indicated in figure 2 and Table 2 respectively. Accordingly, the individual item reliability is satisfactory

(Hair, Hult, Ringle, & Sarstedt, 2017). Secondly, the composite reliabilities of all reflective constructs are greater than 0.7 indicating that the requirement of construct reliability is met (Leal-Rodríguez, Eldridge, Roldán, Leal-Millán, & Ortega-Gutiérrez, 2015).

Table 2: *Measurement Model: Reliability and Convergent Validity*

Items	Loadings	CR	Cronbach	AVE
EP_3	0.850	0.960	0.951	0.776
EP_4	0.870			
EP_5	0.917			
EP_6	0.942			
EP_7	0.916			
EP_8	0.880			
EP_9	0.781			
CS_1	0.671	0.938	0.926	0.604
CS_10	0.793			
CS_11	0.724			
CS_2	0.716			
CS_3	0.843			
CS_4	0.840			
CS_5	0.857			
CS_6	0.821			
CS_7	0.768			
CS_9	0.710			

As indicated in Table 2, the convergent validity is achieved by the latent variables since their average variance extracted (AVE) exceeds 0.5 level (Fornell and Larcker 1981). Also, Table 3 confirms that all the variables met the requirement of discriminant validity. This is achieved from a comparison of the square root of AVE versus the corresponding latent variable correlations. For discriminant validity to be satisfactory, diagonal elements should be significantly greater than off-diagonal elements in the corresponding columns and rows (Roldán and Sánchez-Franco 2012)

Table 3: *Discriminant Validity (Fornell &Larcker, 1981)*

Construct	CS	EP
EP	0.881	
CS	0.725	0.777

In addition, as stated earlier, discriminant validity can also be achieved by comparing the indicator item loadings with cross-loadings. To ascertain satisfactory discriminant validity, Chin (1998) recommended that all the indicator item loadings should be greater than the cross-loadings. Table 4 below compares the indicator item loadings with other indicators. All indicator item loadings are

higher than the cross-loadings as shown in the Table 4 above, recommending acceptable discriminant validity for further analysis. Therefore, in this study, all the criteria for attaining discriminant validity are achieved.

Table 4: *Cross Loadings*

Construct	EP	CS
EP_3	**0.850**	0.616
EP_4	**0.870**	0.601
EP_5	**0.917**	0.645
EP_6	**0.942**	0.688
EP_7	**0.916**	0.657
EP_8	**0.880**	0.635
EP_9	**0.781**	0.623
CS_1	0.416	**0.671**
CS_10	0.688	**0.793**
CS_11	0.586	**0.724**
CS_2	0.388	**0.716**
CS_3	0.577	**0.843**
CS_4	0.592	**0.840**
CS_5	0.566	**0.857**
CS_6	0.540	**0.821**
CS_7	0.559	**0.768**
CS_9	0.610	**0.710**

Structural model

The assessment of structural model includes, testing of path coefficient (hypothesis), assessment of R-square, evaluation of effect size and assessment of predictive relevance of the study model. The study achieved all the requirement of structural model. Therefore, bootstrapping procedure was used in assessing structural model (Figure 2). Table 5 indicates the bootstrapping results which provides t-values that permit the assessment of statistical significance relationship in the research model (Ramayah, Cheah, Chuah, Ting, & Memon, 2017). In this situation, the results significantly support the hypothesis, which defines the direct relationship of Compensation system (CS) and Employee performance (EP) (Beta = 0.725; t=20.529).
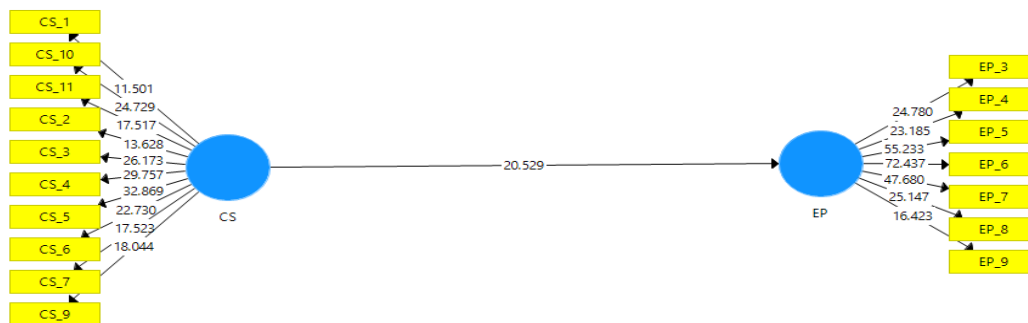

Figure 3: *Structural model*

Table5:
Result of Hypothesis Testing

Hypothesis	Beta	Standard Error	T Value	P Values	Decision
CS -> EP	0.725	0.035	20.529	0.000	Supported

In addition, the R^2 represent the predictive accurateness of the model, it signifies the collective effects of the exogenous latent constructs on the endogenous latent construct as proposed by Hair *et al*.,

(2014). Table 6 indicates the variance explained (R2) in the endogenous variable and the path coefficients for the study model.

Table 6: *Coefficient of Determination*

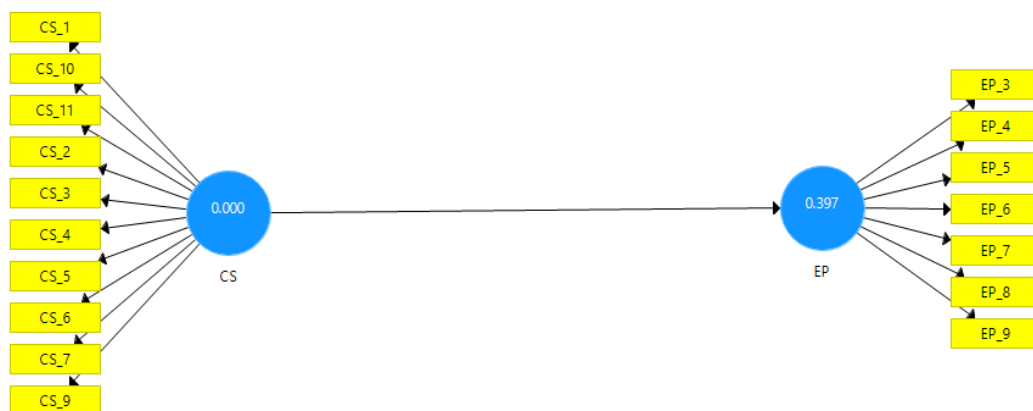| Construct	R Square
EP	0.526

Figure 4: *Blindfolding*

This study used Stone-Geisser test of predictive relevance of the study model using blindfolding methods as indicated in Geisser (1974); Stone (1974). Stone-Geisser test of predictive relevance is used as an additional evaluation of goodness-of-fit in PLS-SEM (Duarte, Alves, & Raposo, 2010). According to Henseler, Ringle and Sinkovics (2009), a research model with

Chin (1998); Henseler et al. (2009).

Q^2 greater than zero is considered to have predictive relevance. In addition, a research model with higher positive Q^2 *statistic* values recommends more predictive relevance. As presented in Table 7 and figure 4, the cross-validation redundancy measure Q^2 for the construct of Employee performance is above zero (0.39), suggesting predictive relevance of the research model as highlighted by

Table 7: *Predictive Relevance*

Total	SSO	SSE	$Q^2 =1-SSE/SSO$
Employee Performance	770.000	464.438	0.397

4. Conclusion and Recommendations

This paper discusses the impact of compensation system on employee performance in the Islamic perspectives. The result indicated that compensation system significantly influences the performance of employee in an organization. Managers at various levels of organization should realize the importance of Islamic perspectives on compensation system because of its benefit to the organization. Managers should therefore strengthen the employer-employee relationship by ensuring the welfare of their employees to the best of their ability. Prompt payment of salaries and wages as well as other entitlements of the employees should be maintained. Managers should also enlighten the employees on the importance of complementing the gesture of the organization as taught by Islam. The management and employees should always be reminded to be careful on how they behave since they are not only being watched by their fellow human-beings, but

also by God. Organizations should therefore be much concerned in measuring and rewarding the performance of their employees. Future research is suggested to test the relationship of other variables that enhances the performance of employees in the organization, such as good working condition, performance appraisal among others.

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