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**THE MEDIATING EFFECT OF EMPLOYEE COMPENSATION  
ON INTEGRITY AND CORRUPTION RISK**

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***Abstract***

Risk management is an important agenda to prevent the unethical behaviour in an organization. In facing the challenging world of business and corruption issues, integrity and employee compensation are important factors in order to develop the organization success. Thus, it is important for the organization to focus on developing and enhancing the quality of employee in terms of ethical, behaviour and moral conduct. The aim of this research is to examine the effect of integrity in corruption risk mediated by employee compensation. The study involves only 50 respondents as it is a pilot study of the actual survey. The sample are respondents from 10 different organization. This study involves three different organizations which are federal government, state government and statutory bodies. The respondents involved in this study are whom that have an authority in making a decision for the organization. The analysis of bootstrapping for this study represent that, all the hypotheses are accepted with the t-value above 1.65 respectively. Hence, it shows that, integrity and employee compensation play important roles in order to prevent the risk of corruption in the organization. Other than that, employee compensation also mediates the relationship between variables

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**Keywords:** Integrity, corruption risk, employee compensation, mediation, partial least square.



## 1. Introduction

In a few analyses and insightful talk, points, for example, public integrity and corruption have been drawn closer in the perspective of globalization (Ewoh, Matei, & Matei, 2013). Characterizing corruption is essential that powerful anti-corruption or government integrity programs rely on establishing clear targets and standards. According to the study by Mohamad, Saadiah, Saad, Hayaati, and Ismail (2014), to enhance the integrity level of employees, factors such as spiritual, societal and intellectual are important. It is because; through integrity it will help the employee to develop a connection with trust value among the employees, management, supplier and other parties. Individual integrity at the corporate level is important to develop a harmony around shared values that are consistently understanding, concerned, transparent, truthful, and principled (Duggar, 2011). Trust expects one to communicate straight forwardly with the administration, groups, and associates; to share similarly of information about the successes and challenges and to learn and develop from one's own particular experiences (Shahid & Azhar, 2013). However, to link with corruption risk, employee compensation also plays an important role to close the risk of corruption. It is because, through fraud triangle, employee compensation acts as a pressure factor to the employee. Remuneration represents the general term that comprises of finance system, payment system and reward system that are being inferred as the pay for workers inside the organization (Muttreja, 2012). The efficiency wage model where salaries that are higher than market-determined minimum rates can increase productivity is one of the way to measure the relationship between compensation and corruption (Gong & Wu, 2012).

## 2. Problem Statement

Corruption is seen as one of the essential issue to the development of a proficient government in light of the fact that it is an indication that something has occurred in the administration of the association. A noteworthy challenge it needs to address in this undertaking is the reinforcing of morals and integrity. The upgrades in the administrative systems, social and profound angle are seen critical towards planning of the Malaysian Vision 2020 (The Malaysian Digest, 2014). Public resources and execution is important and need a protection, because there is a demand that the institution of public sector should enhance the moral conduct, integrity, transparency, responsibility and professionalism of employee. The principles of Corruption Risk Management's (CRM) is to enhance the capabilities of risk intelligence, to identify the risk of corruption that is faced by the organization and to execute the proper controls to treat the recognized dangers. It is important to look at the link between integrity and corruption from globalization perspective. It is mapping a new effect on the development of public integrity strategies and the general framework of national integrity systems (Ewoh et al., 2013). Integrity is a very important criterion that make globalization program will run smoothly and to reduce the level of corruption among the countries. The changing of ethical norm is influenced by religion, technology and culture that is affecting in wrong doing of corruption. Even though there is no standard level of ethics in different culture and social life, the standard of ethics of life should not be changeable (Zekos, 2004). Indeed, ethic is an important element as it guides human behaviour either to goodness or worst and able to improve human capability.

The evidence of unethical behaviour in organizations had been documented in many previous study (Farid et al., 2013). Unethical behaviour in the work environment can take diverse measurements ranging

from lying, cheating, stealing, sabotage, corruption, to covering up or demolition of authority reports (Ugwu, 2011). In other point of view, according Pascual-Ezama, Dunfield, Gil-Gomez de Liano and Prelec (2015) stated that, the situation that can lead employee to dishonest behaviour happened in an unsupervised and isolated situation under competition. According to Schein (1984) unethical behaviour can be learned through relationships with peer groups in which an unlawful demonstration is considered as a way to deal with be recognized in a social event. According to Richard and Hollinger (1983) a person's unusual conduct was frequently concurred or upheld by a gathering, despite the fact that the wrongdoing can be done by a person (McManus & Subramaniam, 2009).

In order to build the efficient and disciplined of management and public services, it is important to the organization to enhance the level of integrity of each of the employees. By improving integrity to public service is an important aspect to make sure that the level of corruption decrease and the capability of public official will increase. In order to increase employee's productivity, it is important to the organization to have a greater accountability of compensation practices (Samnani & Singh, 2014). In order to defeat corruption, employee compensation is one of the important variables that are used by scholars to study the economic inspiration in unethical activities. The basic statement about the link between employee compensation and corruption, when the expectation for service is high, but salaries remain low, government officials may go through to wrong network than what is formally authorised; hence, the corruption issues will increase (Gong & Wu, 2012). In sum, employee attitudes and behaviours are critical issues that are influenced and driven by compensation systems (Rynes, Gerhart, & Minette, 2004; Sweins & Kalmi, 2008).

### **3. Research Questions**

Based on the issues that are highlighted in the problem statement, this study was guided by a few research questions that need to be achieved.

1. What is the effect of integrity on corruption risk?
2. What is the effect of integrity on employee compensation?
3. What is the effect of employee compensation on corruption risk?
4. Does employee compensation mediate the effect of integrity on corruption risk?

### **4. Purpose of the Study**

The effect of integrity towards corruption risk and mediated by employee compensation are the main purpose of this research. As per Eleventh Malaysia Plan for 2016-2020 expands on the administration's sense of duty regarding transforming Malaysia into a high-income nation by 2020, concentrating on advancement and efficiency, human capital, foundation, and comprehensive a green financial development (McCully & Johnston, 2015). In order to achieve the plan, Prime Minister Najib Razak stated in his speech on Malaysian Budget 2016, to outface corruption, government will strengthen integrity and reduce business leakages and corruption (Najib, 2016). Employee compensation is an important component in the organization that can lead an employee to be a good person in the organization that will help to achieve the organization goals. It is thus rational to assume that compensation might mediate the effect of self-confidence and intention of corruption (Liang, Liu, Tan, Huang, & Dang, 2016),

## 5. Research Methods

Pahang is selected as the place to conduct this study which is placed in Eastern Region of Malaysia that is the largest state compared to Terengganu and Kelantan in this region, and 50 respondents from 10 different government agencies participated as it is a pilot study of the actual survey. The organizations were divided into three main categories which are federal government, state government and statutory bodies. The selection of samples for this study used the stratified random sampling technique. Respondents that are involved in this study are related to the organization decision making which starts from the supervisor until the manager of the organization. The questionnaire distributed is divided into three different parts which is for the first part, the questions asked about the respondents' demographic profile while the second section focused on integrity and corruption risk and the third section focused on employee compensation as mediating variable. The significance of integrity to the public service is to make an organization to be effective and restrained by instilling moral value to overcome issues and weaknesses in different parts of management, for example, financial management, handling of disciplinary cases, corruption, abuse of power, law and religion, the hypotheses for this study are:

- H1. There is a significant effect of integrity on corruption risk.
- H2. There is a significant effect of integrity on employee compensation.
- H3. There is a significant effect of employee compensation on corruption risk.
- H4. Employee compensation mediate the effects of integrity on corruption risk.

## 6. Findings

### 6.1. Respondent Profile

A total of 50 questionnaires were distributed to the target population which are Road Transport Department, District Land Office, State Land Office, District Council, Municipal council, Forestry Department, and Royale Malaysia Police, Health Department, Public Work Department, and immigration department. The chosen unit of analysis for this study are individuals whom associated with the decision making in the organization.

### 6.2. Data Analysis

The important part of this study is the analyses of the measurement and structural model. Partial Least Squares – Structural Equation Modelling (PLS-SEM) programming was utilized to analyse the information. This study employed statistical procedures that suggested (Anderson & Gerbing, 1988) which are measurement model and structural model. The measurement model covered the validity and reliability of the measures (Hair, Hult, Ringle, & Sarstedt, 2014; Ramayah, Lee, & Julie, 2011; Ramayah, Osman, Azizah, Malliga, & Ai, 2013). Bootstrapping Method (500 resamples) was used in this study in order to analyse the significance level of construct (Hair et al., 2014).

#### 6.2.1. Construct Validity

Construct validity represents and affirms the strength of the outcomes acquired that the utilization of the measurement can fit with the theories around which the test is gathered (Sekaran & Bougie, 2010).

There are two types of analysis than can be used to assess the construct validity which are convergent and discriminant validity. Firstly, the analysis of loading and cross loading are necessary to assess if there are problems with any particular items. Factor loadings cut-off value at 0.5 as significant (Hair, Black, Babin, & Anderson, 2010). From Table 1 each items measuring a specific construct are highly loading value compared to other construct.

**Table 01.** Cross Loading

Construct	Items	Corruption Risk	Employee Compensation	Integrity
<b>Integrity</b>	QInt_1	0.456	0.275	0.748
	QInt_10	0.431	0.456	0.633
	QInt_2	0.305	0.237	0.735
	QInt_3	0.455	0.406	0.778
	QInt_4	0.563	0.318	0.885
	QInt_5	0.526	0.286	0.865
	QInt_6	0.367	0.168	0.832
	QInt_7	0.461	0.302	0.896
	QInt_8	0.443	0.241	0.878
	QInt_9	0.455	0.294	0.682
<b>Employee Compensation</b>	S3Q1	0.373	0.59	0.247
	S3Q10	0.498	0.72	0.259
	S3Q2	0.561	0.745	0.133
	S3Q3	0.557	0.777	0.241
	S3Q4	0.646	0.898	0.478
	S3Q6	0.284	0.582	0.188
	S3Q8	0.484	0.63	0.305
<b>Corruption Risk</b>	QCR_10	0.781	0.528	0.53
	QCR_2	0.764	0.462	0.477
	QCR_3	0.752	0.403	0.298
	QCR_4	0.802	0.666	0.309
	QCR_5	0.855	0.661	0.573
	QCR_6	0.752	0.444	0.386
	QCR_7	0.758	0.406	0.394
	QCR_8	0.583	0.569	0.345
	QCR_9	0.779	0.559	0.531

### 6.2.2. Convergent Validity

Table 2 represents a convergent validity that measures the important criteria which is factor loading and average variance extracted (AVE) as endorsed by (Hair et al., 2010). Factor loading for all the items need to exceed 0.5 as endorsed by (Hair et al., 2010). The minimum required cut-off level at 0.50, and for this study, all the items exceeded the requirement (Hair et al., 2014). The recommended value of AVE for

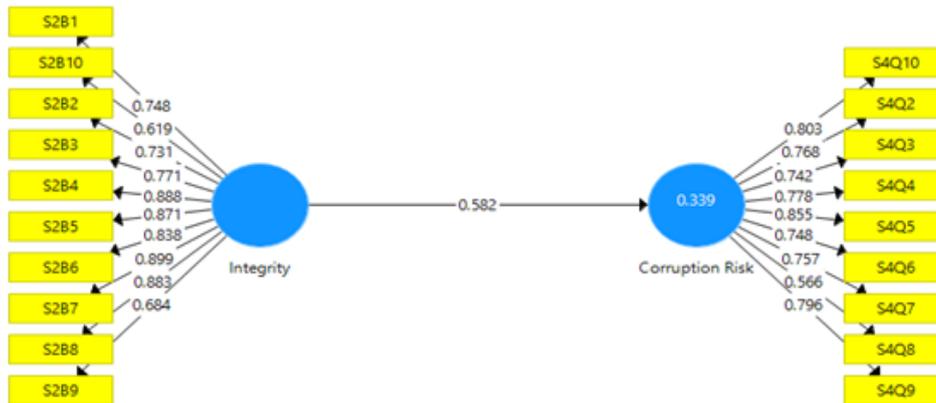
each construct must exceed 0.50 to validate by a construct (Barclay, Thompson, & Higgins, 1995). For this study, AVE for integrity, employee compensation and corruption risk was 0.637, 0.509, 0.580 respectively. Therefore, for this study all AVE values are accepted.

**Table 02.** Measurement Model

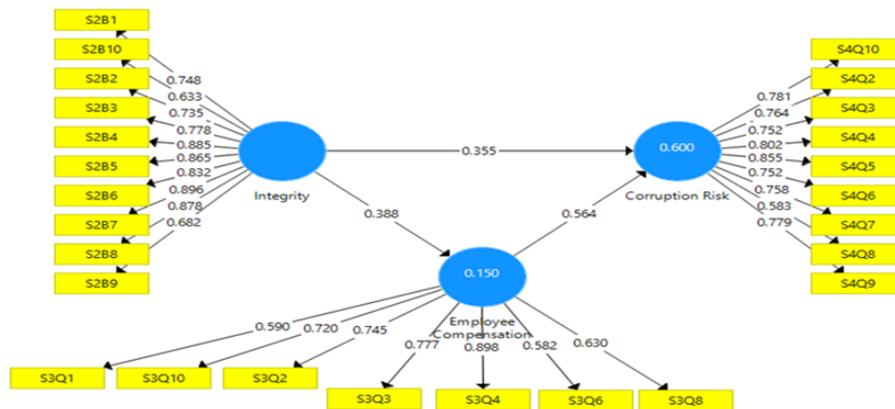
Construct	Items	Corruption Risk	Composite reliability	Average Variance Extracted
<b>Integrity</b>	QInt_1	0.456	0.945	0.637
	QInt_10	0.431		
	QInt_2	0.305		
	QInt_3	0.455		
	QInt_4	0.563		
	QInt_5	0.526		
	QInt_6	0.367		
	QInt_7	0.461		
	QInt_8	0.443		
	QInt_9	0.455		
<b>Employee Compensation</b>	S3Q1	0.373	0.877	0.509
	S3Q10	0.498		
	S3Q2	0.561		
	S3Q3	0.557		
	S3Q4	0.646		
	S3Q6	0.284		
	S3Q8	0.484		
<b>Corruption Risk</b>	QCR_10	0.781	0.925	0.580
	QCR_2	0.764		
	QCR_3	0.752		
	QCR_4	0.802		
	QCR_5	0.855		
	QCR_6	0.752		
	QCR_7	0.758		
	QCR_8	0.583		
	QCR_9	0.779		

(Note: S4Q1, S3Q5 and S3Q7 were deleted due to low loading below 0.5)

Figure 1 represents the measurement model between integrity and corruption risk without mediating construct and figure 2 represent the measurement model with a mediating construct. Based on the figure, it indicated that, all the value of factor loading, R<sup>2</sup> value and path coefficient.



**Figure 01.** Measurement model without mediating



**Figure 02.** Measurement model with mediating

### 6.2.3. Discriminant Validity

In discriminant validity, all the construct was assessed by analysing the correlation between construct of possibly overlapping construct. It is important for each construct to load more strongly on their own construct (Compeau, Higgins, & Huff, 1999). Table 3 demonstrated that, the bold value representing the square root of the AVEs. According to Hair, Hult, Ringle and Sarstedt (2017), to establish discriminant validity, the square root of each construct's AVE must be larger than its correlation with other construct. Hence, this study was achieved the suggested criteria.

**Table 03.** Fornell and Larcker Criteria

Construct	Corruption Risk	Employee Compensation	Integrity
Corruption Risk	<b>0.762</b>		
Employee Compensation	0.702	<b>0.714</b>	
Integrity	0.574	0.388	<b>0.798</b>

#### 6.2.4. Reliability

In terms of reliability, the composite reliability and Cronbach Alpha values for all reflective constructs exceeded the threshold value of 0.70 (Hair et al., 2010; Nunnally, 1978). Cronbach's alpha coefficient was used to assess the inter item consistency of our measurement items. Interpreted like a Cronbach's alpha for internal consistency reliability estimate, a composite reliability of 0.70 or greater is considered acceptable (Fornell & Larcker, 1981b). As such we can conclude that the measurements are reliable.

In terms of reliability, the composite reliability and Cronbach Alpha values for all reflective constructs exceeded the threshold value of 0.70 (Hair et al., 2010; Nunnally, 1978). Cronbach's alpha coefficient was utilized to evaluate the internal consistency of our measurement items. Interpreted like a Cronbach's alpha for internal consistency, a composite reliability of 0.70 or more prominent is viewed as satisfactory (Fornell & Larcker, 1981). Thus, it is concluded that the measurements are reliable.

#### 6.2.5. Path Coefficient

Table 3 below shows the path coefficient of each construct. Based on the result, employee compensation is the factor that affects the corruption risk with the beta value of 0.564, integrity and corruption risk 0.355 and integrity and integrity and employee compensation 0.388. When the path coefficient is positive, indicating a positive influence; when is a negative value as compared to the negative influence (Huang, Wang, Wu, & Wang, 2013).

**Table 04.** Path Coefficient

Construct	Path Coefficient
Employee Compensation -> Corruption Risk	0.564
Integrity -> Corruption Risk	0.355
Integrity -> Employee Compensation	0.388

#### 6.2.6. Hypothesis testing

500 resamples of Bootstrapping procedure was run to evaluate the structural model and generate the t-values. Figure 2 represents the structural model, while Table 5 represents the finding of the hypothesis testing. As shown in Figure 2 and Table 5, the effect of employee compensation on corruption risk represents a positive effect ( $\beta = 0.564, p < 0.01$ ) that clarifying of 60% variance. The effect of Integrity ( $\beta = 0.355, p < 0.05$ ) to corruption risk represents the positive effect and it explains 60% of variance, and the effect of integrity and employee compensation ( $\beta = 0.388, p < 0.01$ ) are also positively related. Thus H1, H2 and H3 were supported. Next is, to test the indirect effect, bootstrapping method was applied (Preacher & Hayes, 2004, 2008). Based on Table 5, it showed that the indirect effect  $\beta = 0.219 (0.388 * 0.564)$  was significant with a t-value of 1.823. Thus, it can be accomplished that, the mediation effect of employee compensation is statistically significant, indicating that H4 was also supported.

**Table 05.** Hypotheses Testing

Construct	Original Sample	Standard Error	T Value	Decision
H1. Integrity -> Corruption Risk	0.355	0.165	2.151*	Supported
H2. Integrity -> Employee Compensation	0.388	0.151	2.574**	Supported
H1. Employee Compensation -> Corruption Risk	0.564	0.119	4.723**	Supported
H4. Integrity -> Employee Compensation -> Corruption Risk	0.219	0.120	1.823*	Supported

Note: \*p < 0.05, \*\*p < 0.01

## 7. Conclusion

In order to prevent and/or detect fraud and corruption, it is important to the organization to implement the proactive measures. Other than that, the process to recognise the appropriate policies and procedures are pinnacle in order to prevention and early detection of fraud and corruption in the organization. The other part that needs to be given more attention is empower the employees to understand the spirit of fraud and corruption, how to report it and the impact. In order to prevent the risk of corruption within the organization, it needs a proactive promotion on the ethical culture. This can be achieved through the implementation of an integrated fraud and corruption risk management process. Other than that, employee compensation also needs a serious attention by the management. It is because, based on the finding of this study, employee compensation is one of the factors that have a significant effect on corruption risk and mediates the relationship between integrity and corruption risk. As a part of limitation, the data collection was collected to the single state that might be a cause for possible responses bias. However, for further study, the mediating variable of employee compensation should be extended to a larger sample and several states in order to generalize the finding.

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