



Book The Complete Guide to Sales Force Incentive Compensation

How to Design and Implement Plans That Work

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Recommendation

Planning the ideal salesforce incentive compensation program is very challenging. Pay enough, and you'll energize your salespeople. Pay too much, and you'll throw money away while turning salespeople into loafers who can get by on fewer sales. Pay too little, and you'll push your best salespeople out the door. But how much is enough, too much or too little? How do you figure out the best mix of salary, commissions and bonuses to pay your salespeople? This comprehensive compensation guide is a good place to start answering these questions. Written by sales and marketing experts Andris A. Zoltners, Prabhakant Sinha and Sally E. Lorimer, this is your essential map for developing and implementing the ideal compensation incentive plan for your salespeople. *BooksInShort* recommends it to sales managers who want to do a better job of meeting their personnel needs and, therefore, their sales targets. (Read this before you negotiate compensation with anyone else.)

Take-Aways

- Creating a great sales incentive compensation plan is difficult. Do it anyway.
- A good plan can boost sales and attract top salespeople. A bad plan can bury your company and make your top salespeople flee.
- Once you create and implement your sales incentive compensation plan, fine-tune it every year, and change it comprehensively every two to three years.
- Don't blame it for low sales. The cause may be something else.
- The plan must fit your firm's strategic needs and satisfy your salesforce.
- It must pass the "3 Cs" test: "consistency," "compatibility" and "consequentiality."
- To determine the right compensation for a sales job, consider industry standards, past pay, budget, corporate culture and the salesperson's work.
- To avoid making your salespeople nervous, communicate fully when you introduce your new sales incentive compensation plan.
- Don't overdo contests and incentives. They deflect attention from sales goals.
- Your capable administration of the new plan can be as important as how it works.

Summary

Getting Sales Incentive Compensation Right...If You Can

Establishing the right sales incentive compensation plan is challenging, but it's worth the trouble. Getting this right can help you retain and recruit top-selling talent and increase sales, which is the whole point. Alas, getting it wrong can have the opposite effect; you can lose people and sales, and injure your company. The objective is clear: create an effective compensation program. To achieve this goal, you need to take many different factors into account.

"When an incentive compensation plan changes, it is essential that the thoughts and feelings of the people who are affected by the change are acknowledged and dealt with on both rational and emotional levels."

Begin with a budget and ask how much you can allocate to pay salespeople. Consider your experience and theirs to determine what ratio of their compensation should be salary as opposed to incentives or bonuses. Do you want to vary salespeople's pay depending on performance? Do bonuses or short-term incentives emphasize achievement or do they divert salespeople from their main mission? Do cross-selling incentives work? As you establish a plan, avoid complexity. Build on past successes as you keep an eye on your future sales needs. Use your staffers' enthusiasm for the plan as a metric that can indicate if it will work to satisfy the four reasons

that companies offer sales incentive:

1. **“Salespeople drive the company’s top line”** – Companies in competitive industries use sales incentives to stay viable. If the work of your salespeople, rather than your marketing messages, Internet orders or other efforts, is responsible for most of your sales, offer a variable-pay incentive to motivate them.
2. **“The output of salespeople is usually measurable”** – The sales field is bursting with metrics that tell sales managers by week, month, quarter or year how their salespeople are performing against each other, against other sales offices, against their previous work and against quotas. Of course, stats on individuals blur when teams do the selling.
3. **“Variable pay helps ensure that salespeople produce results”** – Salespeople on the road are out of your direct control and largely unsupervised. Variable pay can stimulate such independent people to work harder.
4. **“Variable pay acknowledges a salesperson’s success”** – Sales is a tough racket. Rejection goes with the territory. Prospective customers often adopt an adversarial stance with salespeople. Incentive pay can make up for these occupational challenges.

Adjusting and Updating Your Compensation Plans

Redo your firm’s sales incentive compensation plan periodically so it remains current and continues to engage and energize your salespeople. Most companies make adjustments, at least around the edges, every year, and make wholesale changes every two to three years. Since sales results tie directly to sales incentive compensation plans, sales-oriented firms pay extremely close attention to updating their pay and incentive programs.

“Firms must pay special attention to their top-producing salespeople during times of incentive compensation plan transition. These are the salespeople that the firm cannot afford to lose.”

For example, the leaders of a carpeting manufacturing company with declining sales decided to change their incentive compensation plan to turn things around. Following the norms in their industry, they paid salespeople a draw against a sales commission. Gross margins on their various brands were 25% to 45%. But since the firm paid salespeople strictly on volume, the salespeople felt no real incentive to push the more profitable brands. The executives wanted to revise the incentive plan to target more profitable carpets and increase overall sales, but that was only one of the changes they needed to make. First, the company trained its salespeople to focus more intensely on upscale carpet retailers. Then, it changed its compensation package to 60% salary, plus 40% variable pay, including bonuses for reaching sales quotas and a 3% commission on higher-priced carpets. After a year, sales of the more profitable brands were up 3% and gross margins had increased 12%. The executives attributed the improved sales and margin figures to the sweeping changes they made in sales training and in the sales incentive compensation plan.

Sales Incentive Compensation Plan Requirements

A good sales incentive compensation plan should meet the “3 Cs” rule. It should be “consistent” with company strategy, “compatible” with related programs (like hiring and performance management), and “consequential” – that is, it should change sales results. The plan must help the corporation optimize the following five aspects of sales:

1. **“Company results”** – A sales incentive compensation plan must help the corporation attain its sales goals and build its market share. Measure short- and long-term results.
2. **“Customer results”** – Your plan must meet the needs of your customers, who want superior products and services at reasonable prices. Determine if consumers are buying your products and services at the volume you’ve targeted.
3. **“Salesforce activities”** – Salespeople handle “lead generation, needs analysis, solution development, proposal presentation, negotiation, installation” and more.
4. **“Salespeople”** – Your plan must serve salespeople who want to earn top pay and enjoy their jobs.
5. **“Salesforce effectiveness drivers”** – Pay is the primary driver, but there are others. They include “definers,” which are salesforce parameters that sales managers set, such as new strategies or redesigned sales operations. “Shapers” are driving processes, like “hiring, training and coaching,” that mold salespeople’s approach to their work. “Enlighteners,” such as research, that help salespeople understand their work. “Exciters” are motivational drivers, such as reward programs or inspirational leaders. “Controllers” drive sales effectiveness through supervision, administration and performance monitoring.

“In the United States alone, companies spend \$200 billion each year on variable salesforce compensation – approximately as much as they spend on advertising.”

Satisfying the disparate demands of your company, your consumers and your salespeople with a single sales incentive compensation plan is tricky. But leaving out any of these components of the overall “sales management system” can cause sales problems.

Executives sometimes assume that a drop in sales means the sales incentive compensation plan is flawed. That may not be the issue. The problem may come from any of the components above, or from the salesforce’s structure, size, training or territories. The company may need to redraw territories, hire better managers, provide improved “data and tools,” or make other changes. So before you alter your compensation plan, make sure the other drivers are performing as desired.

“Frequent incentive payment has several advantages. Salespeople usually prefer more frequent payouts.”

When you review your sales incentive compensation plan, determine if it met its budget. See if it fulfilled its sales goals and if those goals still make sense. Assess whether your short-term incentive programs deflected salespeople from their main sales goals or if they helped you motivate and retain good salespeople. Determine if “payout variations” have the desired effect and if the current plan is fair to all your salespeople. Your objective is to establish a clear program that your staffers like, to encourage productive customer relations and to align sales with your goals. Make sure your new compensation plan provides incentives for the achievements you want to foster before you change your current arrangements. Don’t make major changes unless you know that your existing plan, and not some other factor, is the root of your sales problem.

Designing a New Plan

To design a new compensation plan, first define your goals. Then consider other factors, such as marketing, corporate finances, the sales routine, the efforts of your salespeople, “data availability and accuracy,” and management’s conceptual approach and culture. As you develop the new compensation plan, consult internal experts in human resources, finance and marketing. The new plan should account for “pay level,” “salary-incentive mix,” “performance measures” and the “performance-payout relationship,” since they interrelate. Decisions in one area affect the other areas.

“Selecting Performance Measures”

Before you can reward performance, you must establish the right criteria for evaluating it, including sales and customer results. Measure “gross margin, orders, collections, sales per rep, market share [and] value perception.” On the customer end, factor in your number of repeat buyers, how much merchandise customers send back, how deeply you have saturated the market, how much sales are increasing, and whether consumers are content and loyal. Monitor how well your reps handle prospecting, sending out proposals, serving customers and controlling account turnover. Create “objective, measurable, fair, adaptable and understandable” criteria that measure only those factors that salespeople determine by their own actions.

“Finding the Best Salary-Incentive Mix”

Develop a “pay mix scorecard.” Include these categories:

- **“Sales process and roles”** – Assess each person’s sales routine, customer conversations, administrative management, frequency of sales calls and other measures of achievement.
- **“Salesforce causality”** – To what extent are your salespeople themselves responsible? How much of your sales volume is due to their efforts?
- **“Measurability”** – Consider outcomes that can be quantified as well as the person’s track record and your industry’s standards.
- **“Culture”** – In your company, does the firm or the salesperson own each account? Determine whether your salespeople should focus on the customer or the transaction. Examine whether the company should prioritize short-term bursts of activity or long-term results, and team cooperation or competition. Make sure your salespeople are flexible about adjusting their processes to serve customers.
- **“Management philosophy”** – Define management’s expectations and see if salespeople meet those standards.

“When cutting salesforce pay, be prepared to lose some salespeople, particularly if the pay cut makes the firm’s salesforce pay scale less favorable than that of other firms in the industry.”

Consider how each of these elements should affect your salary-incentive mix. Weigh each factor based on your company’s circumstances.

“Determining the Right Performance-Payout Relationship”

If your salespeople work independently to make sales happen, use a commission plan. Bonus plans give managers flexibility if needed, for instance, to reassign territories. Make sure that performance drives sales earnings, not individual geographic assignments. If numerous corporate divisions share the same salesforce, don’t create an incentive plan with different performance metrics for each unit. That encourages salespeople to cherry pick the simplest process for earning their pay. Aggregate your performance measures to ensure a “balanced selling effort.” Set sales goals that build excitement. Increase the payout rate as people come close to their objectives. Keep the plan simple, fair and encouraging.

So, How Much Should You Pay?

Figure the range of average compensation for each sales job. Then, calculate what people will earn at each sales achievement level. Pay too little and you won’t draw top people. Pay too much, and you throw away profits and make your salespeople feel entitled. Consider current “labor market values” for your sales jobs, as well as past pay levels, budget, the degree of control a salesperson exerts over sales and customers, what your competitors pay, and the role each salesperson plays, internally or out in the field. Look at how much authority salespeople have to drive sales. Consider your firm’s salary standards, and local and industry compensation norms. Seek data on pay standards when you interview prospective or departing salespeople. Complex or highly technical sales work should earn more. Consider other factors, from security to the pool of available personnel.

“We work for money, but we strive for plaques.” (Andy Anderson, former vice president of sales, Searle)

Limit special performance contests so you don’t deflect sales reps from their main strategic sales goals. Use such programs only for “short-term causality” or for special promotions to keep salespeople engaged. Recognition programs for reps who work alone show the company’s appreciation, and often prove more beneficial than contests and special performance programs. New pay plans break the routine. Since that may be unsettling for your salespeople, clearly communicate any new plan’s rationale, how it works and why it will benefit them. Effective administration of your new sales incentive compensation plan is very important, but not easy to achieve. Make sure you have the staff and administrative procedures and personnel you need.

About the Authors

Andris A. Zoltners and **Prabhakant Sinha** teach college business courses. They co-founded a business-consulting firm. **Sally E. Lorimer**, business consultant and writer, is a former principal at Zoltners and Sinha’s consulting firm.
