HARVARD | BUSINESS | SCHOOL

9-517-090
REV: MAY 21, 2019

DOUG J. CHUNG

Kjell and Company: Motivating Salespeople with Incentive Compensation (A)

Malmö, Sweden: April 10, 2015. It was a sunny spring afternoon at the headquarters of Kjell & Company (pronounced "shell"), a retail electronics chain that cited customer service as its foremost value. Thomas Keifer, Kjell's CEO, was meeting with the head of Sales, Joel Rönneman, and the CIO, Martin Knutson. The meeting's main agenda was to decide whether to change the compensation structure of Kjell's in-store salespeople. The proposed change involved the frequency of quotas—that is, how often individual sales performance should be evaluated.

At the time, salespeople were evaluated each month, against a monthly quota, and compensated accordingly. Anecdotal evidence from regional sales managers and feedback from the field suggested that salespeople who fell short early in a given month simply gave up because they had no realistic chance of meeting the quota. To tackle this problem, shorter-term quotas had been proposed. If such a change were authorized, however, Keifer insisted on strong alterations to the compensation structure, not just tweaks; he viewed minor changes as inadequate to motivate behavior change. In fact, Keifer was considering transitioning employees to a daily-quota structure—that is, salespeople's performance would be evaluated each day against a daily quota, and their commission would be calculated accordingly. The idea was to give salespeople a fresh start each day, so that their past performance would not undermine their present or future motivation. Keifer anticipated that a daily-quota plan would mitigate the resigned attitude of salespeople who had had bad luck early in a month.

However, Keifer recognized the possible negative effects of a shorter-term quota plan, which could provoke anxiety and stress; salespeople, constantly worrying about meeting their quota, could lose motivation. Also, they might prefer the flexibility to vary their effort depending on their recent performance.

Keifer was also undecided about how to implement a change in the compensation structure across the firm's 84 stores. Should he first introduce a new plan experimentally, limiting it to salespeople at a few selected stores, or launch at all 84 stores simultaneously? If the former, how many stores should be involved? Experimenting with a select group of salespeople would help his team more precisely analyze the plan's effectiveness and correct for potential problems before introducing a full-fledged transformation. But this approach had its own flaw: a special compensation plan for a select few employees was at odds with Kjell's "one-for-all" human resources (HR) policy. The firm prided itself on its fair and straightforward HR policies, including compensation. The one-for-all policy had a

Professor Doug J. Chung prepared this case. It was reviewed and approved before publication by a company designate. Funding for the development of this case was provided by Harvard Business School and not by the company. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

motivating effect on employees that Keifer valued highly. He worried about the effect on motivation and morale if employees learned that some salespeople were being treated differently from others.

Sweden

As of 2015, Sweden, geographically, was Europe's third-largest country; situated on northern Europe's Scandinavian Peninsula, it boasted a landscape of dense forests, tall mountains, and a rugged coastline. But it was also among the most sparsely populated European countries, with a population of less than 10 million, 85% of whom lived in urban areas.[1] Like most western European countries, Sweden was a parliamentary democracy; general elections were held every four years. Sweden was known for its history of international neutrality and its high standard of living. In 2015 Sweden ranked as the ninth most competitive economy in the world, with a 2014 GDP of $448.25 billion, partly attributable to innovation and technological advancement.[2] Fully 82% of adults aged 25–64 had completed upper secondary education.[3]

Sweden's advanced comprehensive welfare system, largely funded by taxes, provided generous social benefits, including free health care, free university tuition, and at least five weeks of annual paid vacation. Swedish culture emphasized fairness and equality: the fundamental principle was that everyone should enjoy the same opportunities, rights, and obligations in all areas of life. The country's commitment to gender equality was embodied in the government-mandated parental-leave policy, which allowed a couple to share 480 days, or around 16 months, of paid parental leave when a child was born or adopted.[4]

Kjell & Company

Kjell first opened for business in 1988 as a telephone and electronics accessory shop in Sundsvall, a small city on Sweden's northeast coast. As the business grew, its founders—the brothers Marcus, Mikael, and Fredrik Dahnelius—opened a second shop in Malmö, Sweden's second-largest city, located only 25 miles from Copenhagen, Denmark. Business flourished; by 2015 Kjell had 84 stores, all company-owned. Most were located in the centers and outskirts of Sweden's three most populous cities: Stockholm, Gothenburg, and Malmö. (See **Exhibit 1** for the locations of Kjell & Company stores.)

In fiscal 2014, Kjell recorded revenue of 1.04 billion Swedish krona (SEK), or roughly $107 million (see **Exhibit 2** for 2012–2014 financial statements.) The second-largest retailer of home electronics in Sweden (with a 17% market share), Kjell closely trailed Elgiganten, which operated throughout Scandinavia and had a 20% market share in Sweden. Kjell's products consisted mostly of accessories for home electronics and phones (e.g., networking accessories, headsets, and phone cases) and parts for consumer electronics and appliances (e.g., semiconductors and switches); the stores also sold small to medium-sized electronic goods, such as wireless routers, data storage devices, network appliances, and DVD players. Kjell carried 9,500 SKUs in nine product categories. Prices ranged from less than SEK 10 ($1.1) to SEK 5,000 ($550) or more; the average item was priced slightly over SEK 200 ($22).[a] At any given time, the firm employed a direct sales force of about 350 salespeople.

Kjell was renowned for exceptional customer service. In-store salespeople were highly trained to be knowledgeable about technical specifications; as a result, customer loyalty was high. Tech-savvy customers particularly valued Kjell's high-quality service. Typically, an entering customer took a wait number from a dispenser; when the number was called, a salesperson would determine the customer's

[a] Converted to US dollars using the exchange rate 0.11 (April 10, 2015).

needs, locate suitable products in the adjacent warehouse, and finalize the sale. (See **Exhibit 3** for photographs of the in-store experience.) In-store assistance was also provided on an ad hoc basis. Customers valued the breadth and depth of Kjell's product portfolio, as well as the staff's helpfulness and technical expertise. Excellent sales assistance and service paid off: Kjell enjoyed a net profit margin close to 10%, quite high in the retail business.

Kjell's Sales Force

To build a strong sales team, Kjell recruited candidates passionate about electronics and seeking a long-term position rather than a placeholder job. Technical expertise, though not required, was highly valued, because customers' needs were becoming ever more sophisticated. Sales associates received technical training immediately after being hired and at regular intervals thereafter. Compensation was only slightly higher than the industry average, but Kjell was considered a fun and fruitful work environment; the firm valued its people and provided ample opportunities to climb the ladder. In fact, most senior managers, including Rönneman and Knutson, had begun their careers with Kjell as sales associates. Each store was staffed by 3–9 salespeople and a store manager; regional sales managers typically oversaw 10–12 stores.

The Sales Force Compensation Plan

As of April 2015, Kjell's sales force compensation plan consisted of a fixed salary (averaging SEK 21,000, or about $2,300) based on tenure at the firm, and a variable commission on sales. The commission rate (and thus the amount of commission) was determined by sales performance, measured in average sales per hour (SPH). The compensation plan had five tiers, as illustrated in **Table A**. If a salesperson's average SPH was SEK 1,500 at the end of the evaluation period, he or she would receive a commission of 0.27% on total sales. An average SPH of SEK 2,500 or more would earn the highest rate of commission, 2.0%. Because quotas were calculated in average SPH rather than absolute amounts, and because of the discrete nature of the tiers, variable pay was characterized by a "kink" at each tier level that resembled a quota-based commission-plus-lump-sum bonus scheme. **Exhibit 4** illustrates the variable pay of a salesperson assigned 140 hours a month: as he or she reached each quota level, there was a step-jump in pay due to discretely accelerating rates. A salesperson would earn SEK 10,000 in variable pay if his or her monthly sales totaled SEK 500,000.

Table A Kjell's Variable Compensation Plan

Tier	1	2	3	4	5
Quota (SEK/hour)	1,400	1,800	2,000	2,350	2,500
Commission (%)	0.27	0.67	0.9	1.5	2

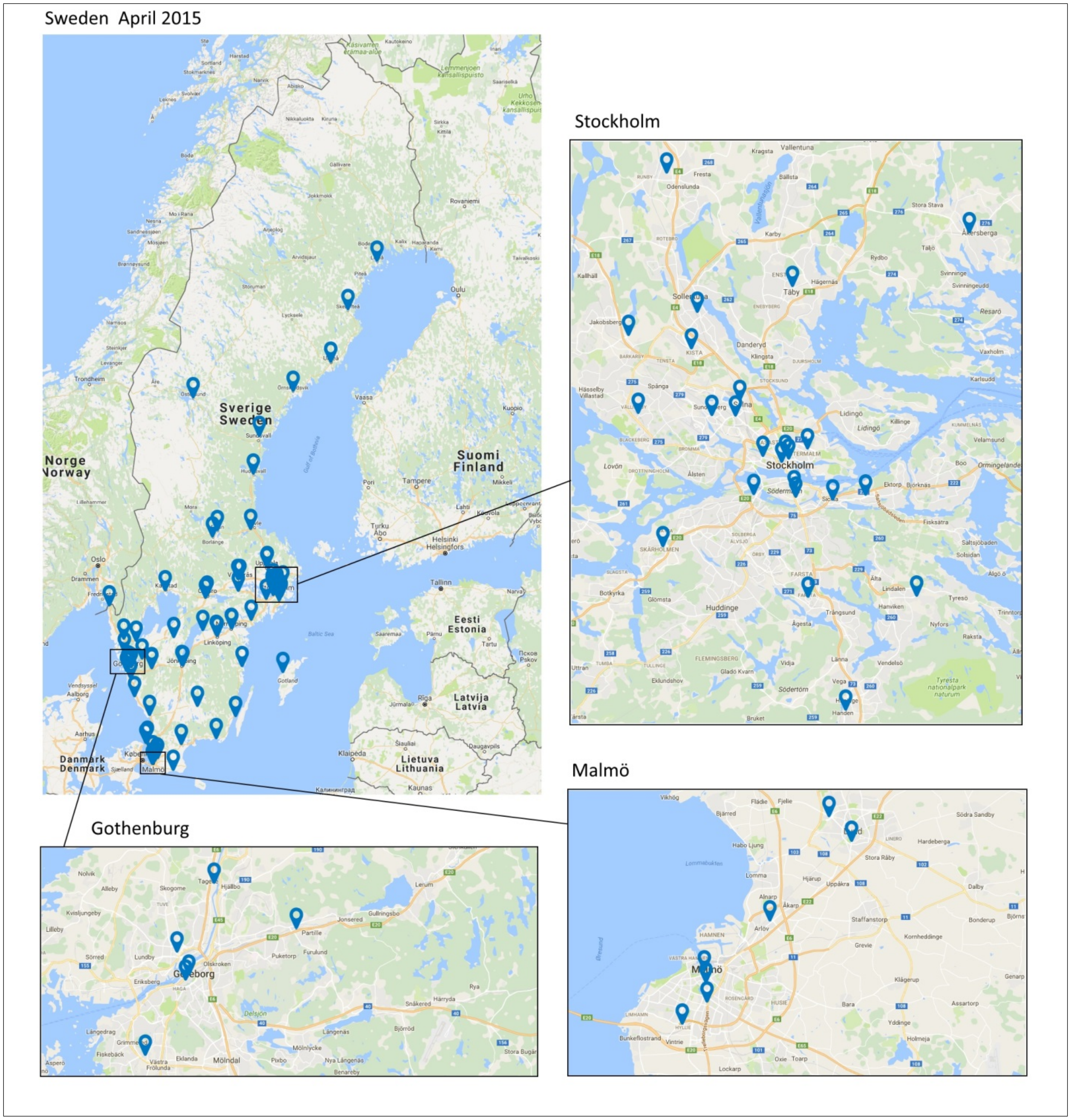
Source: Company documents.

Next Steps

During his numerous field visits, Keifer heard from sales associates that, if they fell behind in sales during the first week of a month due to bad luck (e.g., good weather), it was very difficult to meet the quota even with extra effort. In keeping with this common complaint, he noticed a tailing-off in sales at the ends of months, especially for low-performing salespeople; regional managers reported having observed the same trend. Keifer was thus eager to change the compensation structure from a monthly- to a daily-quota plan in order to better motivate salespeople. Sales toward a daily quota would accumulate for only positive sales and not returns, the same as the accumulation method used for monthly quotas. The key rationale for daily quotas was to give salespeople a fresh start every day to maintain motivation throughout the month. But several features of the plan worried Keifer. First, having to think about meeting a quota day in and day out could increase salespeople's anxiety and stress. Second, a daily-quota plan could merely provoke daily-income targeting without increasing motivation. Third, a daily-quota plan would reduce salespeople's flexibility, making them less able to concentrate their efforts on particular portions of a month in accordance with their individual needs.

If the daily-quota plan was green-lighted, furthermore, the implementation of the change was an additional worry. One option was to include all salespeople in the new scheme from the start; the other was an experimental launch at a handful of stores, comparable to a pilot study, to analyze the results before launching at all 84 stores. Experimentation had certain advantages, but Keifer favored introducing the change at all the stores at once. He valued the one-for-all HR policy's emphasis on fairness, which was the backbone of employee-firm relationships at Kjell. Keifer feared a severe loss of trust if it were to come to light that different plans existed for different salespeople. Most of upper management agreed; many had begun their careers at Kjell in sales, and the one-for-all policy was the foundation of aspiration at Kjell. A decision had to be made soon. Implementation of such a drastic change would require several days of planning, including coordination with information technology (IT), HR, and the Sales department.

Exhibit 1 Kjell & Company Store Locations, April 2015



Source: Company documents.

Exhibit 2 Kjell & Company Financial Statement, 2012–2014 (amounts in SEK thousands)

Key Figures / Year	2014	2013	2012
Net sales	1,040,031	930,529	814,330
Other revenue	1,350	919	1,494
EBIT	101,774	81,491	59,736
Profit after financial items	101,220	80,857	59,537
FTE employees	524	463	407
Revenue per employee	1,985	2,010	2,001
Cost of personnel per employee	358	503	474
Operating profit, EBITDA	115,140	93,419	70,596
Change in net sales	0.1177	0.1427	0.1901
Du Pont model	0.2523	0.264	0.2242
Net profit margin	0.0979	0.0876	0.0734
Gross profit margin	0.5359	0.5303	0.5115
Working capital/revenue	0.159	0.0921	0.089
Solidity	0.4592	0.3449	0.3495
Liquidity ratio	0.8427	0.4948	0.5077

Source: Company documents.

Exhibit 3 The In-Store Experience, Kjell & Company

1) Ticket dispenser

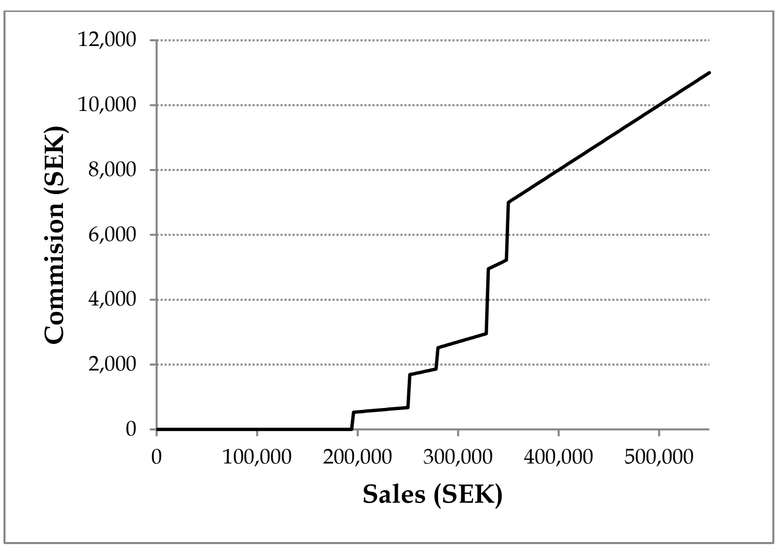
2) Ticket-number indicator

3) Sales assistance

4) Warehouse

Source: Company documents.

Exhibit 4 Existing Relationship between Monthly Sales and Commission



Source: Casewriter, drawing on company documents.

Note: The exhibit illustrates monthly commission pay for a salesperson assigned 140 hours a month, April 2015.

Endnotes

[1] Yearbook of housing and building statistics 2007, Statistics Sweden, http://www.scb.se/en_/Finding-statistics/Publishing-calendar/Show-detailed-information/?publobjid=4638, accessed January 18, 2017.

[2] Michael B. Sauter, Thomas C. Frohlich, Samuel Stebbins, and Evan Comen, "The Best and Worst Economies in the World," 24/7 Wall St., September 30, 2015, http://247wallst.com/special-report/2015/09/30/the-best-and-worst-economies-in-the-world/2/, accessed January 18, 2017.

[3] "Sweden," Organization for Economic Cooperation and Development, http://www.oecdbetterlifeindex.org/countries/sweden/, accessed January 18, 2017.

[4] "Gender Equality in Sweden," Swedish Institute, https://sweden.se/society/gender-equality-in-sweden/, accessed January 18, 2017.