



Sales Compensation Best Practices

Compensation models for maximising sales performance

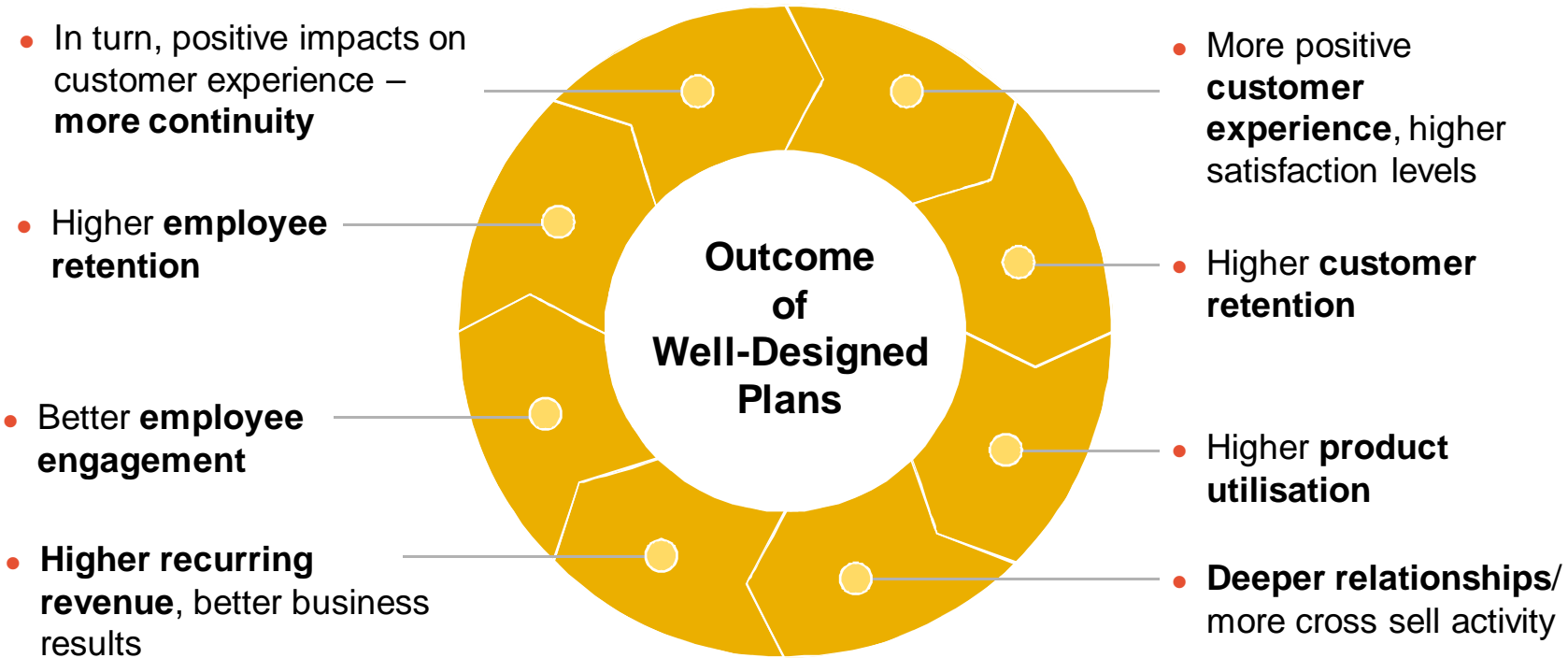
Sales Institute of Ireland

12 October 2011

Why do we have unique sales incentive plans?

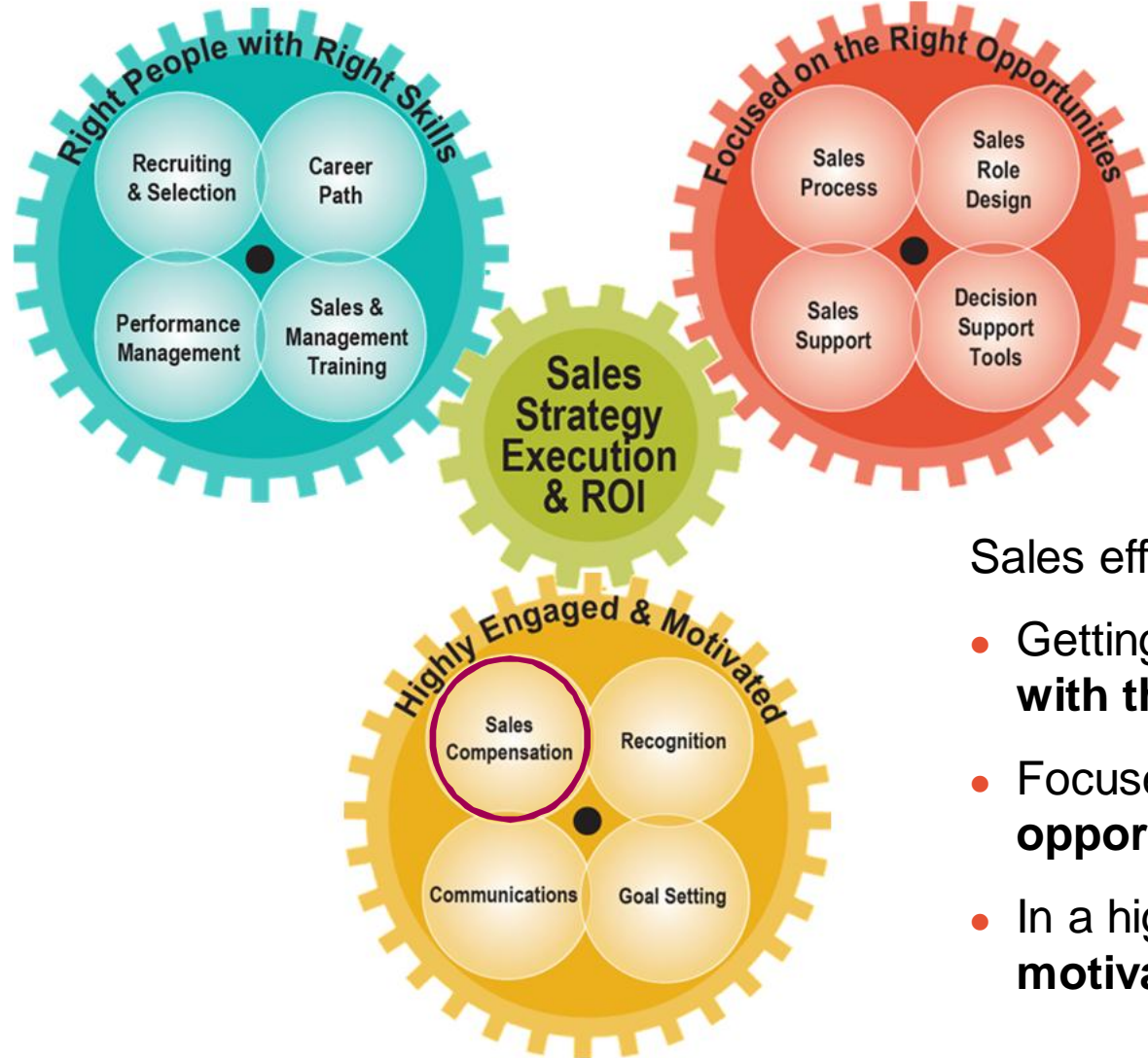
Incentive Compensation Objectives

Attract and retain	Focus effort	Motivate performance
--------------------	--------------	----------------------



Well designed incentive plans focus, motivate, and engage talent

Sales compensation is only one of a variety of tools at management's disposal



Sales effectiveness is all about:

- Getting the **right people with the right skills** . . .
- Focused on the **right opportunities** . . .
- In a highly **engaged and motivated** fashion

What makes for an effective sales compensation plan?

Outcomes of Effective Sales Compensation Plans	Means of Achieving
I. Reinforce strategy and desired behaviours	<ul style="list-style-type: none"> • Utilise the right performance measures with appropriate weights
II. Reflect the nature of the sales role in compensation	<ul style="list-style-type: none"> • Manage sales incentive eligibility • Clarify sales roles • Ensure pay mix and incentive form align with the role
III. Maximise motivational impact of incentive earnings	<ul style="list-style-type: none"> • Pay distribution • Pay differentiation • Pay and performance correlation
IV. Support top talent attraction and retention	<ul style="list-style-type: none"> • Competitiveness of total compensation • Maintain appropriate internal pay equity
V. Govern plan design and administration	<ul style="list-style-type: none"> • Track and manage compensation cost of sales (CCOS) • Identify potential financial and behavioural risks • Create a formal governance process

Performance Measures

Best Practices

- No more than three different measures per plan
- Tied in some manner to individual performance or to a carefully defined group with “shared dependency” in a process or outcome
- Results-based rather than activity-based
- Relevant and controllable by the individual
- At least 20% of incentive pay per element



Key Considerations

- **Strategic** — Does the measure align with the strategic direction of the company?
- **Measurability** — Can the measure be calculated from available data?
- **Manageability** — Do managers’/employees’ actions readily affect the measure?
- **Sustainability** — Can the measure accurately forecast the trend of future results?
- **Communicability** — Can the measure be easily explained to managers, employees, and owners?
- **Unifying** — Can the measure be used by other functions with shared destiny?
- **Stability** — Can the measure be developed so as to prevent manipulation or gaming?

Eligibility: Establish sound criteria to determine sales incentive eligibility

If the position:

- Is directly involved in the sales process
- Spends a majority of time on selling activities (preparing for, following up to, AND conducting customer sales calls)
- Plays a prominent 'customer facing' role
- Has the ability to impact and influence customer buying decisions
- Generates, qualifies and/or pursues sales leads
- Is expected to close sales
- Serves as a designated customer relationship manager
- Manages a group of salespeople

Then...

'Sales' incentive plan is most appropriate

If the position:

- Writes proposals, but has little to no direct customer interface
- Conducts research and analysis for the sales force
- Serves as an administrative assistant to a sales person
- Develops marketing and sales strategies, conducts market research, or develops marketing and sales tools
- Develops and/or manages products
- Spends some time on sales but the majority on other tasks (service, operations, etc.)
- Contributes to sales, but does not close sales

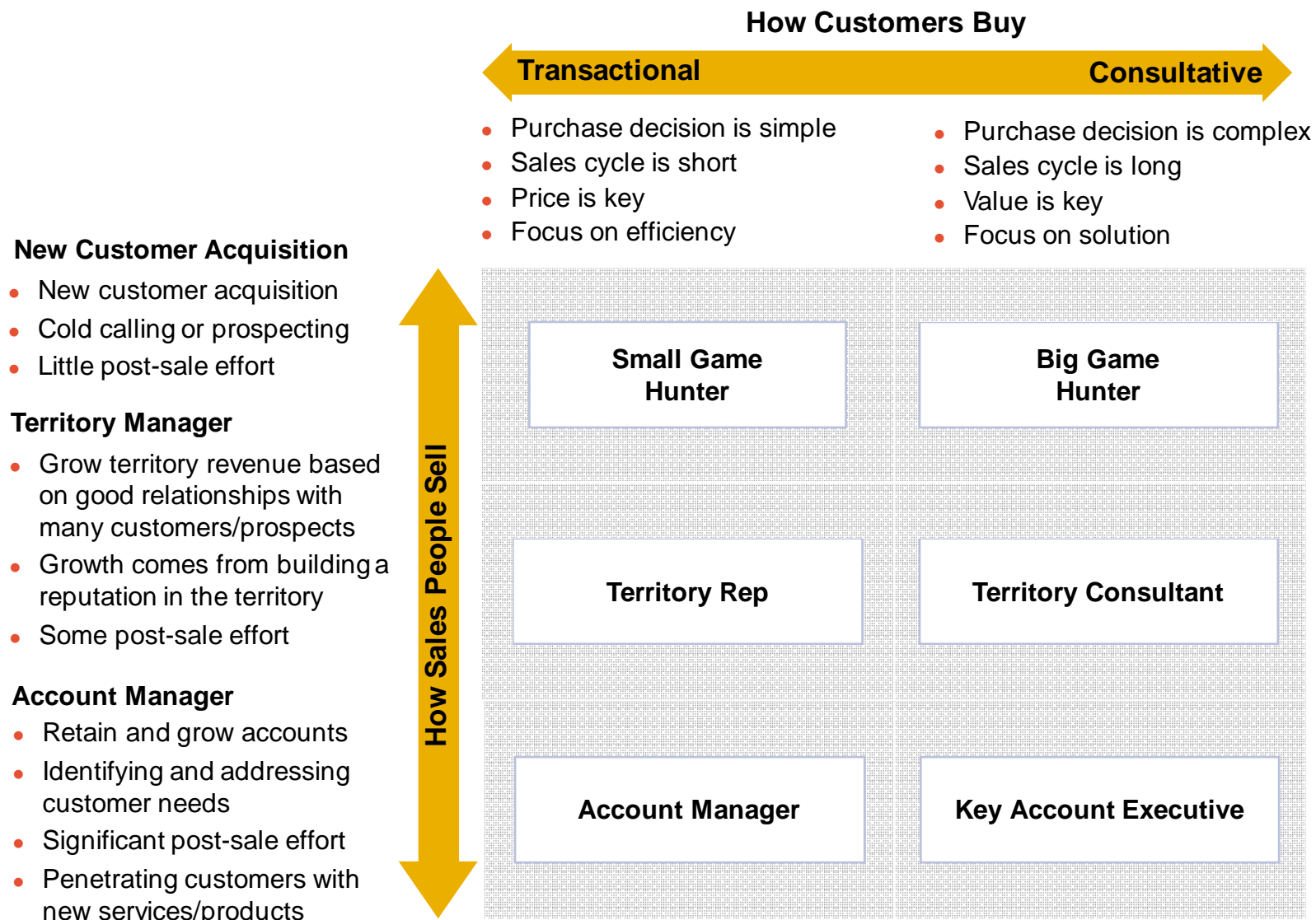
Then...

Corporate incentive plan, with some customisation, is most appropriate

Pay mix implies a trade off between the degree of management control and sales force urgency

Pay Mix	Sales Force Perception	Degree of Management Control	Sense of Urgency
90%/10%	Asleep	Highest	Lowest
80%/20%	Motivational	High	Some
70%/30%	Gets attention	Good	Meaningful
60%/40%	Drives behaviour	Only key things	Significant
50%/50%	High risk	Limited	High
> 50% at risk	Make quota or quit	Minimal to none	Very high

Sales role clarification is the foundation of the sales compensation design process



Sales compensation implications of role differences

- Framework Drives:**
- Pay mix
 - Upside earnings potential
 - Performance area
 - Incentive form

New Business Acquisition

Territory Manager

Account Manager

How Sales People Sell

How Customers Buy

Transactional ← → Consultative

<ul style="list-style-type: none"> • Highest variable pay • Fewest performance areas (1 – 2) • Commission oriented 	<ul style="list-style-type: none"> • High variable pay • Few performance areas (2 – 3) • Commission/bonus oriented
<ul style="list-style-type: none"> • High variable pay • Few performance areas (2 – 3) • Mix of commission and bonus 	<ul style="list-style-type: none"> • Moderately high variable pay • More performance areas (3 – 4) • Mix of commission and bonus
<ul style="list-style-type: none"> • Low variable pay • Few performance areas (2 – 3) • Bonus oriented 	<ul style="list-style-type: none"> • Moderate variable pay • Most performance areas (3 – 4) • Bonus oriented

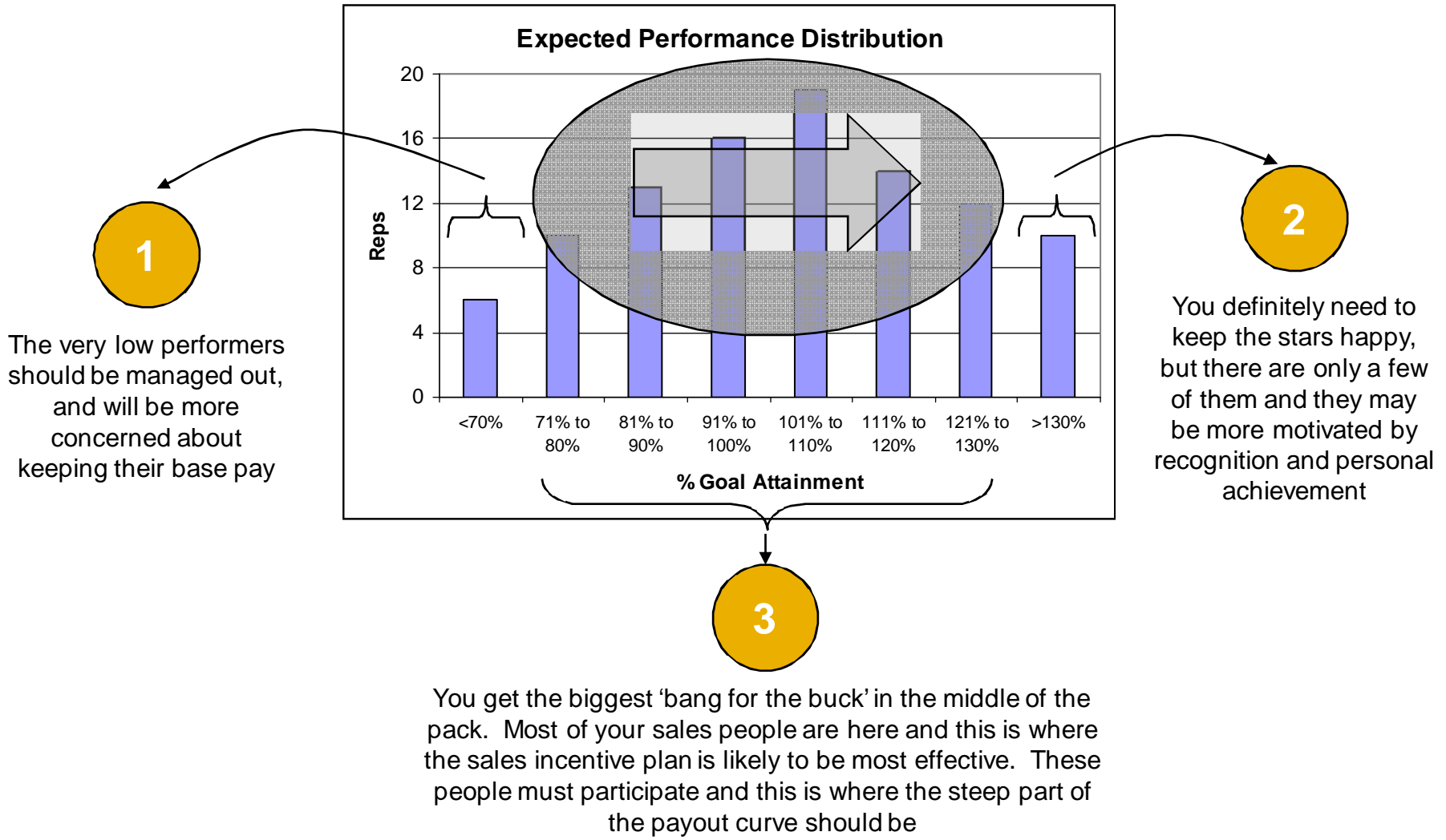
- Position Drives:**
- Pay levels
 - Performance measures
 - Incentive plan mechanics

Mapping roles to the matrix helps narrow the choice of optimal plan designs

Commission vs. bonus — which makes sense?

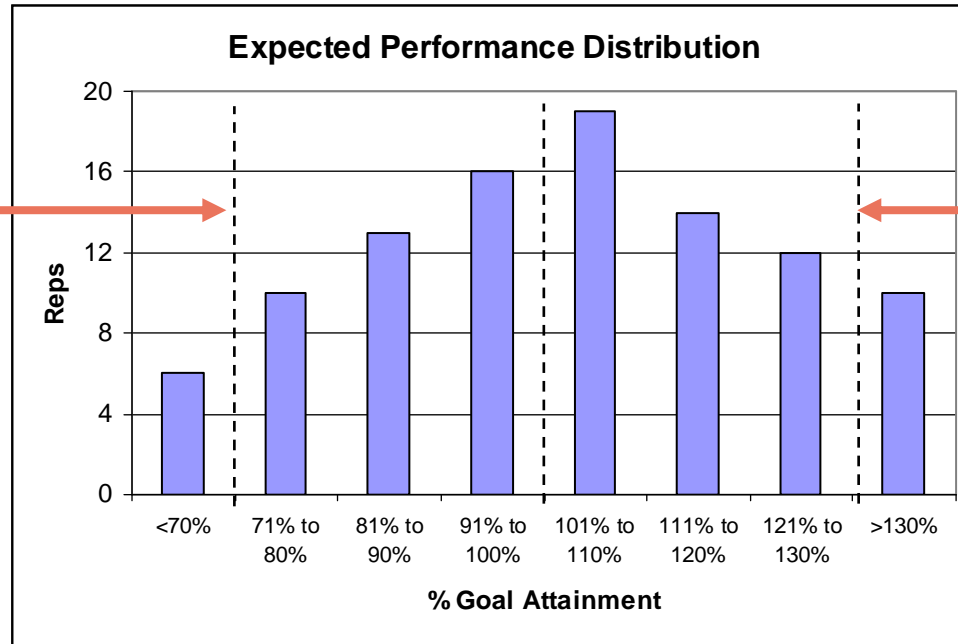
	Definition	When is it appropriate?
Bonus	A planned (or target) payout (\$/€/£) for reaching a predetermined objective(s); typically expressed as percentage of a target bonus or base salary, or as a flat currency amount	<ul style="list-style-type: none"> • Cost of labour philosophy • High goal-setting confidence • Mature business/industry • Low or high prominence • Unequal territory sizes
Commission	A piece of the business or a percentage of the take; typically expressed as a percentage of gross sales or profit \$/€/£, or as a currency amount per unit sold	<ul style="list-style-type: none"> • Cost of sales philosophy • Low goal-setting confidence • Immature business/industry • Moderate to high prominence • Equal territory sizes

The most effective sales compensation plans move the middle and celebrate the stars



Best practice sales incentive design has 85% to 90% of the population earning at least some incentive

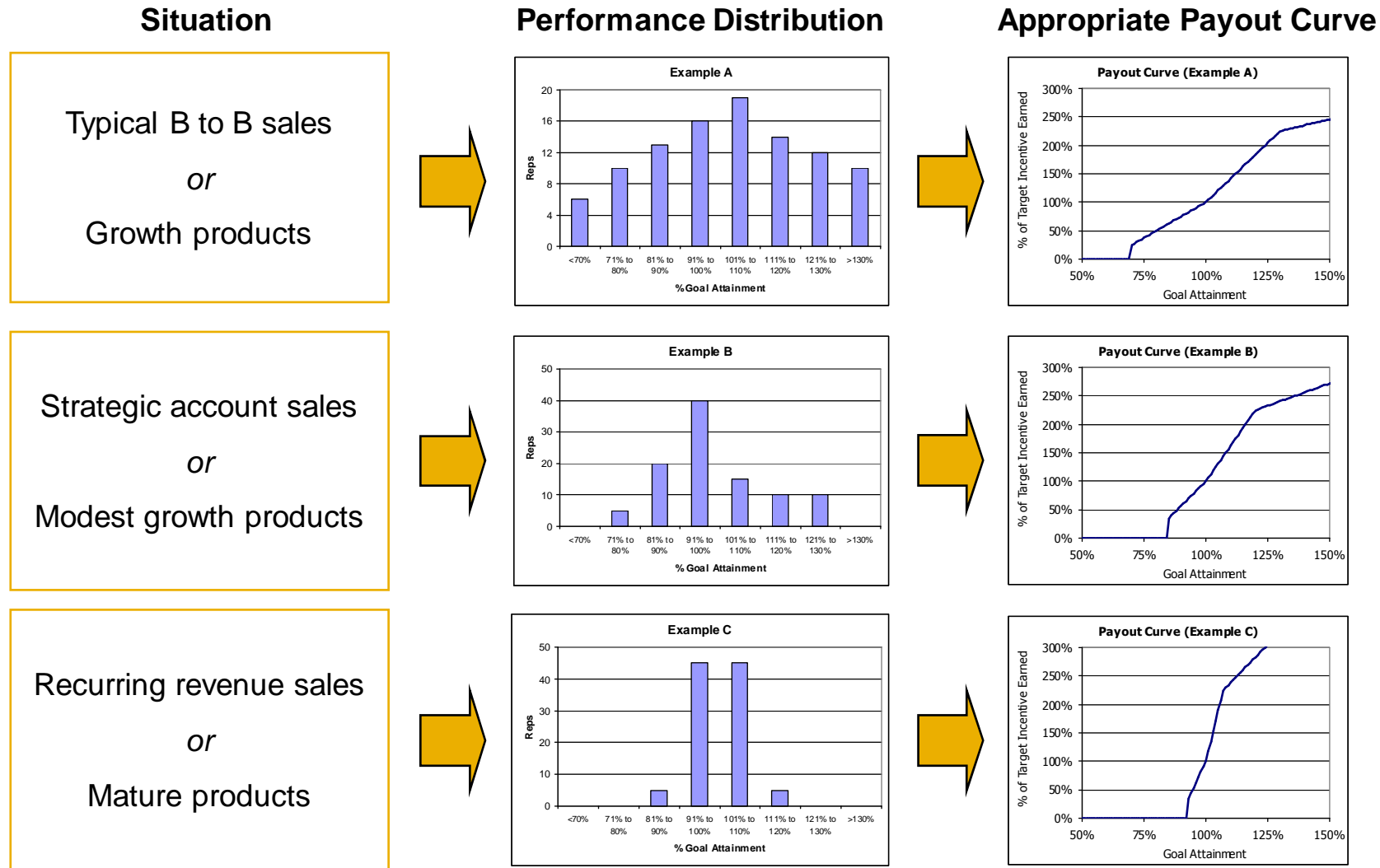
Threshold is the point below which no incentive is paid. It represents 'unacceptable' performance, usually defined as the 10th or 15th percentile.



Excellence is the point at which target leverage is paid. It represents 'outstanding' performance, usually defined as the 85th or 90th percentile.

	Performance	Below Threshold	Target (100% of goal)	Excellence	Above Excellence
Rules of Thumb	Percent of Population	10-15%	55% above, 45% below	10-15% above excellence	
	Amount to Pay	10-50%	100%	200% to 300%	(avoid caps)

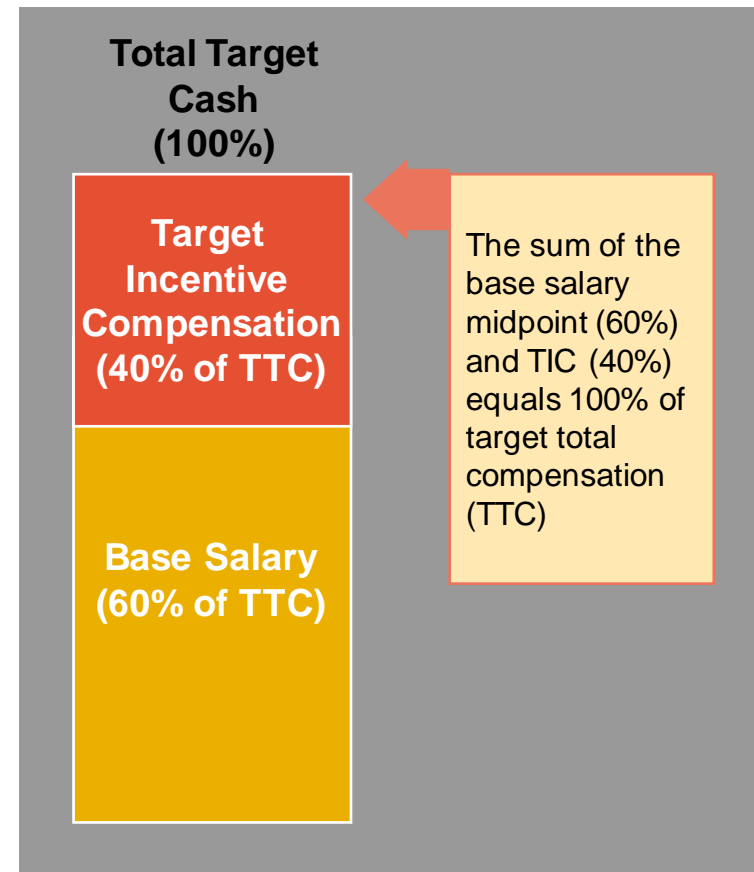
If you expect different distributions of performance, you should have different payout curves



Evaluating target total cash compensation annually helps ensure competitive 'on target earnings'

Key Considerations

- Role specific requirements (experience level, education, specialised knowledge, risk tolerance)
- Company pay philosophy
 - Cost of sales
 - Cost of labour
 - Percentile at which to benchmark pay levels
- Competitive practice
 - Product/service competitors
 - Labour market competitors
- Need for appropriate mix of base salary and incentive
- Need for meaningful and motivational incentive levels
- Justification for different pay levels within and across the sales organisation (e.g., by role, geography)



Most sales organisations target delivering compensation between the market 50th to 75th percentile for 'on target' performance

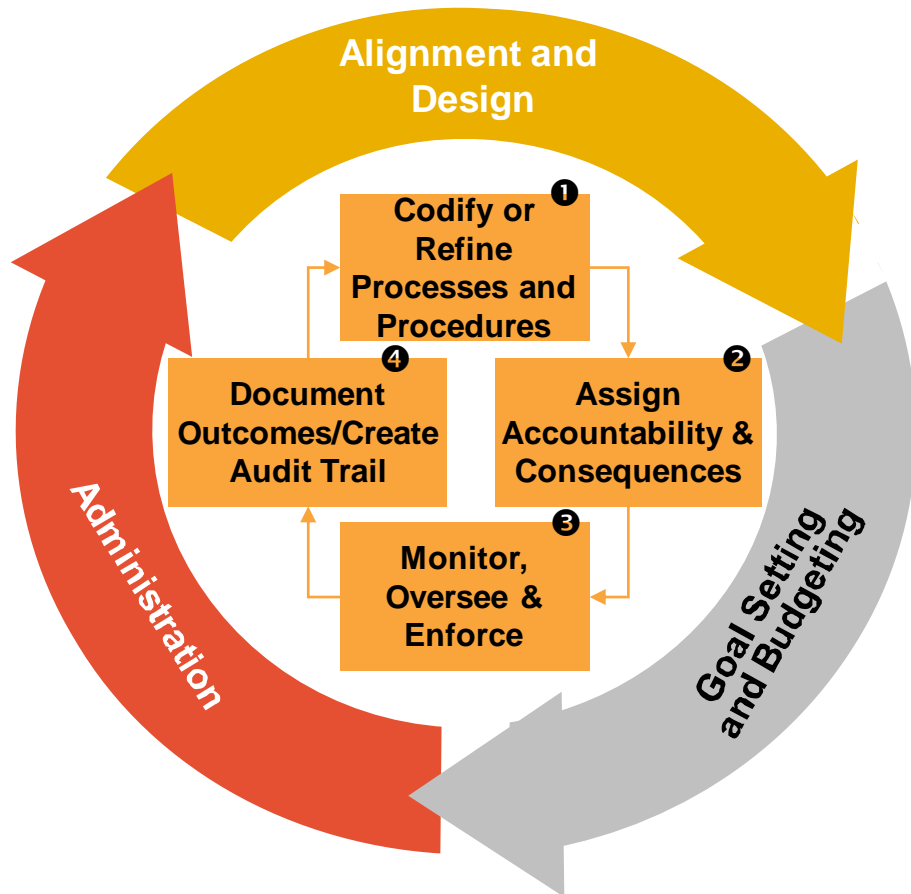
Studies show sales compensation governance is often sorely neglected

“In most organisations, the term *sales compensation governance* is an oxymoron.

Sales compensation is often a free-for-all, ‘owned’ by everyone and no one at the same time, subject to a wide variety of individual pressures, governed by exception and loosely run on an ad hoc basis”*

* Source: Gundy P. and Gaeta E., “*Sales Compensation Governance: The Last Frontier of Corporate Reform*,” Benefits Quarterly, First Quarter 2004.

Creating a plan governance framework



Alignment & Design

- Compensation philosophy
- Incentive plan design
- Scenario modelling and costing

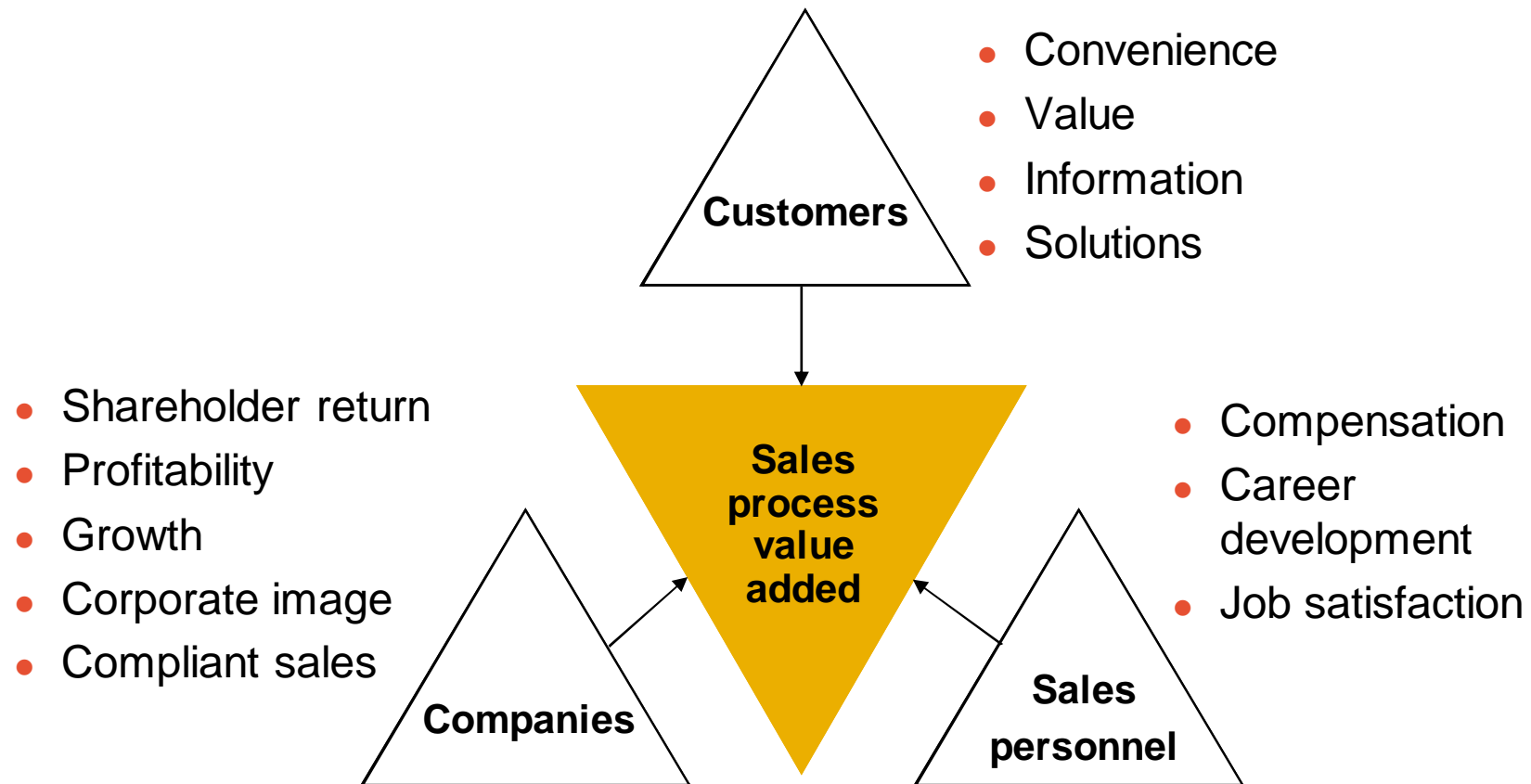
Goal Setting and Budgeting

- Goal setting
- Budgeting, forecasting and accruals

Administration

- Collecting and validating performance data
- Calculating award amounts
- Communicating, motivating and reporting
- Managing exceptions, disputes and adjustments

Done well, sales compensation serves to align the interests of different stakeholders



The topics discussed today are critical to realising this alignment

Thank you!

Ron Burke

Director, Sales Effectiveness & Rewards

Towers Watson

71 High Holborn

London

WC1V 6TP

+44 (0)20 7170 3257 office

+44 (0)7989 337 248 mobile

ron.burke@towerswatson.com