



The Fifth Annual Synggy

Incentive Compensation

Conference and Expo

# How Different Measures Can Be Used in a Sales Incentive Plan



September, 2001  
John F. Tallitsch  
Managing Director

# Sales Representatives as Assets

- Sales representatives are both intellectual and physical assets
- With physical assets, your ability to leverage them—to get additional business value out of them—is limited



You can't use the same school bus on 5 different routes at the same time

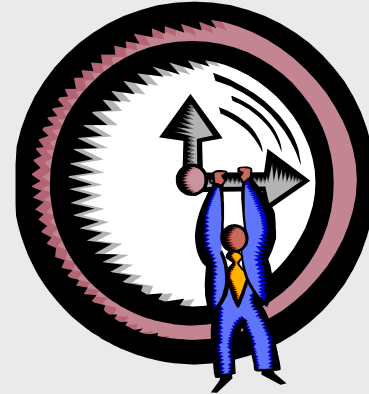


You can't put the same driver on 2 buses at the same time

- With a physical asset, such as a school bus, management decides which route it's going to take

# Sales Representatives as Assets

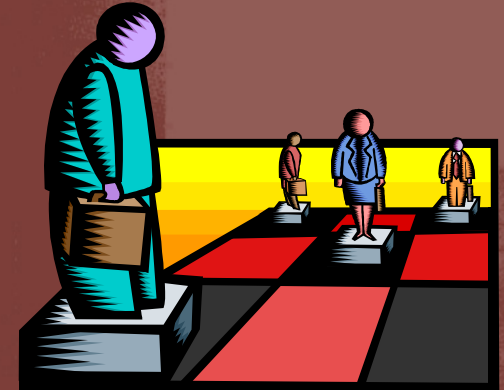
- Current customers
- Prospective customers
- Company's products and services
- Field sales management



**Rivals for the specific uses of  
your Sales Representatives**

# Sales Representatives as Assets

- Sales Reps make daily decisions about whom to call, what product to sell and what selling activities are important
- All these decisions determine how your sales assets are tactically allocated



## Customer-Oriented

- What geography to focus on
- What industry to call into
- Higher vs. lower volume segments
- Highly vs. less profitable segments
- New vs. existing customers
- Headquarters vs. field calls

## Product-Oriented

- New vs. existing
- High vs. low volume
- High vs. low margin
- Easy- vs. hard-to-sell
- Hold price vs. "win" sale

## Activity-Oriented

- Hunting vs. farming
- Selling vs. servicing
- Consultative vs. transactional selling
- Control costs vs. distant location travel
- Leverage self vs. do all personally
- Compete internally vs. cooperate

# Sales Representatives as Assets

- In the end, the burden is on Sales Representatives to decide which:
  - ✓ Accounts to target
  - ✓ Individuals to call on
  - ✓ Products to propose
  - ✓ Prices to present
  - ✓ Customers to serve



**What's available to sales management to guide Sales Representatives' decisions?**

# Performance Measurement as Management Tool

- The fundamental role of a sales force is to:
  - ✓ Sustain existing valuable customer relationships
  - ✓ Achieve profitable revenue growth
- Regardless of whether a company has a “controlling” or “empowering” sales force culture, performance measures can influence sales activity and performance

“ Alignment is the essence of management.”

– Fred Smith, Chairman,  
*Federal Express*

**The purpose of performance measures is to translate business objectives and sales and marketing strategies into specific selling priorities**

# The Anatomy of "Profitable Revenue Growth"

## Profitable

- Margin
- Price Realization
- High Value Products
- Product Mix
- High Value Customers
- Lifetime Value of Customer
- Move Customer to More Efficient Distribution Channel
- Advanced Assessment of Customer Credit Worthiness
- Days of Receivables
- Corrupted Sales Job: Non-Sales/Low Value Sales Tasks
- Band Width Pressures: Too Many Tasks In One Job
- Inappropriate Double Attribution of Results
- Sales Force Deployment
- End-to-end Customer CRM

## Revenue

- Customers
- Prospects
- Markets
- Vertical Markets
- New Products
- Cross-selling: Full Line Product Selling
- Consultative Selling: Value-adding Customer Solutions

## Growth

- Period-over-Period
- Linearity
- Customer Penetration
- Market Share
- New Markets
- Mix of Performance: Resources & Territories
- Channel Partner Performance
- More Customers Buying More
- Order Size
- Replace Low Performers
- Retain High Performers
- Competitive Win-backs

# The “1st Principles” of Performance Measure Selection

- Performance measures should ...
  - ✓ Be consistent with business objectives and aligned with sales and marketing strategy
  - ✓ Be specific to sales role
  - ✓ Reflect nature of sales process
  - ✓ Reflect sales force competencies
  - ✓ Reflect what sales force members can influence directly
  - ✓ Be objective and clearly definable
  - ✓ Have endurance capability
  - ✓ Be capable of providing accurate results and timely participant feedback and payout
  - ✓ Be impartial (not biased toward a participant group or individual)
  - ✓ Be limited – 3 to 5 in number

“  
Simplify,  
always  
simplify.”

– *Albert Einstein*

# Integrating Financial Measures

## Conceptual Incentive Alternative #1

- Sales Goal: Revenue Growth and Priority Product Selling
  - ✓ Part A: Quarterly bonus opportunity for results vs. goal (could be uncapped)
  - ✓ Part B: Quarterly bonus determined by number of quarterly product goals met

### Part A

Territory's Aggregate Revenue vs. Goal	Quarterly Bonus Opportunity
≥ 150%	\$11,500
130%	\$6,500
100%	\$3,000
≥ 90%	\$1,000
< 90%	\$0

+

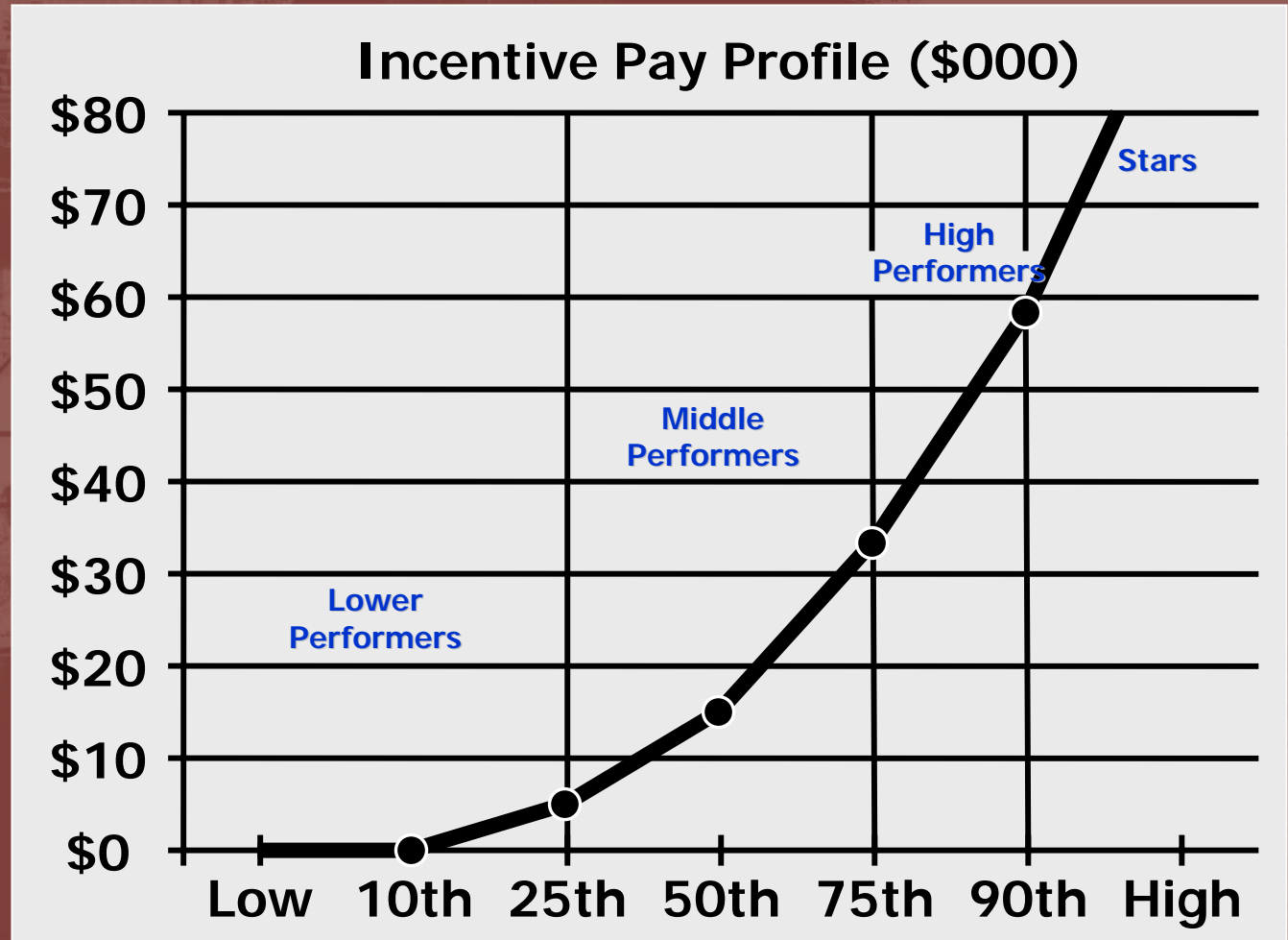
### Part B

# High Priority Product Goals Met	Quarterly Bonus Opportunity
5	\$4,000
4	\$2,000
3	\$1,000
≤ 2	\$0

# Building an Incentive Pay Profile

## Identify Incentive Pay Opportunity

- Pay-to-performance correlation
- Pay winners like "winners"
- Pay losers like "losers"



**Ideal Incentive Pay Profile**

\$0

\$5

\$15

\$33

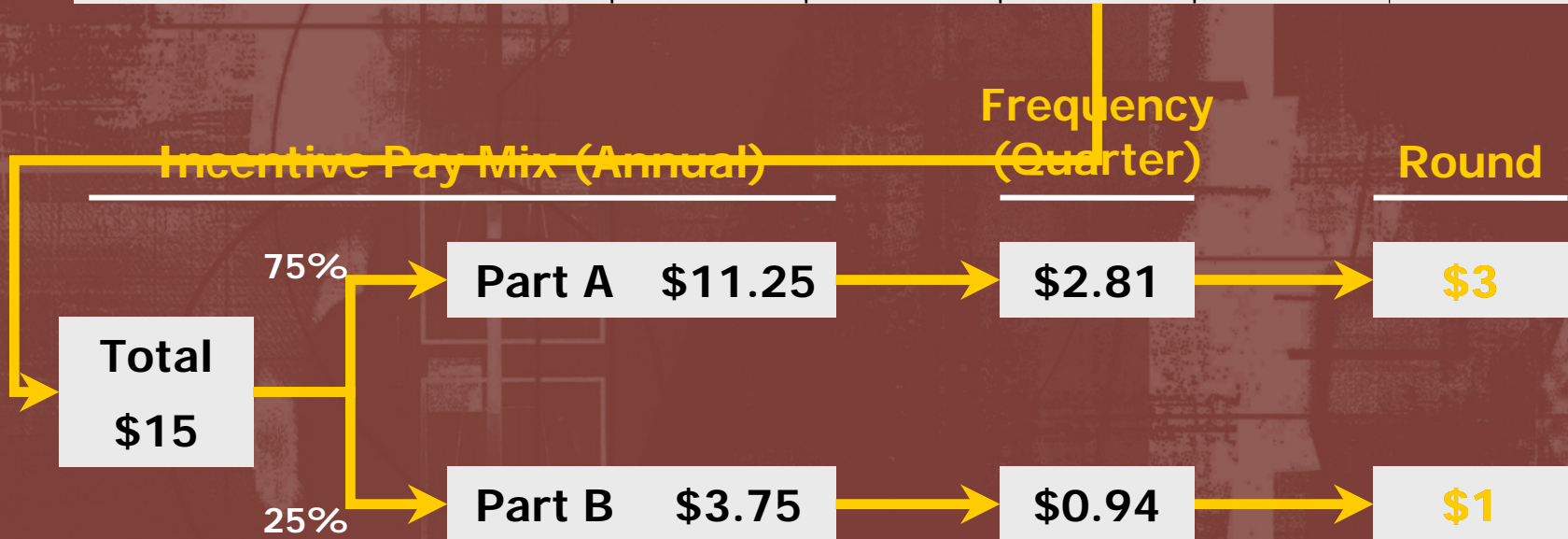
\$58

# Building an Incentive Pay Profile

## Apply Incentive Dollars to Metrics

- Determine incentive pay mix and pay frequency – allocate resultant incentive dollars to each plan metric
- Round values to so that dollar amounts “sing”

Pay Component	Performance Level				
	< Min.	Min.	Target	Excel.	Out.
Incentive Opportunity	\$0	\$5	\$15	\$33	\$58



# Building an Incentive Pay Profile

## Calibrate & Communicate Performance Measures

- Establish performance expectations that are tied to organizational objectives – goals should be challenging, yet attainable
- Communicate rationale for measures and individuals' earning potential for achieving objectives

### Part A

Territory's Aggregate Revenue vs. Goal	Quarterly Bonus Opportunity
≥ 150%	\$11,500
130%	\$6,500
100%	<b>\$3,000</b>
≥ 90%	\$1,000
< 90%	\$0

+

### Part B

# High Priority Product Goals Met	Quarterly Bonus Opportunity
5	\$4,000
4	\$2,000
3	<b>\$1,000</b>
≤ 2	\$0

# Building an Incentive Pay Profile

## Footnote: Incentive Multiples

- Incentive multiples can be used to gauge award discrimination between performance levels
- This can be helpful when trying to determine the “value” of higher performance

### Part A

Territory's Aggregate Revenue vs. Goal	Quarterly Bonus Opportunity
≥ 150%	\$11,500
130%	\$6,500
100%	\$3,000
≥ 90%	\$1,000
< 90%	\$0

$$\frac{\$11,500}{\$3,000} = 3.8$$

- Example: “Outstanding” performance pays 3.8 times “target” performance

# Integrating Financial Measures

## Conceptual Incentive Alternative #2

- Sales Goal: Revenue Growth and Price Realization
  - ✓ Part A: Uncapped quarterly commission on aggregate territory revenue. Commission rate accelerates as revenue delivered exceeds results from prior same period and quota

### Part A

Territory's Aggregate Revenue Performance Range	Commission Rate on Incremental Revenue
> 120% of Quota	8%
110% to 120% of Quota	4%
100% to 110% of Quota	2%
≥ 80% of Prior Year's Result to 100% of Quota	1%
< 80% of Prior Year's Result	0%

# Integrating Financial Measures

## Conceptual Incentive Alternative #2

- Sales Goal: Revenue Growth and Price Realization
  - ✓ Part B: Price realization multiplier elevates the ultimate commission earned on revenue

Part A

X%



Part B

Quarter's Price Realization (PR)	Commission Multiplier
$4\% \leq PR < 6\%$	1.50%
$2\% \leq PR < 4\%$	1.25%
$0\% \leq PR < 2\%$	1.10%
$PR < 0\%$	1.00%

# Integrating Financial Measures

## Conceptual Incentive Alternative #3

- Sales Goal: Retain and Grow Gross Profit From Current High-Value Customers. “Win” New, High-Value Customers. Commercialize New Products
- ✓ Part A and B: Quarterly bonus opportunities on results generated from high-value customers. Eligibility for Part B dependent on threshold performance being attained for current customers, i.e., “don’t seek new customers without first attending to current customers”

### Part A

Current High-Value Customers' Gross Profit \$ vs. Goal	Quarterly Bonus Opportunity
≥ 150%	\$16,000
130%	\$8,000
100%	\$4,000
≥ 90%	\$1,000
< 90%	\$0



**Part B:** Is revenue from current high-value customers ≥ 75% of Goal?  
If yes, Bonus Opportunity is...

New High-Value Customers' Revenue vs. Goal	Quarterly Bonus Opportunity
≥ 150%	\$5,000
130%	\$2,500
100%	\$1,500
≤ 50%	\$0

# Integrating Financial Measures

## Conceptual Incentive Alternative #3

- ✓ Part C: New product revenue should be sought from current and new customers



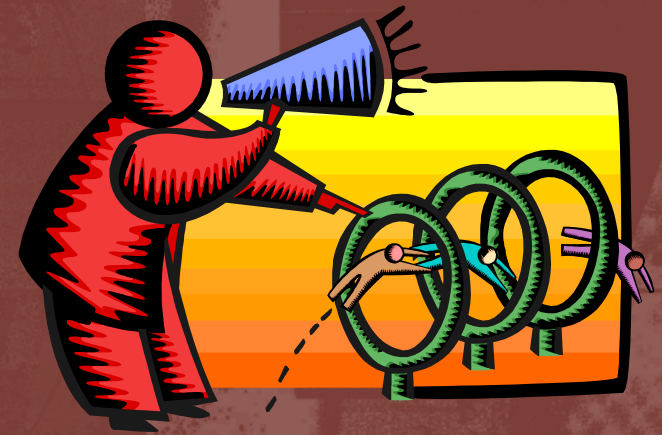
Part C

2% Commission on quarter's revenue from new products

# Financial vs. Non-Financial Measures

- Salespeople are pushed to achieve sales results, but increasingly are not asked to hit a “magic number” before earning their incentive pay
- Today’s Sales Representative functions as a resource coordinator, an account strategist, and steward of the customer relationship

Effective incentive designs incorporate a variety of performance measures, some of which are removed from traditional markers like revenue goals or sales targets



# Non-Financial Measures

- Whether it's customer satisfaction, repeat business, or profitable revenue, companies are trying to align sales force behavior with corporate goals to create long-term, valuable customer relationships
- Companies are driven by several indisputable market conditions:
  - ✓ The marketplace is competitive. Losing current customers will cost you
  - ✓ It is difficult to recruit superb sales people; it pays to improve the quality of current resources

“  
What gets measured gets done.”

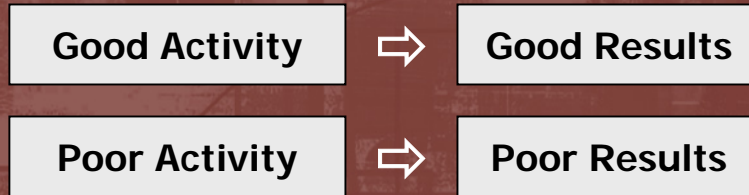
– William Hewlett,  
Hewlett-Packard

**Non-traditional measures give management the ability to tailor incentive designs to the performance opportunities and developmental needs of individual sales people**

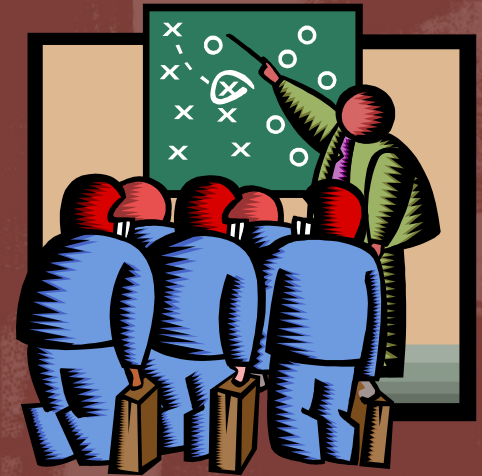
# Financial vs. Non-Financial Measures

- Should sales people be paid on financial or non-financial measures?  
A case for *activity*...

- ✓ Sales force activity drives company results



- ✓ A company benefits when its sales force successfully implements an effective selling process
- ✓ If true, why not pay on activity? Or, non-financial measures?



**The traditional and ultimate measures of corporate success (revenue, cost, profit) may be too historical in today's business environment, which is functioning at ever-increasing speed**

# Non-Financial Measures

- To achieve world class performance, companies must measure the effectiveness of the non-financial activities that produce the financial performance they desire
- Non-financial measures, coupled with a first-rate CRM system, provide timely and actionable information to affect real-time performance
- The subtle, but important characteristic of non-financial measures: most financial results have non-financial underpinnings



**Non-financial measures can be leading coincident indicators and effective enablers of desired financial results**

# Non-Financial Measures

- Why incorporate non-financial measures in your sales incentive plan?
- Is your sales force perfectly...
  - ✓ Recruited?
  - ✓ Trained?
  - ✓ Structured?
  - ✓ Sized?
  - ✓ Deployed?
- Are your sales and marketing objectives and strategies understood by the field organization?
- Do you have the best sales pay strategy and sales incentive design?



# Non-Financial Measures

**YES!**

Management can  
get out of the way  
and let the sales  
force sell



**NO!**

Ongoing systems  
and processes are  
essential

**Even within an empowered employee culture,  
non-financial performance measures can be used  
to leverage sales management's other tactical  
productivity drivers**

# Non-Financial Measures

- Understanding the chain of drivers and outcomes that lead to revenue and profit is essential for the effective use of non-financial performance measures

“ Management by objective works, if you know the objectives. Ninety percent of the time you don't. ”

– Peter Drucker,  
Management Expert

## Common categories of non-financial measures

Enablers or Drivers	Capabilities	<ul style="list-style-type: none"> <li>■ Product, customer, and market knowledge</li> <li>■ Selling skills: prospecting, targeting, needs identification, presentation, persuasion, negotiation, closing</li> <li>■ Analytical, computer, and time &amp; territory management skills</li> </ul>
	Activities & Behaviors	<ul style="list-style-type: none"> <li>■ Work activities (attention to high-value products and customers)</li> <li>■ Planning and organization</li> <li>■ Behaviors (teamwork, leadership, impact)</li> </ul>
End-Results	Outputs	<ul style="list-style-type: none"> <li>■ Customer satisfaction, retention, and conversion</li> <li>■ Expense control</li> <li>■ Performance rank</li> </ul>

# Non-Financial Measures

## Advantages and disadvantages of non-financial measures

	Enablers or Drivers	End-Results
<b>Advantages</b>	<ul style="list-style-type: none"> <li>■ Greatest opportunity for behavior modification</li> <li>■ Encourage customer relationships</li> <li>■ Recognize cause and effect</li> <li>■ Communicate "how you sell" is important</li> <li>■ Longer-term focused</li> <li>■ Lead to organization-wide distribution of "best practices"</li> <li>■ Consistent with environment of complex and longer sales cycles - e.g., interim milestones promote successful end-results</li> <li>■ Recognize end-results are often driven by opportunities, not individual abilities</li> </ul>	<ul style="list-style-type: none"> <li>■ Ease of design and on-going management - fits with large sales forces</li> <li>■ Performance assessment is simplified - e.g., avoids measuring and rating "intangibles"</li> <li>■ Shift "employability" to individual - may be counter to current HR cultures</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>■ Necessitate individual-level customization</li> <li>■ Require individualized performance assessment</li> <li>■ Call for formalized performance management process - e.g., observation, measurement, assessment, training, coaching</li> <li>■ Require management discipline and impartiality</li> <li>■ Can be viewed as management control of sales process</li> </ul>	<ul style="list-style-type: none"> <li>■ Focus on ends vs. means</li> <li>■ Short-term oriented</li> <li>■ Do not foster professional growth</li> <li>■ "One size fits all" approach - inconsistent with natural variations in situations and opportunities confronting field resources</li> </ul>

# Non-Financial Measures

Traditional performance measures should be augmented in 4 selling environments

Situation	Potential Complications	Augmentation Measures
<p>Sales cycles typically exceed 12 months</p>	<ul style="list-style-type: none"> <li>■ Annual quotas/goals are inappropriate</li> <li>■ Annual incentive plans create cash flow problems for Sales Reps</li> <li>■ Infrequent payouts compromise motivation environment</li> </ul>	<ul style="list-style-type: none"> <li>■ Value proposition that motivates customer to make long-term financial commitment - requires consultative selling competencies</li> <li>■ Milestones tied to accomplishment of sales actions</li> <li>■ Contract signing bonuses</li> <li>■ Performance against account management plan</li> </ul>
<p>Multi-year contracts are the norm</p>	<ul style="list-style-type: none"> <li>■ When should revenue be recognized for incentives?</li> <li>■ What if contract is cancelled?</li> <li>■ What is incentive value of initial vs. continuing revenue?</li> </ul>	<ul style="list-style-type: none"> <li>■ Comprehend contract life revenue, cost-to-serve, and profitability</li> <li>■ Sales tasks and incremental results accruing from cross-selling, avoiding "annuity" mentality</li> </ul>

continued...

# Non-Financial Measures

Traditional performance measures should be augmented in 4 selling environments

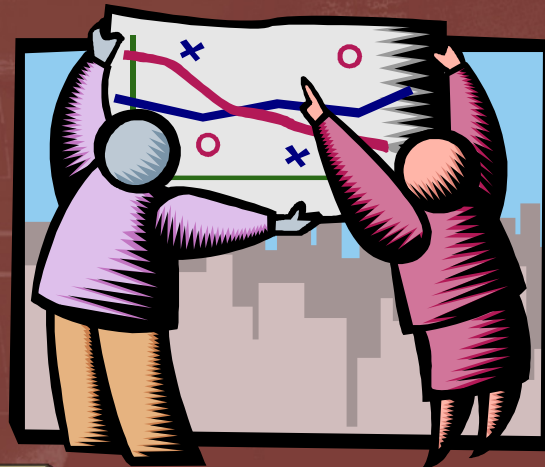
Situation	Potential Complications	Augmentation Measures
<p>Global account sales are prevalent</p>	<ul style="list-style-type: none"> <li>■ Cross-functional and technical-team members are required in sales process</li> <li>■ Worldwide sales and implementation activities must be coordinated</li> <li>■ Global customers often expect unique services and benefits not comprehended by traditional sales goals</li> <li>■ Cross-location customer information is neither uniform nor complete</li> <li>■ Performance tracking and reporting are complicated</li> <li>■ Selling attention is focused on one or few current customers or targets</li> <li>■ Long sales cycle</li> <li>■ Country vs. global and cross business unit attribution of results</li> </ul>	<ul style="list-style-type: none"> <li>■ Short-term financial results and milestones tied to accomplishment of strategic sales and implementation actions</li> <li>■ Identification of opportunities to capture future opportunities - where the product is designed, decision to make or buy is made, supplier/operations linkage exists (end-to-end customer relationship management)</li> <li>■ Incentive funding on customer/deal P&amp;L, emphasizing return on cross-functional investment</li> <li>■ Accommodate dedicated vs. borrowed or virtual resources and specialized customer coverage</li> <li>■ Comprehend external partners integrated in custom solution or implementation</li> </ul>

continued...

# Non-Financial Measures

Traditional performance measures should be augmented in 4 selling environments

Situation	Potential Complications	Augmentation Measures
<p>E-commerce is or can be significant sales channel</p>	<ul style="list-style-type: none"> <li>■ Extent that field sales organization is responsible for generating e-commerce results and providing fulfillment - assisted or unassisted e-commerce sales</li> <li>■ Need to avoid channel conflict, enabling migration of appropriate customers to e-commerce channel</li> </ul>	<ul style="list-style-type: none"> <li>■ Differentiate profit definitions - assisted vs. unassisted e-commerce channel sales, customer incentives to encourage e-commerce channel usage</li> <li>■ Segment performance measures between sales force's direct and e-commerce sales roles</li> <li>■ Short-term financial results and milestones tied to accomplishment of strategic sales and implementation actions</li> </ul>



# Customer Satisfaction as a Measure

- Customer satisfaction may be a better measure of sales success when results are heavily affected by factors outside the Sales Reps' influence
  - ✓ Economy
  - ✓ Market conditions
  - ✓ Competitors
- However, sales people are not in control of every part of company or customer interaction (e.g., order entry, manufacturing, billing, repair)
  - ✓ Technical details must be overcome
  - ✓ Customer satisfaction is not a valuable performance measure in some industries



# Customer Satisfaction as a Measure

- Some argue that linking compensation to customer satisfaction through 100% commission is most effective
  - ✓ Unhappy customers won't buy
  - ✓ Satisfying the customer produces sales, repeat business, and commissions for the Sales Rep
  - ✓ Case in point: the success of distributors and manufacturers' reps (who are typically on commission-only plans) during the 1990s

## Potential proxies for customer satisfaction

- Number of sales-force-oriented customer complaints
- Percent of customer's purchases from company
- Customer's purchase size as percent of average customer purchase
- Customer's price as percent of company's average price received
- Percent of sales derived from existing customers

“The purpose of business is to create and keep a customer.”

– Theodore Levitt,  
Edward W. Carter  
Professor of Business  
Administration Emeritus,  
Harvard Business School

# Integrating Non-Financial Measures

## Conceptual Incentive Alternative #4

- Sales Goal: Achieve and Surpass Gross Profit \$ Goals
  - ✓ Part A: Quarterly, quota-linked variable commission on gross profit

### Part A

Product Category	Commission Rate on Gross Profit \$	
	< Quota	≥ Quota
A, B and C	2.0%	4.0%
D and E	4.0%	8.0%

# Integrating Non-Financial Measures

## Conceptual Incentive Alternative #4

- ✓ Part B: Quarterly bonus tied to results of 3 Key Performance Goals (KPGs) which are territory-level critical success factors



### Part B

KPG #1	Performance Consistency	Was GP\$ $\geq$ quota for 2 or more consecutive quarters?	Bonus if # consecutive quarters $\geq$ quota is...		
			2	3	4
			\$2,000	\$4,000	\$8,000
KPG #2	Priority Customers	Priority customers' % of quarter's aggregate gross profit \$	Bonus if priority customers' gross profit is...		
			< 50%	50% to 60%	> 60%
			\$0	\$2,000	\$4,000
KPG #3	Quota Attainment Rank	Was quarter's quota % among top 3 Sales Reps?	Bonus if...		
			No	Yes	
			\$0	\$3,000	

# Integrating Non-Financial Measures

## Conceptual Incentive Alternative #5

- Sales Goal: Achieve Revenue Growth Through High Customer Satisfaction and Internally Comparable Personal Performance
  - ✓ Part A and B: Quarterly bonus for revenue results vs. quota, but not without attention to customer satisfaction

### Part A

Territory's Aggregate Revenue Performance Range	Bonus Percent of Base Salary
> 120% of Quota	50%
110% to 120% of Quota	30%
100% to 110% of Quota	20%
≥ 80% to 100% of Quota	12%
< 80% of Quota	0%



### Part B

Sales Force Customer Satisfaction Score	Bonus Multiplier
Outstanding	1.50
Excellent	1.25
On Target	1.00
≤ Min. Acceptable	0.50

# Integrating Non-Financial Measures

## Conceptual Incentive Alternative #5

- ✓ Part C: Quarterly bonus for performing well within the sales organization



### Part C

Account Development and Service Indicators	Bonus % for Rank Within Sales Force			Result	Earned Bonus
	Bottom 25%	Middle 50%	Top 25%		
Account Penetration Ratio	0%	10%	20%	Middle 50%	35% of Base Salary
New Account Conversion Ratio	0%	8%	15%	Top 25%	
Revenue Per Account	0%	5%	10%	Top 25%	

# Integrating Non-Financial Measures

## Conceptual Incentive Alternative #6

- Regional Manager's Sales Goal: Revenue Growth and Direct Reports' Performance Improvement
  - ✓ Part A: "Traditional" annual bonus based on regional revenue vs. goal

### Part A

Region's Aggregate Revenue vs. Goal	Annual Bonus Opportunity
≥ 150%	50%
120%	30%
100%	20%
≥ 80%	12%
< 80%	0%

# Integrating Non-Financial Measures

## Conceptual Incentive Alternative #6

- ✓ Part B: "People" measures enabling current and future performance success



### Part B

Improvement Over Prior Year	Weight	Rating (1 - 10)	Weighted Rating	Bonus Opportunity
# Direct reports growing territory revenue	35%	7	2.45	\$1,600 per point ≤ 5 plus \$4,400 per point > 5
# Direct reports growing priority acct revenue	25%	8	2.00	
# Direct reports achieving price realization goal	20%	5	1.00	
# Direct reports completing sales skills training	20%	10	2.00	
<b>Total</b>	<b>100%</b>		<b>7.45</b>	<b>\$18,780</b>

# In Summary...

- There are many rivals for your Sales Reps' time and effort: customers, prospects, products, and management
  
- Performance measures:
  - ✓ Translate business objectives and sales/marketing strategy into specific selling priorities
  
  - ✓ influence sales activity and performance, helping Sales Reps to decide which:
    - Accounts to target
    - Individuals to call on
    - Products to propose
    - Prices to present
    - Customers to serve

# In Summary...

- **Effective incentive designs incorporate a variety of performance measures**
  - ✓ **Sales Reps today function as resource coordinators, account strategists and stewards of customer relationships**
  - ✓ **Companies are competing to create and sustain long-term, valuable customer relationships**
  - ✓ **Use of financial and non-financial measures give management the ability to tailor incentive designs to the performance opportunities and developmental needs of individual Sales Reps**

# In Summary...

- Non-financial measures can be valuable incentive plan features in at least four situations
  - ✓ Sales cycle exceeds 12 months
  - ✓ Multi-year contracts are the norm
  - ✓ Global account sales are prevalent
  - ✓ E-commerce is, or can be, significant sales channel
- Adhere to “1<sup>st</sup> Principles” of performance measure selection when choosing your metrics