



E-Book Digest- Choose The Right Sales Compensation Plan

This is a short digest of a e-book I wrote that analyses in depth the notion of sales incentives and guides an institution to choose the right one for its business. As per the content below is goes beyond the common knowledge and explains all around the different choices.

CONTENT

1. INTRODUCTION
2. PURPOSE OF THE INCENTIVES SCHEME
3. THERE ARE MANY TYPES OF INCENTIVES
4. INTRODUCING THE TWO MOST COMMON INCENTIVES SCHEMES: BONUSES AND COMMISSIONS
5. THE IMPORTANCE OF SELECTING THE RIGHT SYSTEM
6. HOW TO DESIGN A SALES INCENTIVES SCHEME
7. HOW TO CHOOSE BETWEEN A COMMISSION OR BONUS SYSTEM
8. WEIGHING THE BENEFITS AND DISADVANTAGES
9. THE CONSEQUENCES OF CHOOSING THE WRONG SCHEME
10. OPERATIONAL FACTORS TO KEEP IN MIND WHEN CHOOSING AN INCENTIVES
11. ALTERNATIVES TO THE BONUS OR COMMISSION MODELS
12. CONCLUSION

Designing an effective sales incentive scheme is complex and requires careful consideration of numerous factors. Decisions include the type of incentives, such as commissions, bonuses, flat payments, or point systems, and specifics like payment triggers, methods, and timing. The scheme must align with the company's strategy, motivating the sales team to achieve specific objectives, whether promoting new products, securing profitable deals, or meeting sales targets.

The purpose of an incentive scheme goes beyond simple payment; it should drive behavior that supports the company's goals. Various incentive types, such as a 50/50 split between fixed and variable pay, must be considered, with specific examples including year-end bonuses, commissions, or payments triggered after reaching revenue milestones.

Two common schemes, bonuses and commissions, each serve different purposes. Bonuses are lump sums awarded at specific times, influenced by both quantitative and qualitative factors, and can vary. Commissions offer more structured, predictable payments based on specific sales achievements, motivating continuous performance.

Selecting the right scheme involves three key technical aspects: identifying eligible roles, determining total compensation for each role, and deciding the mix between basic salary and incentives. Following this, four vital steps should be taken: understanding company objectives, delineating sales roles, deciding the payment mix, and creating a mathematical formula that translates goals into a workable scheme. These steps ensure the incentive scheme effectively supports the company's strategy and motivates the sales team appropriately.

Choosing between a commission or bonus system for sales incentives involves considering six key factors: sales roles, sales process, organizational culture, market conditions, company objectives, and the relationship between salespeople and clients. Each factor influences which system is more suitable for a particular company.

1. Type of Sales Roles:

- Bonus system: Ideal for team-focused environments, complex sales processes involving many people, situations influenced by external factors, and territories with different growth rates.
- Commission system: Best for roles with direct customer influence, independent targets, measurable success, and equal sales territories.

2. Sales Process:

- Bonus system: Suitable for long, team-oriented sales cycles with qualitative goals and dissimilar territories.
- Commission system: Effective for short sales cycles, standardized products, easily measurable performance, and sales-focused roles.

3. Organization's Culture and Market Position:

- Bonus system: Fits companies where sales roles include non-sales tasks, and where forecasting costs is challenging.
- Commission system: Works for companies reliant on direct sales, aiming to motivate high performance without caps on earnings.

4. Market Conditions:

- Bonus system: Good for new or crisis markets focusing on customer retention.
- Commission system: Suitable for stable, well-known markets with defined opportunities and mature company presence.

5. Company Objectives and Goals:

- Bonus system: Enhances existing commission systems for additional tasks and broader objectives.
- Commission system: Targets short-term revenue goals and high unit sales.

6. Relationship Between Salespeople and Clients:

- Bonus system: Useful when products generate regular revenue without direct sales efforts.
- Commission system: Effective when individual sales skills and relationships drive success.

When selecting the best incentive scheme, it's crucial to consider all these factors collectively rather than focusing on just one. Each factor contributes to forming a comprehensive picture that guides the decision.

Choosing the right incentives scheme, whether commission or bonus, involves weighing the benefits and disadvantages carefully due to their significant impact on company performance and culture.

Benefits and Disadvantages:

1. Commissions Give More Control:

- Benefit: Incentivizes salespeople to focus on specific sales activities, driving them to sell products tied to higher commissions.
- Disadvantage: Less motivation for non-sales activities.

2. Bonuses Are Better For Role Expansion:

- Benefit: Encourages salespeople to engage in additional activities beyond direct selling, ensuring they are rewarded for all efforts.
- Disadvantage: Less direct control over specific sales activities compared to commissions.

3. Commissions Work Best For Individual Targets:

- Benefit: Promotes a strong focus on individual targets and high performance, ideal for companies with clear, measurable goals.
- Disadvantage: May lead to a less team-oriented approach.

4. Bonuses Work Better For Broader Targets:

- Benefit: Encourages focus on broader company goals like customer retention and support, which are hard to quantify with commissions.
- Disadvantage: Less direct reward for individual sales achievements.

5. Commissions and Direct Effort-Payment Relationship:

- Benefit: Clear motivation for salespeople when they see a direct link between their effort and their commission.
- Disadvantage: Less effective in complex sales processes involving multiple team members.

6. Bonuses and Indirect Sales-Payment Relationship:

- Benefit: Suitable for situations where many people contribute to the sale or the sales cycle is long.
- Disadvantage: Less direct correlation between individual efforts and rewards.

Consequences of Choosing the Wrong Scheme:

1. Reduced Motivation:

- Mismatched schemes can demotivate salespeople, especially if their broader efforts aren't rewarded or if high earners see reduced compensation.

2. Rising Costs:

- Bonus System: Generally predictable and budgeted.
- Commission System: Costs can rise unexpectedly if not properly capped or designed.

3. Poor Sales Results:

- The wrong scheme can fail to incentivize high achievers, leading to suboptimal sales performance.

4. Negative Effects on Company Culture:

- An ill-suited scheme can harm company culture, reducing future profitability, sales, and morale.

Effective schemes should align with company strategy and culture, motivating salespeople and fitting managerial objectives.

Overall, an effective incentive scheme should:

- Motivate salespeople to align with company objectives.
- Integrate with the company's strategy and desired culture.
- Function as a tool for managers to guide specific sales activities.

Selecting the right scheme requires careful consideration of all these potential outcomes to ensure it supports the company's goals and maintains a positive work environment.

When choosing an incentives system, several operational factors must be considered. Calculating payments in a commission system requires more time and data processing, demanding resources and access to accurate information. Effective communication between managers and staff is crucial, particularly in commission systems, which need detailed explanation and training to ensure staff understand the scheme. Territory and quota management must be balanced to ensure fair rewards for equal efforts across different regions. Additionally, the involvement of various teams in designing, managing, and administering the incentives scheme needs careful planning.

Alternatives to bonus or commission models include points systems, which allocate points based on performance, translating into monetary rewards. Individual commissions can be tailored for unique roles with different territories or responsibilities. Pool group incentives combine all incentive monies into a single pot distributed among team members, promoting teamwork. Hybrid systems mix both bonuses and commissions, motivating different aspects of sales roles. Payment per unit focuses on rewarding salespeople for each unit sold rather than meeting revenue targets. MBO/KSO systems set key sales objectives linked to strategic goals, while custom systems allow organizations to create tailored incentives schemes, though these must be tested thoroughly to avoid costly errors.

In conclusion, a successful sales incentives scheme considers various factors and aligns with the company's objectives and culture. While bonuses and commissions are common, exploring different models and carefully planning the scheme ensures it effectively motivates staff and supports the company's goals.

If you need a copy of the E-Book, contact me.