QUANTUM SALES COMPENSATION
Launching Your Plan
(Covering All the Bases)

Good morning everyone. This is Randy MacLean. I'm the president of WayPoint Analytics, and I want to welcome you to the fourth and final session of our series on NBC Profit-based Sales Compensation.

In the first three sessions, we talked about the benefits and the issues that we're trying to address by going to a profit-based sales comp system. In the second, we talked about the elements of a plan and how to go about making your plan. In the third session, we talked about the mechanics of setting up the numbers and the metrics and whatnot that are required to make the plan function. In this final session, we're going to talk about launching the plan. This may be one of the most important sessions.

The launch phase of the plan is probably one of the most critical things. There have been innumerable plans that have been invented by terrifically intelligent people that have flocked after they have been rolled out because the launch phase wasn't planned out with the same care and detail as the rest of the plan mechanics. So it's very important to do a good job on the launch. Here are the six points that we're going to be covering this morning:

1. You want to plan in private but not in secret, so we'll talk about how to go about doing the planning phase.
2. You want to use or develop flexible rules for the plan, because none of us are smart enough to anticipate everything that's going to come down the line.
3. You want to plan the crediting rules. Crediting rules are the rules that you use to say what is and is not included in the plan, and that's very important.
4. You want to use true-ups particularly on a profit-based plan because it's very difficult to know profit in real time and true-ups are the mechanisms that help resolve that issue.
5. You want to have a transition component so people can move from what is now to what will be in the future gracefully, and that will prevent you from having high levels of anxiety that can sabotage your ability to get on with the plan.
6. You want to communicate intelligently because communication, setting proper expectations, is really critical to getting people to think about the plan itself and start acting on the plan.

Plan in Private (But Not in Secret)

So the first thing we'll talk about is planning in private. It's almost impossible in most organizations to make a decision to change the compensation plan and then spend weeks, in some cases months, putting together the plan without anybody discovering that it was going on. Inevitably, what happens is when that's discovered, the first instinct of the sales force is that the purpose of the plan is to take money away from them and make the company more profitable at their expense. Left to their own devices, all kinds of things will be generated in the rumor mill which will not be good.

So one of the things that we recommend is that you plan in private so that you can have the space to consider alternatives which may be unpopular. You may discard or use those alternatives, but at least you'll be able to go through them without getting people riled up. On the other side, people will discover that you're planning and if you're in a black-coat mode, that's going help perpetuate the idea that you're trying to do something that they're not going to like.

What I normally do is I'll let the sales force know that we're taking a look at plan alternatives and we think there's a better way of rewarding people for the things that matter to the company. The underlying plan in the vernacular might be something like "We're intent to make another million dollars next year and we're finding a way to share that with you." So there's something for them to look forward to that will gain their curiosity and they'll be looking to you to deliver something later on that looks something like that. And so in your plan delivery mechanism or your communication, it's important to let them know what you're trying to achieve for the company and for them, and why it's going to be better for people.

You will undoubtedly have people that get weirded out about this thing and some of them may find a lot of enjoyment in raising a ruckus or in getting people riled up. It's important to identify those people early on and to make sure that you have a mechanism for being able to talk to them and letting them know that it's not appreciated for them to be speculating on this stuff. You should keep your ear to the ground and respond back when rumors crop up. I wouldn't make it into a knee-jerk reaction, but what I would do is just watch things, and if things start to get disruptive, then call a meeting and straighten a few things out or give them some idea of the progress of what's going on.

One of the best things that you can do in those kinds of discussion is you can say, "This is the phase that you are going through. We're looking at plan alternatives and we're looking at things that work well with our numbers and with each salesperson's numbers to make sure we come up with the right amount of pay for people and that the people that are helping us move the ball down the field are getting better pay.

So that’s the first phase we’re looking at and when we’ve completed that phase, then we have to look at what the numbers are and how we can basically outline the four stages of the plan. You can tell them that you’ve done Phases 1 and 2, you’re working on 3, and 4 is still to come. Just give them some information saying what’s going on. I would just be vague and general about it. If they’ll press to ask exactly what’s going on, say “Things are in a state of flux and things are changing every day as we discover things that we want to fine-tune, so we’re just going to hold off until we have it complete plan and we’ll bring it to you.” Give the sales force an opportunity to feel like they’re being communicated to and they know what to expect, because it will affect them.

I think it’s very important to recognize who the opinion leaders are. You’ve been in meetings before, and when somebody says something, all heads turn to the one guy or gal whose opinion they’re waiting for. Then when that person speaks, everybody will kind of get on board with that person and you’ll know who that is. I would suggest that you could second them by bringing them in to the planning process; you might even make them part of the planning committee if they’re the right kind of person. If you don’t do that, then what you may do is that when you get to the launch phase, you may bring them in early and start asking them for any of supposedly alternatives or about the plan itself. Give them an opportunity maybe to suggest some tweaks to the plan to give them some sense of ownership of the plan, so that when the plan comes out and all heads turn to them, they’re nodding yes.

That can’t always be done. There are certain kinds of people that are difficult to get onboard, and if you have one of those in this kind of a role, then you have a greater challenge than most companies do. But for the most part, the senior people that are more successful are the people that have the company’s heart interest in heart and are usually easy to count on to use their leadership role to help the company advance its objective.

Use Flexible Rules

When you’re putting things together, it’s important that you use flexible rules. Like I said, nobody’s smart enough to anticipate everything that’s going to happen in the future. As a numbers guy, I have a great deal of empathy for other numbers guys that like square corners on the boxes and everything inside the circle. But the world’s a messy place and we’ll inevitably wind up with something somewhere that’s not functioning properly, and common sense will tell us and the salespeople that there’s something wrong with it.

It’s not a good practice at the corporate level to be so spot on a plan that you’re going to stay with it even when it’s obvious to everybody that there’s something wrong The problem that you will have will be middle management people that may be involved in this that have that tendency and don't feel they have the authority to make a change and just have to represent the company's point of view. I think it's important to work with those people to make sure that you have a feedback mechanism in payroll or HR or other places that when a legitimate problem arises that the intention of the company is to give careful consideration to what's going on with the problem and do its level best to find a modification that will repair the plan.

Sometimes it's the plan itself, sometimes it's crediting rules around the plan, sometimes it's the timing of payments in the plan, and sometimes it's a territory rebalancing that will spin the day, and not all those things have to do with plan modifications. You can look at that using those kinds of things, but remember the critical object of the plan, and that goes back to Session 1 where we're looking at the fundamental purposes and we'll review them at the end of the session.

- Avoid rigid mathematics. Now mathematics should add up, but what I mean by avoiding rigid mathematics is taking a look at crediting rules and other things. If you must, you can change the actual metrics in the plan to work on something that better suits the current environment, but use that sparingly because you don't want to have a situation where somebody in the chain gets bullied into modifying piecemeal virtually every part of the plan and you wind up with a plan that malfunctions financially.
- Work the outliers. In every case, there's going to be a certain circumstance or somebody's handling a territory and the territory goes in zero for some uncontrollable reason. Keep an eye out for those kinds of things; learn from them, figure out what you need to do with them, if anything, The company can usually tolerate a little unexpected variance, but if you have too many variances all going in the same direction, it's usually not a good thing. Have a mechanism to spot the outliers and think what you're going to do for them.
- Prepare for course corrections. One of the things that we recommend is we're going to run our plan and we're going to do it every quarter to see how it's performed in the quarter for the first year. In the quarter, we'll reserve the right to make course corrections if there's something going wrong with the plan. You can just announce that up front so that people don't feel that it's being imposed and it's a brick wall and they can't go anywhere if there's something wrong. The idea is to let them know that you're going to be responsive to what's going on.
- Schedule it. A really good plan will come out as something that has a certain amount of fine-tuning when it sees the real world. Scheduling those things in rather than the "once I'm done" type of philosophy will probably lead you to something that can last for decades and provide very, very good benefits for the company and for the sales force.

Plan Crediting Rules

Now let's talk about crediting rules for a moment. In compensation design, crediting rules is one of the things that's most often overlooked. Crediting rules essentially say what does and what does not qualify to have incentives and how it will have a function of timing. But essentially we'll say things like "We pay on this but we do not pay commissions on service," "We pay commissions on new sales at a different rate than we do on old sales."

It's essentially the rules that surround how we translate an invoice amount into an incentive amount. This is the place where you have to consider the breadth of the product line and the service envelope for your customer, understanding how commissions are going to be triggered, and making sure that you consider the timing of the commission payments and the time frames of the commission payments.

Those need to be properly articulated. It's necessary for the people that calculate the payroll to be able to calculate the payroll period. Unless you use some kind of system like WayPoint Analytics System for commissions, somebody's going to have to know what the rules are so that they can come up with the right numbers and then people have to know when they're going to get paid on certain things and what things qualify and don't.

It's perfectly obvious that this needs to be done. Most people think intrinsically that it's going to happen but if it's not properly planned and considered, there will be gaps. This is the first and most common place where the plan will start to have holes is when the crediting rules aren't completely considered and documented.

Use True-Ups

I want to talk about true-ups. For most profitability plans, we have a time-facing issue. The issue with profitability, as you know, is we don't know everything that has happened in a particular period or quarter or even year and all the things that affect the financials for that period are considered. The reason why most companies take about three weeks to close a period and could take that or more to close a quarter, and certainly more than that to close a year, is because there's a lot of follow-on things that would wait for invoicing the period until after the period from our vendors on those kinds of things.

Because of that, profit-based plan is taking real costs into account and will not likely have all of the information available at the time the commissions need to be calculated. The most common case where the typical or average case within the universal WayPoint plans that close a period, if they're on a calendar month, they may close the period at the end of March, say, but they won't actually get the books closed for about three weeks.

But in the most common case, the commissions for the period are due in the middle of the following period, and so they really only got 15 days to do the calculations and be back up for the payroll system. The payroll service they want, they only have 10 days. In the worst case scenario, there may be two weekends in that 10-day period, and that means they may only have four days between the time that they are ready to go.

I suppose you also should consider that some companies don't close all their billings on the last day of the month; there may be a two-day window to close the billings out. So in the worst case scenario, the payroll people may only have two days of working time before the payroll has to be calculated so that it can go out. In those scenarios, you'll have to use estimates.

In the WayPoint case—I remind everybody that's using WayPoint—we won't know what the financials are until the end of the period at best, and then they have to be processed in the system, so WayPoint always uses the last known metrics for how the costs are structured in the company until it gets the updates from the finance team.

In order to make WayPoint function, on the first of January it's going to be calculating costs and profitability and it's going to be using the numbers from the previous year. It's going to continue doing that for all of January until we get to the end of January and we put the January numbers in and then the January numbers are going to be restated. The same thing will happen quarterly and we may not have financial information until the end of the first quarter, so maybe late April before we get the real numbers for up to the end of March. We've already paid the three pay cycles perhaps and then we're into the fourth before WayPoint really knows what the real profits were.

So what do you do with that? The answer is that in high-end designs you use a process called true-ups. The way that it really works is this: At the end of January, WayPoint will tell you what it thinks the commissions were and you will pay according to the profitability that was generated; or it will tell you the estimates the profits using the latest numbers, and you may pay on that. At the end of February, the same thing will accrue. At the end of March, the same thing will accrue.

In April, you'll get the real numbers, and so for the April time frame, what you would do is you would calculate all of the pay that should have been paid for the first four periods and you would deduct from that the amount of pay that has already been paid and you would pay the balance. If the rep has been underpaid, then the company will make good on that by saying, "Well, we made more profits that we thought we did and here are some more money than you've already been paid," and that would be good. The other thing that may happen is the rep may have been overpaid and the company will say, "Well, we pre-paid some of the money that you hadn't yet earned, and so you already have it and here's the rest."

If you have wild gyrations because of that, it's not going to be good and you may give some consideration to what kind of other mechanics you might add into how you do the true-up. If you have somebody that has made a whole lot of money and then after you get the calculations you find out they made zero on what should be really a neutral case but if that kind of thing happens and, of course, you can't just tell the person to suck it up, you're probably going to have to do something, and that's where the flexible rules come in. But you want to make sure that that works.

So the whole purpose of the true-ups is to make sure that things are synchronized at the end of each quarter, at the end of each financial period, and certainly at the end of the year, so that the right amount of money has been paid and the right amount of money has been earned, and everything is exactly as it was promised.

Now these things work perfectly fine. We've had lots of people that have programs that are similar in terms of the payouts having draws against commission, that kind of thing. They are fairly common in sales and they frankly don't cost any issues, unless you're not clear in your communication and you didn't set good expectations of what is actually going on. If people go in cold and you sort of forget to tell them about this, then you will have a problem. So it's very important to communicate accurately.

By the way, if you bought Callidus that would cost about a million dollars for a sales incentive system to install in your company and you set something up that takes anything into a kind of Callidus system to have the capability of calculating real profits but it does have the capability of putting in things that are surrogates for profits and you paid $100,000 or half a million dollars for a company that I used to work for to do this, then there would be a true-up in the system for sure. We almost always did true-ups in high-end plans for big companies that have thousands, or sometimes tens of thousands of sales reps.

Have a Transition Component

It's very important to have a transition component for your plan. The idea of the transition, as we spoke of a little before, is to have a way of getting from here to there. Most transition plans are on at least six months; some of them last a year. The best transition mechanics that I've seen is where you could put people on to the plan and you're giving them the opportunity to go and change the nature of how they do business with their customers or how they work with their customers to change the profits that they generate. On Day 1, of course all customers are going to be doing the same dysfunctional things they were on the day before, and they need a little bit of time to get there.

The best mechanics I've seen suggested by a really, really sharp HR consultant up in Rochester, New York, was this: She suggested that for the first quarter that the sales reps get either whatever the new plan paid or what they made the same quarter the previous year, whichever was higher. In the second quarter, they would get 90% of whatever the new plan pays or 90% of what they earned last year. In the third quarter it went to 80%, in the fourth quarter it went to 70%, and after that they were on the new plan.

It was a very successful launch for this company and it's one of our stars, one the companies that has really changed their game. They have changed from an average or break-even level company—a money-losing company, in fact, when I first met them—to a solid, profitable company for five consecutive years, not only generating industry-leading profitability but they've also increased their revenue between the beginning of the recession and now by 40%. They did that with about 60% of the number of customers that they had at the beginning.

They did that by being very aggressive with this kind of plan, getting the sales people through the transition, firing a few salespeople that weren't ready to get onboard and replacing them with people that were more willing to play, and getting super focused on customers that made the most money. Their reps made substantially more, and they have a gain-sharing bonus for the entire company. Last year, that gain-sharing bonus was $6,700 per employee, and they paid that out of $76,000 per employee of profit gain over the year before. So these things can be very successful, but that transition component was very important.

Stick to the plan. There's always going to be somebody that will make a lot of noise about this and "how it's terrible and you should go back to it." It's not a good idea to back down if you plan and do it properly. If you made a mess with the plan and everybody's in complete disaster mode, then shame on you and you have to go back to the drawing board. If you have one or two squeaky wheels, then you have to figure out what you're going to do about that, but you should stay with it because if you get to the end point, it pays.

Communicate Intelligently

It's very important to document the plan carefully. Rates and calculations, crediting rules, timing and transition all need to be documented thoroughly. In the delivery paperwork that we would provide when I was in the sales compensation game, it would include a complete document of the sales that each sales rep signed off on and went into the record. Along the way, acknowledge rumors and deal with them, make sure that you communicate the plan and objectives. Once again, that really is “the company wants to make more money and to find a way of sharing it with the people that are helping us get it.”

The last point I made is provide the plan to the reps and have them sign it so that they understand that they are on the plan and that you have a record of it. In some jurisdictions, it’s really important and you’ll know who you are in that case, but if you’re not in a jurisdiction where that’s a requirement, it’s actually a very good idea.

Common Failure Modes

Common failure modes are not planning for the outliers and running into too many of the exceptions that happen in here because you haven’t built them into your crediting rules or haven’t built them into the plan mechanics or haven’t found ways of recognizing them. One of the things that you’d be looking at in outliers is individual salespeople and if you have a plan and you haven’t tested it for each salesperson, then you run the risk of looking at somebody coming in with half of their expected pay or a quarter of their expected pay or 500% of their expected pay. Those are the things that you’re going to be dealing with later in the most difficult situations, so you want to make sure you got that worked out on your map and the mechanics. Having inadequate transition will cause it to fail.

Failing to set proper expectations. That really comes down to “Look, guys, we’re doing the best we can, we got the best systems on earth and we’re working on them hard, but we don’t know what we don’t know until we know it. That is the world that we live in every day and it’s a world that you’ll be living in as well while we’re making our best faith efforts to pay what is due and then making sure that the right amount is paid as soon as the information is available.” Go to the people and let them know that.

Inadequate communication, not working to get buy-in from the people by gathering feedback or at least getting their opinion leader involved or not taking the time to let them know what’s in it for them, and then most commonly chickening out. You get into the thing and you just don’t have the guts to get to the next level. That happens and it’s unfortunate because we always like to think we’re managing the business rather than letting the business manage us, but in some cases, now really the latter is true. In that kind of an environment, it’s almost impossible to meet increased or better objectives. It’s tough to be a management team and to be successful if you can’t get hard things done.

Remember: Five Principles of a Good Plan

- You're supposed to pay for persuasion. People aren't being paid to maintain a territory; they're being paid to persuade the existing customers to buy more broadly and more deeply and to bring new customers into the territory. That's what you're paying for.
- You want to protect the best reps. The people that are contributing the most to the profit and the profit gains are the people that need to make the most money. People that are doing the opposite should be funding the people that make the most money through reduced earnings.
- You want to prevent runaway earnings. You want to have situations where people can have high earnings but only where the company also has high earnings. NBC or commission-based plan has that intrinsic in its nature.

These principles are fully taken care of in any kind of a profit-based compensation plan. The good news is that a management team would love to have million-dollar sales reps, a whole flock of them, if the company is making millions whenever the rep makes a million. So that's a good thing.

By the way, as an anecdote, one of the best companies in our entire WayPoint universe had this sales force where the lowest paid rep makes over a quarter million dollars a year; highest paid makes about three-quarter million a year. They've been paying on the profits for a very long time. That company is an absolute cash cow and one of the most difficult commoditized businesses in one of the most competitive and crowded markets in the entire country. They are an absolute standout there.

- Make sure that you're operating within the budget so that the proper plan is always paying out of profits that are coming in and that you're never reducing the profitability of the company when you're increasing the pay of the sales force.
- A good plan will provide performance insurance for the management and ownership of the company. A good plan will always provide for a good manager to make good money even if some of his people are underperforming, because others will be over-performing and being well rewarded for that, and that will make sure the branch manager is on up, will always be able to meet our goals if they have at least a good proportion of their sales force also meeting their goals.

So having a good plan will prevent forever situations where you have to pay big incremental commissions out to sales rep where the company is losing even more money than it has in the past or the branch is underwater and those kinds of things.

I want to encourage you to give careful consideration to this. This is one of the most valuable tools you can use to drive profitability and gains in profits in your business. It doesn't come without a cost, anything worthwhile requires some effort, but if you're willing to make the changes, it is almost impossible for one of these plans to fail. If you follow these rules, it is impossible for the plan to fail and not deliver you a very increased and in many cases, extraordinary results.

So I want to thank you for spending time with us talking about this. I do hope that this information is going to be very valuable as you begin to map out your own plans and have your ability to get your company to the next level and have the sales force fully onboard and invested in generating increased profitability for your business. I'd be delighted to talk to you offline and after the fact. If you have questions or there are things you want to discuss about your company, I'd be happy to entertain your calls and we can discuss it further.

So for now, thanks a lot for spending time with us. I look forward to speaking to you in the future.