

Sales Compensation

Sales compensation can be defined as the total cash-compensation opportunity provided for an organization's salesforce. As such, sales compensation is the key to motivating the right behaviors by the salesforce that will enable an organization to successfully implement its sales plan. Given its importance to the organization's success

in implementing its business strategy, one should understand the key elements of sales compensation and the role they play in creating success for the organization.

Back to Basics is intended to provide entry-level information on issues relevant to compensation, benefits and the work experience. Though factual in nature, nothing herein is to be construed as legal, accounting, actuarial or other such professional advice.

Purpose

A sales compensation plan provides financial incentives that are linked to salesforce success in accomplishing specific objectives related to the selling process. Sales compensation, by placing a significant portion of pay at risk and being dependent on the accomplishment of these business objectives, focuses the salesforce and drives behaviors that enable the organization to succeed.

Key Components

When developing a sales compensation plan, it is important to understand the objectives of the organization and what the salesforce needs to do to assist the organization in achieving these objectives. Partnering with your sales executive and finance executive is important to understanding the business context and how the sales compensation plan should be designed to drive the right behaviors. The design of the sales compensation plan will determine several important factors that define the financial incentive available and how this incentive is earned. These factors include:

Pay mix: Pay mix is the proportion of total cash compensation that is fixed versus variable. The fixed portion of pay mix is referred to as salary. The variable portion of pay mix is incentive compensation that is linked to the accomplishment of defined objectives in the sales compensation plan. Pay mix is typically expressed as a ratio, e.g., 50/50, 60/40, 70/30, etc.

Leverage: Leverage works together with pay mix to determine the total cash-compensation upside for the portion of the salesforce that achieves the "excellent" level of performance. Upside compensation is available to all salespeople who over-achieve target objectives. Leverage is typically expressed as a multiple of the variable or incentive compensation opportunity, such as 2X or 3X target incentive.

Performance measures: Performance measures define the way success is measured for the salesforce. They communicate precisely what is expected of the salesforce to receive payment of the variable or the incentive portion of the pay mix. Generally it is best to use three or fewer measures in a sales compensation plan to clearly focus the salesforce on specific objectives and behaviors.

Team or individual measurement: Performance may be measured on either an individual or a team basis or a combination of the two. Individual measures are typically used for individual contributors who work independently in accomplishing their performance objectives. When performance is dependent on a team, team-based measures may be appropriate.

Administration: It is important for a successful sales compensation plan to pay the salesforce accurately and on time. It is also important that the sales compensation plan is clearly understood by all those affected by the plan. Keys to administrative success include clearly defined roles and responsibilities, documented processes, and effective tracking and measurement tools and systems.

Conclusion

Sales compensation is an important part of an organization's total rewards strategy. Sales compensation is a key enabler of the organization's sales plan and to successful implementation of the business strategy. Understanding of the basic elements of sales compensation can open the door to partnering opportunities for the compensation practitioner with the sales management team. Partnering with your sales management team in the design and development of your organization's sales compensation plan is a great opportunity to contribute directly to your organization's bottom line. 

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