



Using Sales Compensation to Drive Strategy

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June 2006

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When is incentive compensation really not an incentive? That sounds like a riddle and for many companies it is, but there's nothing funny about it. Incentive compensation is less than an incentive when commission calculations are wrong, current attainment and earnings results are less than obvious, the plan inadvertently incentivizes behavior that is inconsistent with corporate strategy — in short, when the link between behavior and reward is obscure or delayed. What makes a bad situation even worse is that few companies are aware of the true state of their sales compensation management process, and even those that are aware, tend to think that there is no cure for the chronic pain and limitations they endure.

The root cause of this condition can be traced to the primitive, in-house developed compensation systems that are inadequate to handle the complexities and dynamics of sales incentive management. Frequently running on spreadsheets, such systems are inherently fragmented, labor-intensive, error-prone and cumbersome to control, track, analyze, report, and maintain. These systems fail to provide the strategic tools to align and drive sales performance. Perhaps worst of all, in-house sales compensation systems are not even cheap — according to one estimate they average over \$200 per sales representative per month.

A new class of on-demand business solutions has opened the doors for sophisticated sales compensation management tools, historically only affordable for the largest companies. On-demand sales compensation management solutions are accessible, cost-effective, and easy to deploy and use. Through simple integration with customer relationship management (CRM) and sales force automation (SFA) tools, these solutions automate the sales incentive management process to deliver real-time visibility not only into actual results but also into forecasted commission earnings based on opportunities in the pipeline.

This Beagle Research Group Executive White Paper examines the costs and disincentives associated with in-house compensation management systems and what one company, Centive, is doing to make incentive compensation the carrot it ought to be.

The business problem

In sales, all motivations can be reduced to a single issue: compensation. So it would be reasonable to conclude that sales compensation systems rival sales force automation systems as examples of advanced automation designed to drive peak performance, but noth-

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ing could be further from reality. Some large companies make use of a handful of expensive and inflexible traditional applications designed to manage compensation, but the majority of organizations make do with unreliable spreadsheets that confuse the situation by delivering slow results reporting, inaccurate or incomplete calculations, and by generating too much overhead.

Compounding the problem, inaccuracies are mostly reported only when a shortage is identified by the sales representative. The representatives are constantly calculating their commissions in an exercise of shadow accounting but all agree the time would be better spent selling.

In addition to de-motivating the sales staff, inadequate incentive compensation management affects numerous down-stream departments and their business processes including finance and accounting, IT and human resources.

Compensation challenges for the sales organization

The goals of the sales representative, the vice president of sales, and the enterprise intersect but they do not fully overlap. The sales representative's primary goal is to maximize the compensation plan while the vice president is being asked to deliver a variety of results that only begin with revenue. For example, representatives ordinarily look for the easiest way to make plan and while some products — especially new products — may carry higher compensation multiples, in many organizations it is still possible to make plan without selling the newer, less familiar, and therefore harder to sell products.

The difference for the organization is striking. Representatives who make plan without selling new products meet their objectives but the organization falls behind, and new product introduction is only one example. Many organizations now routinely layer multiple goals on managers that can include revenue, new customers, customer satisfaction, margin, new product introductions, and more.

Managers need to pass these goals on to sales representatives but, historically, tracking multiple goals accurately has proven too difficult, so in the end all goals get reduced to revenue. In tracking multiple goals many organizations are finding that simple spreadsheets and home-grown tracking systems are inadequate. The expanded challenges below illustrate common problems that many sales organizations face.

1. **Implementing new revenue generation programs.** The inflexibility of in-house solutions makes it difficult and time consuming to adapt old systems to new or modified business models and strategies, new products, new programs, SPIFs, or new channels. Business is changing faster than the systems supporting it.
2. **Aligning sales incentives with corporate goals to motivate specific behavior.** The difficulty involved in coding what are often complex and numerous new plans — as well as plan modifications — is that they rarely keep pace with the changes that are necessary to drive specific sales behavior. Rather than motivating selling, such systems motivate distrust and shadow accounting, resulting in sales representatives spending up to 2-4 hours per pay cycle away from business-generating activities.
3. **Accuracy in revenue forecasting.** Even using SFA tools and advanced methodologies, a sales forecast is frequently an overly optimistic document. Sales managers reassess forecasts based on their intuition because disparate systems make it difficult to get the information needed to verify a forecast. Finding ways to motivate sales representatives to more diligently enter and maintain their opportunity data would improve forecast accuracy. Linking compensation management and

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SFA/CRM promotes an integrated business process that enables sales representatives to assess their current positions and to adjust them based on this visibility.

4. **Limited access to current performance data to motivate sales.** In-house and Excel based systems provide no visibility into daily or weekly performance attainment — in fact, that information often isn't available until days or weeks after the close of a period. Consequently, neither the manager nor the representative knows the status of performance against plan in time to make adjustments to help reach multiple targets.

Compensation challenges for the Finance, IT and HR organizations

Down-stream from sales, other departments are also struggling with the effects of antiquated systems. For example, organizations find that building and maintaining incentive compensation systems requires input from IT for data and programming. Given IT's many other responsibilities, programming a departmental system is frequently not a high priority. On the other hand, going the spreadsheet route may require less IT input but it requires more manual effort from sales administrators and there is a danger that without adequate staffing, compensation issues will simply back up. Taken together some of the common problems faced by other departments using home grown incentive compensation systems can be summarized as follows:

1. **Inefficient process.** It often takes heroic efforts to calculate and validate commissions, approve and post results and deal with dispute resolution. As a result, 100-hour weeks by sales administrators are not uncommon at the end of pay periods leading to burn-out and churn. Sales compensation analysts spend most of their time in manual, tactical calculation efforts, not having the time and tools to engage in more value-added activities, such as plan review and analysis, trend discovery, and ongoing improvement of plan effectiveness.
2. **Limited cost control.** Lacking the tools to perform analysis, model compensation plans, and run what-if scenarios, and without timely access to attainment data, finance struggles to understand and control incentive costs. Spreadsheet-based systems make it difficult to estimate cash requirements for proper accrual.
3. **Lack of financial integrity and compliance.** Spreadsheet-based compensation solutions leave CFO's with a big hole in their financial compliance initiatives. Based on manual processes, these home-grown solutions lack the security, consistency, and reporting structures used by other significant cost centers, such as audit trails of changes made over time.

Hidden costs of manual compensation management

Despite the many problems with out-dated compensation management systems now in use, many organizations do not recognize that they have a problem or that solutions for this common problem exist. As a result they spend more time and resources than necessary on tactical compensation issues and fail to gain all of the positive and strategic benefits that sales compensation should generate.

For example, the direct and indirect costs associated with obsolete compensation management systems can be eye-opening. According to a recent study by Growth Solutions, LLC, of Naperville, IL, (Table 1) on average, the annual direct cost to administer a sales compensation program is \$1,140 per payee which includes costs for personnel who administer the sales compensation program, as well as any associated system/IT costs. In addition, annual indirect costs such as those associated with sales force time spent reviewing and

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fixing incentive payments, are even higher, averaging \$1,319 per payee. According to the report, the total monthly direct and indirect costs associated with managing compensation is \$205 per payee — an amount that invites commercial solutions and offers the promise of a rapid payback for organizations that invest in those solutions.

Table 1 Costs from inefficiencies of in-house developed systems

	Annual	Monthly
Direct	\$1,140	\$95
Indirect	\$1,319	\$110
Total	\$2,459	\$205

SOURCE: GROWTH SOLUTIONS, LLC

But as important as costs are, they are not the only reasons for resolving the inefficiencies in sales compensation. If compensation is the motivator organizations use to influence the behavior of sales representatives, the reward must be delivered as close to the execution of desired behavior as possible or it will lose its impact. Moreover, the payment has to be right. When organizations get their sales compensation programs wrong, it causes a variety of unwelcome consequences from taking attention off the job of selling to outright attrition.

If sales representatives spend 2 to 4 hours in shadow accounting per pay period, it is not simply their time that is lost but also their productivity. The same is true for front line sales managers. According to the same study by Growth Solutions, front line sales managers spend 79 days per year (about a third of their time) on administrative issues compared to just 60 days spent on staff development.

The on-demand revolution and “long tail” applications

Many enterprise level applications that are common today — like SFA —started in much the same way as sales compensation — as spreadsheets or in-house developed solutions. Typically, as the demand for specific solutions increases, commercial software vendors build packaged solutions which become industry standards. The major drivers that determine an application’s viability include size of the market and cost of development and deployment. That process has been accelerated by the emergence of on-demand computing which greatly lowers barriers to entry.

The on-demand paradigm enables a vendor to develop and deliver solutions faster and at much lower costs than traditional computing solutions. More importantly, the on-demand model enables vendors to consider building applications that are highly specialized and aimed at smaller companies, which have been referred to as “long tail” applications for their position on a typical distribution curve. With conventional applications, the cost benefit analysis is limited to the single organization licensing the software. In the on-demand model, it is cost effective to support even small groups of users, which enables vendors to offer specialty applications like sales compensation management. The result is

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more powerful, accurate, and professionally designed applications that can replace spreadsheet-based solutions.

Compensation management is ideally suited to the on-demand model because it is an application that few organizations do an adequate job of building for themselves. A professionally designed and developed on-demand compensation management system is self-contained and secure, and easily follows highly active, mobile sales representatives. Even on the phone, managers and representatives can examine the same data and strategize solutions that hit multiple targets — even in the middle of a reporting cycle.

Attributes of an ideal solution

An effective compensation management system should work the way modern sales organizations work.

1. **Integration with CRM/SFA tools.** It should be able to track and display the pipeline for each individual, enabling each representative and manager to prioritize opportunities based on revenues, incentives, and objectives. Therefore, it should be integrated with the enterprise's SFA system for easy access to relevant deal and opportunity data.
2. **Real-time access to performance feedback.** Sales performance and earnings information should be available anywhere and at any time. Having real time access to critical information gives managers and representatives the tools they need to influence outcomes.
3. **Simple to use.** Representatives should, at a glance, be able to not only see where they stand in the current period but also to quickly prioritize what they need to do to achieve targets.
4. **IT-independent.** Though important, sales compensation is only one of the many administrative and technical chores faced by the finance and IT departments. Effective processing can save time and labor as well as improve accuracy delivering a win/win solution for all parties. An IT-independent incentive management process will empower compensation analysts to quickly design and update plans and data so they are responsive to market, product and organizational changes.
5. **Accurate and efficient process.** As an inherent attribute of sales incentive management, accuracy should permeate calculations and payouts, as well as prior period adjustment processing — even for the most complex plan logic, including multipliers, credit splits, accelerators and roll-up results.
6. **Financial compliance and cost control.** Accuracy, reporting, security and consistent processes form the backbone of financial compliance. An effective compensation management system should provide the ability to analyze trends and forecast sales incentive costs, which is vital to the financial wellbeing of the organization.
7. **Cost-effective.** The new on-demand delivery model effectively enables companies to syndicate the cost of enabling technology and thus be able to afford powerful sales compensation management solutions at a fraction of the cost of enterprise on-premise systems.

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From prospect to paycheck with Centive

Compel from Centive is based on two important capabilities that provide significant advantages over spreadsheets and home-grown solutions. Compel is based on a real database and it is delivered in an on-demand mode.

1. Compel's database enables it to track multiple promotional programs, incentives and metrics, and rewards to enable a more dynamic approach to managing sales people. Unlike a static spreadsheet, the database, combined with a powerful reporting engine, enables users to get current insight into each sales representative's progress against plan and every plan's effectiveness at any point in the quarter.
2. Because Compel is delivered as an on-demand solution, it is available anywhere there is access to the Internet and, more importantly, the cost is low enough for it to out-compete conventional in-house solutions — especially when the true costs of in-house developed solutions are understood.

As an on-demand solution, Compel is architected to be simple to understand and use for sales representatives, managers, and plan administrators. Compel is integrated with Salesforce.com, and is available through the AppExchange on-demand platform. In addition to its integration with Salesforce.com, the product can also import data from any SFA application through industry standard *.CSV files. Tight integration gives users near real time access to information in both systems so that reports, calculations, and queries can reflect the current status of the reporting period.

How it works

Figure 1 (next page) shows the main screen for a typical sales representative. The column labeled "Total" shows earnings to date while the next column, "Total with Opportu

Case Study

Founded in 1980, Quantum is a global leader in storage, delivering highly reliable backup, recovery and archive solutions that meet demanding requirements for data integrity and availability. The company employs approximately 120 sales people.

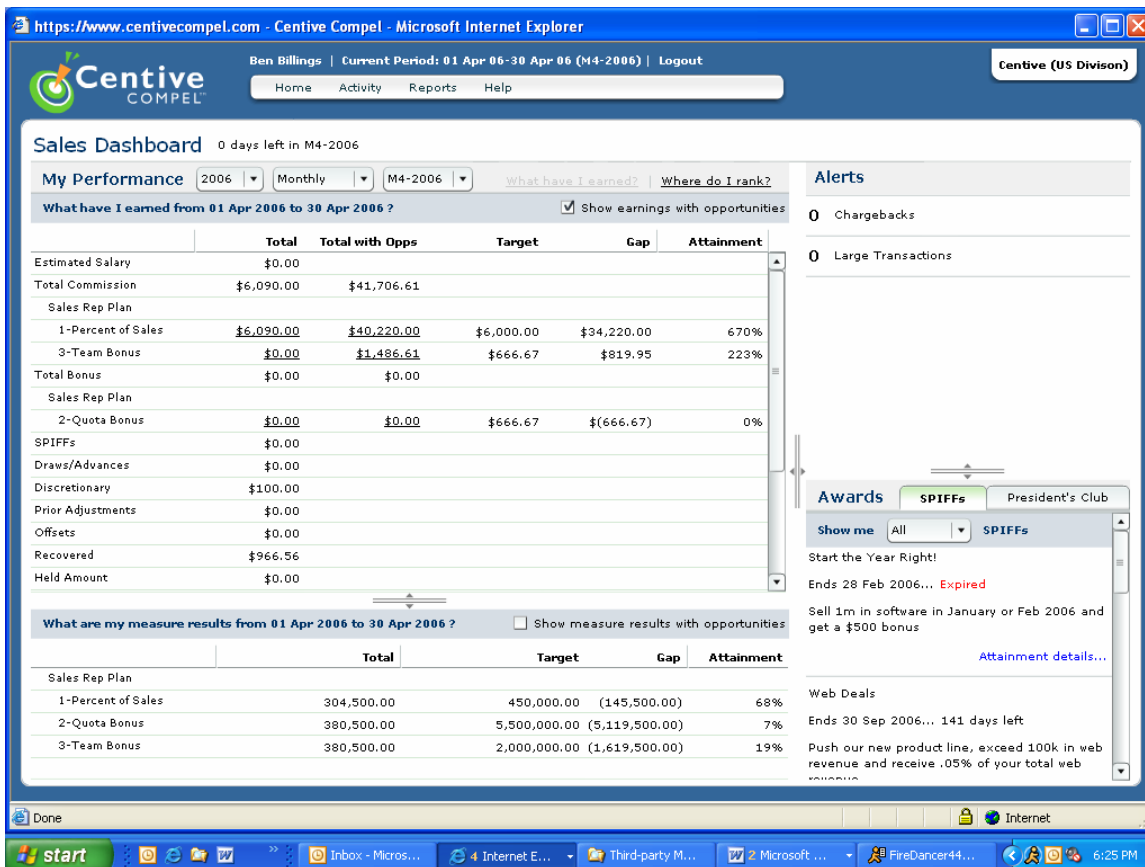
Quantum made several attempts at managing sales compensation that included spreadsheets, a small application based on MS Access, and an ERP system, but none was satisfactory. As Tony Anderson, director of world wide sales operations observed, "We had two compensation analysts for 120 sales people, which should have been adequate, but it wasn't. Our analysts were working 100-hour weeks and the sales representatives were not satisfied with the level of support they were getting because the manual reports had errors."

In October of 2005 Quantum went live with Centive. Already a user of Salesforce.com, Quantum immediately took to the idea of an on-demand solution for sales compensation management. "For us on-demand was an advantage," said Anderson because, "We already had Salesforce.com and it meant we didn't have to bother our IT group for support."

More importantly, the advantages Centive delivered to Quantum were obvious and immediate — sales representatives and managers found that information was more readily available. For managers, that meant they were able to better strategize with their representatives, and sales people became more trusting of the compensation reports because they were accurate. After just a few months sales representatives were performing less shadow accounting because, as Anderson put it, "They know they can log in at any time, and they're trusting the data more." Anderson sees things continuing to get better. He has high praise for Centive's support staff — "We've bumped into few issues and the people at Centive have been great in dealing with any issues that come up."

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Figure 1 Sales Dashboard – My Performance



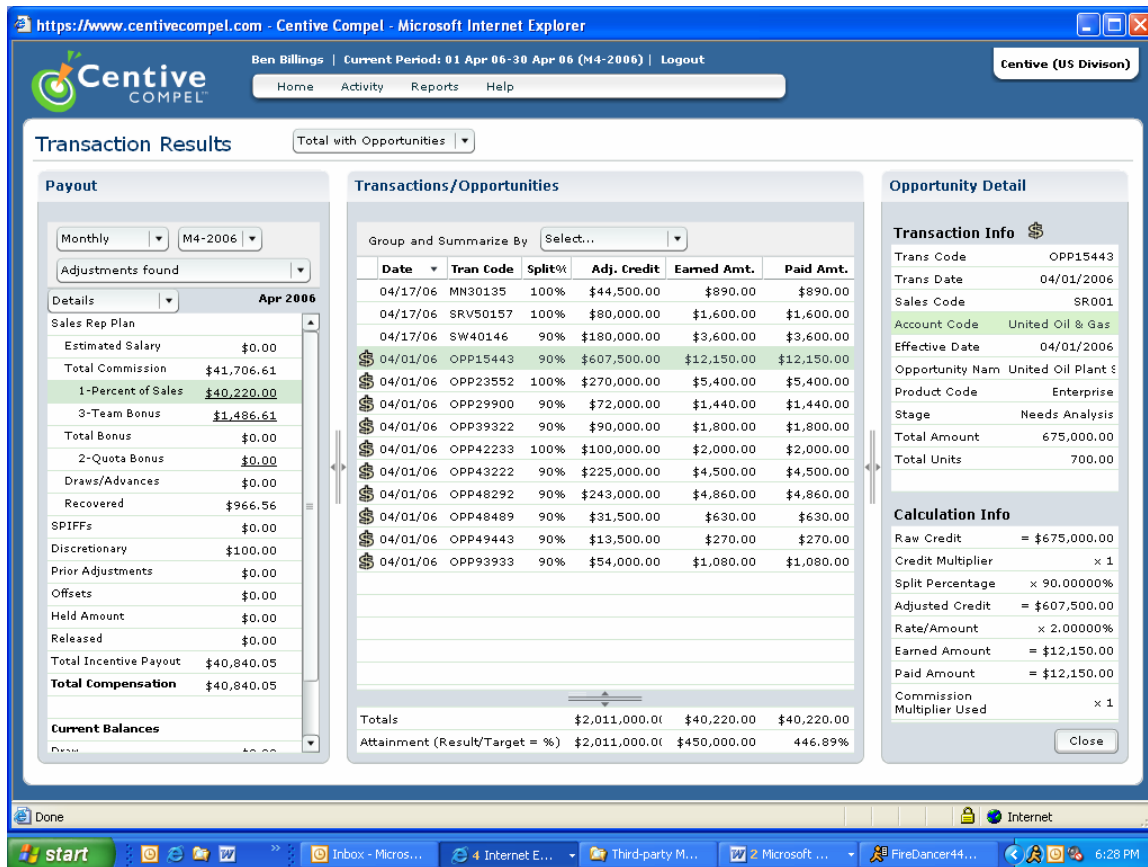
SOURCE: CENTIVE, MAY 2006

nities”, shows what total earnings would be if all pending deals close. The underlined items are links to additional detailed information and clicking on them enables users to drill down and expose detail for each opportunity. For example, clicking on the \$40,220.00 in the Percent of Sales measure row under the Sales Rep Plan will bring up a detail screen with all relevant opportunities and closed deals in the relevant period.

Figure 2 (following) shows a detail screen listing all transactions in the representative’s territory. The “\$” sign shows the deals that have not closed yet — these transactions represent the forecasted opportunities from the SFA/CRM system. Sales representatives can use filters to evaluate specific opportunities and then stack rank those opportunities by their value or commission, for example, so the representative and manager can focus on the most lucrative opportunities and develop closing strategies.

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Figure 2 Sales Dashboard – Transaction Results



SOURCE: CENTIVE, MAY 2006

The column at the far right of Figure 2 shows all compensation and relevant calculation details. For example, if the United Oil & Gas opportunity closes, it will generate \$12,500 in earnings based on a 2% flat commission rate and a 90% split. Opportunity-based earnings can be prioritized by customer, stage, split, earned and paid amount, and other attributes.

At a glance, this screen can be a powerful motivator because it provides an unbroken chain from SFA to compensation – a process Centive calls “from Prospect to Paycheck.” More importantly, with the calculation information already presented, there is no need for shadow accounting and questions about commission credit and how it was calculated are significantly reduced. Should questions arise, though, representatives are provided an easy interface for initiating a workflow to resolve the issue.

When the system is initially deployed, Centive works with customers to configure their compensation plans and the measures within those plans — including commission rates, multipliers and split rules — so that the system can calculate compensation on the fly for each user as the reporting period evolves. The value of opportunities can change from day to day based on plan changes, attainment of accelerators and position in the reporting cycle — automatically, without additional effort.

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Analysis and Conclusions

Administering sales compensation is a silent drain on many enterprises – a drain that costs more than many people think in lost productivity, errors, de-motivation of the sales staff, attrition; it can even put the company at risk of failing to execute its strategy. More importantly, as organizations focus their sales teams on achieving more than just revenue goals, they need tools that will enable them to manage their businesses to achieve these new targets. Nothing drives sales so much as compensation, but in-house developed sales compensation solutions are simply inadequate to the modern task of sales compensation management.

In business, there is a long history of departments making do with self-developed systems which are eventually superseded when it becomes cost effective either to ask the IT department to build and maintain those systems or when such systems become commercially available. Sales force automation is one example of an application that grew out of tracking deals on paper and spreadsheets. Sales compensation management is following the same trajectory as SFA but more rapidly thanks to the evolution and acceptance of on-demand computing.

On-demand based compensation management solutions, such as Compel from Centive, have reached a cost-benefit point where they provide much more value than the cost of buying or maintaining systems in-house or tracking transactions with spreadsheets. Moreover, a well designed and thoughtfully employed compensation management system can be used by organizations to fine tune their sales activities and elevate sales compensation from a tactical exercise to a strategic tool resulting in optimized earnings and better alignment with company goals.

Compel is an example of a compensation management solution that helps to improve business processes not only in sales but in finance, IT and human resources, as well. By providing accurate commission accounting anytime, anywhere, Compel helps sales executives stay focused on business and helps managers direct the troops to the most profitable outcomes. Compel also offloads IT by interfacing directly with SFA systems and empowering sales compensation administrators to manage the system independently. Compel enables finance to meet compliance objectives and provides powerful tools for commission cost control and forecasting. Through its database and reporting tool Compel takes the manual labor out of tabulating sales results.

Just as SFA has become ubiquitous for helping manage the work of selling, compensation management solutions are now becoming an essential part of managing the last half of the “prospect to paycheck” business process. On-demand sales compensation management is a low cost solution that generates significant value and for that reason alone, we expect this solution to continue to gain prominence in the market.

About Centive

Centive, a privately held company headquartered in Burlington, MA, is a leading provider of strategic on-demand sales compensation management used to cultivate peak performance from sales representatives. Companies use Centive Compel to accurately calculate commissions and bonuses and gain real-time visibility into sales performance metrics. As an on-demand subscription service, Compel is a cost-effective solution that allows executives to be strategic and sales representatives to stay motivated and focused on selling.

To learn more about Centive, please visit www.centive.com or call 1-877-CENTIVE.

About Beagle Research Group

Beagle Research Group is a consulting and market research organization focused on emerging technologies and companies that will have an important impact on the way business is conducted in the years ahead. Our work is based on professional standards of quantitative and qualitative research which informs all of our publications.

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