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Defining What's 'Good' in a Sales Comp Plan

The first step in designing an effective pay plan is to define parameters for business success. (This article was first published in WorldatWork's Sales Compensation Focus newsletter.)

As a sales compensation practitioner, I'm often asked by business leaders to review their sales compensation plan documents and provide feedback. It's a reasonable request, but the answer is limited to what I observe in the document. There are multiple elements to a good sales compensation plan, one of which is how the company defines "good" in this context.

Defining Good

The first step to evaluating a sales compensation plan is to establish a set of standards for the best outcomes. I generally categorize standards in terms of the following:

- **Business results (namely revenue growth).** It's difficult to maintain a good sales compensation plan if the business is flat or shrinking. Other results connect to the company's growth strategy and can include market share, new customers and growth in strategic product sales.
- **Spend-to-revenue.** Often referred to as compensation cost-of-sales, this is essentially the share of revenue spent on sales compensation.
- **Employee engagement.** Good plans motivate the salesforce. Sales employee surveys can measure how well the plan motivates and engages salespeople.
- **Administrative.** This is the degree to which the plan design facilitates error-free transactions, payment calculations and reporting. Specific standards measure error rate per transaction and per commission dollar, as well as the share of administrative headcount per sales employee.

In each of these categories, management should establish competitive benchmarks from a set of companies that serve as a comparator group. Publicly traded competitors report revenue and growth data, but managers can acquire competitive benchmarks for the other metrics through syndicated surveys, system vendors or custom research initiatives.

Often, competitive benchmarks are not representative of good practice, yet this data can still represent a standard. Management should evaluate these standards relative to the company's performance in each of these areas in order to determine what good practice is.

Strategic Alignment

When working with finance and HR executives, I frequently hear that the sales compensation plan pays for behaviors incongruent with the business strategy. There is a practical approach to testing for this type of strategic alignment: Listen to what the leadership says, read the plan documents and get a sense for the different jobs and how the company organizes its sales resources to execute on the sales strategy. Sometimes these inputs don't line up. To go deeper, analyze the incentive payment history for a look at who gets paid for what. Some plans include specific metrics for growth, such as new customers or strategic products. Do reps get paid for meeting their goals on these metrics in line with management's expectations? Are salespeople who fall short of their sales quota able to earn their on-target pay? Good plans pay for the outcomes needed to execute the company's overall sales strategy.

Most of the plans I see use quotas to measure performance. There is a saying that goes, "A quota-based plan is only as good as the quotas." Indeed, quota attainment can have a significant impact on a sales team's engagement and earnings. Oftentimes the plan structure — the metrics used and degree of incentive leverage — looks right for the particular job, industry and company's stage of growth. If management struggles to manage quotas, however, I advise management to reduce the incentive leverage because in an environment of poorly managed quotas, the quota achievement score isn't a reliable measure of a representative's performance.

Pay Competitiveness

Competitive pay benchmarking is seen as a necessity today to developing a good sales compensation plan. Most of the companies I work with use published survey data to keep track of market pay trends for specific jobs and career levels. In a tight labor market— including most of the United States and Western Europe for many technology salespeople— it's critical that management keep abreast of competitive pay trends. Otherwise, the company can lose critical talent to the competition, chase elusive competitive offers, or face an uncompetitive valuation due to an excessive rate of spend-to-revenue.

A good plan is one that pays its salespeople competitively for strategically important outcomes. While benchmarking target pay establishes a foundation, assessing actual pay competitiveness is arguably more important for sales jobs. If your company does not pay high performers in line with actual pay benchmarks for high performance, you're likely to lose them. But paying low performers too much is not good either.

Employee Engagement

What do your salespeople say about the compensation plan? When evaluating a plan, I often ask the plan participants to explain how the plan works. It's not unusual to hear a different description from two or more representatives that use the same plan. Or, to hear, "I don't know." Both responses suggest dysfunction in the company's approach for communicating and supporting the plan.

The more complex the plan, the more resources you must invest to ensure salespeople understand how the company calculates their incentive pay. This point alone makes a strong case for a simple plan. Even simple plans, though, can cause employees to disengage if they don't believe their pay is in line with their contribution. The first-line sales manager can play a key role to ensure that employee engagement and communication is part of the sales compensation strategy. As key stakeholders of the company's sales compensation program, salespeople need to believe the plan is a good one.

Administrative Burden

Complex plans require lots of resources for communication, reporting and processing. An overwhelmed administrative system is likely to make errors, miss deadlines, frustrate the salesforce and bring an otherwise good plan down. Some companies maintain an effective administrative function, but at a significant cost and with limited flexibility for plan changes.

Whether your company uses a sophisticated software application or only a collection of spreadsheets, the plan needs to fit with the system used to support it. While that may sound backward, in practice, even the most flexible software applications have limitations. A good plan is one that your system of choice can handle without significant and timely reconfiguration.

Based on the many variables that go into determining a good sales plan, the plan document is only the beginning. However, it's an important starting point, and says a lot about a plan: whether management is clear and thoughtful in its expectations from salespeople, and whether the calculation methodology makes sense. But you can't judge a book by its cover. There is a story behind each plan — factors tied to strategic intent, cost effectiveness and employee motivation — that really determines whether the sales compensation plan will motivate and deliver the kinds of business results the company is after.

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