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## Changing With the Times

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Published: 11/06/2006

### Changing With the Times

When Magnet Street launched in 2000, it had 15 employees, and two part-time salespeople on a 100% commission compensation plan, according Tim Bates, director of sales. Today, however, the company, with just over \$20 million in revenue and 160 employees, is maturing, and additional sales channels and marketing efforts have shifted its thinking on sales compensation.

"We were a young company with young employees," says Bates. "The high performers were doing very well for people in their mid to late 20s, but now the job has changed."

Magnet Street, a Blaine, Minn.-based manufacturer of full-color refrigerator magnets, has implemented various marketing plans and direct sales through its website in recent years, which have attributed to its growth, and by 2005, Bates knew the company needed a new sales compensation strategy. He asked the company's sales team how much of its gross sales were generated by individual sales efforts versus all the other sales programs: the answer was 50%, reinforcing the company's need for a change.

In rethinking the strategy, Bates started with the salesperson's total income for the previous year. The new plan would pay half of it as salary and the other half as commission. Additionally, the commission would be based on meeting a sales goal of 120% of last year's sales for each salesperson. This plan promoted less risk for the salesperson, as he would receive a steady salary, but more risk for the company, since the salary represented a fixed expense unrelated to the level of sales. However, to make up for the risk to the company, Bates smartly instituted the 120% sales goal to help promote company growth.

The salespeople happily accepted the plan because it was not complicated and allowed them the opportunity to make the same amount of money as the previous year. Furthermore, they were told there would be a change well in advance, allowing them time to offer feedback and suggestions while Bates formulated the new compensation strategy.

The development of a successful sales compensation plan is a process that combines what the company wants to accomplish and what the salespeople need to receive in compensation in order to meet the company's goals. Paul R. Dorf, PhD, APD, and managing director of Compensation Resources, Inc., a sales compensation consultancy based in Upper Saddle River, N.J., spells it out literally: F.A.R.M. Each successful sales compensation plan should include the following characteristics.

**Focus:** You need to pay attention to desired results and not allow the salesperson to decide what to sell.

**Attractive:** The plan has to offer enough compensation to make the salespeople happy; otherwise, they will be job-hunting very quickly.

**Retain:** It is important to pay commissions over time. A quick commission payment has many drawbacks including a customer not paying as quickly, a customer canceling an order after the commission is paid, and reduced sense of loyalty on a salesperson's part. By paying commissions over time, such a month after delivery or customer payment receipt, your salespeople will be motivated to stick around.

**Motivate:** Provide the carrot that keeps the salespeople selling, such as higher commission rates for certain products or services.

In order to meet these objective you have to create and implement the appropriate compensation package for your situation. Generally, sales compensation plans are designed around the two basic pieces: salary and commission.

How these are combined is based on the company's sales objectives and marketing plan, and a company needs to understand the risks and benefits of employing each 100% as a compensation strategy before committing to a plan.

**Salary:** At 100% of the compensation, paying a salary allows the company to have full control of the salesperson (think department store clerk) as well as keep its payroll expenses predictable. Sales

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objectives are easily dictated and are likely outlined in the job description. A 100% salary compensation also generally means the company has a robust marketing and promotions plan, requiring minimal sales effort in making the sale.

The risk an owner runs in this type of sales compensation package, however, is a lack of motivation. If salespeople are not receiving a direct reward for their efforts, it's likely they will have little concern for their level of sales.

**Commission:** In a 100% commission situation, the company doesn't have to pay salespeople unless they make sales. For start-ups this is particularly attractive, as it requires no upfront financial commitment and little in the way of marketing budget, as the salespeople are responsible for 100% of the revenue. For the salespeople, working for commission only can be highly motivating--or highly stressful--depending on their level of confidence and skill set. A poor performer may leave the organization quickly as they are not making enough money, where a real "rain maker" may see this as a "sky's the limit" opportunity to create personal wealth and become a major source of revenue for the company.

This arrangement, however, is probably the riskiest. Companies with little to no marketing budget offer salespeople few resources to sell with, and a lack of brand recognition or consumer knowledge of the product or service can make sales difficult. There also is minimal control over the salesperson. Since all of their income is in "their hands," salespeople can have a "whatever it takes" attitude toward making sales, which could lead to not meeting your company's specific sales objectives. Additionally, payroll in this situation is not predictable, making it difficult to forecast and budget.

The ideal situation is to create compensation strategy that includes salary and commission. A salary plus commission compensation strategy offers you and your salespeople some stability, while keeping in play the motivation factor that helps you increase your revenue. This type of arrangement requires a detailed plan, which strikes a balance between risks for both parties.

In Magnet Street's case, its marketing efforts increased, and sales revenue was no longer solely reliant on the salespeople's efforts. Bates' plan took these factors into consideration, offering continued growth for the salespeople and accounting for multiple sales channels.

Magnet Street has had their new compensation plan in place for almost a year now, with very positive results. The plan initially was instituted to respond to its own changing needs, but it turned out that it also responded to extenuating factors. Despite its industry's "down market" this year, the new plan has allowed its salespeople to have a steady income, and the company's sales goals are still within reach as the company enters its busy season. Bates feels confident that his salespeople will make as much as they did last year, only this year, he's offered them more stability in an unpredictable market-- an added benefit to be sure.

#### SIDEBAR--When It's Time For a Change

How do you identify when your sales compensation plan is not working? Donya B. Rose, managing partner of The Cygnal Group, a sales compensation consultancy based in Chapel Hill, N.C., who assisted Bates in his restructuring, suggests that companies watch for these red flags:

"Your salespeople are acting like teenagers. They are looking out for themselves only." According to Rose, this indicates the wrong balance between salary and commission/bonus.

"Your salespeople appear to be coasting. They are too comfortable." Rose explains that this is due to continued commissions/bonuses on previous sales. Most of the time the salespeople are only required to renew existing business, and not obtain new clientele. In this case there needs to be a higher commission rate on new business and less commission paid on existing business.

"Your sales compensation costs are going up faster than your profits." Not only do you have to watch your salespeople but also you have to watch how your plan affects your bottom line. High commissions may be fine for a start-up that cannot afford to pay salaries, but eventually there comes a time to re-evaluate.

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