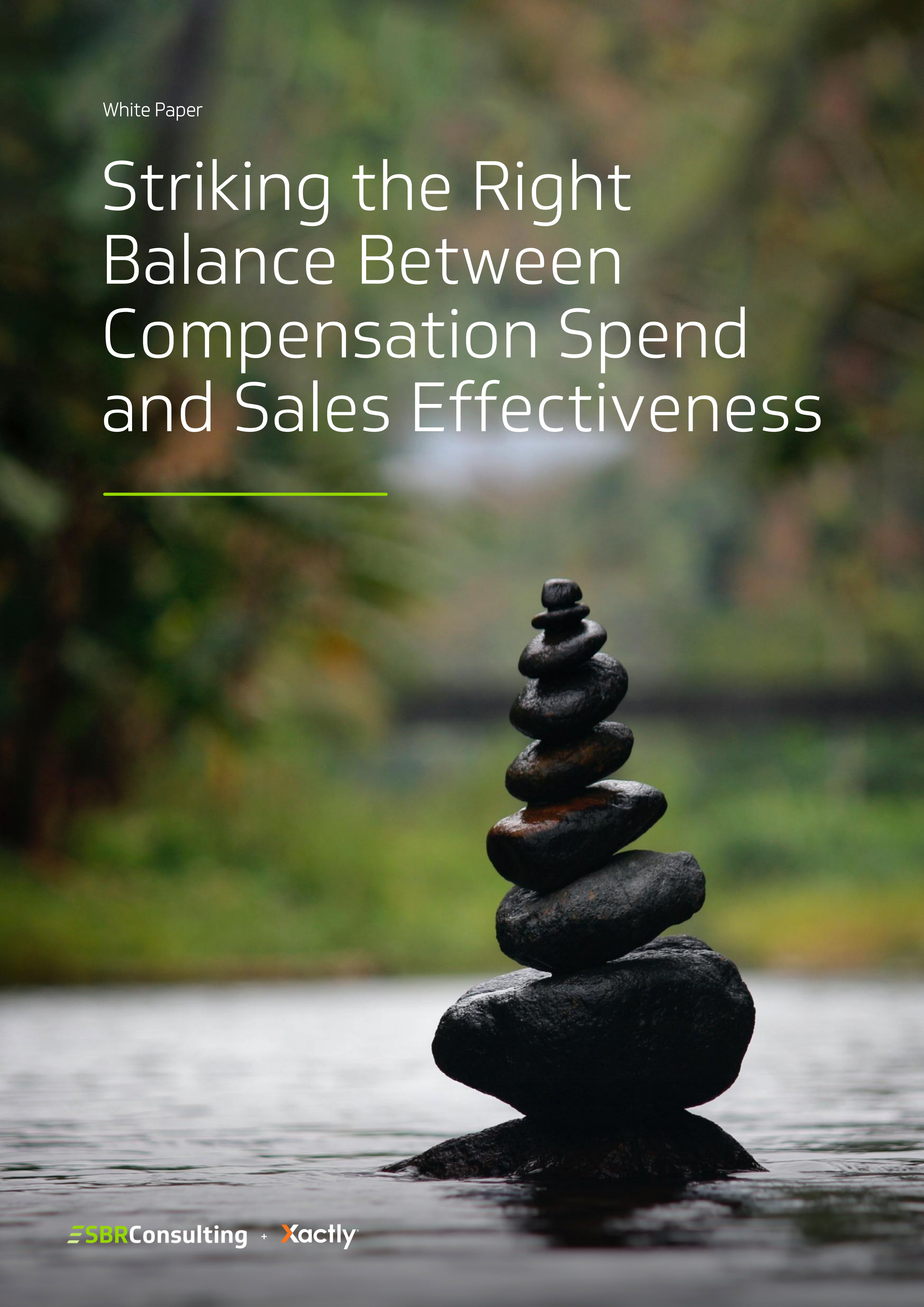
White Paper

Striking the Right Balance Between Compensation Spend and Sales Effectiveness

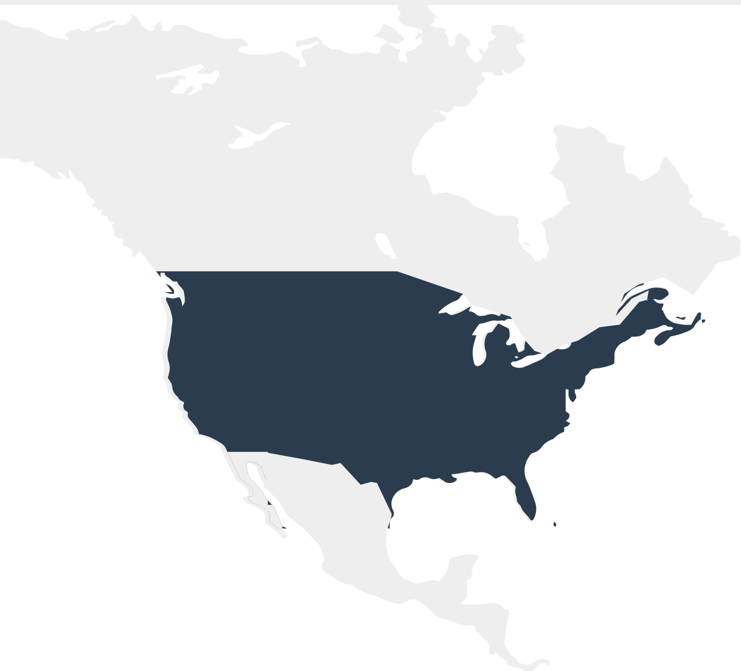


SBRConsulting + Xactly

Introduction

In the current economic climate, post-pandemic, the war in Ukraine, the cost of living crisis, inflation, and increasing interest rates, organisations are facing unprecedented cost pressures. These pressures are leading businesses across all industries to tighten their budgets and strive for maximum return on investment. As evidenced by the recent increase in job cuts in the Tech sector, organisations are seeking to manage their costs more efficiently than ever before.

> Sales force costs represent the largest marketing expenditure for many firms, accounting for an average of 10% of sales revenues and up to 40% in certain B2B industries.” [1]



The annual spending on sales force management in the US alone exceeds $800 billion, with $200 billion devoted solely to compensation. This is comparable to the estimated spending on media and digital advertising, highlighting the importance of effective management of sales force costs. [2]

Recent studies have found that up to 10% of compensation spending is ineffective, representing as much as 4% of annual revenue in certain B2B industries - that’s an enormous and unnecessary cost for any business. [3]

Common Trends & Challenges

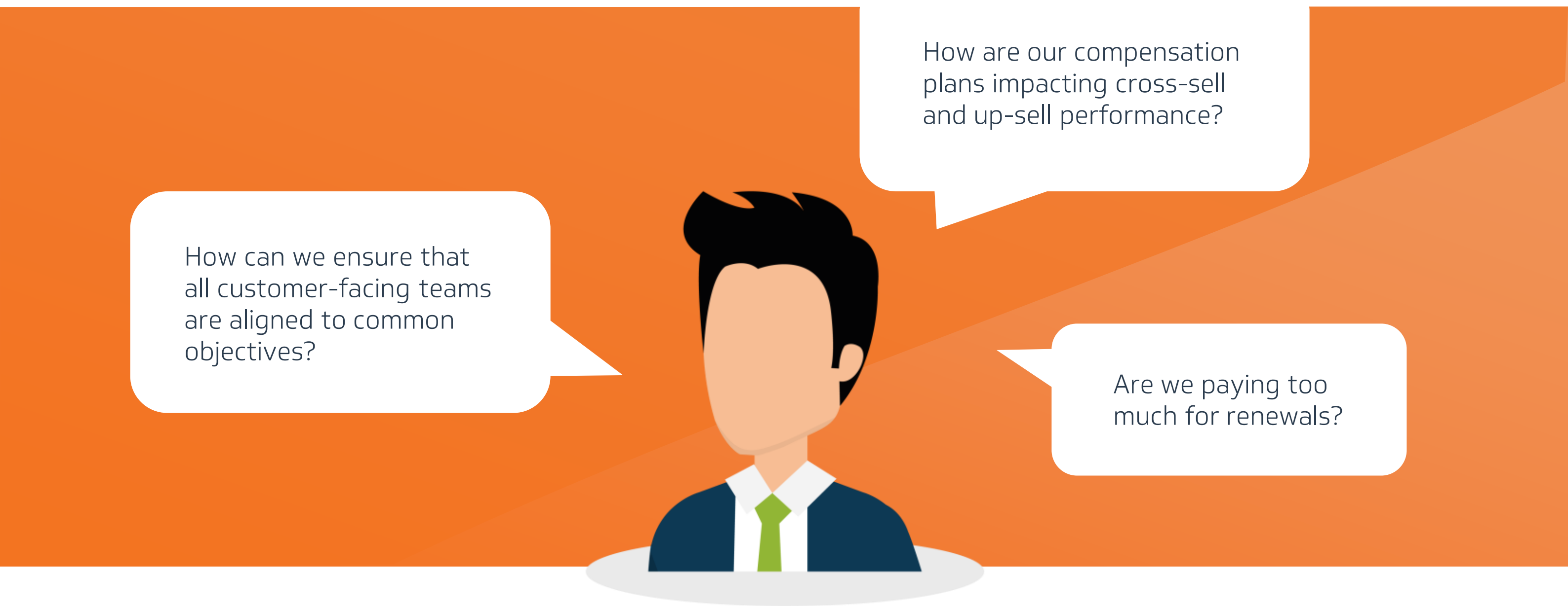
In today's market, customer retention is even more crucial than ever, and for good reason. Acquiring a new customer costs about 5 times more than retaining one. Naturally, organisations are focusing on strategies to retain their customers and keep them satisfied.

As a result of growth, many businesses turned to mergers and acquisitions, as well as investing in product innovation. These businesses are now focusing on selling their newly developed products and services to customers. The ability to cross-sell has become a critical element of their strategy to boost the average order value and maximise every transaction.

Following organisational restructuring, businesses are looking for ways to create efficiencies by breaking down silos and aligning teams with common objectives. The question of whether SDRs should be credited at the point of a meeting booked, held, opportunity creation, or order placed remains hotly debated in (virtual) meeting rooms worldwide. This debate reflects the challenges that organisations face when trying to balance their priorities and optimise sales effectiveness.

Common Trends & Challenges

As businesses strive to balance their sales effectiveness with compensation expenditure, they are taking a closer look at their compensation plans. This scrutiny is driven by the need to optimise customer retention, cross-selling, and new business development while keeping costs under control. To achieve these objectives, leaders are grappling with a number of questions:



As you know, creating an effective sales compensation plan is easier said than done. The challenge is a complex one, as these plans must reflect the specific industry sector and product offerings, while also taking into account the unique circumstances of the company. Furthermore, the plan must be effective for a wide range of performance levels, support effective onboarding, and be flexible enough to handle special or temporary assignments.

Sales compensation plans must also be aligned with functions beyond sales, such as pre-sales and tele-marketing. To ensure maximum effectiveness, these plans should be designed to promote collaboration between teams and avoid silos that can impede sales performance.

The good news is, despite the complexity, there are certain principles that have stood the test of time when it comes to sales compensation plan design. Let's take a closer look at some of these principles with a particular focus on the questions asked above.

THE 6 KEY PRINCIPLES

1 Simplicity

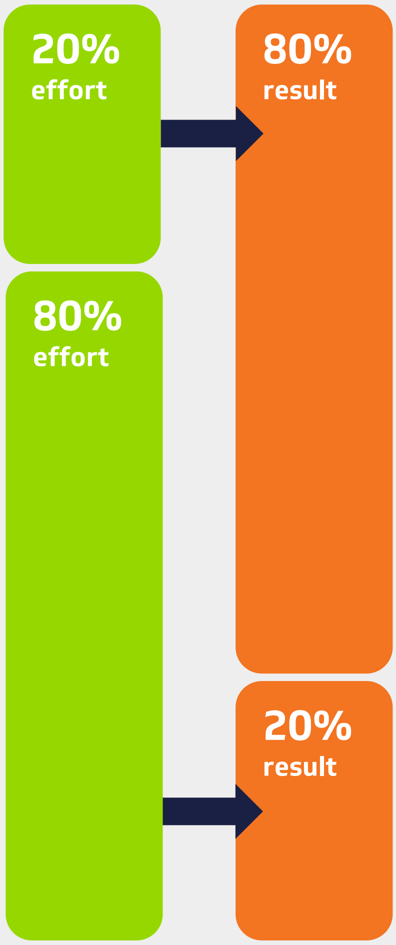
When creating sales compensation plans, involving too many stakeholders can lead to a complex design with numerous elements, resulting in disaster. The key to successful plan design is simplicity with a maximum of 3 focused elements on the highest priority outcomes, with no element valued less than 15% of the total On Target Earnings (OTE) for the year. Although there may be multiple plans for various roles, such as hunters, farmers, pre-sales, or new salespeople, each plan must be as simple as possible.

How do I apply this to the trends and challenges above?

Apply Pareto's 80/20 principle to your commission plans and identify the components that have a significant impact on cross-sell and up-sell performance for a large portion of your team. By doing so, you can determine which components are making minimal difference for only a few individuals, and consider reallocating the commission earned from these components to incentivise the achievement of broader business goals. Utilising Incentive Compensation Software allows organisations to analyse this data in real time, offering valuable insights into the components that have limited impact, equipping administrators with the necessary tools to optimise commission spending and maximise its effectiveness.

According to an article by McKinsey, top-performing digital companies are willing to dust off their metrics and think strategically about what types of measures and incentives will engender the outcomes they want."

This doesn't mean loading up more and more components to a commission plan, but simplifying and reallocating commission spend to components that are really going to move the needle.



THE 6 KEY PRINCIPLES

2 Transparency

Transparency is crucial in sales compensation plan design as it ensures that salespeople and leadership can quickly and accurately understand the plan's structure and their compensation.

Achieving simplicity in plan design is one way to help achieve transparency. By keeping the plan simple, salespeople can easily calculate the payout they will receive for winning a deal, reducing time spent on resolving commission plan queries. In addition to simplicity, transparency also requires alignment between the sales management plans and the plans of individual performers. Targets set for individual performers must roll up into the overall targets set for the team or organisation. Misalignment creates unproductive tensions as salespeople receive conflicting messages from their compensation plan and their line managers.

Organisations with transparent sales compensation plans achieve 19% higher year-over-year revenue growth than those with opaque plans. [6]

How do I apply this to the trends and challenges above?

It is important to first create alignment between different teams by incentivising them by the same measures. Once you have this clearly defined, it needs reinforcing through consistent communication. Each team should understand how other teams are incentivised and how this rolls up through the business and performance should be assessed and communicated in a regular cadence. This will not only ensure transparency, but also encourages cross-team collaboration and helps break down silos.

THE 6 KEY PRINCIPLES

3 Feasibility

The plan must be feasible in the sense that the metrics being used are ones that salespeople can actually influence. The cardinal principle of simplicity should help here. Make sure that additional metrics are not being added to the plan which salespeople cannot significantly impact: bad debt, usage levels, delivered margins are all examples of unhelpful metrics that dilute plan impact.

It is important to note that a successful plan must be based on what can be reliably, unambiguously and efficiently measured and data must be captured rapidly enough to match the cadence of the plan's pay-out cycle.

How do I apply this to the trends and challenges?

When it comes to compensation, you can only manage what you can accurately measure. If you want to create rewards for cross-selling, you really need to know what people are currently selling and how to recognise revenue for additional product lines. If your billing system only enables reporting by invoice line, and not by product line, you'll need to update your systems before you can incentivise sales people effectively. By launching a commission plan without considering systems, you'll only be encouraging the Sales team to engage in 'creative accounting' - all of a sudden you'll start seeing professional services revenue appear in that cross-sell revenue line!

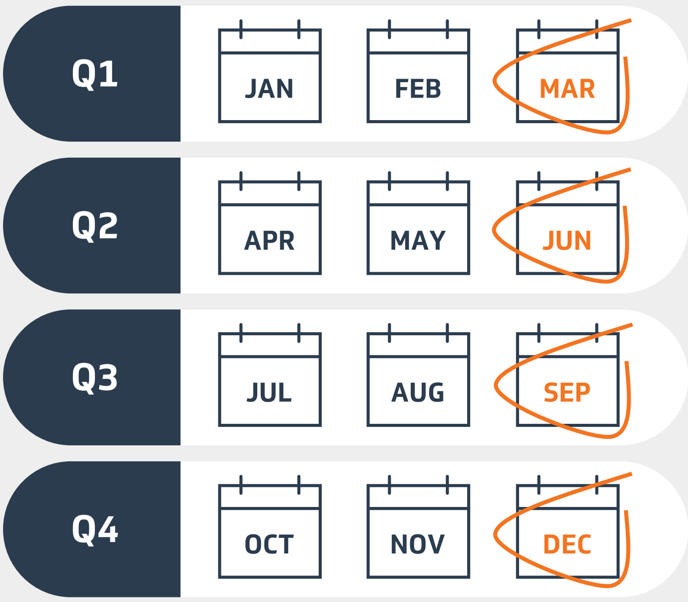
THE 6 KEY PRINCIPLES

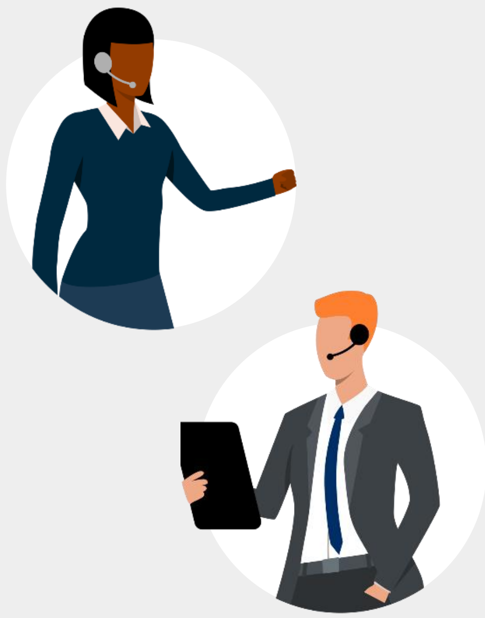
4 Consistency

While it's important for companies to adjust their compensation plans each year to align with evolving business challenges and budgets, too much change can create unnecessary complexity and confusion. Salespeople rely on consistency and stability in their pay structure, and frequent changes can lead to a lack of trust in the leadership's vision along with waste valuable sales time as individuals try to understand how they can earn their OTE. This is especially true if the new plan introduces a significant amount of complexity.

How do I apply this to the trends and challenges above?

Try to avoid muddying the waters by introducing too many SPIFs through the year – they add complexity and may well have unintended consequences. It may be tempting to introduce a cross-sell or up-sell SPIF for the last month of the quarter, but if your sales cycle is typically 180 days, you're just going to be paying out more commission for the same result. Not only that, but if you do this consistently, it'll encourage sales people to hold onto deals until the next SPIF.





THE 6 KEY PRINCIPLES

5 Cadence

At the top level, the plan and associated targets must be agreed and ready to communicate within 10 working days of period start. This is not a trivial challenge, and the danger is that neither Sales (focused on Year End performance) or Finance (focused on budgets) make the necessary time available in Q4.

Simplicity and consistency will both help, but ultimately there must be a clear project plan with owners to ensure that the sales compensation scheme is formulated and approved on time. It won't happen by accident.

The objective in execution is to minimise the gap between achieving the goal and receiving the pay-out. If the cycle time is too long, salespeople may forget which deal contributed to the pay-out, which significantly reduces their motivation. Implementing a straightforward plan, using achievable metrics, and automating processes can all aid in achieving this goal.

How do I apply this to the trends and challenges above?

The key for this is really to ensure that commission plans for next financial year are review months in advance so that everything can be ready to go for the new fiscal year. A very effective way to help get commissions plans out at the start of the year is by implementing an Incentive Compensation Management (ICM) solution. Xactly and Salesforce commissioned Forrester to conduct a Total Economic Impact™ study to examine the potential return on investment and found that by using Xactly Incent, organisations realised a 60% reduction in time needed to configure payment plans and calculate commission payments (the TEI study can be found in the sources below).

60%

reduction in time needed to configure payment plans and calculate commission payments

THE 6 KEY PRINCIPLES

6 Affordability

The company's ability to afford salespeople's pay-outs is crucial, but it can become complex when different parts of the company portfolio have different margins, or third-party elements are involved, or the business model is transitioning. However, it's important to shield this complexity from salespeople and manage it through good pricing discipline/approval processes instead of creating a separate compensation plan for every product line or adjusting the plan for every deal.

How do I apply this to the trends and challenges above?

The common stance of CFOs is often questioning the need to pay for renewals when the initial sale has already been paid for by the business. However, retaining customers relies on various factors such as product quality, customer service, and effective account management. In order to achieve high renewal rates and maintain healthy profit margins, it is necessary to invest in these efforts. To maximise return on investment, it is crucial to compensate account managers who truly make a difference. If the current churn rate is 10%, it is important to reward exceptional performance beyond that threshold. Compensation plans should be activated for performance exceeding 90%. To achieve outstanding results, it is essential to delve deeper and analyse the breakdown of net retention, including cross-sell, up-sell, and renewal indexation/uplifts. While avoiding unnecessary complexity in commission plans, it is vital to manage performance at a more granular level so that individuals can understand how to achieve their objectives and impact the wider business goals.

According to Gartner, offering salespeople incentives for renewals achieve renewal rates that are

5%

higher than those that do not. [5]

Benefits of paying commission on renewals

1

Increased motivation and loyalty among sales reps: Paying commission on renewals can motivate sales reps to focus on retaining existing customers, rather than solely on acquiring new ones. By ensuring that commission is paid in advance, sales reps are incentivised to continue working with those customers and maintaining those relationships over the long term. This can help to build loyalty among sales reps and reduce turnover.

2

Better customer retention: By incentivising sales reps to focus on renewals, organisations can improve their customer retention rates. This can lead to increased revenue over time, as existing customers are more likely to make additional purchases and refer new business.

3

More predictable revenue streams: By focusing on renewals and paying commission in advance, organisations can create more predictable revenue streams. This can help to improve forecasting accuracy and reduce the volatility of revenue from quarter to quarter.

4

Improved profitability: Renewal sales typically have a lower cost of sale than new sales, since the customer is already familiar with the product or service. By incentivising sales reps to focus on renewals, organisations can improve their profitability over the long term.

Conclusion

It is important to note that there isn't one silver bullet to create a high performing sales culture. Introducing sustainable change requires a comprehensive approach that includes skills development, systems implementation, and sales motivation. However, an effective and evolving sales compensation plan is such a critical component of the sales transformation process, as it plays a key role in driving sales motivation.

By aligning your sales compensation plan with other elements of your sales transformation process, you can create a holistic approach that drives sustainable change and improves sales performance. So, take the time to design a sales compensation plan that reflects your specific circumstances, supports collaboration across teams, and incentivises your sales team to achieve their goals.

Typically, the biggest challenge we see to improving compensation effectiveness is not the ability to introduce new compensation plans that tick all of the boxes above - this should be achievable in every organisation. It is the fact that the process of reviewing compensation takes months, not weeks. Don't leave it too late.

While you are reviewing your compensation plans, one thing that can be done in parallel is reviewing your internal systems, including whether an Incentive Compensation Management solution is a good fit. If there are changes that need to be made, you'll want to get ahead of the game and introduce those changes before the start of next financial year so that they can be tested sufficiently ahead of time.

Sources

1. Chung , Doug J . , Byungyeon Kim , and Nilad ri B . Syam , (2020) "A Practical Approach to Sales Compensation: What Do We Know Now? What Should We Know in the Future? " , Foundations and Trends® in Marketing 14, no. 1.

2. Motivating Salespeople: What Really Works by Thomas Steenburgh and Michael Ahearne: Motivating Salespeople: What Really Works (hbr.org)

3. Angelos, J. and M. Wachter (2016), "Sales planning like it's 1999? Take the guesswork out of target setting. " Accenture Strategy 16-3256.

4. How B2B digital leaders drive five times more revenue growth than their peers October 10, 2016 | Article How B2B digital leaders drive five times more revenue growth than their peers | McKinsey

5. Sales Compensation Planning How to create an effective sales compensation plan Sales Compensation Planning | Sales Insights | Gartner.com

6. Benefits of transparent sales compensation plan – Xactly Corp.

About SBRConsulting

SBR Consulting is a specialist global consultancy that focuses on growth and revenue acceleration. We leverage our experience of 1000+ clients over the last 20+ years to help our clients transform, enable and increase the effectiveness of their revenue org.

Get in touch:

info@sbrconsulting.com

+44(0)20 7653 3740

63-66 Hatton Garden, 5th Floor, Suite 23, London EC1N 8LE

www.sbrconsulting.com

About Xactly

Xactly was founded by a sales leader, for sales people everywhere. Xactly's AI-powered Intelligent Revenue Platform gives Revenue Operations teams the data they need to power sales leaders to plan with agility, motivate with intention and predict with conviction. We are on a mission to transform the sales industry with AI to power reps and leaders to deliver results regardless of circumstances

Get in touch:

connect@xactlycorp.com

+1 (866) 469-2285

1 Fore St Ave, London EC2Y 5EJ

xactlycorp.com