Compensation Plan Design: Principles of Success

By Dan Jensen, Compensation Plan Consultant

In the history of direct selling, we have seen great companies emerge as industry leaders. There have also been hundreds of not-so-great ones. What's the difference between those that have the 'Midas touch' and those who seem to hit a brick wall? What do the industry leaders know that the rest don't grasp as well?

In my 25 years in the industry working with hundreds of companies, I've found that those who rise to the top follow some timeless principles of success in direct selling. Space allows me to share only a few of them with you:

- Balance the key sales force behaviors using your compensation plan
- Always have a strong retailing emphasis
- Build strong managers
- Build strong leaders
- Build a "retention culture"

If a company gets these principles right, they can usually make mistakes in other areas and still move upward. Get these wrong, however, and welcome to the brick wall.

Balance the key sales force behaviors

The money spent on sales force compensation represents your single largest expense. The return on investment for this large expenditure must be measured in terms of behaviors. What behaviors do you get back for the money you spend on commissions? What are the behaviors that you need to build the business? I call them the *Five Golden Behaviors*:

1. Retailing
2. Recruiting
3. Building Managers
4. Building Leaders
5. Retention

Looking at your plan and the behaviors it supports

There's a simple way to analyze your plan for the behaviors it supports. Take each type of commission at the lowest granular level of detail and ask yourself, *"if this was the only type of commission the plan paid, what would it make me do?".* For example, if your plan paid out 6% for four levels of sponsors, isolate the level one commission in your mind (a commission on those who are personally recruited). Look at it as if it was the only commission paid in the plan. What would a level one commission make you do if it was the only type of commission paid? I see a level one commission engendering two behaviors: recruiting and teaching to sell. It would make me recruit new people and teach them to sell so I could get paid on their sales. It would not create managers or leaders. It does not make the sponsor sell more product (retail profits from personal sales do that). A level one commission simply generates recruiting and 'teaching to sell' behavior (which is what a manager must learn to do).

What if the plan only paid 6% on level two (no level one, three, or four commission is paid)? What would that make you do? For me, it would make me sponsor a couple of people on my first level and then teach them to recruit others. It would make me also teach them how to get others to sell so I could make a commission when they did. Go through this mental exercise of isolating each type of commission in your plan and note for each commission type which of the Five Golden Behaviors it creates and which behaviors it fails to create. On my web site (www.jenetek.com), you can download a *Plan Behavior Analysis Worksheet* that has a template for this type of analytical exercise. When you have looked at each type of commission, also look at the big picture to see how well your plan addresses all of the Five Golden Behaviors. Is it well balanced, or lop-sided (out of balance)? For example, does it spend most of its money on recruiting and very little on building managers and leaders? You want to see a somewhat balanced picture between these behaviors.

Building a Strong Retailing Ethic

Of all of the Five Golden Behaviors, this one may have the greatest impact on your success for several reasons:

1. Retention of new recruits: Industry wide, most attrition occurs during the first sixty to ninety days of a new recruit. Why? Most find that their participation in the business opportunity simply is not worth their time. They don't earn enough in their first few weeks to justify their time involved. In addition, we find that that about 70% of new recruits do not sponsor even one person in their first ninety days! Very few sponsor two or more. What this means is this… Your compensation strategy must provide a way for your new recruits to make at least $25 to $35 per hour in their first ninety days <u>without a downline</u>. If you don't, you'll struggle to keep the majority of your new recruits. What would <u>you</u> do if you put 40 hours into your new business as a new recruit and received only a $16.83 downline commission check in your first month? $25 to $35 per hour is usually what it takes and in almost all cases, downline commission checks can never achieve that in the first ninety days.
2. DSA statistics suggest that 54% of all new recruits were customers before they decided to become distributors. If you develop a strong retailing ethic, you not only build sales but you also create a huge pool of great recruiting prospects with your customers.
3. Companies that build a strong retailing ethic find they can enroll many new customers for every new distributor.

If you want to build a strong retailing ethic, consider these suggestions:

- Build a culture that respects the difference between a retail customer and a distributor. Retail customers generate retail commissions which is essential to retain your new recruits and help them achieve that $25 to $35 per hour target.
- Don't make it too easy to join as a distributor or you will cut off the profits your distributors make from retail sales. If you were a distributor selling to a new customer and they learned that they could buy the product at wholesale if they only sign a form and pay $10, what would they do? They'd gladly pay the $10 to save even more on their price. Who loses? The distributor loses their retail profits and never achieves the $25 per hour target. Eventually your company loses as you see your new recruits leaving through a revolving door. Companies that build successful retailing cultures quickly learn that they must have a small 'barrier to entry' to differentiate between a customer who just wants to buy product and a distributor who wants to build a business. They learn that they must aggressively protect the distributor retail profit.

- If you are a party plan company, be careful not to encourage your distributors to aggressively recruit their hostesses unless the hostess really wants to build a business. Some hostesses can do more for building sales as a repeat hostess than they would as a distributor.
- Have an acceptable retail pricing model. Don't price your products so high that customers get sticker shock. Make it easy for your reps to sell at retail.
- Party plan companies should focus on strong booking success in every party. Indeed, the success of a party should be measured more on the bookings than on the sales volume. A party with low sales volume but with lots of bookings is a great success. Parties without bookings mean that the seller is out of business.

Companies that fail to build a strong retail culture become wholesale buying clubs. I call this the 'internal consumption model' of direct selling. There have been a few successes of this model over the years, but even fewer that have endured the test of time. If you want strong growth over the long term, build a strong retailing ethic.

Build Strong Managers

A manager usually has a group of six to twenty active sales reps who they train and motivate. Managers are experts at selling and recruiting and you depend on them to teach others to do the same. The ultimate goal of a manager is to help others in their group or team to become strong Managers.

Without managers, each recruit is left to figure out by themselves how to succeed in the business and, as a result, most fail. Managers make it happen. They lead by example. "Do what I do" is their cry.

Without this mentoring behavior by good managers, we often see a culture develop of 'throw the mud at the wall and see what sticks', recruiting bodies as fast as they can and moving on to the next new recruiting opportunity. In time, such a culture develops an accelerating revolving door losing as many recruits as those who are joining. Managers believe that every new recruit in their group is precious and deserves the help they need to succeed in the business. Managers are your future leaders.

To build managers, your compensation plan must have the right incentives for distributors so they will want to be managers. Their income must be well worth the challenge and time commitment. The plan must compensate well for building and training a personal group and ultimately helping others to also become managers.

Building Strong Leaders

Your success will be no greater than your success in building a group of strong leaders in the field. Leaders provide the strength that sustains and builds the business over time. If you want to make it in the long term, and make it big, there's no other way. But how do you develop a large force of strong sales leaders?

- To develop strong leaders, you must develop strong managers. All good leaders were strong managers, first.
- Second, the compensation plan must reward leaders for leadership behavior. What is leadership behavior? The development of new managers and leaders below them and helping them, in turn, to develop other managers and leaders. For a leader to grow their business, they must develop strong managers and leaders and nurture the process continually. They must often work deeper in their downline often outside their own group and do this hand-in-hand with other downline managers and leaders. Great leaders hunt for their downline rising stars and mentor them into tomorrow's great leaders. This is how great leaders build extremely successful downline organizations. There's no other way. Long term

growth that exceeds your rate of attrition comes from developing people into better managers and leaders.

How can a compensation plan reward leadership behavior? By rewarding the development of managers and leaders from deep within their downlines. If a leader sees little reward for developing tomorrow's leader in their downline, they won't bother. Instead, they will work shallow (a manager behavior). If there are strong rewards for developing managers and leaders from deep within their downline, your strong leaders will do so. They always follow the money. They always look to leverage themselves to get the most return on the time they spend with others. If your plan rewards this behavior, you will see a constant stream of new leaders rising to the surface and your business will enjoy long-term health and growth.

Build a Strong Retention Culture

No amount of recruiting will compensate for poor retention. No matter how many are recruited, you can lose just as many as you recruit. The key to growth is retention and it's often the most elusive. Successful companies quickly learn that retention must become part of their "culture" of success.

Earlier in this article, we noted that new recruits need $25 to $35 per hour to make it worth their time and keep them in the business. We noted that most attrition occurs very early in the life of a new recruit (60-90 days). But how do we keep our recruits who have weathered the storms of their first ninety days? How do we keep our leaders and managers from jumping ship?

Here are some tips you'll want your compensation plan to address to keep your people working hard month after month:

- Use "golden handcuffs" to keep them engaged in the business. Would you walk away from a $300 per month income stream? Your compensation plan needs to help people develop a recurring income stream as quickly as possible of at least $300 per month. This is done by rewarding the right behaviors as early in their career as possible. An example of what not to do would be to provide meager commission percentages to new people until they develop a large team. In short, get early money into the hands of your young sales reps as quickly as possible. You'll keep them longer.
- Use both a stick and a carrot. When a person fails to meet their minimum requirements, don't continue paying them as if they had. Use a "paid-as title" as well as a recognition or "badge" title. In short, they have two titles. Pay them well as they perform, but match their earnings to the true level of their performance each month.
- Handsomely reward your strong managers for their team building results. As they work with their team members, you'll see retention increase.
- If you reward managers more for their personal sales than for their team building, you'll see them sell more but fall down in their team building. This will cause an increased attrition rate. Your compensation plan needs to carefully balance incentives between personal sales commissions and team building commissions.
- Use recognition at every opportunity to affirm the right behaviors that build successful teams and downline organizations.

Apart from compensation and incentives strategies, companies that successfully retain their managers and leaders find ways to earn the trust of their people. A company that has a great compensation plan but proves to be untrustworthy to their field will find their people leaving out the back door. Mistrust trumps a good compensation plan. In the end, it all boils down to "trust". You have to show them that you can be trusted with their precious customers and downline recruits.

Training – often the missing ingredient

Successful companies quickly learn that they need both motivation (compensation plan and incentives programs) as well as training programs to build lasting success. Motivation without competence doesn't work. Be sure your compensation plan has a strong and effective training program that is in perfect alignment with its principles and techniques for building success. You could have the best compensation plan in the world but fail miserably because you don't train your people how to use it to their advantage.

Conclusion

Follow these timeless principles of success and you can't go wrong.

- Balance the key sales force behaviors using your compensation plan
- Always have a strong retailing emphasis
- Build strong managers
- Build strong leaders
- Build a "retention culture"

Then, watch your bottom line grow.

About the Author

Dan shares his passion for sales force compensation with his consulting clients and through his executive training seminars around the globe. In 1978, Dan founded Jenkon, a leading software provider to the Direct Selling industry, and since then has worked with hundreds of direct selling companies. His expertise has helped many new startup companies and industry leaders dramatically accelerate their growth and sales. His web site is found at www.danjensen-consulting.com.