Navigating The Turbulent Seas Of Sales Compensation

GCCBA Meeting: May 24, 2017

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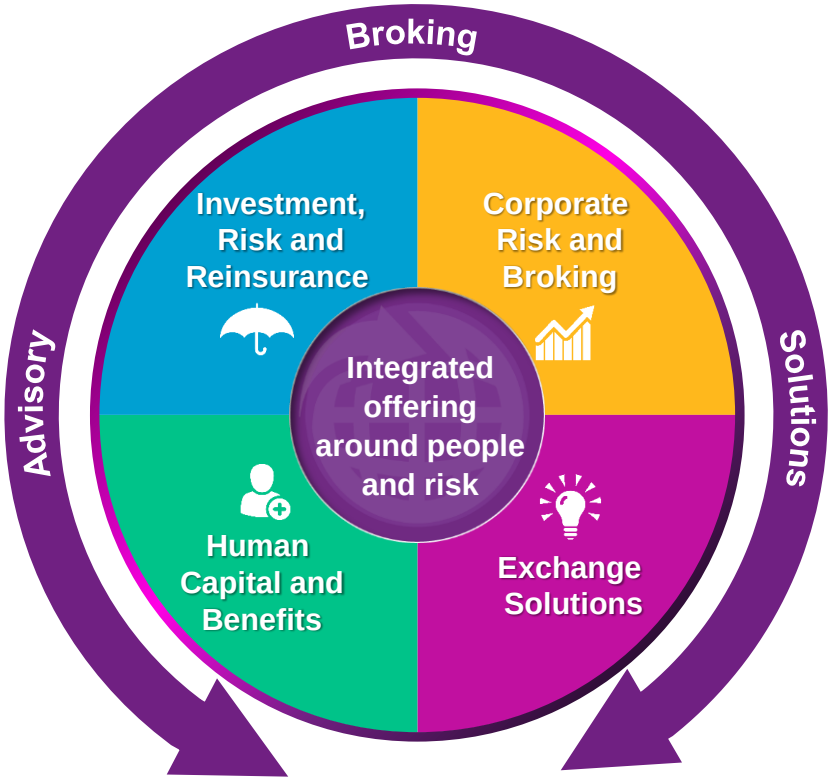
Willis Towers Watson

Introductions

- Joe Clarkson
- Chicago
- Global practice leader
- 20 years consulting
- 15 years industry
- 25-30 client engagements/year

Willis Towers Watson

Integrated advisory, broking and solutions designed to meet our clients' risk and people needs

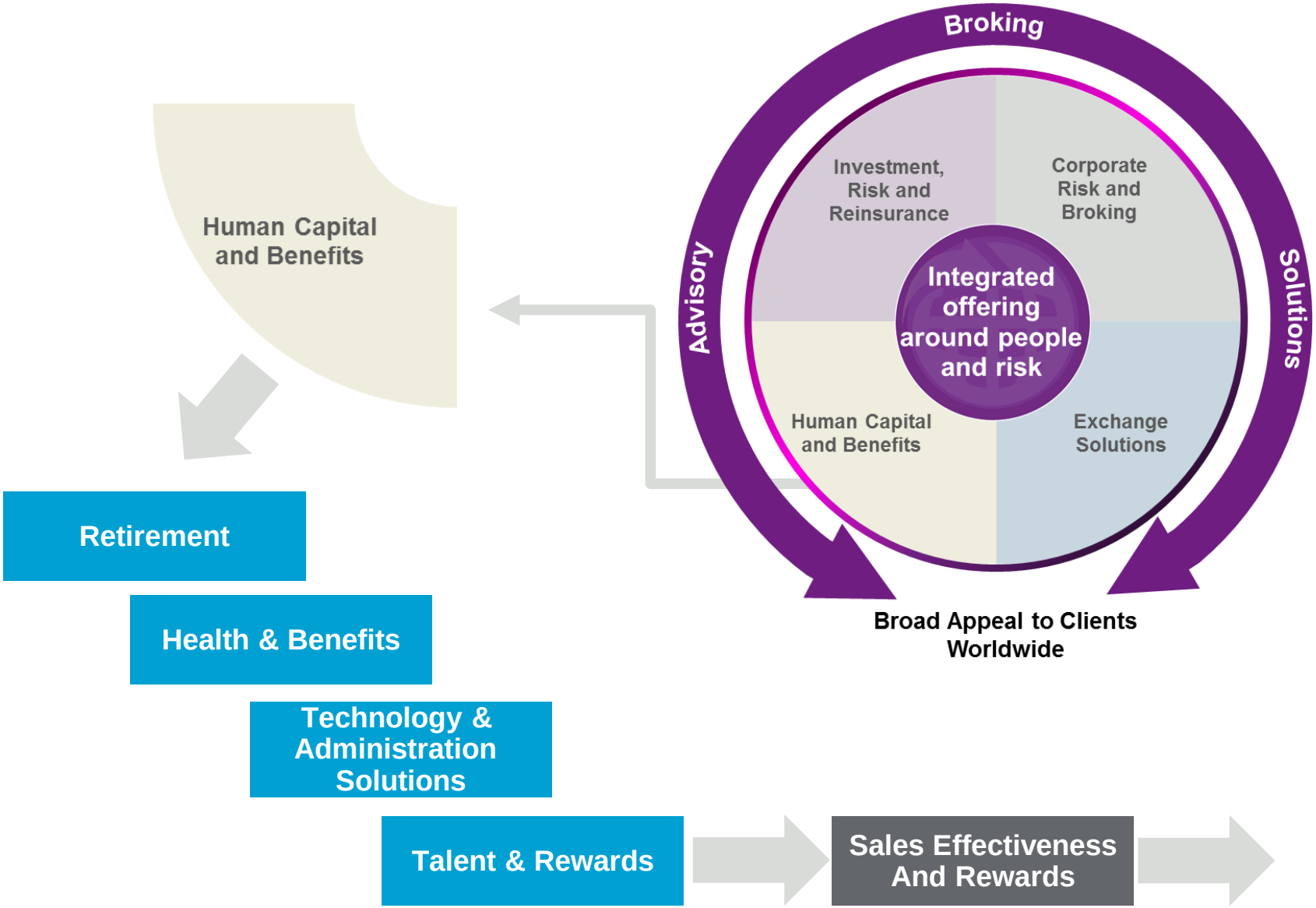


39,000 colleagues in **120+ countries**

Scale, diversity and financial strength:
$8.2 billion revenue

A deep history dating back to **1828**

Willis Towers Watson



We are global and local

Sales Effectiveness & Rewards Team:

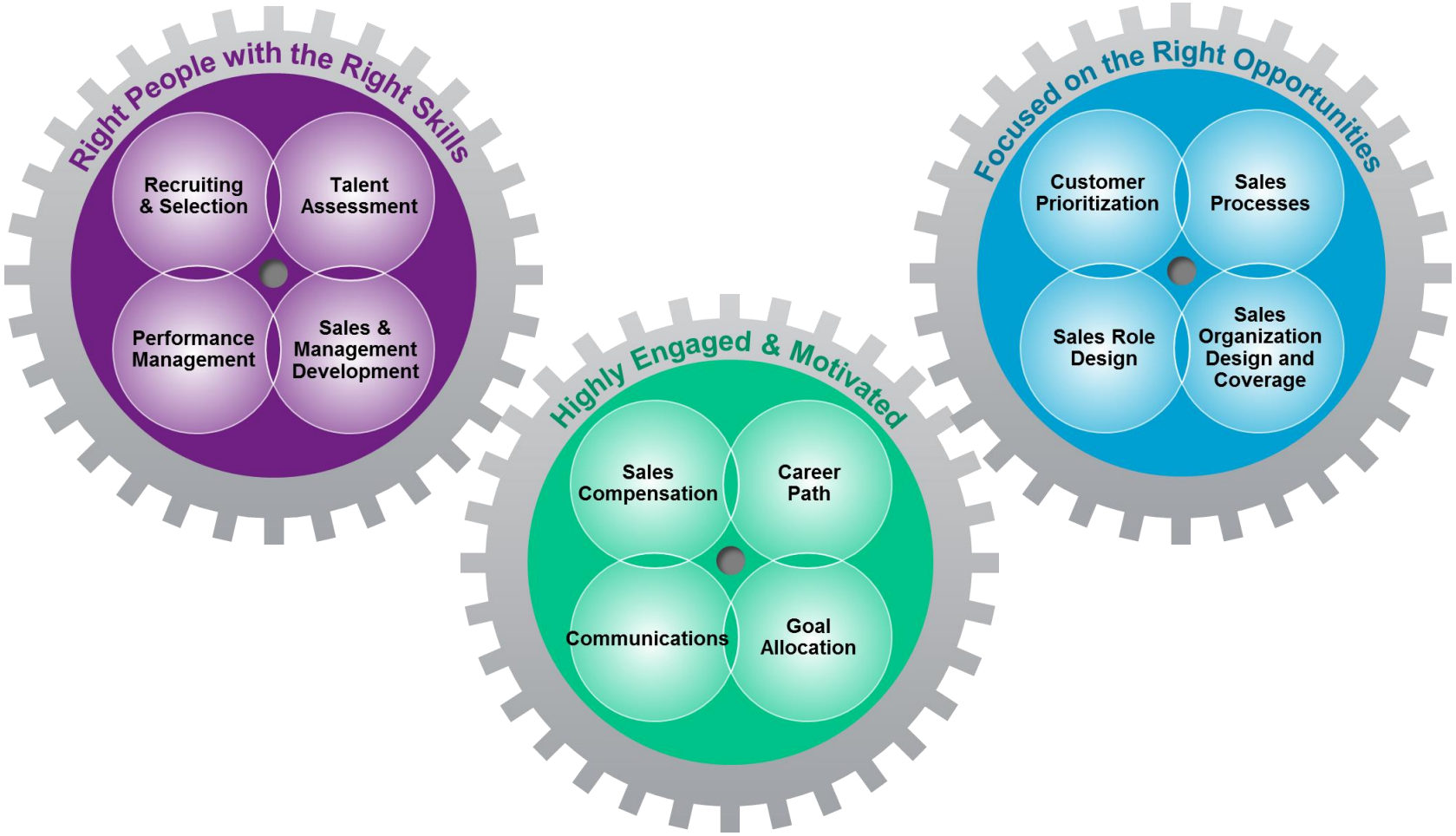
- **80+ consultants**
- **35 cities across 22 countries**
- **200+ sales compensation projects annually**
- **>35% with global sales forces**
- **Access to the world's most comprehensive databases of pay levels and practices**

Converting strategy into results through your human capital programs

Willis Towers Watson's Model for Sales Effectiveness

Change Management | **Tools and Technology** | **Governance**

Multiple disciplines need to be synchronized



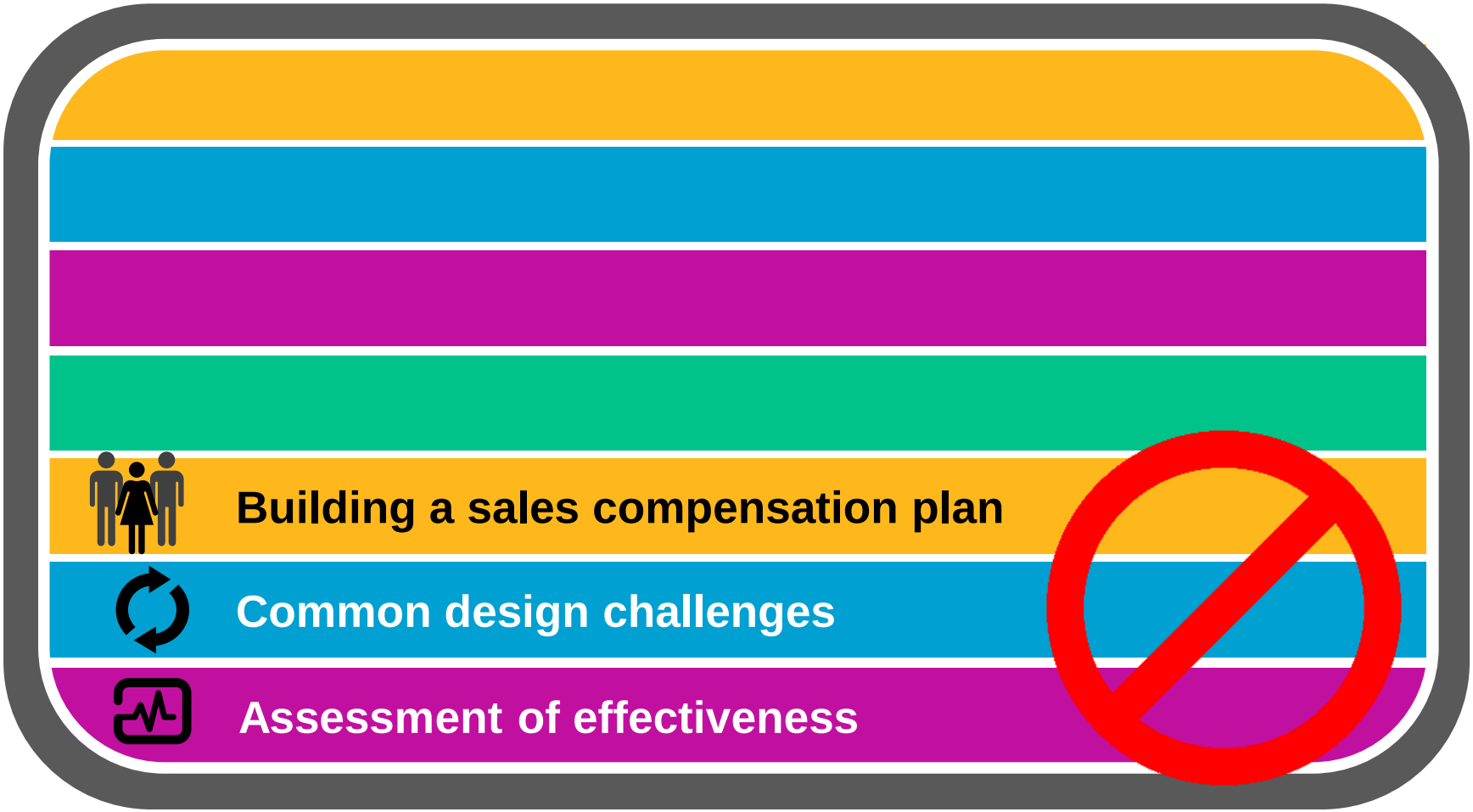
Sales compensation is just one tool in the arsenal

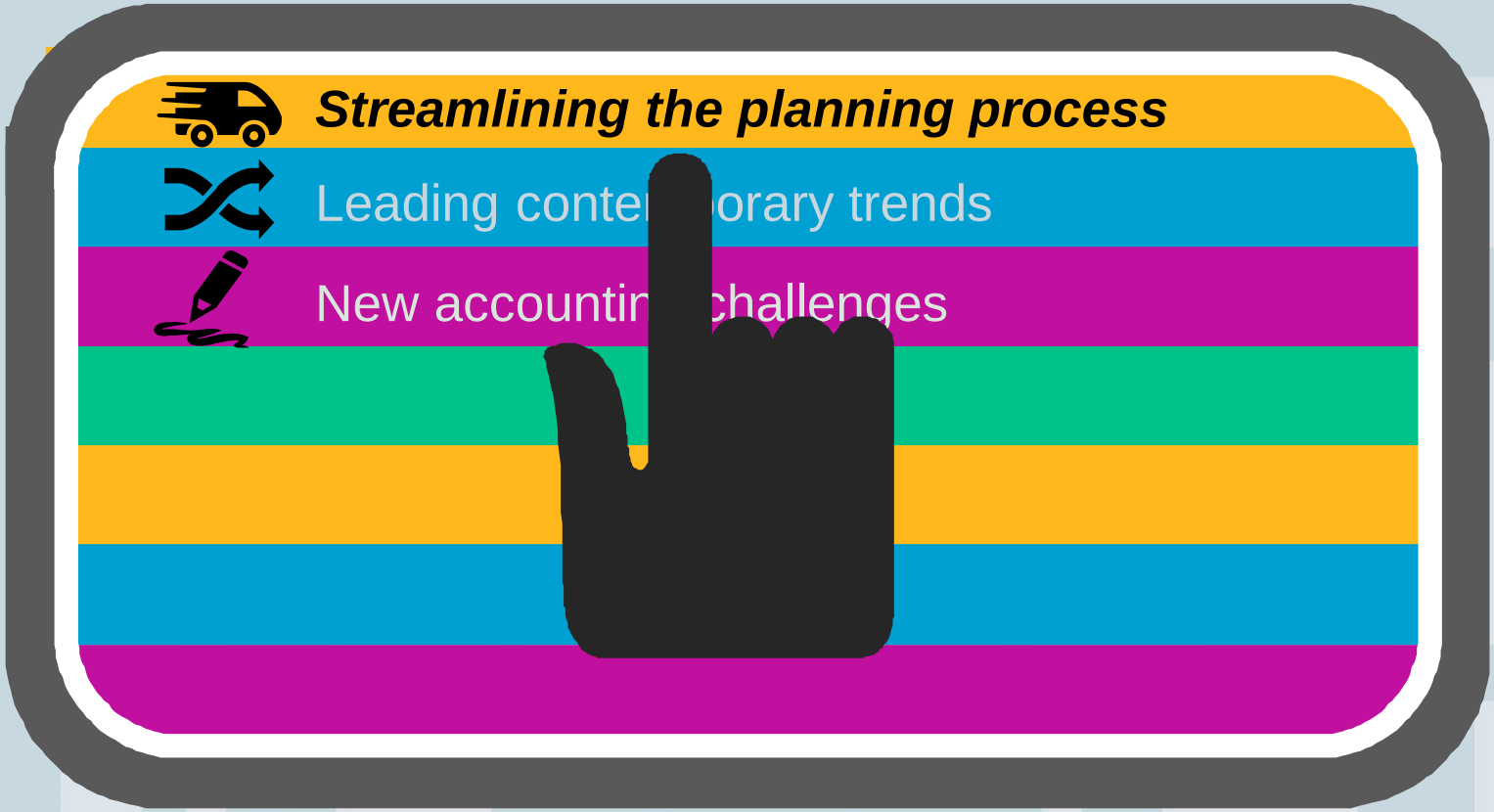
Today's agenda

Objective: to address contemporary issues that are creating challenges

- **Streamlining the planning process**
- **Leading contemporary trends**
- **New accounting challenges**

What today is not about





What's the challenge?

There's just too many people wanting to get involved

We can never get our plans out on time

Everyone has a different agenda of priorities

The plans are all messed up; there's too many changes and too many plans

We can't get everyone at the table together

Why do we start so late? There's not enough time

We blew the compensation budget

Key ingredients for success (and failure)

Leadership commitment and ownership

Top executives, not process owners

Multi-functional stakeholder participation

Operations, Sales, Marketing, HR, Finance, IT

Defined work plan, timeline, accountabilities

Proven process; rigorously iterative decisions for design elements

Field/local input and challenge teams

Listen to plan participants initially and before implementation

Define strategy, let tactics follow

Requirement specifications from strategy; tactics in the plan design

Active participation of your project team

Build buy-in and consensus; transfer tools, techniques and process

Well-planned and executed communication

Multiple media focused on first line supervisors as communicators

Leadership involvement is complex

What leaders should be involved?

PRIMARY	OTHERS
▪ Sales	▪ Marketing
▪ Sales Ops	▪ Manufacturing/R&D
▪ Finance	▪ CEO
▪ HR	▪ COO

What is their role?

- Steering committee: Direction/guidance
- Project team: Hands-on
- Challenge team: Review and react

What are their priorities?

- Sales: Top line
- HR: Pay levels, talent attraction/retention
- Finance: Costs, ROI
- Others: Working capital, utilization

How best to manage them?

- Identify *ALL* stakeholders
- Assign a role: Steering committee, project team, challenge team, ad-hoc updates/feedback

A common approach to the process

Phase 1: Assessment and Strategic Context	Phase 2: Detailed Design	Phase 3: Implementation
▪ Develop a fact-based case for change ▪ Identify strengths, weaknesses and opportunities for improvement	▪ Develop detailed plan designs ▪ Model the plans for fiscal impact ▪ Consider transition requirements	▪ Effective rollout of new incentive plans
A collection of inputs	Participative and interactive	Choreographed events with collateral material

Most organizations wait until late in the year to start – why?

Business strategy and job role definition are key drivers of sales incentive plans

Strategic Requirements

Strategy

- Corporate Objectives
- Channel and coverage model Sales and Service Strategy
- Compensation Strategy and Philosophy

Roles

- Account Responsibilities
- Product Responsibilities
- Sales and Service Process Responsibilities
- Rules of Engagement

Sales Compensation Philosophy

Job Value

Target Total Compensation

- Pay Philosophy
- External Practice
- Internal Equity

Salary / Incentive Mix

- Personal Influence
- Nature Of Sales and Service Process (Length, Complexity, etc.)

Incentive Delivery System

Measures and Weights

- Alignment
- Control
- Focus
- Feasibility

Plan Mechanics

- Bonus vs. Commission
- Thresholds
- Accelerators, Decelerators, Caps
- Linkages
- Measurement Period
- Payout Frequency
- Crediting Rules

Validate This

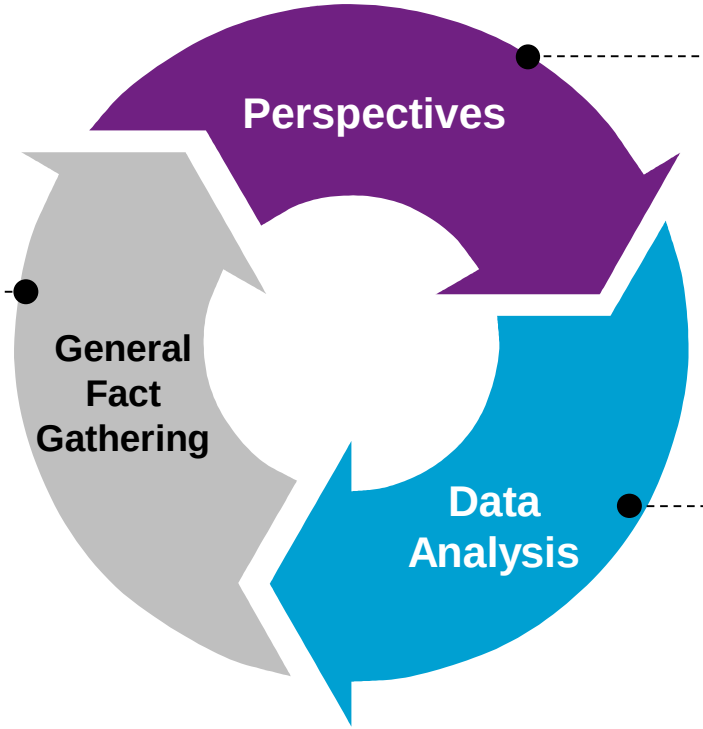
Review and Redesign This

Validate your business strategy and job

Phase 1 is a collection of data inputs

General Fact Gathering

- Organization charts
- Incentive plan documents
- Goal setting and goal management processes
- Crediting rules
- Administrative processes and systems capabilities and limitations

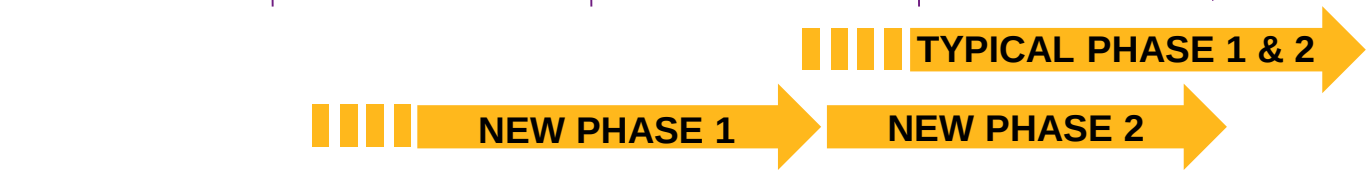


Interviews & Survey

- Executive Leadership and management
- Incumbents across roles in scope

Data Analysis

- Historical pay and performance data analysis
- Market benchmark data



This can be conducted much earlier than the typical project start

Mapping roles streamlines the design process

Transactional

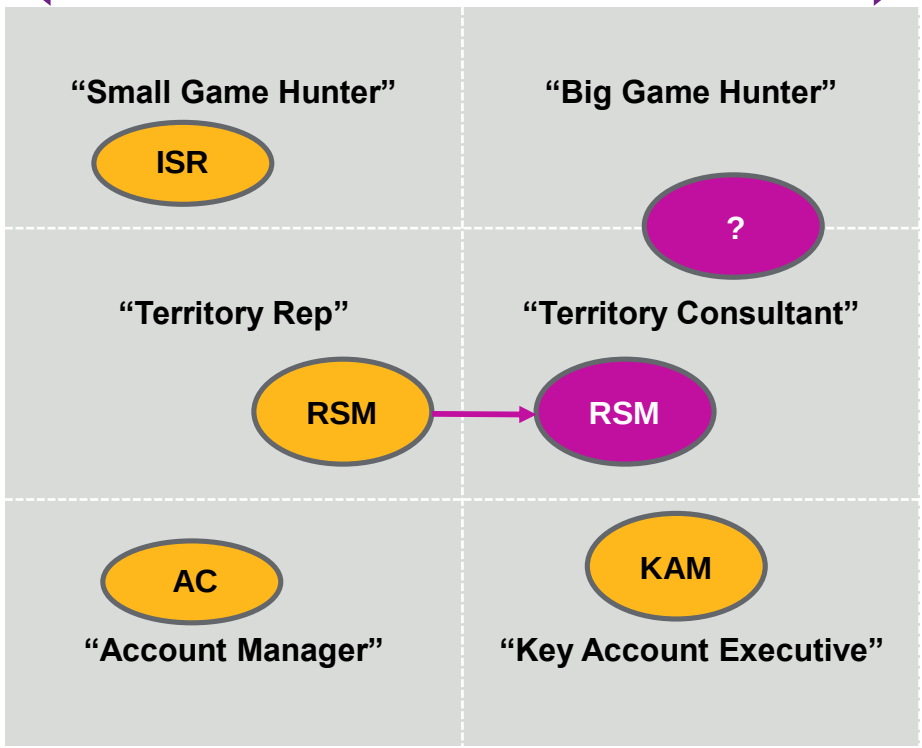
- Purchase decision is simple
- Sales cycle is short
- Price is key
- Focus on efficiency

Consultative

- Purchase decision is complex
- Sales cycle is long
- Value is key
- Focus on solution

How Customers Buy

How Sales People Sell



"New Business Acquisition"

- New business acquisition
- Cold calling or prospecting
- Little post-sale effort

"Territory Management"

- Grow territory revenue based on good relationships with customers/prospects
- Growth comes from building a reputation in the territory
- Some post-sale effort

"Account Management"

- Retain and grow accounts
- Identify and address customer needs
- Significant post-sale effort
- Penetrate customers with new services/products

Leading contemporary trends

Simplify

Diversify

Guide

Communicate

1: Simplify

"There is nothing wrong with having a single measure"

- **Wireless:** Activations
- **Insurance:** Premium
- **Payments:** Volume
- **Medical Device:** Sales
- **Technology:** Bookings

1: Simplify (Cont.)

"We have 4 payout curves for all our sellers around the world"

Performance	Payout Curve 1		Payout Curve 2		Payout Curve 3		Payout Curve 4	
	% Quota	% Payout	% Quota	% Payout	% Quota	% Payout	% Quota	% Payout
Threshold	85%	50%	75%	50%	50%	25%	0%	0%
Excellence	120%	200%	135%	200%	150%	200%	200%	200%

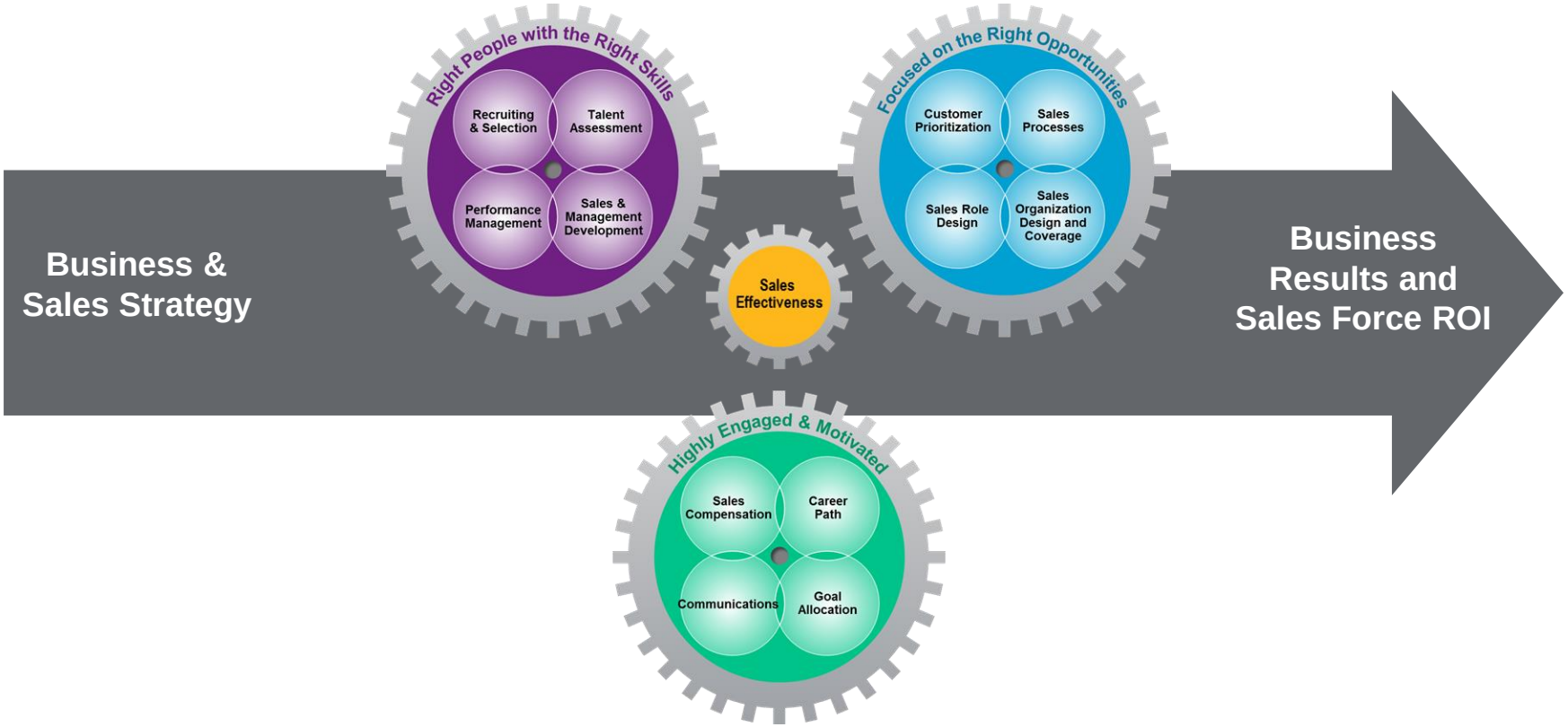
Situation

- Large global sales force selling in very different markets
- Sales incentive plan participants assigned a "payout curve" based on market characteristics (supported by historical data analysis)

2: Diversify

"Sales compensation is only one of the dials that can be tuned to drive sales effectiveness"

Willis Towers Watson's Model for Sales Effectiveness



Change Management | **Tools and Technology** | **Governance**

2: Diversify (Cont.)

"Managing sales people is easy; I've been doing it for years"

Darwinian Be[illegible]

- Sales emplo[illegible]es are money-[illegible]vated a[illegible] self-managing
- Strong prod[illegible]rs will thriv[illegible]d stay with[illegible] company
- Weak perfor[illegible]rs will [illegible] find a way to [illegible]prove or exit

Is this a smart strategy?

2: Diversify (Cont.)

"Pay is NOT a driver of sustainable engagement…which it what you need to earn the extra effort to get people to go above and beyond"

Rank	Attraction Drivers	Retention Drivers	Sustainable Engagement Drivers
1	Pay	Pay	Supervision
2	Job security	Opportunities to advance in my career	Clear Goals & Objectives
3	Organization's products or services	Trust/Confidence in senior leadership	Senior Leadership
4	Flexible work arrangements	Job security	Image & Integrity
5	Health care and wellness benefits	Ability to manage work-related stress	Performance Review

Source: WTW 2016 Global Workforce Study - North America/Sales Roles

2: Diversify (Cont.)

"Our sales managers are the critical lynchpin for sustainable engagement and talent management"

1. Goals and objective
2. Performance reviews
3. Stress, balance and workload
4. Recruiting and selection
5. Enablement
6. Supervision

Most organizations report that they have under-invested in this role but that they are turning much greater attention to it

3: Guide

"We want to balance consistency with flexibility"

Global Consistency

- Transparent
- Culturally neutral
- Facilitates mobility and communication

BUT …

- HQ-centric
- Not market responsive
- Some programs may be ineffective

"Find the balance"

Local Market Design

- Market responsive
- Aligned with local deployment
- Strong sense of ownership

BUT …

- Less transparent
- Communication and mobility challenges
- More labour intensive design/administration

Step 3: Guide (Cont.)

"We want to save ourselves from reinventing the wheel"

Low/No — **Level of Governance & Consistency of Plan Design** — **High**

Local Plans	Guidelines/ Principles only	Guidelines/ Principles with Governance	Incentive Framework	Global Plans
• No global governance • ***Plans are designed at the local level***	• Provide high-level guidelines/principles, grounded in best practice, to assist in the design of any sales incentive plan across the enterprise • Allows for potentially significant different local plan designs, but establishes some guidance for best principle design practices • ***"Voluntary" adherence to guidelines***	• Provide high-level but specific guidelines/principles to underpin the design of any sales incentive plan across the enterprise • Allows for potentially significant different local plan designs, but establishes some guidance for where things should and should not be different • ***Plans must be approved by a "central" governing body to ensure adherence to guideline***	• Fully detailed plan designs for 'generic' sales roles that can be applied globally • ***Provides actual plan designs to local countries, for them to install locally with some modification and adaptation, as required***	• ***Sales incentive plans are global with little/no local modification and adaptation (typically only to adhere with local regulations)***

4: Communicate in a world of information overload

I don't care/this isn't a priority

I don't understand

There are too many places to go

Only
1 out of 4
companies sustain gains over the long term.

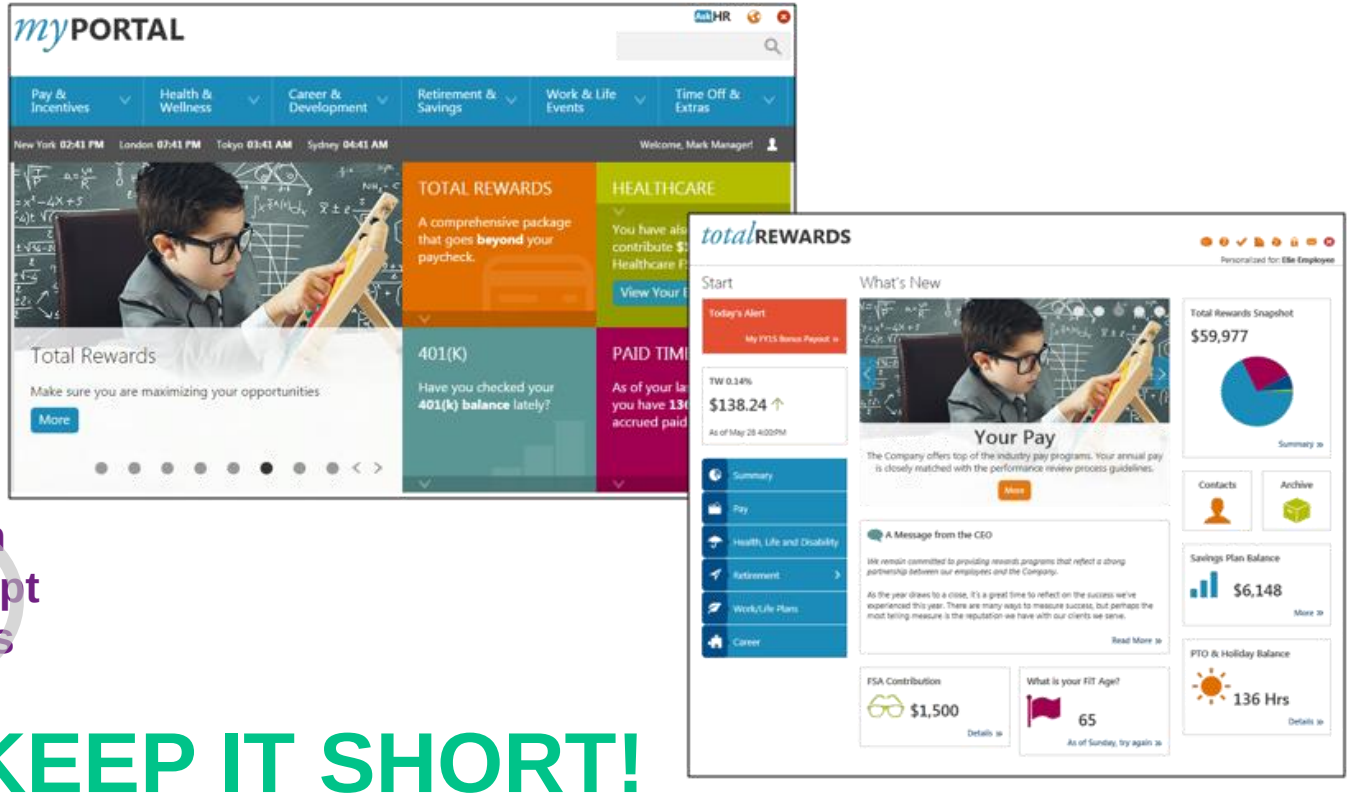
About half **(55%)** of change initiatives meet their initial objectives.

Because only
out of
frontline employees are in the know

Good communication is a critical element of incentive plan implementation … especially when the impact of the change is significant

4: Take a marketing approach

"Rewards communication doesn't have to be boring"



Text-heavy emails

Letters in non-descript envelopes

Printed Plan Guides

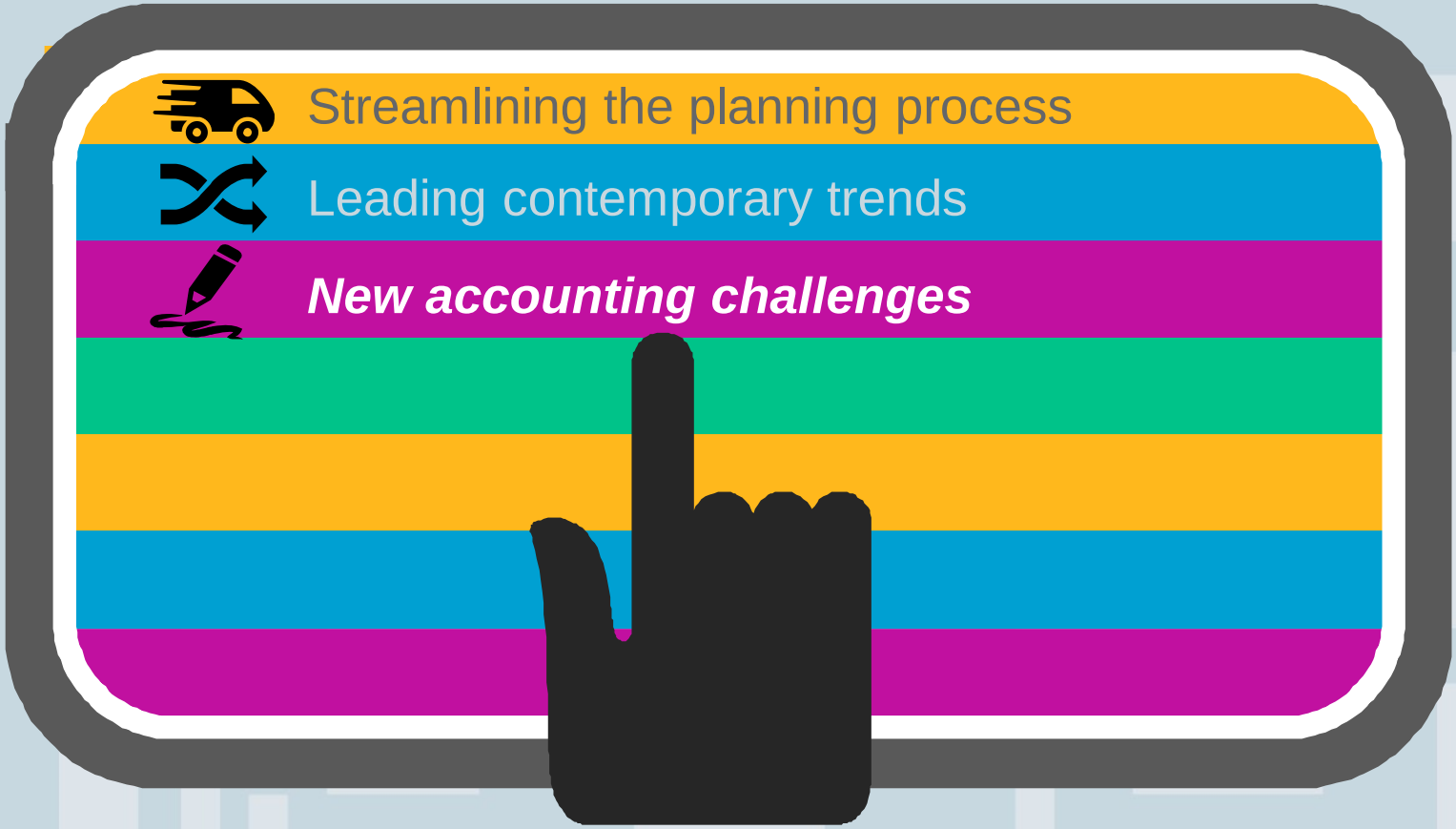
Long animated PPTs

KEEP IT SHORT!

Videos – less than 2 minutes

Examples and calculators

Emails – 200 words (or just pictures)



What are these?

Financial Accounting Standards Board

FASB

IASB

International Accounting Standards Board

Accounting Standards Codification

ASC 606

IFRS 15

International Financial Reporting Standards

"Revenue from Contracts with Customers"

This could potentially create upheaval in sales compensation design

So how does this affect sales compensation?

The W's	The Highlights
Why do this?	▪ Under GAAP, industries had their own rules-based standards ▪ Standardize the way revenue is recognized ▪ Make financial results more transparent and comparable

Who is impacted and **when**?	▪ Issued in 2014, effective for annual reporting periods after 12/15/15 for public and non-public entities, but deferred...
	▪ Now effective for annual reporting periods:
	  ▪ After 12/15/17 for some companies (public, certain NFP)
	  ▪ After 12/15/18 for others

What does it mean?	▪ Revenue is recognized when the goods/services are delivered ▪ Revenue and expenses must be allocated over time
So what?	▪ Complicates accounting – changes how revenue is calculated ▪ Impacts compensation plans based on revenue metrics ▪ Especially with recurring revenue or subscription business model

Not yet on the radar of most sales compensation teams

Understanding some common terms

Type	Meaning	Value
Bookings	A customer commitment to spend	Measures impact and growth of your sales from orders/contracts
Billings	Invoice sent to customer for payment	Request for payment but not aligned with RecRev unless product is already delivered
Recurring Revenue	Contract amortized into subscription revenue	Tracks your momentum as a subscription business
Recognized Revenue *	Revenue accrued for product/services delivered	Allows you to make accurate predictions regarding cash flow and manage financial health of your business
Deferred Revenue *	Revenue not yet earned for product/services still owed	Same as above but a liability
Cash Collections	Actual cash collected from customer	Knowing how much you can spend

** RecRev and DefRev are new accounting standards per FASB and IASB*

An illustration

Type	Jan	Feb	Mar	Apr	…	Jan
Booking	$36,000[1]					
Billings	$12,000					$12,000
MRR[2]	$1,000	$1,000	$1,000	$1,000		$1,000
RecRev	$1,000	$1,000	$1,000	$1,000		$1,000
DefRev	$11,000	$10,000	$9,000	$8,000		$10,000
Cash	$12,000[3]					$12,000[3]

1: Assume 3 year contract

2: MRR = Monthly Recurring Revenue

3: Assume 1 year pre-payment

Do not mistake cash collections with revenue; pre-payment is good, but revenue is not recognized until services are delivered; until then, the revenue is still a liability

Be aware of the "Rule of 78"

Year 1

Deal	Jan	Feb	Mar	…	Full Year
1	$10,000	$10,000	$10,000		$120,000
2		$10,000	$10,000		$110,000
3			$10,000		$100,000
12					$780,000

- Actual portfolio of deals is unlikely to be "smooth and consistent" like this but a portfolio of diverse contracts acquired at uneven intervals throughout the year
- **Sales can be measured 4 ways:**
  - **$4.32m of bookings (assume avg. 3 year term = TCV)**
  - **$1.44m of ARR (=ACV)**
  - **$120,000 of MRR**
  - **$780,000 of RecRev (same as in-year revenue or IYR)**

Year 2

Deal	Jan	Feb	Mar	…	Full Year
1	$10,000	$10,000	$10,000		$120,000
2		$10,000	$10,000		$110,000
3			$10,000		$100,000
12					$780,000

- Prior year sales will deliver year two revenue of $1.44m, assuming all retained
- Plus year two new RecRev of another $780,000
- **Total year two RecRev = $2.22m**

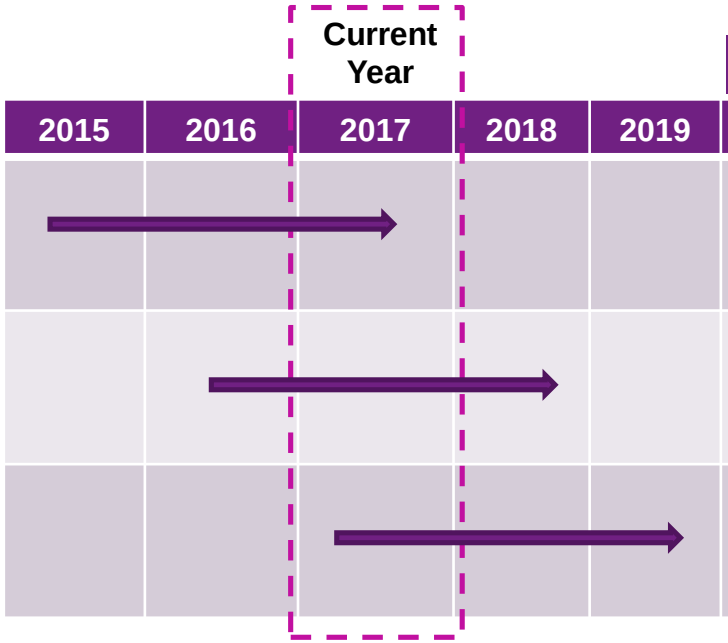
Year 3

Deal	Jan	Feb	Mar	…	Full Year
1	$10,000	$10,000	$10,000		$120,000
2		$10,000	$10,000		$110,000
3			$10,000		$100,000
12					$780,000

- Prior two years' sales will deliver year three revenue of $2.22m, assuming all retained
- Plus year three new RecRev of another $780,000
- **Total year three RecRev = $3.0m**

In a subscription model, selling $10,000/mth of new MRR = $780,000 of RecRev

Must the sales rep wait for RecRev?

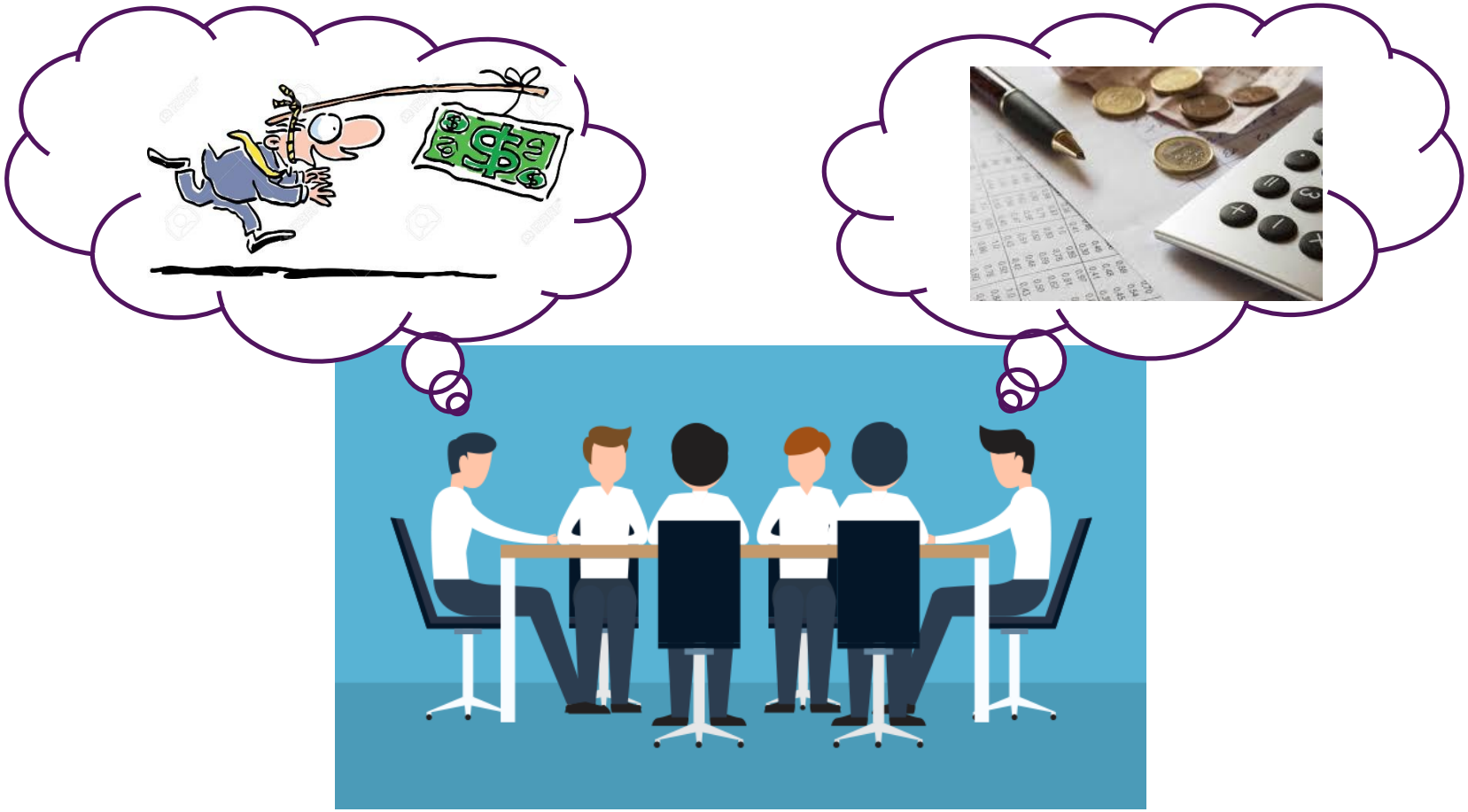


Basis for Sales Person Compensation	
Bookings	**RecRev**
Deals sold in 2015 generate commissions paid in 2015 but none in 2016 or 2017	**Commissions are paid in the year that revenue is recognized, regardless of when it was booked**
Deals sold in 2016 generate commissions paid in 2016, but none in 2017 or 2018	
Deals sold in 2017 generate commission paid in 2017, but none in 2018 or 2019	

Compensation Cost of Revenue	Disconnect	Aligned*
Reward the Compensable Event	Aligned*	Disconnect

** Depends on the desired responsibilities of the role (in terms of account acquisition / retention / renewal / growth)*

Accounting regulations apply to RecRev, NOT to how or when sales people get paid



The compensation team will need to balance potentially competing needs

Questions?