

Automating Commission Computation

Commission serves one purpose – motivating salespeople. But what should a commission plan motivate them to do?

That's easy. It should motivate them to reach or exceed the company's marketing objectives.

Simple commission plans, however, motivate them only to maximize volume. For example, if salespeople get a straight percentage of revenue, they'll do as well selling a low-margin product as a more profitable one.

Most companies have a more sophisticated marketing strategy than simply "sell as much as we can, of anything we can, to anyone who'll buy it," so they need a commission plan more sophisticated than "incent salespeople to sell as much as they can, of anything they can, to anyone who'll buy it."

For example, maybe you want to:

- Promote certain product lines, either because they're the most profitable lines or because you're trying to break into a new market.
- Authorize salespeople to give discounts, but make sure they don't give away the store
- Have salespeople spend their time prospecting for new customers, rather than just raking in easy commission on repeat orders
- Coordinate your selling efforts with seasonal promotions.
- Reward salespeople for their help collect overdue invoices, or penalize them if their customers don't pay on time.
- Encourage people to cooperate by splitting commissions fairly.
- Negotiate different deals with various independent reps, depending on each reps' needs and opportunities.

Every company is unique, so every company has its own marketing strategy. The list above is just a small sample of what well-designed commissions can accomplish.

However, it's one thing to design a good commission plan. It is something else altogether to implement it. Standard accounting systems simply cannot handle the unique variable inherent in a complex marketing strategy. The result? Probably that someone in your accounting department will spend hours, days, or weeks every month computing, checking, and adjusting commissions.

However, when the calculation time exceeds about one day per month, this method breaks down because:

- Human beings cannot spend hours on manual calculations and retain accuracy. Industry sources say that, typically, manual computation results in 2-5% errors. This results in substantial overpayments, since salespeople are generally better at finding underpayments than overpayments. At the same time, errors make salespeople lose confidence in the integrity of the plan – they wonder what they’re missing – and to waste time they should be selling on “shadow accounting”.
- Commission recipients don’t fully understand how their commission was computed, because the plan is so complex. This reduces both your salespeople’s moral and the plan’s effectiveness.
- The accounting department spends time trying to compute the plan, and then more time checking and correcting the first set of computations. In some cases, this actually results in an increase in manpower. More often, at small and mid-sized companies, it’s done by existing staff, but wastes time that could be put to more profitable uses.
- Sometimes computation becomes so complex that the marketing department cannot add refinements to motivate salespeople even better. Accounting just couldn’t keep up with the improvements.

What’s the solution? Again the answer is easy. Automate the computations. Good commission software will eliminate errors, produce clear commission reports, cut the computation time by 90%, and handle almost unlimited complexity.

Or maybe the answer isn’t so easy. At one time automating complex plans was an option only for large companies, mainly because only they could justify the cost but also because the software was complicated to use. Typically, the software started at \$100,000. We know of one large drug company that spent more maintaining their commission software than they paid out in commission!

Fortunately, that time has passed. Now *rule driven* commission software – the sort that large companies have always used because of its flexibility – is practical for small and mid-sized companies. That means, of course, that the price has dropped dramatically. Typically automation, including implementation, now costs \$3,000-\$10,000, depending on the specifics of your plan. Equally important, the software is easy to understand and use, and it’s very reliable.

Now it’s practical for small and mid-sized companies to automate even “impossible” commission plans, and typically to earn back their investment in the first six months – and then earn it back again every six months thereafter.