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3 Keys to Changing Sales Compensation Plans During Coronavirus Disruption and Economic Uncertainty

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Initiatives:Sales Strategy and Operations **and 1 more**

Sales compensation plans break down quickly under extreme disruption such as the coronavirus pandemic. Sales operations leaders must refresh their guiding principles, plan distinct phases for short- and long-term incentive plan change, and consider quota relief and other options to contain risk.

Overview

Impacts

- Sales operations leaders will face difficult trade-offs between protecting sellers' incentives earnings and meeting company cash-flow needs.
- Promptly updating an incentive plan improves seller morale, but moving too quickly in changing conditions may necessitate more changes later on.
- After the most acute phase of selling disruption ends, available revenue forecasts will still be highly uncertain.

Recommendations

To balance their sales compensation plans' motivational impact, stability and fiscal responsibility during times of disruption and uncertainty, sales operations leaders should:

- Reaffirm the core principles that govern compensation plan design by convening the company's executive leadership to update sales compensation guidelines in response to current challenges.
- Change incentive plans in two phases by separating options with immediate impact and feasibility from those that require a wait-and-see approach before finalizing.
- Identify the most effective short- and long-term incentive plan adjustments by thoroughly considering both familiar and less conventional redesign options.

Analysis

One of the most pressing — and vexing — challenges that sales operations leaders face during times of severe sales disruption and extended global economic downturn is determining what changes, if any, they should make to sales compensation plans.

Even seasoned sales operations leaders may find that little in their professional experience prepares them adequately for a global pandemic. Leaders serving in senior sales roles today have never had to design sales incentives in conditions like today's complete selling disruption and long-term economic uncertainty.

Compensation design challenges caused by extreme uncertainty are compounded by the difficult trade-offs sales operations leaders face. Some of these trade-offs are amplified versions of the tensions inherent in any sales compensation design process, but others confront sales operations leaders with unfamiliar, emotionally complex decisions such as:

- How to balance the desire to "keep sellers whole" (i.e., pay the average seller at target regardless of company performance) with the responsibility to optimize company cash flow
- How to provide sellers with dependable information about their incentives when predictions about customer access and demand are unstable
- How to preserve selling capacity to respond quickly to economic upturn just as customer order delays and cancellations are putting short-term pressures on company cash flow

In this note, we provide three recommendations to help sales operations leaders navigate disruption and uncertainty in their sales compensation plans (see Figure 1). Most sales operations leaders should begin with the first two recommendations to realize a more effective decision-making process and improved seller morale. Sales operations leaders who are ready to begin implementing changes now can begin with the third recommendation, which includes a comprehensive list of incentive plan elements to consider adjusting, along with corresponding decision-making guidance.

Figure 1. Impacts and Top Recommendations for Sales Operations Leaders

Impact Appraisal for Sales Operations Leaders

Impacts	Top Recommendations
Sales operations leaders will face difficult trade-offs between protecting sellers' incentives earnings and meeting company cash-flow needs.	• Include the right stakeholders in decision making. • Reach agreement among key stakeholders on the company's guiding philosophical principles before making design decisions. • Explain to sellers how the guiding principles shaped compensation decisions.
Promptly updating an incentive plan improves seller morale, but moving too quickly under changing conditions may necessitate more changes later on.	• Decide which elements of sales compensation can be changed and communicated immediately and which require a wait-and-see approach before finalizing.
After the most acute phase of selling disruption ends, available revenue forecasts will still be highly uncertain.	• Identify the most effective incentive plan adjustments by thoroughly considering both familiar and less conventional redesign options.

Source: Gartner

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Impacts and Recommendations

Leaders Will Face Trade-Offs Between Sellers' Earnings and Company Cash Flow

Because commercial leaders are generally optimistic about revenue and protective of sellers' earnings, they may not be adequately prepared to make difficult trade-off decisions under time pressure. Sales operations leaders, therefore, should prepare company leaders to take informed, decisive action by initiating a review (or creation) of the core guiding principles for sales compensation design.

Because these guiding principles reflect broad company values, the head of sales operations should convene the right set of senior, cross-functional company leaders long before difficult decisions are needed. Aside from sales, this process typically includes finance, HR, legal and compliance, and IT. The head of sales operations may include other functional leaders as appropriate for company culture but should bear in mind the need to reach consensus quickly.

A list of discussion questions, customized to company circumstances, can facilitate this leadership meeting (see Table 1). The meeting output — a statement of the executive leadership's compensation design principles updated for current challenges — will serve as a reference point for all subsequent decisions about compensation plan changes.

Table 1: Discussion Questions for Developing and UpdatingSales CompensationGuiding Principles

Category	Questions
Prioritizing Values	▪ What core values and cultural traditions already in place must we consider when making sales compensation decisions? ▪ How important is the continuity and stability of sellers' incentive plans compared to agility in sales compensation and responsiveness to changing market conditions? ▪ What steps must we take to avoid unintentionally incentivizing sellers to risk their own health or the community's well-being?
Spreading the Impact	▪ Do we prefer to spread the impact of disruption and reduced demand equally among all sellers or allocate it unevenly based on other criteria (e.g., a role's ability to generate short-term cash, a role's long-term strategic importance, a seller's actual performance relative to peers) ▪ Do we want sales compensation changes to favor higher-performing sellers over others? ▪ Should our approach to changing seller incentive compensation be consistent with our approach to nonsales positions in the company? ▪ Should high-risk/high-reward roles bear more of the impact from coronavirus disruption?
Defining Decision Thresholds or Trigger Points	▪ Is there a point at which we prefer to reduce sales force size rather than change sales compensation plans? If so, how should we define that point? ▪ How much margin reduction or pressure on cash flow can we tolerate before we must directly reduce spending on variable sales incentives?

Source: Gartner

Recommendations:

- Identify nonsales leaders whose input sales operations leaders need to update guiding principles, such as finance, HR, legal and compliance, and IT.
- Reach consensus among top sales and nonsales leaders on the guiding principles that will shape sales compensation changes.
- Include a summary of the relevant guiding principles when communicating changes to sellers.

Prompt Incentive Plan Updates Improve Morale, But Moving Too Quickly May Necessitate More Changes Later

Sales operations leaders must balance the boost seller morale receives from quick decisions about incentive plans with the risk of launching changes so soon that they won't stand the test of time. The sooner sellers get details about plan changes, the faster they can adjust their activities to maximize their earnings. But if companies rush compensation plan changes into production, they are more likely to need additional adjustments as the selling outlook comes into sharper focus. Multiple rounds of compensation plan adjustments create legal, technological and operational risk. Even worse, they may cause changes intended to increase transparency and reduce seller distraction to ultimately undermine morale and sellers' trust in leadership.

Sales operations leaders should manage this inherent tension between decision-making speed and plan stability by dividing compensation action plan changes into two phases:

- Phase 1 — Short-term sales compensation adjustments based on what little is known now (if anything)
- Phase 2 — Long-term adjustments that will be developed only when enough information is available to create reasonably stable plans

Communication about short-term compensation plan changes (Phase 1) should emphasize the company's commitment to helping sellers stay financially solvent during the initial, highly uncertain disruption. When communicating short-term changes, sales operations leaders should explain the risks of committing to a permanent change when market uncertainty remains high. At the time short-term plans are announced, sales operations leaders should also announce the expected timing for rolling out long-term compensation plan changes.

Recommendations:

- Assess short- and long-term outlooks separately. Distinguish between the immediate disruption to selling due to travel and meeting restrictions and the adjustments needed in response to reduced demand over a longer time horizon.
- As soon as possible, communicate to sellers that short- and long-term changes to sales compensation plans will be based on organizational values, guiding design principles and market conditions.
- Communicate the dates when short-term changes will be announced and long-term changes are expected.

After the Most Acute Phase of Selling Disruption Ends, Available Revenue Forecasts Will Remain Highly Uncertain

Once local limitations on selling activities are lifted and market outlooks come into better focus, revenue projections' accuracy will begin to improve. However, these forecasts will still be far less reliable than the projections normally used in sales compensation planning. Instead of incorporating the less reliable projections directly into sales incentive adjustments, sales operations leaders should understand and account for elevated uncertainty in redesigning compensation plans.

Some sales stakeholders may not appreciate the risks of taking new forecasts at face value and using them for compensation plan redesign, and they may therefore favor quota adjustments linked to new projections. However, while quota relief or restatements may be appropriate (especially with mechanisms added to contain uncertainty), companies may achieve the desired results more effectively and with less risk by changing other plan elements besides quotas themselves.

Guided by their reconfirmed compensation design principles, sales operations leaders should understand and consider the full range of options at their disposal (see Table 2). Note that quota adjustments come in different variations, each with pros and cons depending on circumstances. Equally important is to consider adjustments to plan elements besides quotas — either as stand-alone changes or in combination with other adjustments.

Table 2: Options and Decision Guidance for Adjusting Sales Compensation Plan

Options for Adjusting Sales Compensation	Comments and Considerations
Quota adjustments ▪ Reduce quotas for affected territories only during disruption. ▪ Proactively reduce quotas for all sellers based on updated revenue forecasts. ▪ Announce a retroactive quota reduction, the size of which will be determined after the full impact of disruption is known. ▪ Index quotas (i.e., "grade on a curve") so the average seller earns 100% (or a lesser amount).	▪ Even when conducted with high analytical rigor, retroactive quota changes can seem unfair to sellers. ▪ Proactive quota changes do not bring the stability that sales operations leaders desire because updated forecasts are likely to be inaccurate. Additional rounds of quota relief may be required. ▪ Quota indexing has the advantage of fiscal certainty for both company and seller because, by definition, team performance will center around 100% attainment. However, this can create significant pressure on margins (and cash flow) when revenue comes in far lower than what is justifiable. If every 55% attainer is paid at 100% of their target because that's the team average, the cost structure of the plan will break.

Draws, guarantees and other adjustments to target pay ■ Pay all sellers "at target" (or a fixed percentage of target) during disruption. ■ Pay sellers at target during disruption and true up payouts after the crisis has passed. ■ Pay sellers at target during disruption, but do not true up payouts after the crisis has passed. ■ Reduce target pay by a fixed percentage for all roles as a cost-cutting measure.	■ The decision of whether to true up sellers' payouts when they were paid at target depends on what leaders believe about the company's recovery. ■ Truing up and recovering overpayments is appropriate if leaders see disruption as a pause in selling activities that will be corrected after selling resumes. ■ An alternative to an announced true up is for sales leaders to communicate that if lost revenue is not made up, some overpayments may be forgiven. ■ Reducing targets by a fixed percentage can be combined with quota attainment indexing to control the distribution of rewards and the overall spending risk.
Activities ■ Pay sellers based on activities or MBOs during disruption.	■ Under normal circumstances, companies often avoid using activity metrics for compensation plans because activity plans are perceived as inconsistent with a pay for performance sales culture. ■ Compensation plans with activity metrics do not differentiate volume from quality. ■ However, during periods when selling activities are not possible, paying sellers temporarily on activities that are known to drive commercial outcomes is considered an effective option.

Payout curve changes ■ Eliminate or lower thresholds. ■ Reduce the slope of payouts to dampen the effect of uncertainty. ■ Implement ranking plans.	■ Adjusting the design of payout curves is a powerful technique for offsetting the impact of forecast volatility or uncertainty. ■ Removing payout thresholds can increase seller motivation by rewarding successes even when the original sales forecast used to create quotas is miscalibrated for current demand. ■ Decreasing the slope of payout curves also dampens the effect of unachievable sales forecasts because lower attainments correspond to higher payouts than they would receive without the decrease. Conversely, higher attainments earn lower payouts, which can be demotivating for sellers who deliver exceptional outcomes despite reduced opportunity. ■ Ranking plans have the advantage of fixed, predetermined payout totals. However, many sales leaders avoid them because they pit sellers against one another as they compete for higher positions on the leaderboard.
Contests and spiffs ■ Pay a kicker or bonus for identified activities that position the sales force for increased competitiveness when the crisis passes.	■ Contests are unpopular among many sales operations leaders because they can be difficult to govern and to coordinate with sellers' main compensation plans. ■ However, the nature of downturns and selling disruptions can increase contests' impact as a motivator for sellers. As long as parts of the selling landscape remain disrupted, companies may ask sellers to achieve nonstandard objectives. ■ For example, renegotiating a customer contract to drive a deeper and longer-term customer commitment is difficult to predict but generates measurable value. A contest that pays a one-off bonus for achieving this objective can motivate sellers toward these outcomes.

Source: Gartner

Recommendations:

- Determine which elements of the sales compensation plans can change now and which require a wait-and-see approach before finalizing.
- Use established guiding principles to shape the details of all changes.
- Consider all elements of the compensation plans before finalizing a decision.
- Emphasize continuity and stability for sellers by limiting changes to only what is necessary to address disruption.

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Controlling Sales Compensation Spending Risk Without Demotivating Sellers

Leading Sales Operations Through the Coronavirus Pandemic

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