Principles of a Successful Compensation Plan

by Daniel O. Jensen

Introduction

A compensation plan that fails to motivate distributors can stagnate a company as fast as any other factor. While there are many factors which contribute to the success or failure of direct selling companies, the compensation plan is one of the biggest. There are many who ask us *what's the best compensation plan out there?* Unfortunately, there is no answer to this question, but there are proven principles of success common to virtually all successful plans. What makes a compensation plan great? This article may help to identify the real success factors of a compensation plan.

These Golden Rules should *always* be followed:

- Always provide incentive dollars for an expected behavior. Don't waste incentive dollars on behavior which provides little value to you or the distributor. Question each *type* of compensation and verify that it will provide the expected return on investment.
- Leverage the principle of *relationships.* Most people recruit others they already know. They want to work *with* them. Be sure your plan builds on these relationships. A plan where a new recruit is trained or mentored by a person other than the sponsor usually results in poor recruitment and weak relationships.
- Recognition is as important as compensation.
- "Distributors will work for money but they'll kill for a cause." - *Jim Adams*

The five objectives of a successful compensation plan

1. Sell Product to end consumers

- Retailing products to end consumers is key to moving products from garages to customers. Corporate failure is inevitable as people stop buying product which they do not (or cannot) sell.
- Have a motivating retail/wholesale profit – a minimum of 25% discount from retail or 33% markup over wholesale. This retail profit is the basis on which people are motivated to retail products. Other motivations are usually artificial and will not withstand the test of time.
- Have a realistic retail price otherwise people won't be able to sell it to end consumers. Don't sell products whose wholesale price is *really* the market retail value and then add an artificial retail price even higher.
- Requires heavy emphasis on retailing from field leaders, training and marketing materials.
- Retailing products based on the hope of future rewards will never result in movement of product to retail consumers. If distributors are selling product promoting the dream that the buyer will earn future commissions when they, in turn, sell the product to others, you'll eventually be sitting on a "time bomb" of unhappy distributors with lots of inventory to sell in their garage. Companies that do this always fail. Proper retailing moves the product from distributor to end user in volumes justified by natural consumption.

2. Build organizations (recruit)

- Done by placing incentives on group volume building. Recruits must easily see that it is easier to have others do the selling to build their business *in addition* to their own selling.
- Recognition and reward should be built into the plan especially for the new recruit. Most recruits are lost in the first 60 days because they lose confidence that they will succeed in the long term. Rewarding them early on keeps their interest and excitement.
- Lack of rewards for new recruits results in sales leaders promoting 'buy in' organization building. They pitch people that a 'buy in' is an investment in their future. The new recruit has greater 'equity' (inventory) to keep them in longer but quickly become disillusioned. They are quick to complain to regulatory officers that 'they were taken'. Regulators are always on the watch for 'investment schemes' of this nature.
- Rewarding people early is done by building a series of goals and rewards. As they reach each goal, they are recognized and compensated. It builds their confidence that they can achieve their future dreams.
- This process builds the initial skills required to eventually become managers. Lack of early incentives builds ineffective field managers who do not have the skill to sell and recruit based on product viability.

3. Build Managers (people who train others to sell and recruit)

- Must follow 'Build Organization' step otherwise the field force will have many ineffective managers who do little to earn their compensation.
- Managers are built by learning the basic skills of success for distributors: product retailing and recruiting. Once they learn these skills, they become managers as they teach others (those they recruit) to do the same. Successful managers learn the power of *duplication.*
- Incentives are placed on group activities: Group Volume and Recruiting. Group Volume incentives usually rewards both selling and recruiting.

4. Build Sales Leaders (people who train others to manage)

- Incentives must exist to motivate and reward managers who build other managers. Avoid disincentives which penalize a manager when a new manager is created otherwise managers will work hard to suppress their own star performers from reaching their full potential for fear of losing significant compensation in the future.
- Provide incentives which reward managers for several 'generations' of other downline managers so they will want to train their managers to build other managers as well.
- Avoid making it too easy to become a sales leader. Distributors who don't know how to build other managers or train other managers to succeed should not be entitled to become sales leaders. If they do, the field organization will be superficial and weak.
- Remember that building strong sales leaders takes time, money, and effort. Invest in training them to become effective sales leaders, to build effective managers, and to recruit product retailers and recruiters.
- Provide incentives for your top performing sales leaders. Avoid having the plan quickly 'max out' otherwise the top performers will wonder "what's next" and you won't have an answer.

5. Retention

- Retain people by helping them receive significant reward for their time. You compete for their time and attention with many other opportunities and distractions. Make it worth their while early on.
- As a distributor works the business, they build an ‘equity investment’ in their downline organization. They will continue to work the business if their downline continues to work the business. This is why a balanced emphasis on product retailing and recruiting is so important.
- Distributors who build a downline are far more likely to continue to be active than those who do not.
- If your product is consumable, use an “Auto Ship” program to build repeat business, both retail or preferred customer, and wholesale (to distributors).
- Promote contests and competitions which can be won by everyone. Avoid ‘top ten’ contests where everybody loses except the top 10 performers.

Other principles of a successful compensation plan

- **Reasonable compensation percentages:** Most compensation plans of today pay between 30% to 50% to field distributors. If a company promotes a plan paying only 25% or so, they will have a hard time recruiting and keeping distributors unless other factors offset this competitive weakness. These factors might include how well the public accepts the product (telephone service or other common consumables) or intangible incentives which motivate distributors. Real percentage pay out should fall between 35% and 42%, in my opinion. Higher percentages are possible with high product margins. Theoretical pay out (the percentage the plan would pay if all commissions were paid out in every case) should not be more than 8% above actual to avoid disappointing distributors expecting more.
- **Keep it simple:** Unfortunately, many plans are designed by MLM professionals for MLM professionals. These plans often assume most people already understand terms and principles of MLM or can at least learn them quickly. This is most definitely not the case. While experience is essential when designing compensation plans, one must never forget that *ordinary people are the ones who must be motivated by it.* If new recruits aren’t motivated early, they quickly fall away. The more complex a plan becomes, the fewer people it will motivate. The plan needs to affect the heart of a distributor first, *before* it can affect his pocketbook.
- **Avoid novelty or "fad" plans:** Changing a compensation plan is costly in terms of lost momentum and distributor commitment. When a distributor recruits another person, the compensation plan is often a significant part of the selling process. To change it later is, in essence, admitting that the original plan was not very good after all. Some people may perceive the change as a "bait and switch" tactic. By staying within more traditional plans, plans that have proven themselves over the years, a new MLM company can still be innovative but know that the plan has staying power. It's often joked that compensation plans are like men's ties; when one plan goes out of fashion, you can count on it coming back a few years later. Stick to more traditional plans that won't need to be changed as new fads come and go.
- **Don't put too much credence in the impact of your compensation plan:** Many entrepreneurs come to Jenkon convinced that they have the best possible compensation plan imaginable. When asked what product or service they will sell, they sometimes respond, *we're still looking for the right product.* Obviously, these well intentioned people have focused on only one issue of starting

their business thinking that the compensation plan is the key to their future success. The facts, however, are different. Many companies have gained great success despite poorly designed compensation plans. Put simply, the plan is only one part of the puzzle; it isn't the *only* part.

- **Don't change it often:** Those that experiment with the compensation plan are asking for frustrated distributors to join other more stable opportunities. Even good change can be traumatic. Be very reluctant to change the plan.
- **Avoid recruiting "heavy hitters":** These very successful MLM professionals can bring tremendous short term success but can also be a major cause for failure when they grow bored with your company and join another, often taking thousands of their downline with them. Wise companies always build slowly for the first few years until they have the critical mass to handle changes in business volumes. Don't design your compensation plan to focus on attracting these heavy hitters.

Five Objectives of a Successful Compensation Plan