



# Profit Matters

## Lesson 3 – Sales Compensation Models and their Impact on Gross Margin

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## Key Considerations

- Recruitment and retention is becoming increasingly important
- Compensation model drives behavior
- Your sales compensation model impacts GROSS MARGIN **only** if you allow your sales staff to negotiate prices on products and services
- Our analysis today will assume that sales staff **CAN** negotiate prices
- Do you want to allow sales staff to see product and services cost?



# Sales Compensation Models

- Salary only
- Salary plus discretionary bonus
- Straight commission on sales
- Base salary plus commission on sales
- Base salary plus commission on profits
- Sliding scale commission on price point



# Salary Only

## When to use it:

- This structure is ideal for companies where sales rep retention is critical to the success of the sales organization. The company is actively investing in the success of a given rep while presenting a no pressure shopping experience to their customer.
- Should incorporate price negotiation limits

## Pros

- Better employee retention
- Fixed sales labor cost in \$ terms

## Negatives:

- No incentive to achieve higher sales growth or profits
- Creates widely variable selling cost as % of sales \$

## Impact to Gross Margin

- Can be significant if pricing constraints aren't defined



# Salary Plus Discretionary Bonus

## When to use it:

- This structure is ideal for companies where sales rep retention is critical to the success of the sales organization. The company is actively investing in the success of a given rep while presenting a no pressure shopping experience to their customer.
- Should incorporate price negotiation limits

## Pros

- Better employee retention
- Flexible bonus criteria (individual or company sales goals or profit)
- Bonus offers **some** incentive to achieve higher performance

## Negatives:

- Minimal incentive to achieve higher sales growth
- Bonus is often vague and hard to gauge until year-end

## Impact to Gross Margin

- Can be significant if pricing constraints aren't defined



# Straight Commission on Sales (with or without draw)

## When to use it:

- This structure is usually leveraged by startups or other businesses that might lack reliable access to capital. In a lot of ways, it amounts to a pay-as-you-go plan — that often suits businesses that don't have the resources to provide competitive base salaries.
- Can be executed as a DRAW on earned commissions
- Should incorporate price negotiation limits

## Pros

- Great for high-performing sales staff
- Fixes labor cost in % of sales \$ terms
- Highest incentive to achieve higher top-line sales revenue
- Easily trackable by staff
- Pay-as-you-go plan (no sales no cost)

## Negatives:

- Recruitment and retention can be a challenge
- Gross margin can be sacrificed for higher commission \$

## Impact to Gross Margin

- Can greatly impact or even destroy gross margins



# Base Salary plus Commission on Sales

## When to use it:

- This structure is ideal for companies where sales rep retention is critical to the success of the sales organization. The company is actively investing in the success of a given rep while incentivizing their performance.
- Standard salary to commission ratio is 60:40
- Should incorporate price negotiation limits

## Pros

- Most conventional and popular model for sales compensation
- Employee recruitment and retention is good
- Provides good incentive to achieve higher top-line sales revenue
- Easily trackable by staff

## Negatives:

- Gross margin can be sacrificed for higher commission \$
- Somewhat variable sales cost as a % of sales \$

## Impact to Gross Margin

- Can significantly impact gross margins if pricing constraints aren't defined



# Base Salary plus Commission on Profits

## When to use it:

- This structure is ideal for companies where sales rep retention is critical to the success of the sales organization. The company is actively investing in the success of a given rep while optimizing gross margin on sales
- Standard salary to commission ratio is 60:40
- Must allow sales staff to see cost

## Pros

- Hybrid of the conventional and popular Base + Commission model
- Employee recruitment and retention is good
- Provides good incentive to achieve higher gross margins

## Negatives:

- Some sales loss if pricing becomes a customer sticking point
- Somewhat variable sales cost as a % of sales \$
- More complicated to understand, calculate, and track

## Impact to Gross Margin

- Can significantly improve gross margins and profitability





# Base Salary + Sliding Scale Commission on Price Point

## When to use it:

- This structure is ideal for companies where sales rep retention is critical to the success of the sales organization. The company is actively investing in the success of a given rep while optimizing gross margin on sales
- Standard salary to commission ratio is 60:40

## Pros

- Hybrid of the conventional and popular Base + Commission model
- Employee recruitment and retention is good
- Provides good incentive to achieve higher gross margins
- Does not require exposing cost to sales staff

## Negatives:

- Some sales loss if pricing becomes a customer sticking point
- Somewhat variable sales cost as a % of sales \$
- More complicated to understand, calculate, and track

## Impact to Gross Margin

- Can significantly improve gross margins and profitability

Industry Sales / Salesperson Averages

= 10/01/2019   = 09/30/2021   = Year Over Year   = Delivered Sales

Search

Data Updated Through:   Data Sample Size:

12/20/2021   High

Delivered Sales

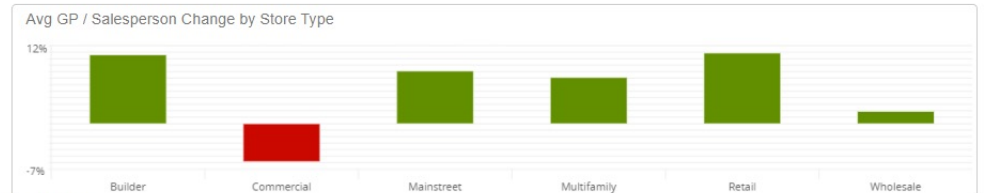
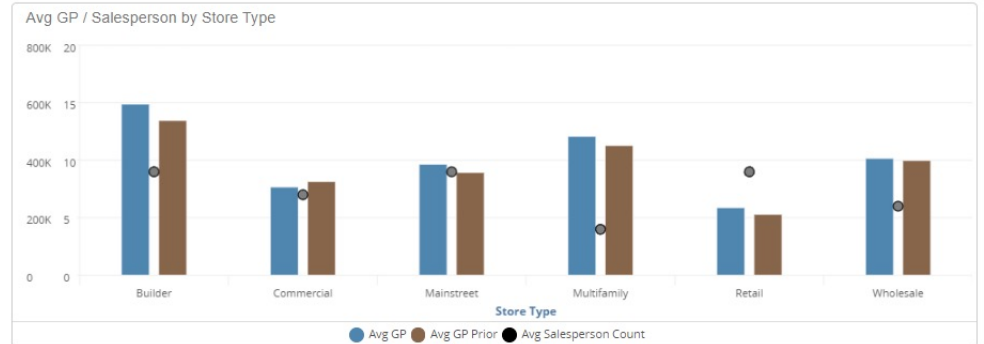
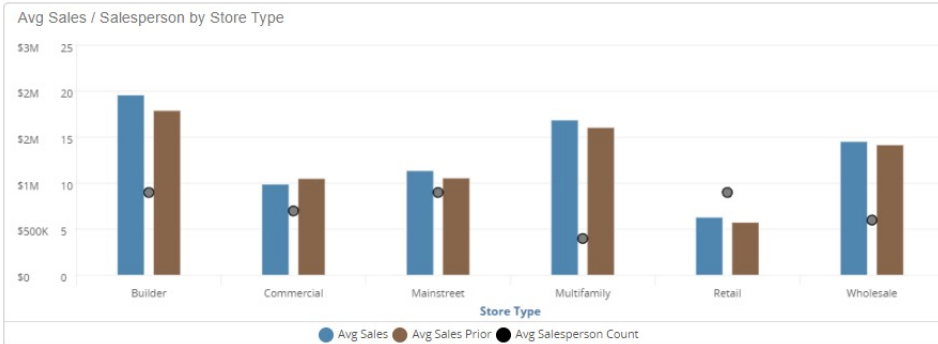
Avg Sales by Store  
**\$8,169,920**

Avg Salesperson Count by Store  
**8**

Avg Total GP by Store  
**\$2,735,847**

Avg Sales / Salesperson   Avg Sales / Salesperson Prior   Change  
**\$1,021,240**   **\$946,877**   **↑ 7.85%**

Avg GP / Salesperson   Avg GP / Salesperson Prior   Change  
**\$341,981**   **\$314,238**   **↑ 8.83%**



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## 2021 Average Sales Compensation by Industry

- Wholesale and Manufacturing Sales Representatives: \$61,660
- Insurance Sales Agents: \$50,600
- Advertising Sales Agents: \$51,740
- Real Estate Brokers and Sales Agents: \$50,300
- Securities, Commodities, and Financial Services Sales Agents: \$64,120
- Door-to-Door Sales Workers, News and Street Vendors, and Related Workers: \$26,430
- Sales and Related Workers, All Other: \$33,220



# Example



# Thank you!

Q/A

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