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Motivating Salespeople: *What Really Works*

Companies fiddle constantly with their incentive plans—but most of their changes have little effect. Here's a better approach. *by Thomas Steenburgh and Michael Ahearne*

SALES EXECUTIVES ARE always looking for ingenious ways to motivate their teams. They stage grand kickoff meetings to announce new bonus programs. They promise exotic trips to rainmakers. When business is slow, they hold sales contests. If sales targets are missed, they blame the sales compensation plan and start from square one.

The finance organization, meanwhile, views the comp plan as an expense to manage. That's not surprising: Sales force compensation represents the single largest marketing investment for most B2B companies. In aggregate, U.S. companies alone spend more than $800 billion on it each year—three times more than they spend on advertising. So naturally finance tries to ensure that comp plans have cost-control measures designed into them. Some companies offer flat commission rates so that compensation costs rise and fall with revenues. Others cap compensation once salespeople hit certain performance targets. Still others use bonuses to control spending by pinning salespeople's quotas to Wall Street revenue targets. (See the sidebar "When Finance Calls the Shots.")

But a few progressive companies have been able to coax better performance from their teams by treating their sales force like a portfolio of investments that require different levels and kinds of attention. Some salespeople have greater ability and internal drive than others, and a growing body of research suggests that stars, laggards, and core performers

are motivated by different facets of comp plans. Stars seem to knock down any target that stands in their way—but may stop working if a ceiling is imposed. Laggards need more guidance and prodding to make their numbers (carrots as well as sticks, in many cases). Core performers fall somewhere in the middle; they get the least attention, even though they're the group most likely to move the needle—if they're given the proper incentives.

Accounting for individual differences raises the odds that a compensation plan will stimulate the performance of all types of salespeople. In this article we will discuss how companies can do this to deliver greater returns on investment and shift their sales-performance curve upward.

Motivating Core Performers

Ironically enough, many incentive plans come close to ignoring core performers. Why does this group tend to be off the radar screen? One reason is that sales managers don't identify with them. At many companies the managers are former rainmakers, so they pay the current rainmakers an undue amount of attention. As a consequence, core performers are often passed over for promotion and neglected at annual sales meetings. But this is not in the best interest of the company. Core performers usually represent the largest part of the sales force, and companies cannot make their numbers if they're not in the game. Here are some proven strategies for keeping them there.

Multi-tier targets. A project that Mike recently worked on with a national financial services company shows that such targets help motivate core performers. At the company a major proportion of the salespeople fell into this category. In bearish months they almost always found a way to hit their targets, but in bullish months they seldom exceeded their numbers substantially. In an effort to nudge them upward, the company experimented with tiered targets.

The first-tier target was set at a point that a majority of the company's sales agents had historically attained, the second-tier target at a point reached by a smaller percentage of the sales force, and the third-tier target at a point hit only by the company's elite. All the firm's agents were divided into two groups: The first was given targets at tiers one and three, and the second group got targets at all three tiers. The hypothesis was that tiers would act as stepping stones to guide core performers up the curve.

The tiered structure indeed had a profound impact. Core performers striving to achieve triple-tier targets significantly outsold core performers given only two tiers. By contrast, multi-tier targets did not motivate stars and laggards as much: No significant differences in performance were found for those segments.

These results suggest that core performers exert more effort if given additional tiers. Stars are presumably unaffected by the extra stepping stone because they view the top tier as attainable regardless of the number of targets. And the inattentiveness that laggards show suggests that they typically aim for and are satisfied with achieving the first-tier target.

Prizes. A research project that we're both currently working on investigates how prize structures in sales contests can engage core performers. The problem with contests is that stars usually win them. Knowing this, core performers don't bump up their own efforts. You can handicap contestants on the basis of their prior performance, which alleviates the problem to a certain degree. But that creates its own problem: What's fair about core performers' and laggards' taking home the top prizes, if stars are left with lesser prizes or no prize at all?

Ideally, sales executives would design contests so that both stars and core performers would go home satisfied. This isn't easy to do, but if you keep in mind that people are hardwired to adapt to their position in a social hierarchy, it is possible. The key is to offer gifts (not cash) for the lower-level prizes that can be seen as equal, or even superior, to the top-level prizes

A PERFORMANCE CURVE FOR THE SALES FORCE

A typical sales force has a clear majority of "core" performers, a small but elite group of stars, and a group whose performance trails. It's possible to boost performance at all points on the curve—but the wise sales executive uses different tools for each group.

Idea in Brief

A growing body of research suggests that the laggards, core performers, and stars who make up a sales force are each motivated by different facets of the compensation plan.

Yet very few companies focus on getting the most out of the full range of their salespeople. Instead, most firms zero in on their stars—even though it's their core performers whose improved performance will move the needle. Additionally, many companies respond to cost-cutting pressure from the finance department with incentives that backfire.

Companies that take individual differences into account will realize better results across the performance curve—and see a higher return on sales expenditures.

on some dimension. Suppose a prestigious golf vacation is awarded as a top prize and a local family getaway is awarded as a lower prize. The family getaway has a lower market value than the golf vacation, but core performers can adapt to their central position on the performance curve by shifting their preferences. They can rationalize their prize by saying, "I've golfed plenty lately—what's important to me is spending time with my family." We consistently find that core performers work harder and perform better in contests of this kind than they do in contests with cash prizes. Furthermore, their increased effort does not come at the cost of decreased effort from stars or laggards.

However, this approach won't work if the gifts offered at lower performance tiers are simply lower-grade versions of those at the top tier. Core performers will never perceive 18 holes at a run-of-the-mill golf course as more desirable than 18 holes at a prestigious course. The lower-level prize must have some quality that the higher-level one does not. In this example, it was the local getaway's family appeal that allowed core performers to remain engaged in the contest.

We've also seen that core performers near the bottom of their cadre are motivated by incentives designed to improve the performance of laggards. This happens because they fear falling into the lower category. Now let's take a look at the incentives that work for the salespeople in that group.

Motivating Laggards

The low-performing group in a sales force is usually heterogeneous: It may include new hires in need of training and senior salespeople who have become complacent, as well as people who are simply less talented and motivated than their colleagues. Most laggard groups we've observed have members whose performance can improve if the right incentives are in place. The following strategies (which include both carrots and sticks) effectively motivate the "good" laggards to move up the curve.

Pace-setting bonuses. A current study of Tom's looks at the most common carrot: the bonus. This study, based on field data from a *Fortune* 500 company that sells durable office goods, separately models the behavior of stars, core performers, and laggards within a number of different compensation plans.

The study found that removing quarterly bonuses from laggards' incentives—and keeping only an annual bonus—would decrease their overall performance (as measured by the revenues they generate) by approximately 10%. The same change would decrease the overall performance of core and star salespeople by 4% and 2%, respectively. There is no downside to including quarterly bonuses. They help laggards contribute to the bottom line without detracting from the performance of other groups.

Pace-setting goals have been found to change the behavior of low performers in other domains, too; education researchers see similar patterns among students. Weaker students need periodic quizzes throughout the semester to keep them on track. In the absence of such mechanisms, they perform poorly on comprehensive exams. By contrast, strong students—like star salespeople—make an effort independently and have less need for intermittent goals.

Natural social pressure. Managers often mention that having a high-quality pipeline of new sales talent naturally puts social pressure on low-performing salespeople. This is commonly referred to as the "man on the bench" effect, because it is similar to the pressure that second-string quarterbacks, say, place on starters in football.

In a current study, we measure the impact of bench players on the performance of existing sales teams. Using advanced econometric techniques, we compare districts with and without bench players.

About the Spotlight Artist
Each month we illustrate our Spotlight package with a series of works from an accomplished artist. We hope that the lively and cerebral creations of these photographers, painters, and installation artists will infuse our pages with additional energy and intelligence to amplify what are often complex and abstract concepts.

This month's artist is **Chad Wys**, whose work explores the objectification of history, people, and artwork. "I openly play with the allure of foreign and aggressive new colors and forms in otherwise familiar and traditional settings," writes the Illinois-based Wys. "Barriers and obstacles are thereby created between the viewer and the object through which one must negotiate an understanding of what is both present and hidden."

View more of the artist's work at **chadwys.com**.

When Finance Calls the Shots

We recently surveyed more than 600 strategic account managers to better understand how their sales and finance organizations worked together.

We found that in slightly more than half the companies, finance and sales jointly developed revenue and expense management plans, especially for strategic accounts. (About a quarter of the firms reported that finance was primarily responsible for creating those plans.)

Nevertheless, around half the strategic account managers stated that the finance organization interfered with their ability to get their job done. When we asked them what they would do if they believed finance was going to impose expense-related controls at the end of the fiscal year (a common tactic), most admitted that they would probably shift customer-related travel and entertainment expenses to earlier in the year. They would also probably try to prepay marketing expenditures to protect them from a freeze.

More often than not, controls encourage salespeople to spend time with customers according to the company's internal needs, rather than when the customer is ready to buy.

We've observed that salespeople in districts with a bench player perform approximately 5% better than those without one. The greatest increase in performance takes place in the laggard group. In the long run the overall increase in revenue easily outweighs the additional costs associated with hiring bench players.

When a company has a disproportionate number of laggards, it's usually the result of sales managers' reluctance to face a difficult transition period. Often managers are forced to make a trade-off between retaining chronic low performers and enduring vacant sales territories. Hiring bench players can help ease this transition.

Program-induced social pressure. Programs that put social pressure on laggards should be implemented with care. Successful programs are born out of rigorous pilot testing and are sensitive to the culture of the firm. When designed well, programs heighten laggards' sense of responsibility to the team and motivate stars to help laggards out. They avoid demoralizing people.

One company we've observed puts laggards' performance under the microscope by occasionally posting sales numbers in ascending order from laggards to stars (rather than the more conventional reverse order). Another company publicly posts a sign in its sales bull pen that lists each of its salespeople in one of three categories: starters, benchwarmers, and the penalty box. While this type of public display is relatively extreme, it seems to work within this company's competitive and transparent culture. Wins are celebrated with ostentatious prizes, such as courtside seats for sporting events and leases for Porsches. Losses are taken bitterly.

Capping commissions when salespeople are hot may control costs, but it also encourages stars to quit selling.

Motivating Stars

Since stars represent the most efficient portion of a company's performance curve, incentive plans should favor them. Yet in many companies sales commission rates are capped and winner-take-all prize structures dominate the incentives. A primary reason is cost control, driven largely by the finance department.

But are these practices rational? The simple answer is no. Executives who impose these cost-control measures encourage the same form of irrational behavior that Colin Camerer and his colleagues discovered in their study of New York City cabdrivers.

Camerer researched whether cabdrivers worked longer hours when more people wanted a taxi ("law of supply") or quit for the day once they reached a certain number ("income targeting"). It wasn't even close: Overwhelmingly, cabdrivers quit for the day once they reached their target. By placing caps on commissions when salespeople are hot, executives encourage stars to quit selling—just as cabbies go home early on rainy days, when their hourly earnings are highest. Companies would be better off if stars worked more intensively during times of high demand.

No ceiling on commissions. A recent study by Sanjog Misra and Harikesh Nair examines the impact of capping salespeople's pay. They looked at the compensation plan of a large U.S. contact-lens manufac-

turer. This company stopped paying commissions once salespeople's performance reached a quota ceiling. In response, the salespeople always held sales under the ceiling. By eliminating it and making other changes to the compensation plan, the company kept its salespeople motivated and increased revenue by about 9%.

Overachievement commissions. These are higher rates that kick in after quotas are met. For example, salespeople may earn a penny on a dollar with their regular commission rate until quotas are reached, but earn two pennies on a dollar on all sales above quotas. Tom's research at the office supply company, mentioned earlier, proves the effectiveness of overachievement incentives. Removing them from a compensation plan would reduce stars' sales by approximately 17%, the research showed. An overachievement commission rate can help keep stars in the field during the fourth quarter—often the period in which customers are most ready to buy.

Multiple winners. A study of Mike's reveals that contests with multiple winners boost sales effort and performance better than contests with winner-take-all prize structures. And Noah Lim, one of his coauthors on the study, has done further work demonstrating that more (rather than fewer) prizes should be awarded as the proportion of stars increases. This finding suggests that executives should offer at least as many prizes as there are stars in a sales force. The reason is intriguing. Increasing the number of prizes in a contest increases the chances that a laggard or a core performer will win a prize in place of a star, which motivates stars to work harder.

On the whole, these results show that frugality toward top salespeople is detrimental to firm performance.

Shift Your Performance Curve Upward

Together, we have more than 40 years' experience working with companies on sales-related problems. When we first meet with executives, we always ask which decisions they sweat over the most. Deciding how to compensate salespeople is invariably at or near the top of the list. When we follow up by asking whether they have enough information to support their comp-related decisions, they nearly always say no.

It's time for that to change. We've reported here on research that reveals that salespeople at different points on the performance curve will respond to different incentives, and we hope that managers will think about the implications for their firms—and follow that stream of research as it develops. But there's no reason to rely just on studies being done by academics. We hope that companies will develop their own field experiments and learn what works best for their salespeople.

The first step for any company is to get a clear understanding of its own performance curve. Ideally, this would be done through sophisticated econometric methods, but an approximation can be obtained as follows: If you simply calculate each salesperson's performance against sales targets and then create a histogram of those data, you'll have a rough understanding of whether your company's curve is normal (mostly core performers, with about equal numbers of laggards and stars), laggard-heavy, or star-heavy. The shape of the curve will suggest which incentives will give you the most leverage. (If you have a disproportionate number of laggards, you'll want to focus first on pace-setting bonuses and natural social pressure, for example.)

But remember, the existing sales culture can't be replaced all at once. Rather than set up a whole new comp structure, you should form a hypothesis about one element of the plan—that your laggards would perform better with more-frequent pace-setting bonuses, perhaps. Design an experiment that includes both a treatment and a control group. Then pilot the change in just one part of the sales organization. Test one hypothesis at a time, in a limited pilot run. (For advice about how to do that, see "A Step-by-Step Guide to Smart Business Experiments," by Eric T. Anderson and Duncan Simester, HBR March 2011.)

Sales compensation plans that take into account the different needs of different salespeople—and that are based on real evidence rather than assumptions—will ensure that your sales department gets a significantly higher return on its investments.

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DIFFERENT STROKES FOR DIFFERENT FOLKS

Quarterly bonuses are especially important to laggards. At the other end of the performance spectrum, overachievement commissions are far more important.