SIP Terms and Conditions:
Why Bother?
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"When everything else fails read the rules."
~Anonymous

Sales compensation Terms and Conditions are not the sexiest part of a plan. They are, however, often the aspect of a plan which contributes to its success for both the company and the sales reps. Unfortunately, all too often, they are at best given cursory attention. The purpose of this white paper is to provide a practical perspective on why Terms and Conditions are an important element of sales compensation plan effectiveness.

What are "Terms and Conditions"?

In the strictest senses, these are general and special provisions, requirements, rules, and standards that form an integral part of an agreement or contract. When talking about sales incentive compensation, the associated Terms and Conditions (commonly called "Ts and Cs") define all of the significant rules under which the plan operates. For plans to function effectively, these "rules of the road" must be well documented to ensure consistency and visibility throughout the organization.

What is commonly included? Typically, Ts and Cs are clear and concise documentation of the vocabulary, corporate policies, employment policies and sales-specific processes and procedures directly related to the payment of incentive compensation to incentive-eligible positions. This is also an opportunity to secure formal acknowledgement from the plan participants that this information has been provided to them.

Why are Ts and Cs Important?

In our experience, providing only the plan mechanics to sales incentive plan participants leaves too many unanswered questions. In turn, this may lead to different answers to the same questions, depending on who is providing the answer. While "rules" may be perceived as inhibiting to sales initiatives, it is incumbent on the organization to ensure a common understanding of such important factors as how performance is measured for the purpose of incentive pay, conditions impacting payout (such as sales crediting practices), and relevant employment policies. While Ts and Cs need not be extensively detailed in a document separate from the plan document, developing documentation on applicable rules is an important tool for the company. Doing so ensures that potentially ambiguous terms and company-specific policies or practices have been clearly and uniformly communicated "in writing".

Issues: "What Could Possibly Go Wrong?"

While the sales organization may be highly collegial, not at all litigious, and open to change, we have found that, as Jack Dempsey said "the best defense is a good offense". However, some clients without documented Terms and Conditions frequently say to us, "We've done fine without all the rules. What could possibly go wrong?" Here some examples of "what could go wrong".

- **Sales Crediting**. These are the rules guiding the allocation of sales results among resources who have participated in the sales process. As one of our clients told us "without the rules, we have too many people on the bus who think they are the driver" (i.e., they all get credit for a sale regardless of how much or little they have contributed to the result). Frequently, this means that all resources get equal credit – resulting in "duplicate crediting" that far exceeds the value received by the company. Case in point: one technology company gained a new $10,000,000 contract and paid out nearly $6,000,000 in commissions because there were no rules in place to define how credit would be "split" or shared across the resources responsible for this single contract. The following year, split credit rules were in place!
- **Customer or Account Net Payment Status.** This refers to status of payment received by the company, product returns, or the credit status of a customer. Unless the impact on

incentive pay of these factors is well-defined, the default position of most sales people is, "Not my job, not my problem, won't affect my pay." If this is not the case (that is, if for example, product returns result in a "clawback" of incentives, or reduced quota credit), then all the associated rules should be determined, documented and communicated at the onset of the plan year. In one client company, a high performing sales person was told that one of his "best" customers had defaulted on the outstanding balance due associated with a large contract; however, while the company would not receive the revenue, the sales person saw no change in his bonus earnings, as any negative impact based on customer default was never defined in the plan documentation.

- **Adjustments to Territory or Quota**. Because the environment in which a sales organization operates is rarely static (e.g., accounts are reassigned, new opportunities emerge, new products are launched), changes to either territory boundaries (geographic or account lists) or quotas, or both, need to be addressed proactively in the Ts and Cs of the plan. Frequently, a phrase such as "the company reserves the right to make changes to territory boundaries or quotas based on defined factors such as……" is deemed sufficient. However, without at least this basic tenet, management may find that changes to either may be perceived as inequitable or discriminatory. For example, in one company, upward adjustment of quotas based on an acquisition were perceived as unfair ("they're trying to cut our pay"), since the quotas given in January were called "annual quota" and there was no policy associated with a change in quota levels across the sales force. The most highly compensated sales people threatened legal action unless the original quotas were used to determine incentive payouts for the balance of the year.

- **Employment Conditions**. Such policies as leaves of absence, change in position, or change in employment status are typically defined in a human resources hand book (or its electronic equivalent) for all employees in the enterprise. Care should be taken to insure that such policies are tailored to the sales organization as well, since they typically impact incentive pay calculations. State and federal regulations are critical factors; this is never an area that can be left to management discretion. In most companies, it is the corporate legal staff or outside counsel that provides the definitive opinion in this area of the plan.

Who Does Ts and Cs?

Developing meaningful Terms and Conditions is an on-going challenge in many companies. While they must provide sufficient information to serve as a solid foundation for decisions that may be problematic otherwise, they should not be so granular and complex that the plan is demotivating for sales people Therefore, it is important for all stakeholders to share accountability in this process. Representatives from Human Resources, Finance, Sales Operations, Senior Sales Management, and Legal need to work together to develop the pertinent Terms and Conditions. Typical accountabilities for each function include:

- **Human Resources and or Compensation**. Typically the process owner, also responsible for documentation of company policies and processes, employment conditions and definition of compensation components
- **Finance**.: Develops measurement and crediting definitions and processes, as well as reporting definitions and processes
- **Sales Management and Operations**. Accountable for performance measures selection and definition; customer, channel, and assignment definitions; description of the quota process, plan framework and plan mechanics

- **Legal**.: Completes a review to ensure compliance with applicable industry, country, local statutes and regulations, including employment law

Once documented, the recommended Terms and Conditions should be reviewed by first line sales managers to ensure that the language is understandable, and the most common issues have been addressed. The process needs to "close the loop" through effective communication to the field sales organization.

Summing Up

Developing, documenting, reviewing and communicating the Terms and Conditions associated with sales incentive pay is an ongoing process. While they do not typically need to change significantly each year, it is valuable to have a process in place to review Ts and Cs to determine any need for revisions. Here is a list of questions to pose to stakeholders that will help to assess any need for change:

- Are there frequent disputes or exceptions?
- Have jobs have changed this year?
- Has eligibility for sales compensation has changed this year?
- Has the company implemented a new enterprise management system?
- Have the incentive plans changed for the upcoming year?
- Have either employment law (in this state, in this region) or accounting rules changed?
- Have we reviewed our documentation within the last two years?
- Have Legal and Finance reviewed definitions and processes for the upcoming year?