

COMPENSATION GUIDELINES for Manufacturers and their Independent Representatives

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Introduction

The following material has been developed by a special IPRO committee comprised of reps and manufacturers. Their mission was to identify and define those elements of the manufacturer and independent manufacturers representative's relationship and compensation mix so that a series of appropriate guidelines and recommendations could be developed which would encourage, motivate and promote a mutually profitable partnership. The study was appropriately dubbed II² ("i-i-squared" for "Increasing Income Squared").

These guidelines are presented as a starting point in helping create mutually profitable compensation programs.

In today's new operating environment for audio-video and professional sound marketing, where specialized user applications and sales support are at a premium, the independent manufacturers representative has become a value-added component in the marketplace. No longer is it just enough to sell products. Representatives must undertake constant factory administered product training, provide pre-and post-sales support, warehouse products, support sophisticated computer systems, and provide a number of marketing services.

The independent manufacturers representative must manage the interface between the manufacturer and the installer, retailer, distributor, contractor and end user.

Increasing income for both the manufacturer and the independent representative creates a significant win/ win scenario which is the key to a **long term** and **mutually profitable** partnership. As the relationship between manufacturers and their independent representatives matures, new and innovative ways should be found to benefit and compensate both parties.

Purpose

These guidelines are presented as a tool to be evaluated and, where feasible, utilized by manufacturers and independent manufacturers representatives to design, implement and measure effective compensation and incentive programs. It is the purpose of these guidelines to explore the entire compensation relationship of sales and marketing services performed by the independent representative in pursuit of the manufacturers goals and objectives.

How Manufacturers and Representatives Mutually Benefit

When compensation is appropriate the representative will build his agency with additional higher quality personnel, at a reduced turnover rate. By strengthening the representative, the manufacturer will strengthen himself, substantially increase market penetration and achieve greater levels of profitability. As more functions move closer to the customer, manufacturers will benefit by being able to convert more fixed costs to variable costs. A well designed compensation program will mutually meet manufacturers goals of:

- Increased Income • Agency Management Skills
- Market Knowledge and Influence • Improved Market Share
- Market Expansion • Sales Force Continuity

And provide the resources for representatives to accomplish their objectives of:

- Increased Income • Management Skills Development
- Market Knowledge and Influence • Improved Market Share
- Market Expansion • Agency Continuity

Overview

When determining an appropriate commission/compensation program it is necessary to define the elements or tasks which make up the total work performed. Historically, the independent representatives task has been loosely described as “sales.” On closer inspection this task is made up of combined sales, marketing and service functions.

The traditional sales function is typically rewarded with a base commission level and may be increased with incentives for growth, price realization, product mix, market penetration, etc., allowing for compensation at different levels of performance and different rates. It is important to note that all representatives need not be paid or compensated alike. The availability of computer generated commission statements makes it possible to compensate representatives differently based on a variety of factors. Many compensation programs are still rooted in custom and were simplistic for the sake of manual accounting.

Services are those functions within the sales/marketing mix which can be selected by the manufacturer to be performed by the independent representative or provided directly by the manufacturer. When these services are provided by the representative, the representative should be compensated. At the same time, a manufacturer should not be required to pay for services that are not used just because the independent representative happens to offer them. The written contract between the manufacturer and the independent representative should delineate all services included in the compensation mix.

Sales and Marketing Considerations

A wide variety of sales and marketing functions are provided by independent representatives. Manufacturers should consider their utilization of these functions in developing the level of a compensation program. The following lists many of these sales and marketing functions.

- Warehousing • Trade Show Costs • Distributor Inventory Control
- Detailed Marketing Forecasts • Joint Calls • Sales
- Factory Dedicated Computer • End User Calls • Sales Planning System • Product Specification • Sales Forecasting
- Market Research • Order Processing • Merchandising
- Price Administration • Customer Service/Expediting • Training
- Incentive Program • Collections • Special Mailings Management • Formal Consulting • New Product Promotions/
- Order Handling • Quotations Introductions
- Buy/Sell • Market Feedback • Marketing/Communications

Compensation and Current Objectives

Compensation programs that are historical in nature frequently encourage independent representatives to accomplish goals that are only a part of the goals of the manufacturer they represent. It is imperative for the manufacturer to develop commission programs that are in concert with their current goals and objectives.

Steps for developing an effective compensation program:

1. Determine what services constitute the basic sales function which is compensated by the base commission.
2. Determine what additional services are needed and develop a fee schedule or added compensation rate.
3. Develop objectives: assign a weight to each – i.e. profits, volume, market penetration.

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4. Define and weigh the tasks necessary to accomplish the objectives. Who performs them? Manufacturer or representative?
5. Determine what new tools or services are required to implement the program.
6. Define an empirical measurement for each objective. Set goals and benchmarks.
7. Create a reward structure to be paid as goals are met or exceeded.
8. Monitor market and redefine program elements as goals are met or as market objectives shift.

9. Keep program growing and make it beneficial to both manufacturer and representative.

Measure Results or Effectiveness

It is appropriate to compensate independent representatives based on a variety of factors. The NEMRA/ NMG II² guideline committee recommends the consideration of at least the following four (4):

- 1.) Gross Volume
- 3.) Market Penetration (Share)
- 2.) Price Realization
- 4.) Service Performed

Any of these factors alone can be used, or any combination in order to support, recognize and differentiate between adequate and outstanding independent representative performance and production.

Methods of Compensation

- Commission • Consulting fee
- Performance incentives • Extended contracts*
- Warehouse allowance* • Factory "800" lines
- Promotion allowance • On site product specialist
- Office equipment allowance • Forms allowance
- Special service allowance

Legal Considerations

Independent representatives are in fact independent contractors. Compensation programs can and should be tailored to the individual firm. There is no legal requirement that all programs be the same.

*See IPRO Guidelines on negotiating contracts for more information on these items.

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