Aligning CRM rewards with corporate goals

By David Hughes

New metrics and rewards structures can help the transition from traditional sales management to customer relationship management, aligning sales representatives’ effort with corporate goals.

Tracing the alignment of rewards
Information technology (IT) has demonstrated Alderson’s point that marketing is most efficient when it moves information instead of moving people and goods. Just as Sam Walton revolutionized retailing by requiring vendors to be linked to the WalMart IT systems (thereby reducing inventory), Dell went a step further and allowed customers to design their own computers, which eliminated most of the personal selling function. In recent times, Google’s stock price has demonstrated the power and value of moving information. In short, IT has dramatically changed basic business units—especially those in marketing—and what, for example, were dull transportation and warehousing activities, are now thrilling logistics strategies.

These IT-driven logistics systems have transformed traditional sales management into Customer Relationship Management (CRM). The vendor becomes closely integrated with the customer’s strategies, thereby changing the role of the sales representative. But do the reward systems reflect the representative’s new roles and direct their efforts to meet the needs of the company as well as the customer? Some additional metrics may help to align reward structures, and therefore CRM efforts, more closely with corporate goals.

Traditional sales management bases for compensation
Traditionally the goals of a Customer Relationship Management business unit are defined in terms of sales volume, margins and Return On Assets Managed (ROAM) and sales representatives’ compensation plans are based on some combination of these. ROAM is defined as the profit or contribution divided by the tangible assets that are managed by an individual. Using ROAM in sales management was first suggested in a Harvard Business Review article in 1967. A 1983 article expanded this concept to help sales representatives allocate their time more productively.

The first three sections of Figure 1 show how a compensation plan based on a goal of sales volume, contribution, or ROAM would direct a representative’s effort toward different customers. If the plan were based on sales volume, the representative would direct his or her effort toward Company X, then Y, and finally Z. But not all products have the same margin and customers do not buy the same mix of products. Customer X may be described as a “cherry picker” because 60 percent of its purchases are for the lowest margin product. In contrast, Z buys 70 percent of its mix in product C, with a 3 percent margin. Multiplying the sales by the margins and the product mix, we find the contribution for each product and the total contribution for each customer. The rank now changes. Company Y will get the greatest selling effort, followed by Z, and finally X. If the representative could help Z with its strategy so it would buy more, this ranking could shift again.

The third part of this table focuses on the ROAM of the assets that are required to manage each customer. These assets would vary by industry and by customer, but for the sake of illustration we will assume that four are common to Companies X, Y, and Z: logistics, accounts receivable, special inventory, and an IT system that is required by the customer. Logistics would be an allocation of trucks, cars, and warehouse space to each customer. Accounts receivable would be the average balance of a customer who is tying up assets by not paying immediately. Inventory would be the value of goods that are held in the warehouse for a specific customer or are in transit. Dedicated IT would be the unique systems that are required by a customer. Logistics would be an allocation of trucks, cars, and warehouse space to each customer. Accounts receivable would be the average balance of a customer who is tying up assets by not paying immediately. Inventory would be the value of goods that are held in the warehouse for a specific customer or are in transit. Dedicated IT would be the unique systems that are required by a customer.

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Two of the popular CRM software programs, NetSuite and Salesforce.com, are perhaps indicative of the current available software.

NetSuite is an integrated platform that includes CRM with features of sales force automation, marketing automation, customer support and service, incentive management, and partner relationships management. It provides realtime dashboards that include performance indicators such as new leads, forecasts, sales, new customers, profit, and operating cash flow. Dashboards also provide customer information, a calendar of events, business news, and automated commission management. Both actual and projected commissions are visible to the representatives and managers. The system supports a commission that is based on quantity, sale amount, profitability of the product, or a percent of quota reached. However, return-on-assets managed is not part of the system.

Salesforce.com analyzes opportunities, leads, demonstrations, proposals, closing rates, accounts, territories, and sales data. In short, it tracks all of the steps in the selling process. Standard applications include project management, all phases of human resources, channel management, managing catalogues and sales material, and other applications that are developed by third parties. But again, it does not include the functionality to track representatives’ ROAM.

New metrics
In many companies, most of the assets go down in the elevator at the end of the day and drive away. These intangible assets are knowledge, organized by job titles such as research, design, engineering, finance, and, of course, sales representatives who have the knowledge to manage the customer relations. It is those
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intangible assets that are becoming more important in all organisations. Gilder notes that, “The central event of the twentieth century is the overthrow of matter. In technology, economics, and the politics of nations, wealth in the form of physical resources is steadily declining in value and significance. The powers of mind are everywhere ascendant over the brute force of things.”

The sales representative must manage the knowledge networks of the company and the customer so that each organisation will be profitable. Today, network organisations are flat, replacing hierarchical structures—and the challenge for sales representatives is to direct and motivate knowledge networks in those environments.

There is extensive research on the subject of networks, for example Cross and Parker provide processes and survey instruments for studying network communications. Additional instruments, publications, conferences, and network research centers can be found, which have lists of software for network analysis.

In part 4 of Figure 1, these intangible assets are represented by an allocation of costs based on the time that sales, design, and engineering staff spend with each customer. We see that Customer Z is a very heavy user of these assets in comparison with X and Y. Adding the...
tangible and intangible assets used for each customer, we derive the total resources used. We can then compute the Return On Resources Managed (RORM) by the representative. Customer Z produces a return of only 25.2 percent, while X produces 41.7 percent.

If the company goal is a 30 percent RORM for each customer, the representative must develop strategies for taking Z to this goal. The obvious strategy is to find out why Z is using so much of the company’s design and engineering resources. Perhaps they are simply avoiding developing their own facilities and buying just enough products to get free consulting. Will they then take this knowledge to develop their own products or use it to get better deals from vendors who do not supply this knowledge? If this is their strategy we need to consider whether we want to continue this account. On the positive side, perhaps they are a new company with great potential and we are in on the ground floor of a long-term positive relationship.

We should not limit our strategies to the short term, but instead examine the growth potential for the customers. In Figure 2, row 5, the estimated growth rate is added below current sales to help develop a long-term strategy. Company X seems to be in a declining industry, Y is static, but Z has a 140 percent growth potential over the time period being considered. Following the analysis down to the RORM we see that Z is predicted to move to 35.2 percent, well above the target of 30 percent, and ahead of Y in ranking. Thus, the long-term resource strategy suggests that the intangibles that are invested in Z may be a good investment.

**Resource-based strategies**

Competitive strategies, according to Collis and Montgomery, require having resources that are unique, making it possible to perform better than competitors.¹¹ Their criteria for a unique resource require it to be difficult to copy, have trust associated with a long-term brand, have causal ambiguity, and have preempted competition by a major investment in a resource. These resources are difficult to value. For example, causal ambiguity is defined as being impossible to disentangle what the resource is or how to create it. It can simply be the company culture.

These resources are at the far end of the intangible scale. Just calling them “goodwill” is not sufficient for analysis. One approach is to measure customer satisfaction (CS) and relate it to profitability. CS has been a very popular gauge and uses familiar survey methods to measure customers’ satisfaction along variables such as the vendor understanding the buyer’s needs, how well prior expectations were met, whether promises were kept, product quality, service after the sale, and overall satisfaction. (Technical note: Using multivariate statistical methods and “overall satisfaction” as the dependent variable, it is possible to identify the importance each of these variables to the overall customer satisfaction. Vavra correlates the overall satisfaction score to profitability to show how much an increase in customer satisfaction is worth in terms of profit.¹² Of course, like all correlation methods, the link between cause and effect can be questioned.)

Many companies link customer satisfaction to compensation.¹³ However, the problem with many CS measures is that the representative may not be able to control the variables that determine overall satisfaction. CS could be used in a reward program if the survey questions included only those variables that the representative could control. These variables could include understanding the customer’s needs, being an advocate for the customer with the company, keeping promises, and service after the sale. An index of only
these variables could be created using multiple regressions so that the representative could see which variables are most important.

The reward programme
The reward programme for a representative cannot be based only on RORM because this goal would encourage the representative to under-invest resources that would increase the sales volume from a customer. The programme should be based on both sales volume and RORM goals. Commissions could be based on achieving these goals, with higher commissions for exceeding them. This type of reward programme would align the representatives’ effort with the corporate and investors’ goals of maximizing ROI and ROE.

Any new plan should be tested using historical data and then implemented as an experiment. Calling it an experiment alerts everyone that it is still being refined. The representative should not be expected to develop spreadsheets like those in the exhibits. Most of the data used for these exhibits are in a company’s database. If the hours spent with a customer are not recorded, they should be. Estimating the growth rate for a client will require some research, including working with the client, industry analysis, and executive judgment.

By incorporating the analysis in these exhibits into the CRM software, the representative can ask “what if” questions and estimate the impact of different customer strategies on personal rewards.

Job description and performance evaluation
The link between the reward programme and the job description is the performance evaluation process. A weak evaluation process can result in demotivation and may even have legal implications. In the United States, the Equal Employment Opportunity Commission (EEOC) extended its investigations from hiring and selection procedures to include evaluation and promotion procedures. A review of 66 cases found that a company had a better chance of winning if written instructions were provided to the evaluators, if behavior-oriented performance evaluations were used instead of trait-oriented appraisals, and if the results of the appraisals were reviewed with the employee.14

The job description is the initial step in the process of aligning representatives’ activities with the corporate goal. It must make clear that the representative manages resources and knowledge networks to maximize sales volume and RORM. Failure to make this link is frustrating to both representatives and managers.

Summary
The computer has transformed personal selling into customer relationship management. However, current CRM software does not appear to support the alignment of representatives’ reward programmes with the corporate and investors’ goals. The software programs examine only sales volume and product profitability; they do not include return on the tangible and intangible assets managed. In my opinion, considering all of the resources managed by representatives can simplify the reward plans and align the representatives’ efforts to the corporate and investors’ goals. The representatives’ reward plans should be based on quotas of sales volumes and RORM. This reward structure should be reflected in the performance evaluation procedures and the job description.

References
9. As an example, see *International Network for Social Network Analysis*. http://www.insna.org/