

From Strategy to Profitability: How EIM Drives Business Performance

Aligning behavior to business strategy via incentive compensation can be one of the most effective catalysts for achieving corporate objectives. By correctly leveraging incentives, organizations are driving activities that increase competitive advantage, profitability and shareholder value.

Enterprise Incentive Management (EIM) solutions are the answer to capitalizing on the power of incentive compensation. EIM technology enables organizations to effectively align sales, channel and other constituents to carry out corporate strategy, thus improving business performance.

Unlike homegrown or legacy systems, EIM systems deliver a single, flexible, transparent and automated solution that addresses the myriad of challenges related to maximizing incentive compensation's potential. EIM solutions enable organizations to model, design and administer compensation plans and process sales credits, measurements, incentive calculations, compensation reports and more.

The flexibility inherent in EIM technology enables organizations to make modifications that reflect changing business needs. An industry-leading EIM system is an indispensable strategic tool for improving organizational agility, gaining a competitive edge, and ultimately increasing shareholder value.



They had closed an excellent deal—or so they thought. Significant profits from the sale of industrial automation software, hardware, and service and support agreements were anticipated. Little did Finance know, the twelve people credited for that sale were the only ones reaping the benefits. Characteristically operating on thin margins, the company was later unpleasantly surprised to find it had barely broken even after all commissions were paid out for the deal.

Accompanying this type of scenario are other common dilemmas organizations face today when it comes to moving from boardroom strategy to corporate profitability. A few such problems include poor sales productivity, paying employees for activities that do not add to shareholder value, lack of trust between Sales and Finance, and lack of visibility into financial and sales performance data. Simply managing the complexities and expenses involved in maintaining changing territories, manipulating performance metrics and adjusting compensation programs can be a formidable challenge.

EIM Defined

In today's resource-constrained environment, forward-thinking organizations increase shareholder value by driving top-line revenue while controlling costs and resources. Enterprise Incentive Management (EIM) solutions boost profitability by helping motivate employees, drive sales force performance and influence channel behavior—all with the purpose of efficiently aligning every constituent's activities with corporate strategy and shareholder value. EIM gives organizations the visibility to strategically leverage compensation and convert it into a competitive weapon that drives business performance.

An EIM system is a solution that automates the administration of incentives. EIM encompasses salespeople, managers and other employees, as well as external agents, distributors, resellers, suppliers and customers.

Organizations gain control over the execution of strategy through EIM. EIM solutions provide the means for selectively influencing sales growth, the sale of specific products and services, customer profitability, sales margin, collaborative activities and business performance as a whole. EIM achieves this by effectively and consistently rewarding behaviors that accomplish organizational goals at the individual, department and enterprise levels.

EIM is the automated administration of incentives for sales reps, agents, distributors, resellers, managers, employees and suppliers. EIM aligns these constituents with corporate strategy to drive business performance, resulting in increased shareholder value.

EIM systems also supply advanced business analytics and tools for what-if modeling and decision making. These enable organizations to analyze, forecast, model and fine-tune all forms of variable compensation for optimal results.

When it comes to gaining and maintaining competitive advantage, compensation management systems are becoming increasingly critical, trends indicate. "Pervasive use of variable pay will drive increased adoption of packaged EIM solutions through 2007," according to META Group, Inc.ⁱ

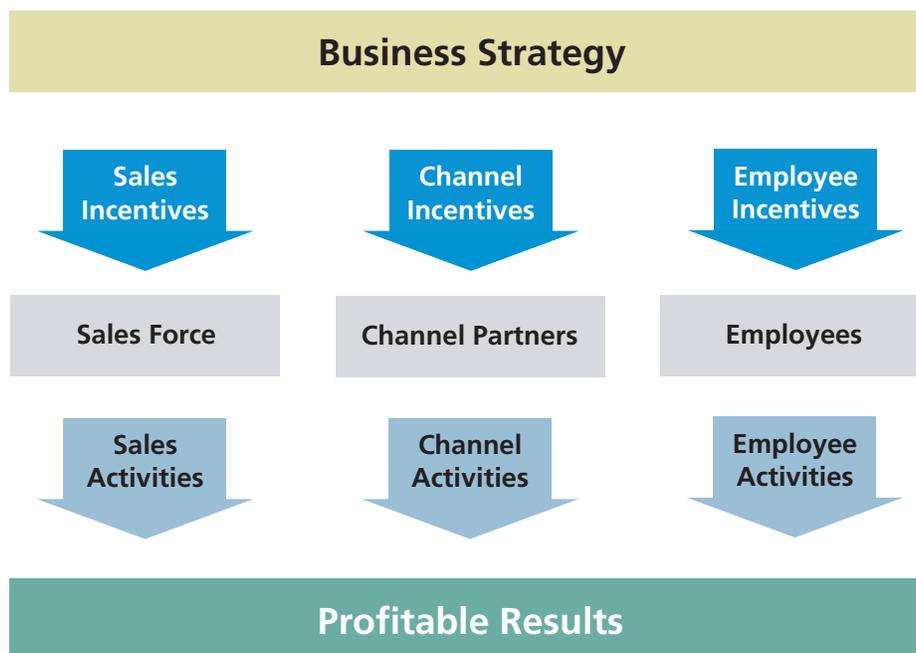
Analyst firm Gartner, Inc., anticipates that "Through 2006, 25 percent of sales organizations with more than 500 payees will evaluate and select a packaged sales incentive compensation management application to replace a homegrown system (0.8 probability)."ⁱⁱ Gartner also makes a strong recommendation, stating "Enterprises should look to replace internally developed commission management systems with incentive compensation management systems to improve the accuracy, timeliness and visibility of their compensation payments to sales representatives."ⁱⁱⁱ

Targeted Constituents

EIM helps motivate and drive the behavior of a wide range of constituents. These can include any individual or entity receiving some form of compensation for providing a product or service. The sales force is most critical, and the most acute pain and greatest opportunities are concentrated here.

The Sales Force

The sales force holds vast potential for driving profitability and is the primary focus of EIM. This group encompasses everyone involved in sales activities across the entire division. Salespeople can be difficult to manage, often because they are much closer to customers than to the organization they serve. In many cases traditional management practices are only marginally effective with this group. Therefore, organizations should rely more on incentives than management techniques to drive sales behavior.



Channel Partners

Channel partners can be independent agents or brokers, or business entities such as distributors or resellers. Original equipment manufacturers (OEMs), subcontractors or other types of suppliers can also fall within this group, which covers the whole value chain from front-end sales back to the parts manufacturers.

Agents, brokers, distributors and resellers serve a similar purpose as the employed sales representative: creating demand and closing deals. Correctly motivating these channel partners can make the difference between a valuable extension to the sales organization and a competing entity that erodes margin and damages customer relationships. Effective channel incentives contribute to improved sales coverage, market specialization and profitable growth.

Non-Sales Employees

While automating sales and channel incentive compensation is a top priority, EIM can be an effective tool for influencing everyone from line workers to senior executives. EIM has the capacity to motivate every employee.

Activities that Impact Profitability

The myriad of business activities in a value chain—such as sales activities, product-related activities—vary by individual and business function. EIM ties incentives to each activity that can impact profitability.

Sales

Top-line metrics such as revenue, unit sales and territory growth require specific ground-level sales activities related to products or services sold. EIM drives the behaviors that impact sales results. One example of this is leveraging Sales Promotion Incentive Funds (SPIFs), which are short-term incentives added to the compensation plan to reward specific sales behaviors.

Products

EIM helps organizations control new product sales, revenue growth in targeted product lines, cross-selling, the combination of products and services sold, and much more. Control of product sales at a granular level means organizations can weight incentives to favor a specific product, service, product mix or product/services mix.

Customers

Organizations can motivate salespeople to focus on certain aspects of the customer relationship or serve customers in a specific way. For example, the goal could be emphasizing customer growth from period to period instead of sales totals. An organization might also link rewards to customer satisfaction, customer retention or customer profitability.

Profits

Price discounting, sales margin and account profitability all affect net profit results. Situations vary widely as to how profits are derived from products, services and customer relationships. Case in point, many organizations are under pressure because customers do not pay promptly. When bookings occur quickly but payments are late, organizations can use EIM to tie incentives to collecting on a sale.

Collaboration

When sales team and/or channel interactions are complex, EIM can motivate individuals to collaborate more smoothly. Team selling and team performance can be powerful momentum-builders with the assistance of EIM.

Business Performance

A number of metrics affect business operations and business performance. With EIM, incentives can help drive the achievement of pre-determined business objectives, improve productivity and throughput, encourage adherence to quality standards, limit defects, streamline inventory management, and more.

Visibility, analysis and modeling are primary compensation plan design elements that drive better business decisions and ultimately impact profitability. Visibility emerges from a compensation plan that accurately reflects business needs, aligns the workforce with corporate objectives and shareholder value, and provides a clear audit trail. Results analysis provides insight into the business impact and cost of a plan, as well as valuable feedback useful for generating future plans. Modeling lets organizations simulate the effects of a plan change while saving the time and expense of experimenting with new, unproven tactics.

Strategic Alignment with Shareholder Value

Finally, using one comprehensive system, organizations have an automated tool for strategically aligning employee behavior, sales tactics and channel activity. When aligned with corporate objectives, the cumulative performance of individuals and entities drives the achievement of those objectives. This increases shareholder value.

Trust: Focusing on Business Results, not Paycheck Accuracy

Drawing from precise data, EIM's fast, accurate, responsive pay for performance and transparent, actionable information engender trust. Confidence among salespeople and channel partners that they will be paid consistently, accurately and in a timely manner allows them to focus on business results instead of their paychecks. "Key benefits of improved timeliness and increased payment accuracy increase the sales compensation plan's ability to drive sales behaviors."^{iv}

Should there be a question about a reward, the EIM system can provide the answer easily and often automatically. Dispute resolution occurs rapidly because compensation data and the applied metrics are correct, accessible and verifiable via a traceable audit trail.

Alignment results when the incentives built into compensation motivate the sales force to meet corporate objectives. Each individual actively carries out corporate strategy, and the outcome is business performance that increases shareholder value.

Methods of Structuring Incentives

Sales incentives can range from commissions, bonuses or a percentage of sales revenues to more complex rewards. Organizations can also make use of strategically designed SPIFs. For example, there might be a commission accelerator or added rewards payment per sale or per unit of sales.

Channel incentives are similar to sales incentives. Channel partner rebates, discounts and market development funds are also effective. Supplier incentives might include payment accelerators or improved payment terms for a new supplier who satisfies certain service level agreements. On the employee side, incentives can range from bonuses, salary increases, stock options, MBO rewards and more.

From Problem to Solution: Driving Tangible Results

EIM's powerful transformational effects create unlimited opportunities to increase shareholder value. EIM can grow customer profitability, penetrate new markets, improve customer service, eliminate low-margin customers, increase inventory churn, drive profitable growth and much more.

The following four scenarios show how EIM transforms common business problems to generate dramatic, ongoing results. The driving force behind each scenario's solution is an organization's ability to modify aspects of the compensation plan using EIM. Unless the plan itself changes, the problem remains. EIM systems deliver the agility and control required for implementing highly effective plans.

Scenario 1: Improve Profitability by Reducing Sales Discounting to Eliminate Profit Loss

Salespeople need the flexibility to discount, but this behavior needs to be commensurate with corporate strategy so discounting does not erode profit margin.

- **Problem:** Rewards are often structured so salespeople can give customers discounts to help make a sale. Offering a discount might clinch a deal while reducing the sales commission by a tolerable amount. Unfortunately, this same discount can simultaneously cancel out all profits for the transaction.
- **Solution:** Instead of tying rewards to a sales volume metric, organizations can use EIM to link them to a profit margin metric. For example, if profit margin is at 10 percent, a salesperson granting a 10 percent discount receives zero commission. Therefore, that salesperson is better off discounting only five percent for a five percent commission—and a five percent profit for the organization.

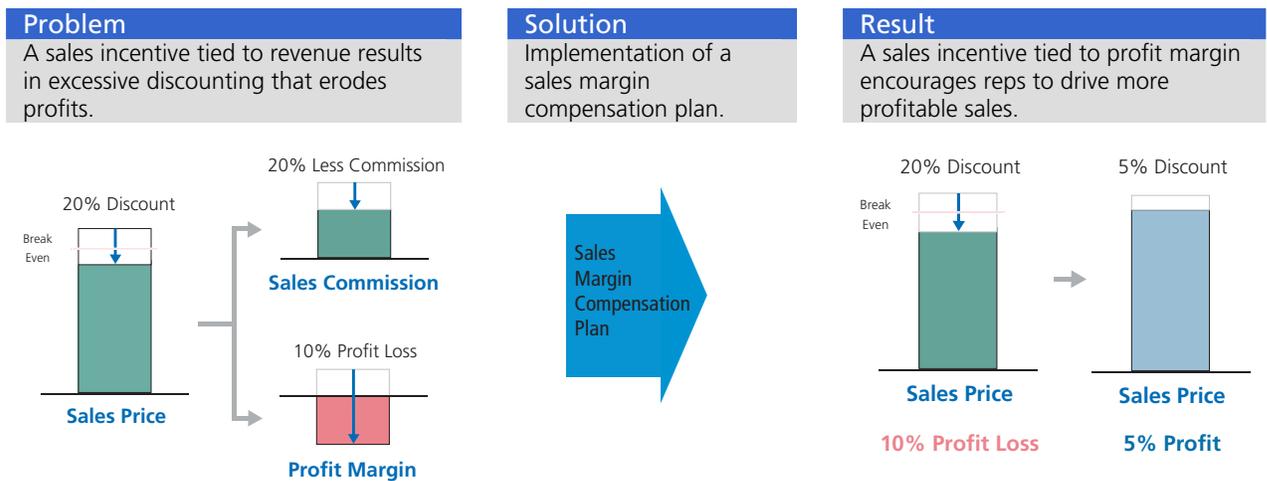


Figure 1 By restructuring incentives to tie rewards to a profit margin metric, organizations conserve greater portions of profit margin instead of losing profits due to sales discounting.

- **Result:** While they can still discount to get in the door, salespeople will consider carefully whether to discount, and if so, how much. As a result, sales discounting drops dramatically, conserving greater portions of profit margin.

Scenario 2: Increase Revenue by Minimizing Channel Conflict

Working in harmony with the rest of the channel, top salespeople are able to pursue new customer opportunities, grow relationships and actively conduct activities that drive profitable sales.

- Problem:** It is common to see highly paid, talented sales reps consumed with routine order-taking activities—often for smaller orders or existing customers. Instead of diligently hunting for new deals and opportunities that will bring in additional revenue, they are doing the work designated for other job roles such as telesales. When sales team members are not doing what they do best, cost-of-sales escalates.
- Solution:** The answer to this problem is incentive design that matches a customer with the right channel and motivates salespeople to focus their energies where their talent and expertise are most needed. Actively crediting them for referring smaller orders to a more appropriate sales channel—such as telesales or online orders—frees time so they can aggressively pursue larger customers and additional accounts. Organizations can also weight rewards on the side of new business. Overall, collaboration and teaming within sales channels should be well organized and incentive-driven so each team member maximizes his/her capabilities and only cross-compensates when necessary.

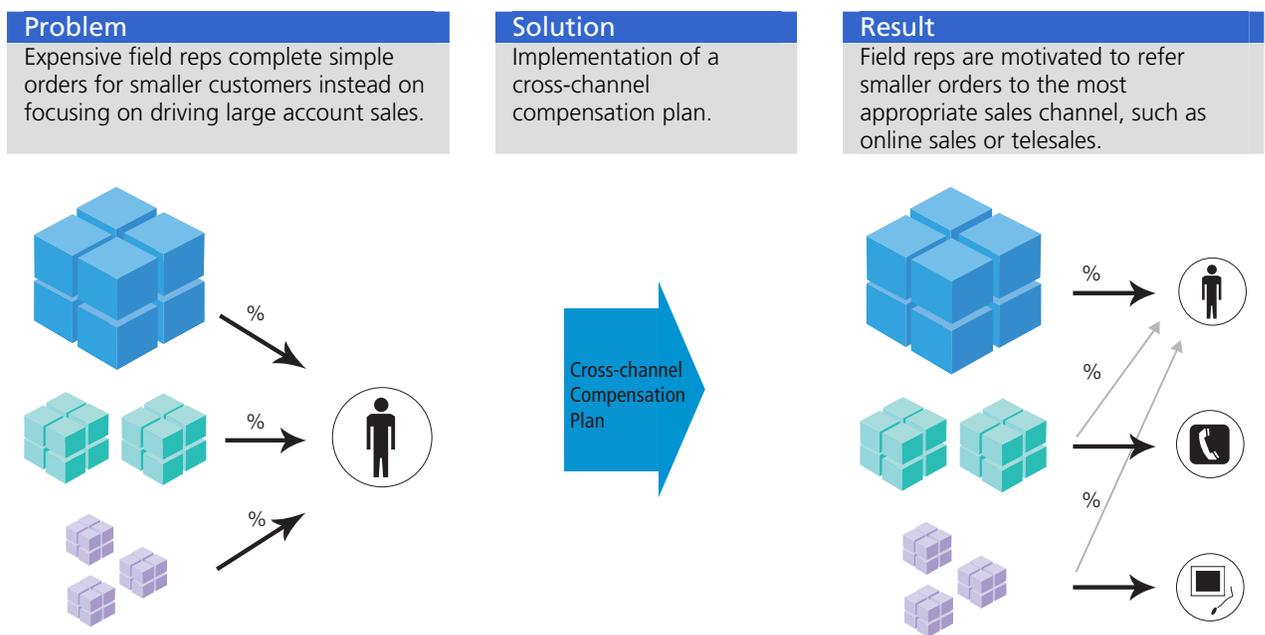


Figure 2 Incentives should drive all channel participants to do the right thing. Strategically targeting incentives to optimize specific talents within the channel lowers average cost-of-sales while maximizing the potential of all sales resources for meeting and exceeding sales goals.

- Result:** Optimizing all sales staff activities according to individuals' areas of expertise and unique value-add reduces the average cost-of-sale and aligns the sales force for revenue growth.

Scenario 3: Increase Focus on New or Strategic Products

Instead of focusing on low-hanging fruit, salespeople can prioritize sales of specific products according to organizational strategy.

- Problem:** Compensation plans are often designed so salespeople simply keep pushing those products that are familiar and/or simpler to sell. Extra work is often required to sell new products, products that carry high profit margins or those that are strategic for other reasons. Selling new products frequently requires training. In addition, unfamiliar discussions and sales situations can be involved. If a plan is not properly designed, such efforts might not generate the kind of rewards that motivate salespeople sufficiently.
- Solution:** The compensation plan, not the level of sales difficulty, ultimately drives sales behaviors. Therefore it is the responsibility of plan designers to incent the sales force to push a given product. In many situations, an organization can use its EIM system to simply add well targeted SPIFs that reward specific behaviors.

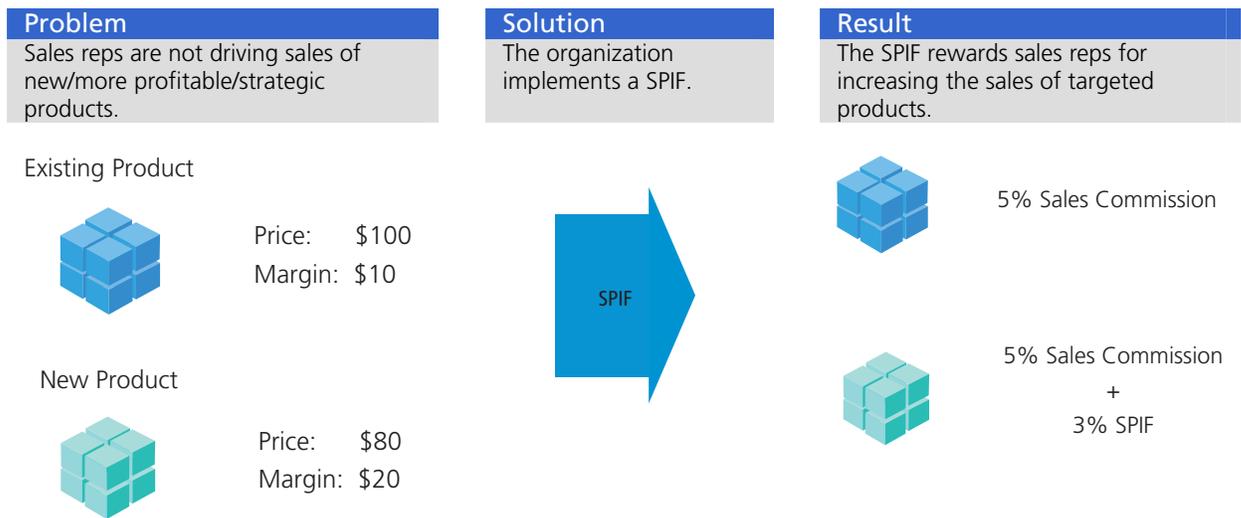


Figure 3 When an organization needs to increase the sales of a particular product or product line, special product incentives motivate salespeople to carry out this objective.

- Result:** Judiciously applied incentives make it advantageous for salespeople to sell those particular products that are new, more profitable or strategically positioned. Salespeople prioritize sales of various products and product lines according to organizational strategy, thus accomplishing corporate objectives.

Scenario 4: Drive Profitability by Selling the Optimized Product Mix

It's important for salespeople to be selling the product mix and/or the ratio of products to services that best meets organizational objectives.

- **Problem:** Often selling a certain combination of products maximizes profits but is not to a salesperson's advantage. When rewards do not motivate salespeople to sell the particular mix of items outlined in the sales objectives, the organization loses out on potential revenue.
- **Solution:** Properly structured incentives can influence salespeople to sell the optimal product mix. To maximize profit margin an organization can, for example, change reward levels so commission rates are highest when selling a specific combination of products.

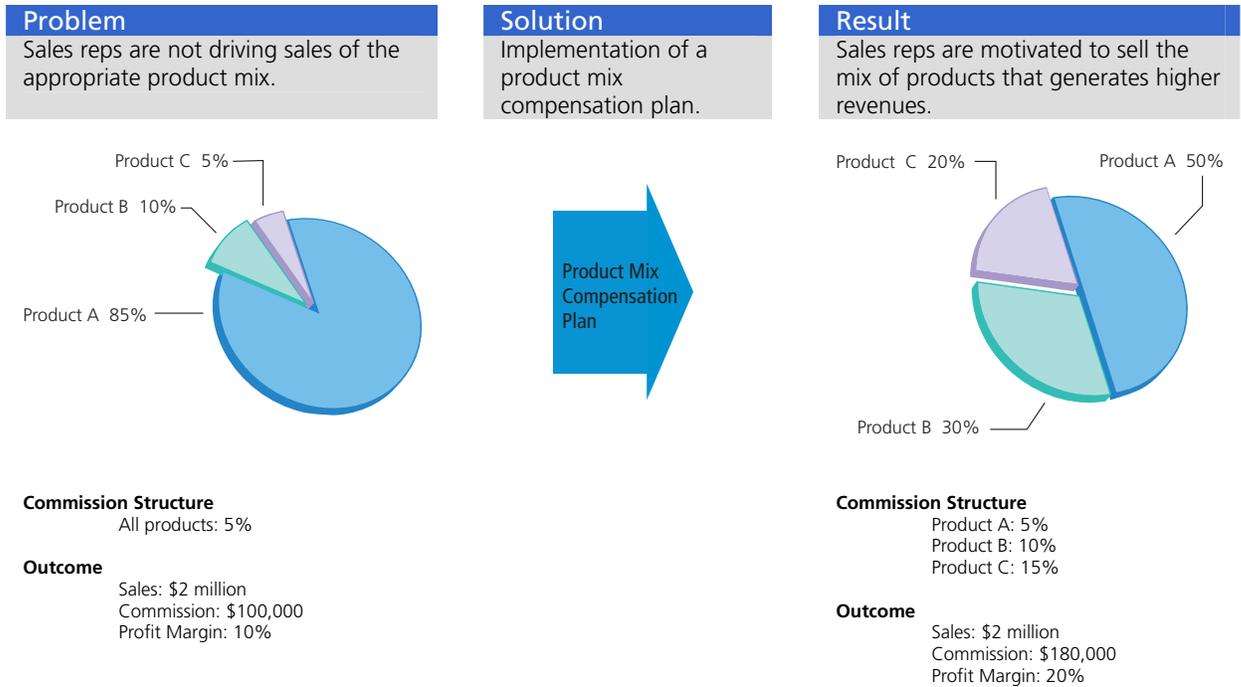


Figure 4 When an organization is optimizing its product mix, an accelerated reward structure can motivate salespeople to promote the combination that generates the greatest revenue and profits for the organization.

- **Result:** Salespeople emphasize the organization's desired product mix as much as possible while focusing on maximizing top-line sales. Executing on the organization's strategy ultimately drives the greatest profits.

End-to-End Automation of Incentives

In contrast to homegrown systems, EIM provides a single, end-to-end automated solution that integrates with existing systems and encompasses all phases of the EIM cycle. This cycle covers planning to execution to results analyses, and continues with the next period's planning.

EIM can also address the contingencies of industry-specific issues. "Vertical industries, such as insurance, banking, telecommunications, life sciences, retail, high technology and manufacturing, are replacing their expensive-to-maintain and cumbersome-to-administer systems with packaged ICM [incentive compensation management] applications."^v

Increased business demands such as accommodating growth and adjusting to market conditions require scalability. An EIM system linearly scales to encompass additional salespeople and more complex plans. Should an organization introduce new technologies, EIM can still integrate and scale with the infrastructure as the number and variety of information sources change, regardless of their heterogeneous nature. Without scalability, organizations face costly workarounds, increased processing times, complex errors and other difficulties.

EIM's flexibility makes it easy to reflect organizational changes via modified incentive plans at a moment's notice. Compensation plan rollouts occur every year, but territories, quotas and special incentives change far more frequently, as can market conditions. EIM enables organizations to adjust incentive plans on-the-fly according to business needs and the economic environment.

The Strategic Value of EIM

The fierceness of competition makes EIM the essential weapon for any forward-thinking organization's arsenal. Because of its effectiveness in aligning behavior to corporate objectives and shareholder value, EIM is a strategic, indispensable component of running a business.

"Compensation models must reflect the strategy of the business and support that strategy at the level of every employee. The compensation system demonstrates to the employees both the company's baseline business goals and values," according to Aberdeen Group.^v EIM communicates strategy to employees through the details of the compensation plan and fast, accurate, responsive pay for performance.

EIM Makes Sense

What happens to strategy after it leaves the boardroom? For organizations struggling with aligning the workforce with shareholder value, EIM is the missing piece that makes it happen.

EIM drives all the elements with which organizations have been wrestling – including margin, product mix, reward accuracy, impromptu plan changes and much more. It makes sense to tie pay to performance using the most effective technology available.

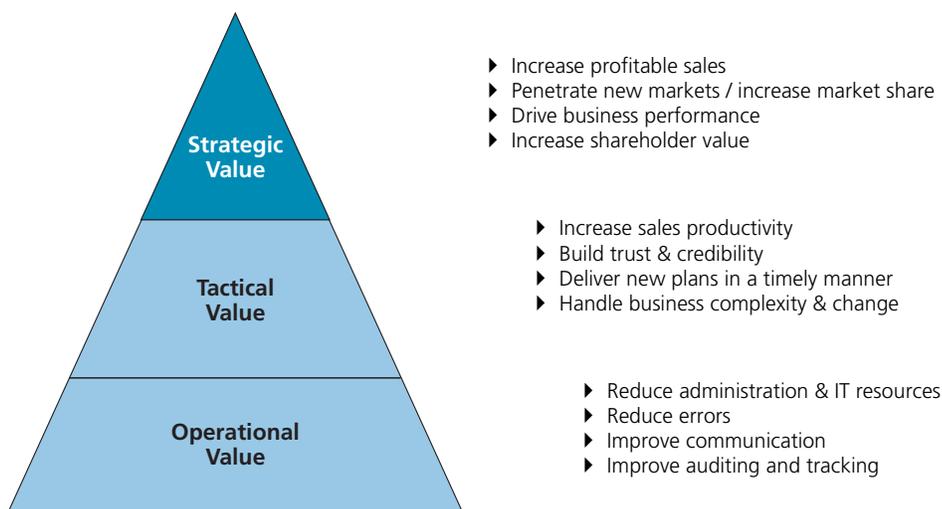


Figure 5 EIM builds on a solid technology foundation for operations, successfully implements business tactics and drives organizational strategy.

The Three Dimensions of Visibility

One of the downfalls of homegrown or traditional systems is a lack of visibility into the details of incentive administration. "EIM solutions reduce operational costs and increase the impact of variable pay by improving payment accuracy and providing increased visibility to enterprise stakeholders."^{vii}

EIM not only automates compensation, but it also gives administrators control and awareness on several levels.

- **Business logic:** Incentive compensation systems should represent and clearly address the business need. Instead of shrouding metrics, measurements and rewards in the mystery of buried computer code, EIM provides a clear understanding the mechanics of a compensation plan. System transparency ensures that incentives are tied to actual strategic goals and drive tangible results.
- **Plan modifications:** While EIM's flexibility allows for making changes on-the-fly, its visibility empowers administrators to see how, when and where a plan changed and who changed it. EIM also provides helpful audit trails, which are particularly valuable when there are multiple administrators. In addition, the ability to go backward and forward in time lets administrators view and analyze past and future plans, and make current or retroactive changes where needed. Visibility improves the results anticipated from existing and future compensation plans.
- **Feedback on results:** EIM provides clear answers to such questions as:
 - Who received credit for a transaction and which metrics were applied?
 - How much did driving a particular type of behavior cost?
 - What incentives were paid to drive revenue from a particular customer?
 - What was the total compensation paid for all incentives last period?
 - What particular incentives drove the greatest revenue?

Analytics

Drawing from the wealth of data generated from the EIM system, analytics tie together pay and performance to evaluate how successfully incentives drove behavior. Analytics also complete the planning/execution/results cycle by supplying critical direction for fine-tuning plans for even greater success.

Modeling

Compensation modeling, another advantage of analytics, empowers organizations to forecast results by creating what-if scenarios. Modeling improves the accuracy and predictability of new and innovative incentive plans because organizations can test them in hypothetical situations. This is particularly valuable under the changing business conditions every organization faces today.

The EIM Solution of Choice

The wisest decision an organization can make is to select the EIM vendor that boosts its ability to achieve its short-term goals and long-term vision. Maximizing the potential of EIM, the Callidus Software EIM product suite represents the lowest long-term cost solution with the highest return on investment.

Leading the product suite is the TrueComp® EIM solution, which uses cutting-edge rules-based Grid computing technology as its foundation. This technology provides for a high-performance, scalable, flexible EIM architecture that is in fact the only architecture capable of maximizing EIM system effectiveness. Grid computing architecture drives reliable, rapid processing of high transaction volumes while providing complete linear scalability. Rules-based software enables flexible plan changes for rapid response to changing business conditions.

The only EIM vendor using rules-based Grid computing architecture, Callidus Software has invested extensive time and effort into developing the TrueComp EIM solution. TrueComp products are robust but easy to administer and change, requiring minimal IT involvement. They integrate with other systems quickly and cleanly.

Making more intelligent decisions that drive increasingly effective business behaviors is a matter of true competitive advantage, adding substantially to company revenue and overall productivity. With more live customers than any other EIM vendor, Callidus Software delivers visibility, scalability and predictable performance in a winning solution where everyone profits.

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Endnotes

¹ Ron Hanscome, *Enterprise Incentive Management Update: Part 1 — Vendor Landscape*, META Delta 2678, META Group, Inc., 22 December 2003.

¹ J. Galvin, *MarketScope: Sales Incentive Compensation, IH04*, Markets Research Note M-21-9631, Gartner, Inc., 28 January 2004.

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¹ *Enterprise Incentive Management: A Market on the Move*, Enterprise Business Applications Hot Topic, Dr. Katherine Jones, Director, Human Capital Management, Aberdeen Group, Inc., 28 October 2003.

¹ Ron Hanscome, *Enterprise Incentive Management Update: Part 2 — Evaluation Criteria*, META Delta 2679, META Group, Inc., 22 December 2003.

Additional Reading

- *Enterprise Incentive Management: Common Goals to Align Sales, Finance, and IT*, a white paper from Callidus Software in collaboration with HR.com, October 2003.
- *The ROI for Enterprise Incentive Management (EIM)*, a white paper from Callidus Software in collaboration with Tom Pisello, Founder & CEO, Alinean, The Return on Investment (ROI) and IT Value Experts™, December 2003.
- *Build versus Buy Executive Summary Analysis*, a white paper from Callidus Software, November 2003.
- *Slim Client Architecture: Leading-Edge Technology for Productive Compensation Professionals*, a white paper from Callidus Software, September 2004.

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