Performance Enhancement
INCENTIVES

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HOW TO FUND AN INCENTIVE PROGRAM

Choose the right funding mechanism for your incentive program

Most executives will agree that a properly planned and delivered incentive program will inspire improved performance by their employees, clients and customers. And those same executives will also say that budgeting, especially in these challenging economic times, can be an obstacle to implementing such a program.

At PEI, we've seen a number of strategies over the years and have found that there are a few basic structures that can be utilized to support and properly fund an effective incentive travel program. Here are a few examples.

1. Self-Liquidating. A "self-funded" or "self-liquidating" program essentially pays for itself and is the method used for most programs. If a participant qualifies, they have generated enough extra profit to pay for their own award and provide extra profit for the company. An example of this is outlined below.

Assume an average salesperson is expected to sell 1,000 widgets at $400 each, generating $400,000 in revenues. The profit margin is 20% or $80,000. The goal to earn the reward is to sell an additional 150 widgets (15% more) at $400 each, generating an additional $60,000. In most cases, the sale of additional product generates higher profit margins since fixed costs have already been covered by the sale of the first 1,000 widgets. Therefore, for purpose of this example, let's say the profit on the extra sales is 50%, or $30,000. If 50% of this additional profit is spent to provide an effective incentive program, that would equal $15,000. The company has earned an additional $15,000 in profit and the salesperson will receive the benefit of an incentive reward program that cost the company $15,000.

If a participant doesn't hit the sales goal, he or she don't secure the reward and the only cost to the company would be any expenses associated with design and promotion of the program. The company still gets the profit benefit from any extra sales that are secured in pursuit of the reward.

2. Line Item Budgeting. A second funding option is to plan for the program in the marketing budget. This is useful when securing additional sales, for whatever reason, is not likely but a business wants to maintain relationships or promote loyalty among its employees or customers. Building it into the budget still promotes extra effort to achieve advanced goals but the funding is not dependent on additional sales.

3. Buy-in. This structure allows a sponsor company to extend the opportunity to a wider group of customers. This is done by creating levels in the award where Level A performers who achieve the entire goal, qualify for the Level A reward. Level B performers who achieve something less than the entire goal, qualify for the Level B reward. But they can also "buy-in" in order to receive the Level A reward. Offering various levels of reward opens up the program enabling more of your employees or customers to participate, not just the top performers.

4. Hybrid Structure. Another option is a hybrid of two or all of the above funding mechanisms. A portion of the incentive program expense is in the budget and additional sales are encouraged to earn additional benefits. This could incorporate award levels, thus expanding the participation of more employees and/or customers in the effort.

Let PEI help you determine the best funding mechanism for your incentive program. For more information, contact Colin Higgins at 978-287-9500.

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