

COMPENSATING MANUFACTURERS' AGENTS

Guidelines for Determining Agency Commissions, Fees and Incentive Programs

How Agents Earn Their Money

Traditionally, manufacturers' agents are paid a commission for what they sell. If they don't sell anything, they are not paid. In the past, this "low overhead" arrangement had been one of the major reasons for using independent agents, as opposed to the use of salaried factory salespeople. The economics of agency selling is still an important consideration, but as times have changed, so have the reasons for selling through independent sales agencies, and so have the compensation methods.

Typically, the manufacturer who turns to agencies to sell its products sees immediate market penetration as a major benefit. An agency in place with established customers can bring in business almost immediately. Also, manufacturers see longevity as an important factor. Manufacturers' agents are business partners who grow with their principals and maintain a steady presence in a territory. Compared with the fairly rapid turnover seen with salaried factory people, this stability is a critical factor today, as competition is intense and getting worse.

For these and many other reasons, manufacturers' agents are paid a commission on the products they sell. But today many agents do more than just sell products for the principals they represent. Many provide warehousing facilities. Some provide extensive engineering consulting services. Others offer installation and maintenance services for the products they sell. And, of course, there are many other things that agents do today that they haven't done in the past. The reasons for all this are many. Products are more complex. Markets are more diversified. Competition, both domestic and foreign, is intense. And agents today are bringing a lot more than just sales skills to the table. In the true sense of the word, agents are providing marketing services that were formerly the province of the manufacturer.

All in all, agents are doing more for their principals, they are fielding larger sales teams than ever before, and they are offering to do more than simply replace the traditional salaried salesperson - they are becoming "partners" of their principals. In doing all this, they are still legally independent contractors who are compensated by commissions on what they sell and fees for the other services they perform.

Developing an Agency Compensation Plan

It's tempting to look at industry averages and peg your commission rate in the middle. But these industry averages often mask a wide range of rates. Why a wide range? The answer lies in a number of things, all of which are determined by what the agent is expected to do, and how much work is involved in doing the job. Pioneering a product, for example, is more difficult and time consuming than taking on a commodity line where there is an established demand.

Considering the pioneering example, it's safe to assume that after a successful pioneering effort, it will be easier and less time-consuming for the agent to sell the line. This is generally true, but how do you build this into a compensation program? Initially, you might start out with a commission rate that is higher than average to compensate the agent for the heavy work needed early on. A formula could be developed by which the commission is reduced as the pioneering work is less demanding until the rate is comparable with others in the same field. Or, rather than play with the compensation percentage itself, you could start with a fair rate, but add on special incentives and fees for the agent who has to pioneer the product.

We use this example simply to show you that compensation systems can and should be developed to suit individual circumstances, not to conform to any industry "standards."

MANA's Survey of Sales Commissions indicates the highest and lowest figures and the average, computed as the arithmetic mean. Most of these figures represent normal statistical distributions...but some don't. Some vary quite widely. The point being that slavishly using these figures as gospel to establish a commission rate might do more harm than good to you and/or your agents. The important point to remember is that a commission rate should be determined empirically to insure that you and your agencies can make money - read profits.