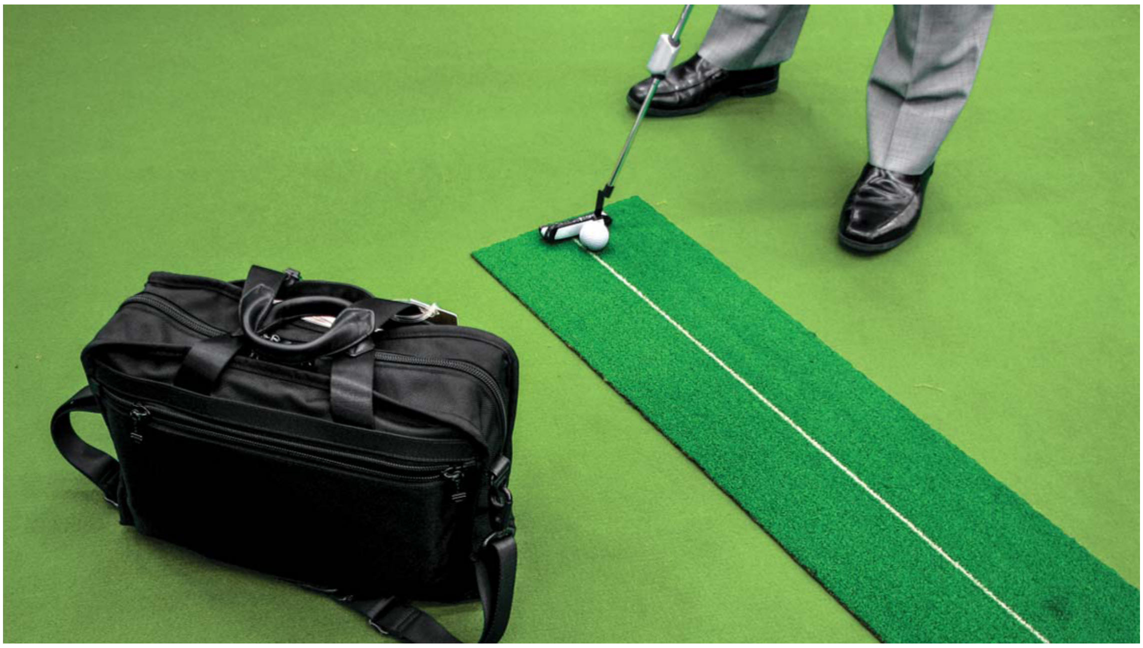


SALES

The Right Way to Use Compensation

by Mark Roberge

From the April 2015 Issue

I was the fourth employee hired at HubSpot. I'd met the two cofounders when we were all pursuing graduate degrees at MIT's Sloan School of Management. They're smart guys with a big mission: to help companies transform their marketing by using online content to draw potential customers to their websites—a practice known as "inbound" marketing.

My job was to build the sales team. An engineer by training, I'd never worked in sales—I'd begun my career writing code. But my background proved to be more of an advantage than I'd expected. It led me to challenge many conventional notions of sales management, using the metrics-driven, process-oriented lens through which I'd been trained to see the world. For instance, instead of hiring by instinct, I meticulously tracked data on sales, identified predictors of success, and looked for people whose traits and skills closely resembled those of our top sellers. Instead of training new recruits by having them tag along on a successful salesperson's calls, I created a regimented training program that gave them firsthand experience with our technology and then taught them to systematically work leads.

That approach worked well: Within seven years of its founding, HubSpot crossed the $100 million run-rate revenue mark and had acquired more than 10,000 customers in over 60 countries. In the fall of 2014 our company went public in an offering worth $125 million.

When I look back on the various strategies I used to grow our sales force from zero to several hundred people, I realize that one of the biggest lessons I've learned involves the power of a compensation plan to motivate salespeople not only to sell more but to act in ways that support a start-up's evolving business model and overall strategy.

Whether you're a CEO or a VP of sales, the sales compensation plan is probably the most powerful tool you have. Most of the critical strategic shifts that HubSpot made as a business were executed through changes to the sales compensation plan. In this article I will look at how we did this and at the general principles you should keep in mind when designing your own firm's plan.

VIDEO: Mark Roberge describes how HubSpot tailored its incentive system to each of its three growth stages.

Knowing What You Need and When

Business leaders often ask, "What's the best sales compensation structure to use?" It's a complicated question. The ideal plan is contextual—tailored to both the type of business and the stage of growth the company is in. Start-ups typically go through three key stages: customer acquisition, customer retention and success, and sustainable growth. In the first seven years at HubSpot, we used three different sales compensation plans, each of which was appropriate for the stage our business was in at the time.

1. The customer acquisition plan.

HubSpot's first compensation plan was oriented toward "hunting" new customers. When we put it in place, we had 100 customers and an annual run rate of barely $300,000. Like most start-ups at this stage of development, we needed to acquire customers quickly so that we could see how valuable our offering actually was to them. We'd been pretty good at gathering feedback from potential customers as we'd developed our product—which is true of most new ventures—but the real test would be asking customers for money.

The first plan paid salespeople a base salary and $2 up front for every $1 of monthly recurring revenue they brought in. To protect the company if customers defected, we implemented a four-month clawback on commissions. This meant that if a customer jumped ship within the first four months, HubSpot took the entire commission back (deducting it from the salesperson's earned commissions the next month). Once a customer had stayed on the platform for four months, the salesperson could keep the entire commission even if the customer later canceled.

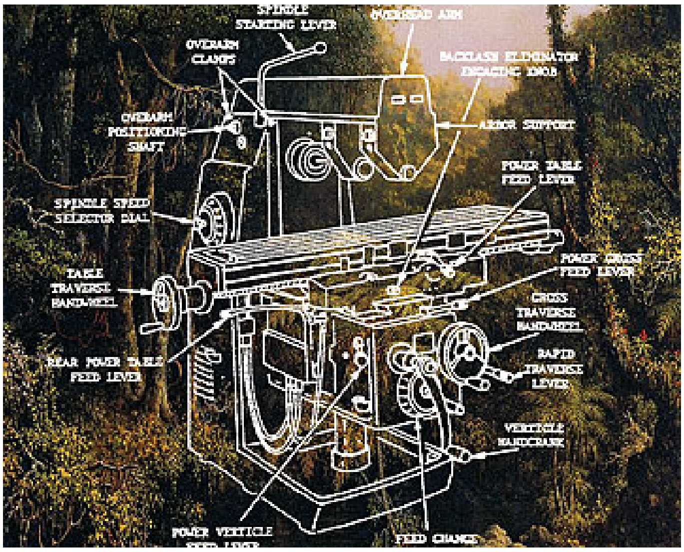
This plan was simple, clean, and hunting oriented. It worked well to accelerate the pace of new customer acquisition. In under six months our base shot up to 1,000 customers, and our revenue hit $3 million.

2. The customer success and retention plan.

With plenty of customers on board, we could now analyze how well the company was progressing toward "product/market fit"—the point at which product features and pricing are aligned with the market's preferences. The biggest sign that the fit wasn't perfect was a clear problem with customer retention. Among our early customers, the level of churn was unsustainable. This was not surprising. It's rare that a start-up finds a fit on its first attempt with customers. That's why a fast feedback cycle, proper diagnosis of the issues, and quick, disciplined iteration are necessary during this stage. At this point in a start-up's evolution, it's key to figure out who your best customers are and what steps will make them successful.

Looking for answers, we studied the data. At the time, each new customer was being assigned a postsale consultant, who would set our service up and train the customer's staff in how to use it. Our first theory was that some of the postsale consultants were doing a better job than others. If we could identify which consultants were most successful, we could dig into their processes, understand what they were doing differently, and introduce the best practices across the team. However, when we examined customer churn by postsale consultant, the levels were similar across the team. That particular theory didn't check out.

FURTHER READING



Motivating Salespeople: What Really Works

Feature by Thomas Steenburgh and Michael Ahearne

Companies fiddle constantly with their incentive plans—but most of their changes have little effect. Here's a better approach.

Next we analyzed customer churn rates by salesperson. Eureka! Here was our answer. Across the organization, there was a more than 10-fold difference between the lowest and highest churn rates among salespeople. We did not have a customer onboarding problem. We had a sales problem. Our customer retention was predicated on the types of customers the salespeople chose to target and the expectations they set with each new account.

I immediately shared the analysis with the sales team, revealing each salesperson's churn rate and how it compared with the team average. I educated the team on the importance of retention, both to our business and to our customers. I said that I would be adjusting the sales compensation plan, in order to align customer retention performance with commission checks.

Sure enough, the next quarter I followed through on my promise. I stack-ranked the sales team from the person with the best retention rate right down to the person with the worst rate. Then I segmented the team into quartiles. The top-performing quartile would earn $4 per $1 of monthly recurring revenue from then on. "Congratulations," I said to this group. "I'm doubling your commission payments. Why? Because you bring in the best customers. Keep it up."

I moved on to the next quartile. “Good work,” I said. “You now earn $3 per $1 of monthly recurring revenue—a 50% increase above your previous rate.”

“For the folks in the third quartile, there is no change. You will be paid the same rate of $2 per $1 of monthly recurring revenue.”

I concluded with the most difficult message. “For the fourth and worst-performing quartile, your earnings are cut to $1 per $1 of monthly recurring revenue. Why? Your customers are not succeeding. On average, they’re unprofitable for our company. More important, you are wasting our customers’ money by not setting proper expectations about how to succeed with our service. We have initiated training on better customer expectation setting. We need you to take that training seriously. We are here to help you through this skill development.”

The combination of a different set of incentives and better training worked: Within six months, customer churn had dropped by 70%. Once again, a sales compensation plan had driven the results of the business.

3. The sustainable growth plan.
Thanks in part to plan two, HubSpot had quickly closed in on product/market fit. Unrealistic expectations set by sales were now almost never among the reasons customers gave for quitting our service. Churn in general was far lower, and the reasons for cancellations were not alarming. It was time for our start-up to focus on achieving faster, profitable growth—in other words, scaling up the business. To do that, we had to align the sales compensation accordingly.

To ensure healthy growth, I needed to incorporate what we had already learned on our journey. I certainly wanted a strong incentive for the sales team to acquire new customers at a rapid clip. However, I needed to keep the team aligned with maximizing customer retention, since that would obviously offset acquisition costs and increase profitability.

FURTHER READING

One important insight we’d had earlier was that it was important for the customer to be committed to adopting inbound marketing.

What Entrepreneurs Get Wrong

Feature **by Vincent Onyemah, Martha Rivera Pesquera, and Abdul Ali**

A global survey shows most company founders regret waiting too long to start selling. An entrepreneur-friendly sales model can help.

Though it can transform the way an organization gets its message to customers, inbound marketing is not a turnkey solution. It takes work. Customers must understand that to succeed. We had already worked to get salespeople to set realistic expectations, but we now had to find a way to focus them on clients who would make a real investment (of time, energy, and money) in learning to use HubSpot's service. How could I align the sales team with this goal in a clear and measurable way?

The answer was advance-payment terms for new customers. When we looked at the data, we realized that our customers who paid month-to-month were less committed to the overall HubSpot service and were far more likely to defect. Those that prepaid annually were more committed to the service and ultimately were more successful. (Of course, advance payments also had a positive impact on HubSpot's cash flow—another factor that becomes important for a start-up as it reaches scale.)

As a result, our third plan was designed as follows: (1) Salespeople would earn $2 per $1 of monthly recurring revenue. (2) The commission would be paid out as follows: 50% on the customer's first month's payment, 25% on the sixth month's payment, and 25% on the 12th month's payment.

So if a customer signed up paying month-to-month, the salesperson would wait a full year to earn the last quarter of the commission for that customer. However, if the customer paid a full year's subscription in advance—a factor that was completely under the control of the salesperson—the entire commission would be earned immediately.

Before this plan was put in place, the average prepayment commitment was 2.5 months. After the plan was rolled out, that average jumped to seven months. Customer churn was checked; in fact, retention improved. The new customers were profitable to HubSpot. Salespeople felt in control of their destiny. Mission accomplished.

Before You Change the Comp Plan...

HubSpot is still a young and growing company, and we may have to adjust the sales compensation formula again as the business evolves. Drawing on what we've learned during our first eight years, my team has developed a few questions that we ask about any potential change: Is it simple? Is it aligned? And is it immediate?

Let me elaborate.

Simplicity.
Salespeople should not need a spreadsheet to calculate their earnings. If too many variables are included, they may become confused about which behaviors will lead to the largest commission check. They might throw the plan aside and just go sell the way they know best. The opportunity to drive the desired behavior through the compensation plan is lost. Keep the plan simple. It should be extraordinarily clear which outcomes you are rewarding.

Alignment.
Look ahead to the next year and ask yourself, "What is the most important goal the company needs to achieve? Customer count? Profitability? Customer success? Market share? New product distribution? New market penetration?" Once you've identified that goal, ask yourself, "How can the sales compensation plan be aligned with

Boosting Performance with Sales Contests

Contests are almost as effective as compensation plans when it comes to motivating the sales team. Contests bring a fun, dynamic aspect to a sometimes mundane daily routine. They can be designed to promote desired behaviors and, unlike commission plans, can be temporary. They can even be used to build team culture.

For these reasons, I ran a sales contest at HubSpot almost every month, especially in the early years of team development. Here are my six best practices for sales contest design:

1. Align the contest with a short-term behavioral change.

For example, fearing a summer slump, you may want to boost activity in June. This increase would be difficult to pull off through the commission plan, but holding an activity-based contest for one month would do the trick.

2. Make the contest team based.

This approach has a remarkable effect on team culture, especially early on. For the first three years at HubSpot, every contest I ran was a team contest. I'd often see high-performing salespeople help out teammates who were lagging, and the low performers would start working late to avoid letting their teams down. When I finally ran a contest based on individual performance, I heard accusations of cheating and saw backstabbing behavior for the first time. We immediately returned to team contests.

3. Make the prize team based.

Choose a reward that the team experiences together: Rent a limo to take the winners to a casino. Buy them a golf outing. Send them sailing for a day. Making the prize team based maximizes the positive impact on culture. The winners return to the office with photos of the great time they had—together. People feel good about their colleagues. Teams feel motivated to win the following month.

4. Send out updated contest standings daily.

At least once a day, publish the contest standings to the entire sales team (if not to the entire company), even if you have to compile and post them

this objective?" Don't underestimate the power of the compensation plan. You can tweak sales training, redesign marketing materials, attend customer conferences—you name it. Regardless of those efforts, if the majority of your company's revenue is generated by salespeople, properly aligning their compensation plan will have greater impact than anything else will.

Immediacy.

When salespeople succeed, they should see it reflected in their paychecks immediately. When they fail, they should feel the pain in their paychecks immediately. Any delay between good (or bad) behavior and the related financial outcome will decrease the impact of the plan.

Whenever I considered changing the compensation plan, I always involved the sales team in the redesign. To kick things off, I usually held a "town meeting" with the team. After communicating the goals for the plan, I would open up the floor to structural ideas. The brainstorming would begin. As the meeting progressed, I would manually. This is such a critical execution point. Without daily updates, contest effectiveness will drop precipitously.

5. Choose the time frame wisely.

The contest period needs to be long enough to bring about the desired behavioral change but short enough that salespeople stay engaged. A daily time frame is too short. Weeklong contests are on the briefer end of acceptable. A quarterly time frame is probably too long. Monthlong contests are ideal.

6. Avoid contest fever.

Don't read this and implement five simultaneous contests. Overlapping contests will dilute one another. Run one contest at a time for a given group of salespeople.

share some of the structures that were being considered and invite people to offer their feedback.

As a follow-up, I often created a page on the company wiki, reiterating the reasons for changing the plan, stating the goals, and describing some of the structures that were being considered. The conversation would then continue online with ideas and reactions. I responded to most comments. This digital format allowed salespeople to catch up on and participate in the conversation when they had time.

The ideal plan is tailored to the company's stage of growth.

Throughout the process, I was very explicit that the commission plan design was not a democratic process. It was critical that the salespeople did not confuse transparency and involvement with an invitation to selfishly design the plan around their own needs. Most of them appreciated the openness, even when changes were not favorable to their individual situations. During the process the sales team contributed some great ideas. Each commission plan change we made included at least one structural element that had originated from a salesperson during our discussions. Because of this involvement, when a new plan was rolled out, the sales team would understand why the final structure had been chosen.

Compensation is just one of the tools I learned to use while scaling up HubSpot's sales force. Our hiring, training, and sales coaching programs have also been vital to our success. The common thread among them is that they rely on close analysis of what works and what doesn't, rigorous use of data and metrics instead of intuition or improvisation, and systematically reducing what does work into a formula that can be replicated.

Am I recommending the same evolution of compensation plans for every business? Absolutely not. The sales compensation plan should reflect the type of business you're in and the stage of business you're at. The evolution of HubSpot's plan illustrates this point and provides a real-world example of the impact that a change in plan can have on business results. It also illustrates how, in an era when managers can access data on everything that happens inside their firms, successfully managing a sales force should be much less of an art and much more of a science.

A version of this article appeared in the April 2015 issue (pp.70–75) of *Harvard Business Review*.

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