



## Is Your Compensation Strategy Costing You Customers?

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When Graham Weston examined his firm's compensation plan two years ago, he realized that something didn't add up.

During one of his regular reviews of the compensation plan, Weston, executive chairman of Rackspace Managed Hosting, saw that the company's plan included an incentive for retention that actually caused customer dissatisfaction. Employees, "Rackers" in the company's parlance, received more money if customers maintained or expanded the Web and IT hosting services they paid for. "When a customer had a legitimate need to reduce its services with us, our retention metric helped foster resistance," Weston says. "We were essentially saying to customers who wanted to cut back on their service, 'No, we're not going to let you do that.' If you focus on certain metrics too heavily, you can end up at odds with your customer."

Unlike the many companies whose current compensation plans neglect customer outcomes, Rackspace detected and corrected the customer service "disincentive" lurking in its compensation plan. Today, a portion of Rackers' pay is determined by a combination of customer service and overall profitability measures. The compensation structure, not to mention Rackspace's organizational structure, supports its commitment to the "fanatical support" (a phrase the company has trademarked) of its customers.

While Weston asserts that incentive compensation related to customer centricity is the glue that holds Rackspace's fanatical service together, he also describes the management of those same measures as a "perilous process" that requires continual refinement.

### Service Disincentives

In fact, what sounds straightforward in theory—pay employees to help make customers happier and more valuable—is as difficult to put into practice in the first place as it is to maintain.

Just ask Lior Arussy, president of Strativity Group and author of *Passionate & Profitable: Why Customer Strategies Fail and 10 Steps to Do Them Right!* He, like many other customer strategy experts, has observed a raft of poorly structured incentive plans that drive employees to confound customers.

For example, one financial services company produced a credit-card advertising campaign so despised by consumers that, research showed, the ads drove customers and prospects to competitors' credit cards. Yet, that effect barely registered with the company's marketing team, which was being measured, and compensated, based on brand recollection—a measure the team achieved, although at the cost of new business. Another large company's sales force routinely accepted orders from customers who did not pay for more than a year. The reason? The salespeople were compensated based on booking orders, regardless of whether payment was ever collected. At another company, collections employees repelled customers, thanks to the nasty tone of their collection tactics. "The collections employees were asked a simple question," Arussy recalls. "Do you want the customer to stay after your interaction with them? They responded, 'We don't know, we just need to get this money because we are being measured on percent collected.'"

Correcting those sorts of customer service disincentives takes time, in large part because the problems run deeper than compensation levers. The right corporate culture, hiring and training processes, organizational structure, measurement, and reporting processes need to be in place if a company is going to motivate its workforce to embrace and execute its promise of customer centricity.

"The alignment between pay and customer service goes well beyond the sales force," says Mercer Human Resource Consulting Senior Consultant Steve Grossman, who notes that the effort requires the involvement of

sales, service, human resources (HR), marketing, product development, and operations. "It has to become part of your culture, not just the theme of the month."

John Reynolds, vice president of global human resources for Carlson Marketing Worldwide (1to1 Magazine's parent company), agrees. For the past 14 months he's helped guide an enterprisewide initiative that blends two interrelated strategic objectives: customer centricity and profitable growth.

During that time the company has completely done away with a traditional commissioned sales force approach and reorganized around multifunctional teams that focus on a portfolio of customers with common needs. It has also begun to implement a team-based bonus structure based on a well-balanced mix of customer service and profitability targets (at both the team level and the enterprise level). The progress has already produced benefits, notes Russ Johannesson, Carlson Marketing's executive vice president, U.S. client services. He reports that the new organizational structure and holistic compensation have fostered greater collaboration between customer teams.

### **Service Stems from Structure**

Rackspace's Weston agrees that a successful link between compensation and a customer-centric strategy necessarily extends beyond compensation. In fact, the link begins with culture and organizational structure.

Rackspace's fervent commitment to "fanatical" customer service—the company recognizes its service champions each year by presenting them with, among other rewards, straightjackets—belies a highly rational commitment to a team-based structure designed to support customers. Those teams serve and manage a portfolio of customers that share common needs. The teams consist of about 12 to 15 employees each, including a team lead, account manager, business development consultant, numerous technical support personnel, a billing specialist, and individuals responsible for data center operations and professional services. The entire team receives incentive compensation based on its success in meeting customer needs while contributing to the company's overall profit (not revenue) goals.

"It is important to be able to unite all the people who touch the customer so that they work together to achieve common goals," Weston says. "For example, if you give a collections person a compensation metric based on how much money you want them to collect, you'll get that money alright, but you'll lose customers... if your collections people collect too aggressively. You need to enable that team to think collectively."

Rackspace's incentive compensation structure does just that. The customer teams receive incentives based on quarterly Net Promoter scores (customers' likelihood to recommend) and a "True Profit" measure. The latter measure, which is based on economic value added methodology, essentially equates to net revenue: new revenue (from upgraded service or new customers) minus churn (customers who dial back their level of service or leave).

"We find the net [measure] is way more valid because it forces our people to work together," Weston says. "Our salespeople are not solely responsible for service upgrades in the same way that Ritz Carlton's reservationists are not solely responsible for booking return customers." Rather, Rackspace customers increase their services or refer other customers because of their satisfaction with all of the Rackers—from the technical support staff to the accounts receivable employee to the salesperson—with whom they interact. And Weston emphasizes that the company's culture and compensation "force our team to work together cross-functionally" to inspire that satisfaction.

### **A Balanced Bonus**

Although many compensation plans contain incentives that indirectly motivate employees to drive customers away, financial incentives and customer-centric incentives can coexist. The trick is striking the right balance.

Rob Kaplan-Sherman, senior vice president and managing director, research, of LRA Worldwide, agrees. He believes that a successful compensation program should aim to generate both high levels of customer satisfaction and impressive financial results. That pitch resonates with the numbers-obsessed culture of the

Professional Golfers Association (PGA) Tour, whose Tournament Players Club (TPC) Network operates more than 20 elite private golf course properties. The TPC hired LRA to help refine and strengthen the links between compensation and customer centricity that the organization first forged two decades ago.

"How you think you're doing and how your customer or member thinks you're doing are usually not the same," says PGA Tour Senior Vice President of Operations John Huggins. With LRA, PGA Tour Golf Properties developed surveys that go to members twice a year: Half of the members receive the electronic surveys in the middle of golf season and half receive them once the season concludes.

"We build our business plans club by club and rely heavily on the member survey results to do so," Huggins says. For example, if the surveys indicate that a particular club needs to get back to basics with its customer service, the annual business plan will contain training programs and compensation incentives related to measurements of name recognition, politeness, appearance, and other customer service fundamentals. This year's survey indicated that pace of play—the efficiency with which golfers can complete a round of golf (without delays caused by following slower-playing foursomes, for example)—needed improvement.

In response, the organization named a "champion," the organization's national director of golf, to lead improvement in that customer satisfaction area. After receiving his assignment, he had 30 days to research pace-of-play best practices by talking to managers whose golf courses posted the best pace-of-play figures and by asking customers for their suggestions. At the end of that 30-day period, the director formulated and recommended pace-of-play "best practices" that were rolled out to every property in the TPC Network. The next membership surveys will measure customers' satisfaction with pace-of-play improvements; the results will directly impact the entire staff's incentive compensation.

TPC Network's process for identifying and strengthening weak links in various customer service areas would not be as efficient as it is without several elements in place. Huggins emphasizes that the organization's hiring and training approaches enable a productive link between compensation and customer centricity.

The recruiting and hiring process is rigorous and includes extensive interviewing, skills and personality assessments, and background checks. What's more, all of the TPC Network's general managers are PGA members, a qualification that reinforces the company's laser focus on golf. Additionally, the company recruits from professional golf management programs at universities and has developed internship programs that attempt to cultivate future talent while gaining a recruiting advantage over competitors.

"It all starts with the hiring process," Huggins says. "If you hire people who can't deliver good service, you will not get there."

Once employees join the organization, they complete an orientation program about the PGA Tour's core values before starting their first shift. Customer service training programs also precede the first day on the job and remain an annual requirement (up to 10 classes per year) for all employees throughout their tenures. Finally, the company reports all of its customer-related measures to everyone in the organization and on the board of directors.

Only with those elements in place can a well-balanced incentive compensation plan tied to customer service objectives thrive, Huggins says. TPC Network's incentive bonus depends on five equally weighted levers that each comprise about 20 percent of a manager's incentive pay: customer satisfaction (as determined by the survey results); enterprisewide net operating income; employee satisfaction (also determined by a survey); initiation fees (revenue); and attrition measures. Of the last two incentives, Huggins notes, "You have to bring members in, and you have to keep them."

### **Perception vs. Reality**

Given the broad scope of successful customer-related incentive compensation programs, executives who realize that their current bonus structures provide little or negative motivation to strengthen service may feel extremely unhappy about the heavy lifting required to right the ship.

That's natural, says Strativity's Arussy, who notes that spotting compensation levers that promote lousy service represents an important first step. He also identifies a measurement progression many companies follow on their way to establishing more productive links between incentive compensation and customer service: They begin by tracking internal measures, like average handle time in the contact center, then they track customer perception (through surveys), and, finally, they measure customer action. "Consider the question, 'Would you recommend us?'" Arussy explains. "That is a perception. If indeed a customer is willing to recommend, the measurement should be, 'The customer provided us with three referrals.' I cannot take perceptions to the bank, but I can take three referrals to the bank."

Even companies with the most advanced compensation–customer-centricity links are only beginning to reach the final level Arussy describes. Both Rackspace and the PGA Tour rely on survey-generated customer satisfaction scores and then balance those measures against more "bankable" metrics, such as overall profitability and net profit on a per-customer basis.

"It's definitely an evolution that takes time," Carlson's Reynolds says. It requires a commitment to continually refine the compensation– corporate strategy equation so the results ultimately add up to customer centricity.