

REWARDING SALES EXCELLENCE

DRAWS AND GUARANTEES



Rewarding Sales Excellence

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A Draw is an incentive payout that is subject to recovery. Payouts received by the individual are advanced or "drawn" on future earnings and therefore are to be recovered against future incentive payouts. A Draw is provided to address short term cash flow issues either at the beginning of an individual's tenure within a sales incentive-eligible position or as a means of smoothing out income for salespeople with sales that occur with irregular frequency.

A Draw is an incentive payout advanced on future earnings to address short-term cash flow issues or irregular sales frequencies in sales positions. These payouts are subject to recovery against future incentive earnings.

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Key Aspects of Draw Duration and Payout

A Draw is defined according to:

Duration

The number of measurement periods for which the Draw is available

- The maximum number of performance measurement periods permitted for a Draw may vary by company, role, and position
- As part of the administration system configuration, the maximum Duration must be defined
- When assigning a Draw, any Duration up to the maximum can be selected
- Duration can be expressed only in terms of complete performance measurement/payout periods (i.e., 2 months, not 2.5 months).

Payout Amount

The discreet dollar amount or the percentage of available target incentive to be paid per measurement period under the Draw program.

- The maximum amount advanced should be 100% of available target incentive. It can be less than the maximum (e.g.: 70% of the target incentive).
- A different amount can be specified for each measurement period. For instance, the Draw could decline in magnitude in each period:
 - Month #1: 100%
 - Month #2: 50%
 - Month #3: 25%
 - Month #4: 0

Payment Type

A Draw can be paid as a lump sum amount or as a "top-up" to existing earnings (see examples below)

- Lump Sum – the pre-determined amount for the measurement period in question is paid in addition to the amount earned in the regular manner through the associated measure
- Top-up – A minimum incentive earnings amount is specified for each measurement period within the duration of the Draw. Should the rep generate incentive earnings in the regular manner through the associated measure that are less than the minimum amount defined, they would earn the actual incentive amount generated by the measure plus an additional amount that would bring them up to the minimum.

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Key Aspects of Draw Duration and Payout

If a Draw is implemented, every measure within the sales incentive plan must be addressed with regards to the Draw and the recovery. The Draw Payout Amount, Duration and Payment Type may vary for everyone, even those in the same position and under the same sales incentive plan based upon their incentive target. The timing of the payout for a Draw is the same as for the measure with which it is associated. For example, a monthly new revenue measure may pay out "... by the last day of the month following the month to which results are attributed". In this case, the incentive payout related to January transactions occurs by the end of February.

The total outstanding amount paid out under the Draw program is accumulated. The recovery of the accumulated payouts begins either at the end of each performance period, or after the expiration of the Draw.



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New Hires

The usual circumstances under which a Draw would be considered are when an incumbent in a sales role is a new hire, has been transferred into a new role, has been promoted, or is returning from an extended leave (maternity/paternity, STD, LTD). The draw provides the salesperson, new in the role, the time to learn the product, contact accounts and determine their needs. They also need to learn the company sales methodology and begin the new business development process. This onboarding period may result in few if any sales, so the draw is crucial to allow the salesperson to meet their personal financial obligations. Often, the Draw for the first few months is deemed non-recoverable. A Draw that is non-recoverable is called a Guarantee.

Generally, a New Hire Draw should be limited to two or three performance measurement periods (unless it is on-gong). Going beyond two to three periods creates complexity with respect to the recovery process which in turn can serve to undermine the goodwill associated with the Draw. It may also increase opportunities for the manipulation of the sales compensation program. For situations where income support is beyond the initial three measurement periods, a Guarantee should be considered.



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New Hires

The example below shows how a new hire draw can be utilized to provide a new salesperson with consistent cash flow while they get established with their new customers and learn the products and sales processes of the organization.

Example: New Hire Draw

Base Salary:	\$0	Hire Date:	January 1, 2022
Annual Incentive@ Target	\$100,000	Draw Period:	3 months
Target Total Compensation	\$100,000	Draw Amount:	70% of Target Incentive = $\$100,000/12 = \$8,333 \times 70\% = \$5,833$
		Draw Recovery:	

Period	Date Range	Draw Amount	% Recoverable	Actual Incentive Earned	Draw Top Up	Draw Paid	Amount Recovered	Incentive Payout
Period 1	Jan 1- Jan 31 2022	\$5,833	0%	\$1,115	= $\$5,833 - \$1,115$	\$4,718	\$0	\$5,833
Period 2	Feb 1- Feb 28 2022	\$5,833	25%	\$2,450	= $\$5,833 - \$2,450$	\$3,383	$\$3,383 \times 25\% = 845.75$	= $\$5,833 - \$845.75 = \$4,987.25$
Period 3	Mar 1- Mar 31 2022	\$5,833	50%	\$3,250	= $\$5,932 - \$3,250$	\$2,583	$\$2,583 \times 50\% = \$1,291.50$	= $\$5,833 - \$1,291.50 = \$4,541.50$
Period 4	Jan 1- Jan 31 2022	\$5,833	100%	\$11,520	\$0	\$0	\$0	\$11,520

The example shows that the plan is a full commission plan with no base salary. The amount of the draw is set at 70% of the Target Total Compensation (T.T.C. = \$100,000; Draw = $\$70,000/12 = \$5,833$ per month). The plan is for a new hire and the first period is in fact a guarantee since the % Recoverable is 0%. Therefore, the Draw amount is guaranteed regardless of the performance in that period. Should the salesperson sell more than the sales target and the incentive payout for the period is greater than the guarantee, the individual would also be paid any commissions that were in excess of the Draw. In this scenario, the amount of the Draw remains the same, but the amount that is recoverable (rather than a guarantee) increases. By the fourth performance period and beyond, any Draw is fully recoverable from future commission payouts.

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Consistent Draw



A **Consistent Draw** is also used in sales roles, markets and opportunities that have higher revenue per transaction and are inconsistent in closing thereby creating potentially uneven income for the plan participant. The Draw (versus a Guarantee) is especially appropriate in situations where:

- The average sales cycle and associated payment timeline is shorter than, or the same duration as, a single performance/payment period.
- When the mix is more heavily weighted towards the variable component or on full commission; and/or,
- An individual is expected to be able to sell at or near target performance after a relatively short period of time.

In these situations, the draw is typically recoverable, but at a rate that enables the participant to maintain their cash flow. The company can typically recover Draw amounts that are outstanding from payouts that exceed the Draw amount within a couple of performance periods.

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Implementing a Draw

A Draw is offered within the context of a particular sales compensation plan and co-exists with the associated measures in that plan. The transactions associated with the measure in question are tracked and generate incentive earnings in the normal manner. The Draw is paid out in addition to any regular incentives earned if the performance and payout is less than Draw amount. The process for implementing a Draw is:

1. Based upon the Base Salary, Incentive target and Target Total Compensation, and the comp plan that the participant is on, decide on the cash flow requirements and amount of the draw (either a fixed amount or a percentage of target incentive).
2. Determine the period of the Draw. Is it a fixed period (e.g.: 3 months, 6 months) or is it an on-going, consistent Draw?
3. Assess whether the Draw should be a lump sum payment, or a "top-up" based upon performance and incentive earned,
4. Identify the strategy/timing for recovery of any outstanding amounts (i.e.: 50% of any incentive payout that exceeds the Draw amount will be applied to an outstanding Draw balance).
5. Document the terms and period of the Draw either in the participant's plan document or in a letter to the individual.
6. Create the tracking and reporting to enable both the company and participant to view the status of the Draw (e.g.: amount(s) outstanding, amount(s) recovered, period remaining).
7. Implement a monthly/quarterly (depending upon the frequency of Draw payout) review/ 1:1 Review with their manager.
8. Regular approval/review of the status of all Draws by the Executive responsible for the sales force.



The amount of the accumulated Draw recovered in each performance measurement period must be defined in terms of the percentage of the actual incentive earnings generated by the associated measure(s) – i.e., 25%, 50%, etc. – to safeguard the individual's cash flow. This is typically expressed as a percentage of any incentive payouts that exceed the Draw amount for the period are applied to the outstanding Draw balance. This would continue in each subsequent measurement period until the total Draw amount advanced is recovered.

Any amounts earned via a Draw should be documented as a separate line item in the payroll system. Once the recovery starts, the total amount outstanding must be readily available, along with a history of payments recovered.

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Draw Documentation

A summary report displaying the following information is required to effectively manage Draws:

- Name
- Title
- Sales Incentive Plan
- Start Date in the Position
- Duration (by Measure)
- Payout % and Amount (by Measure)
- Duration remaining (by Measure)
- Amount Paid
- Amount Recovered
- Amount Outstanding

Contract Language:

As part of the compensation for the role, the Employee may, during his/her employment, receive a payroll advance against future commissions. This payroll advance is called a "Draw". The Employee understands and agrees that this Draw is an advance against future commissions earned, a loan, which the Employee is responsible to pay back to the Employer by way of earned commissions or other means.

The Employer may at its discretion, implement, change, reduce or eliminate the draw amount at any time with 15 days' notice to the Employee. Should the Employee's employment be terminated for any reason (voluntary or involuntary) and should the Employee's commissions earned fail to cover his/her Draw Balance, the Employee understands and agrees that he/she shall be responsible to repay to Employer, upon demand by Employer, any portion of the Draw which was not satisfied by earned commissions. Furthermore, any remaining Draw Balance will be deducted from the Employee's final pay cheque (regardless of the type of pay included in the pay cheque. For example: base salary, vacation payout, commissions, bonus, etc.).

The Draw will be implemented as follows for the compensation plan period:

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Draw Documentation

The Draw will be implemented as follows for the compensation plan period:

Participant's Name:

Sales Role Plan:

Duration of the Draw

The Draw will be implemented for the full plan year unless changed or terminated by the employer at their discretion. The Draw will be spread across each plan measure at the same percentage as the weight assigned to the measure from the individual's target incentive. Draw advances will be paid out at the same frequency as the incentive payouts for each measure (i.e.: if the plan measure pays out quarterly, the Draw for that measure will be paid out quarterly as well). ■

David Johnston, with over 35 years of experience in sales compensation and strategy, brings a wealth of knowledge and expertise to the field of intangible asset sales. As a seasoned professional, Dave has helped numerous organizations navigate the complexities of selling intangibles, driving revenue growth and market success. For more information or to review the status of your current program, reach out to Dave at djohnston@salesresourcegroup.ca or by phone at (416) 805-0208.



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