MAFSI

Manufacturers' Agents Association for the Foodservice Industry

CASE STUDY:
HOW REDUCED COMMISSIONS AFFECT A SALES AGENCY

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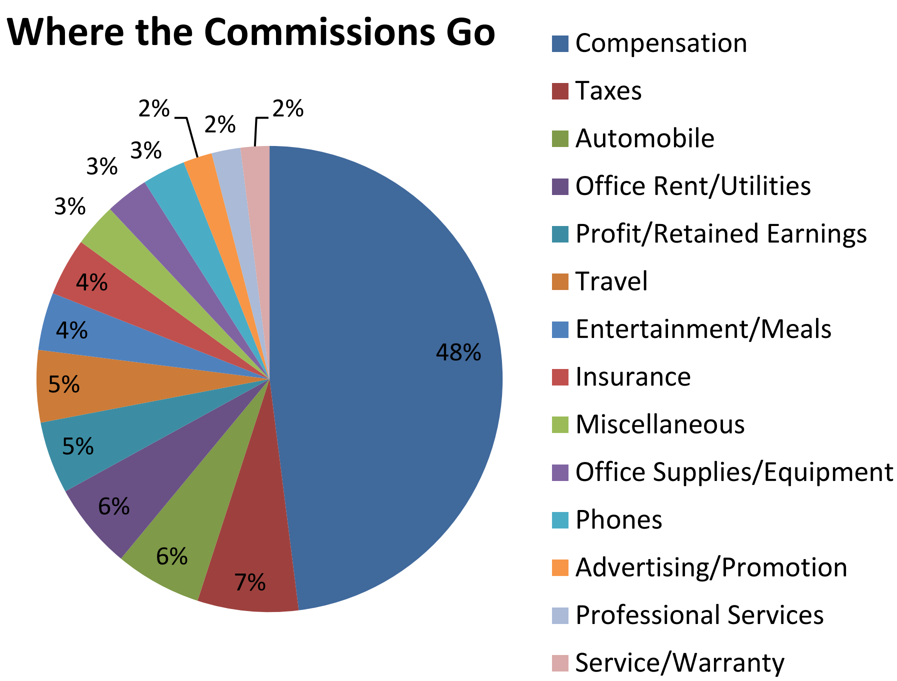
Commission is the life blood of any manufacturers' agents organization. Commission is the gross revenue received from the manufacturer to market their products in a specific territory. In an effort to better educate our members and manufacturers, we have asked some agencies to supply us with percentage information on how their GROSS REVENUE is dispersed within their organizations. Hopefully, we can all better appreciate how our gross revenue is used and understand that when our gross revenue is reduced disproportionally to the manufacturers we all lose.

Sales Agency Gross Revenue Breakdown



Example 'A'

$1000.00 sale to customer (full price)
10% commission line

Gross Revenue to factory	$1000.00
Gross Revenue to Agent	$100.00
Adjusted Gross Revenue to Factory*	$900.00

Factory determines that to get above order it must reduce its price by 5%. At this point, factory has agreed to reduce Gross Revenue to $950.00 for this particular sale.

The FAIR reduction in commission to the agent should be as follows:

Gross Revenue to Factory	$950.00
Gross Revenue to Agent	$95.00
Adjusted Gross Revenue to Factory*	$855.00

The factory has reduced its Gross Revenue by 5% ($900.00 to $855.00 = $45.00 or 5%). The agent has reduced his Gross Revenue by 5% ($100.00 to $95.00= $5.00 or 5%). Commission level doesn't change nor does the effort required in marketing the product. Both factory and agent have agreed to proportionally reduce their gross revenue to achieve the sale.

*Factory Gross Revenue less Agent's Commission (AGR)

Example 'B'	
$1000.00 sale to customer (full price)	
10% commission line	
Gross Revenue to factory	$1000.00
Gross Revenue to Agent	$100.00
Adjusted Gross Revenue to Factory*	$900.00

Factory decides that to get above order it must reduce its price by 5%. Factory has agreed to reduce its gross revenue to $950.00 for this particular order.

Another approach, some factories use is to reduce the commission level proportionally to the gross revenue reduction the factory has agreed to in this case - 5%

A 5% reduction in the agent's gross revenue (commission) for this particular sale would equal a commission rate of 9.5% (10% gross revenue (commission) less 5% reduction = 9.5%) commission rate.

$950.00 x 9.5% = $90.25 Gross Revenue to Agent

Gross Revenue to Factory	$950.00
Gross Revenue to Agent	$90.25
Adjusted Gross Revenue to Factory*	$859.75

In this method, the real % reduction for the factory from the original adjusted gross avenue figure of $900.00 is 4.47%

The gross revenue reduction for the agent in this case would be 9.75% ($100.00 to $90.25).

In effect, the agent has reduced his original gross revenue (commission) from $100.00 to $90.25, a reduction of $9.75 or 9.75% from the original $100.00 gross revenue (commission) amount. The factory has reduced adjusted gross revenue by 4.47%.

Example 'B'	
$1000.00 sale to customer (full price)	
10% commission line	
Gross Revenue to factory	$1000.00
Gross Revenue to Agent	$100.00
Adjusted Gross Revenue to Factory*	$900.00

Factory decides that to get above order it must reduce its price by 5%.

Factory has agreed to reduce gross revenue to $950 for this particular order.

Factory now tells agent that the 5% reduction will be handled as follows:
2 ½% to Factory
2 ½% to Agent

Agent's Gross Revenue (commission) will be reduced from 10% to 7 1/2%—a reduction of 25% (NOT 2 ½%)

Gross Revenue to Factory	$950.00
Gross Revenue to Agent	$71.25
Adjusted Gross Revenue to Factory	$878 .75

The AGR figure of $878.75 is $21.25 below the full price AGR figure of $900.00. The factory actually had a % reduction in AGR of 2.36% while the agent was asked to reduce his gross revenue (commission) from $100.00 to $71.25, an actual reduction of 28.75%.

Conclusion

In all three (3) examples, the gross revenue reduction to the agent has been handled differently.

The factory went from a 5% reduction in their adjusted Gross Revenue figure to 2.36%. The agent went from 5% to 28.75%. The dramatic differences are the result of a simple 5% reduction in selling price.

Can you imagine what happens when a factory discounts an order by 10% and asks the agent to reduce his gross revenue by 50%?

The agent must be a business partner with his or her manufacturer. They must work together to obtain the desired business within each agent's territory. There must be an understanding of each others operations and the costs each has in running their respective businesses!

When a manufacturer disproportionally reduces an agent's gross revenue, he sends a strong signal to the agent indicating:

1. He doesn't want to he a business partner with the agent;
2. His financial stability is far more important than the agents;
3. He has no understanding of what costs are really involved in running an agency.

If a manufacturer reduces an agent's gross revenue by 50%, does that manufacturer expect a 50% reduction in the agents effort to market his products? Will the agent approach the sale of that manufacturer's products with the same enthusiasm and effort, knowing he will always be treated disproportionally if an additional discount is given?

	Standard (FULL)	Example 'A'	Example 'B'	Example 'C'
Sale Price (Dollars)	$1000.00	$950.00	$950.00	$950.00
Gross Revenue Factory (Doallars)	$1000.00	$950.00	$950.00	$950.00
Gross Revenue (Commission) Agent (Dollars)	$100.00	$95.00	$90.25	$71.25
Adjusted Gross Revenue Factory (Dollars Less Agent's Commission)	$900.00	$855.00	$859.75	$878.75
Factory Reduction In Adjusted Gross Revenue	0%	5%	4.47%	2.36%
Agent Reduction (%) In Gross Revenue (Commission)	0%	5%	9.75%	28.75%