

COLUMNS

Inside Network Marketing

Deconstructing MLM pay plans

What you aren't supposed to know CAN hurt you.

by Leonard W. Clements

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Compensation plan design goes way beyond just picking how many levels you're going to pay and how to divvy up the percentages. In fact, compensation theory, as it relates to MLM, is an evolving, every expanding goulash of mathematical, psychological, artistic, and historical factors. Even most professional compensation plan designers have taken little time to study and understand all this (there are a few rare exceptions), let alone those independent distributors who are, for the most and in large part, basing their MLM careers on the quality of their chosen compensation system.

Yes, the quality of one's products should be the dominant decision making factor, and there is certainly a trend over the last few years in that direction, but alas, that's still the way it should be, not the way it is.

The vast majority of MLM compensation plans today are an ill-conceived hodge-podge of bits and pieces of other pay plans that the designers, usually the company founders, just thought were cool. Little, if any, regard is given to how the components work together synergistically, what they are suppose to 'incentivize', how appropriate they are for the types of products being offered, how well they've worked in the past, and in way too many cases what it will cause the plan to pay out— now, and in the future. Many pay plans today were developed with little more study than

who's hot, what kind of plan are they using, and how can we make it just different enough to not look like we copied them?

Fortunately, the compensation plan isn't the most important factor.

Indeed, it is arguably not even an important factor at all! As history has shown us countless times, even a poorly designed, or just weak paying, pay plan can still generate substantial incomes. And conversely, pay plans with potentially superior pay outs routinely fail.

Think of every compensation plan as a big machine. In one end flows product volume, and out the other come your commissions and bonuses. After all, isn't that what a compensation plan is supposed to do— convert sales volume into commissions?

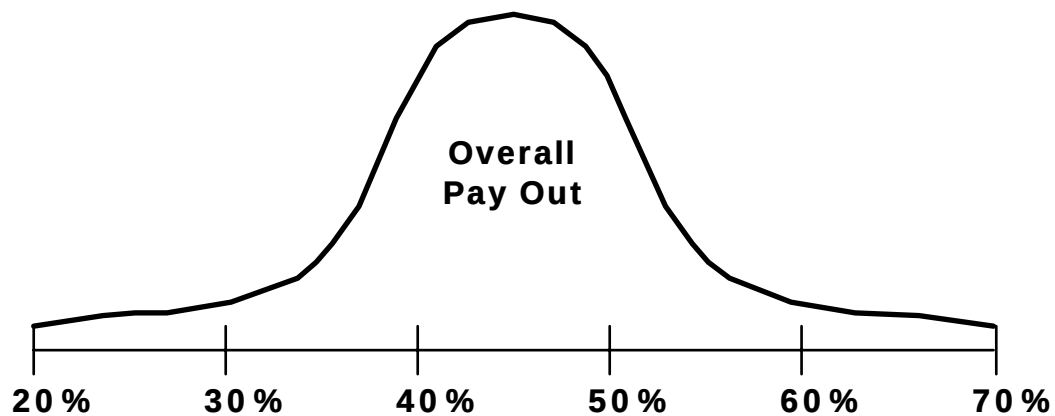
Today it seems every MLM company out there is doing everything they can to convince us that their machine is more efficient at this process than everyone else's.

To show off their compensation machine they paint it with pretty colors, add flashing lights, loud sirens, and all kinds of other fancy bells and whistles. They change the shape and size of the machine, add various accessories and attachments, and sometimes they'll even connect two or three types of machines together.

They'll give them bold, exciting names, make them customizable, and sometimes they'll even claim they've patented their machine (of course, the patent is always "pending"). About the only thing they don't offer is a lifetime warranty! All of this effort to create the perception that their machine works better (translation: pays more), than anyone else's. Do they? Probably not.

Looking at this issue from the most macro view, the plain and simple truth is that if you were to put the exact same amount of product sales volume into 90 percent of the compensation machines out there, just about the same amount of commissions would come out the other end. The vast

majority of them are paying out bonuses and commissions around 45 percent of every commissionable dollar coming in, give or take five percent.



Many prospects today judge a pay plan by doing little more than adding up all the percentages on all the levels, assuming the highest sum must be the best paying. It rarely is. In fact, the total percentage pay out, the number of levels a plan pays, and even the plan type (Breakaway, Unilevel, Binary, and Matrix) are not the most important factors to consider when comparing pay plans. What are? Good question.

There are two things that most determine how well a compensation machine is going to work in actual practice (forget theory— they all make you rich on paper). First, and most important, is how much sales volume is going into the machine. Your machine could be designed to pay 20 percent down each of 10 levels and not a penny will come out the other end if nobody buys anything. 200 percent of zero is zero! Sales volume is the fuel that runs your compensation machine. No fuel, no compensation— I don't care how many levels it pays or what the total pay out is.

The sales volume producing potential of the product line is the primary factor when judging the income potential of an MLM opportunity.

The second factor you should consider is the pay out "weighting". That is, how and to whom the commissions are being paid at various stages in the plan.

For example, let's assume two MLM companies with 10,000 distributors pay \$1-million to the field in commissions and bonuses. In other words, both compensation machines produce the same result, although their mechanisms may be very different. However, one machine distributes \$100,000 to the five top distributors, and \$50,000 to ten others, and nothing to the other 9,985 (this would be a "back weighted" plan).

The other plan pays \$200 to all 5,000 distributors (a "front weighted" plan).

Although both plans are paying out the exact same amount (50 percent of \$1,000,000) they each offer you a very different income opportunity (the examples used here are intentionally and extremely exaggerated).

If you are among the 86 percent (based on a ten year MarketWave survey of over 6,700 distributors) who's "primary" income goal isn't to get rich, but rather to make enough to quit your job and comfortably live off your residual MLM income (they try to get rich later), over half the pay plans offered in the US today are *not* designed to optimize that potential level of income. That is, they are not "middle weighted" plans. And likely over 90 percent of the reps in those MLM programs don't even know it. In fact, based on a more recent MarketWave survey of generally more experienced networkers, 34 percent of them have never even heard the term "pay out weighting" before!

What's even more disconcerting is the realm of compensation theory designed to manufacture well hidden "breakage."

That this, income which the plan was suppose to pay out, but, instead, was retained by the company. Or, those designed to create illusionary income. That is,

income you receive in theory, but usually never receive in real life.

It's the "smoke & mirrors" school of MLM pay plan design. Have you ever heard the saying "If you can't dazzle 'em with brilliance, baffle 'em with BS"? Sometimes I think the guy who made up that line was an MLM pay plan designer.

For example:

Did you know that the ability in some unilevel and matrix plans to "double dip", that is, enroll your spouse, or even yourself, on your own first level, will likely cost you more income than you will gain from the extra position?

Did you know that binary plans, which allow you to place reentry positions *above* your original position, have no greater potential for income than those who require a downline placement— and can even cause your income to increase at a *slower* rate?

Did you know that a plan that pays 10 percent down six levels (60 percent) can easily create a *smaller* commission check than one that pays 9 percent down five levels (45 percent)— even if you have *more* wholesale volume in the six level plan?

Did you know that "infinity" bonuses *never* pay down to infinity, or that "no flushing" binary plans *always* flush?

This is the kind of stuff I'm going to be covering in the next few issues of this TheNetworkMarketingMagazine.com. This installment is more of an overview of things to come.

And don't worry, I'm not going to spend a lot of time dragging you down into the minutia of compensation theory, you won't have to take a crash course in calculus, nor will I even attempt to compare the pros and cons of the various comp plan types (a subject already covered, ad nauseam, by a hundred other MLM authors— with 100 different outcomes).

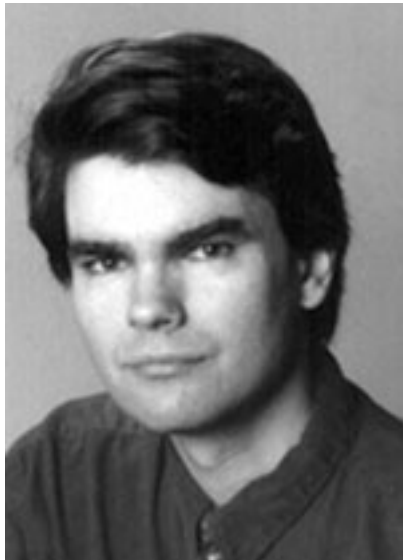
I'm going to render down the whole 'let's compare comp plans' game to only those aspects that really matter.

And, much like a renegade magician who's been ostracized by his peers for revealing how the trick works, I'm going to expose how all the compensation plan tricks work.

My hope is that, like revealing the secret behind an illusion, it will lose its power to persuade.

Third Issue, December 2005:

BV BS – The Use and Abuse of "Bonus Volume."



Leonard Clements has concentrated his full-time efforts over the last 15 years on researching and analyzing all aspects of Network Marketing. He is a professional speaker and trainer, and a court certified expert in the field of network marketing. Len is the author of the controversial book *Inside Network Marketing* and the best selling audios *Case Closed! The Whole Truth About Network Marketing* and *The Coming Network Marketing Boom*.

To learn more about Len and his company MarketWave, receive his free MarketWave Alerts and explore the rest of his resources and products, visit: MarketWaveInc.com or call, toll free: 1-800-688-4766.

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