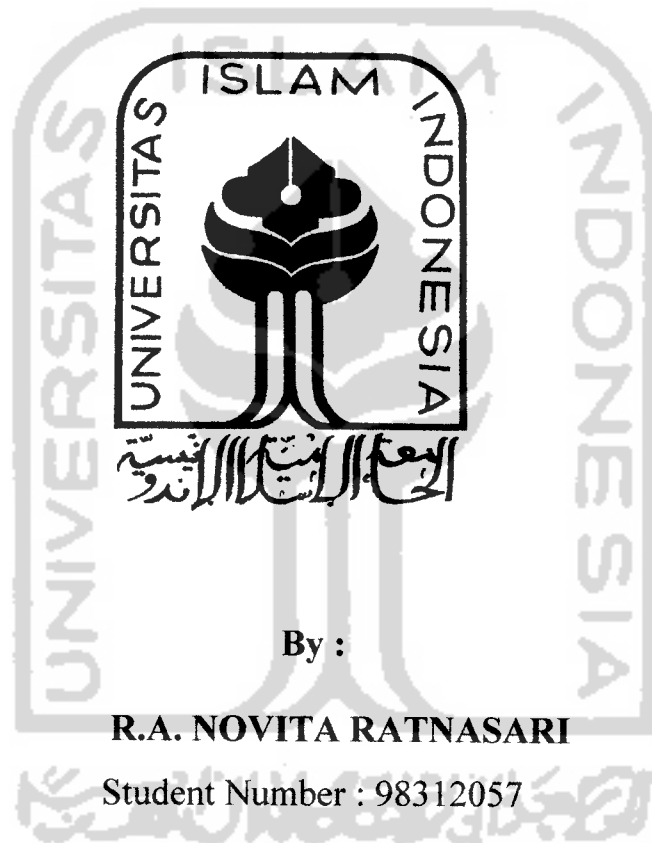


**THE ANALYSIS OF COMPENSATION SYSTEM
(CASE STUDY ON PT. LUXINDO RAYA)**

A THESIS

Presented as Partial Fulfillment of the Requirements
To Obtain the Bachelor Degree in Accounting Departement



By :

R.A. NOVITA RATNASARI

Student Number : 98312057

**DEPARTEMEN OF ACCOUNTING
INTERNATIONAL PROGRAM
FACULTY OF ECONOMIC
ISLAMIC UNIVERSITY OF INDONESIA
JOGJAKARTA
2005**

**THE ANALYSIS OF COMPENSATION SYSTEM
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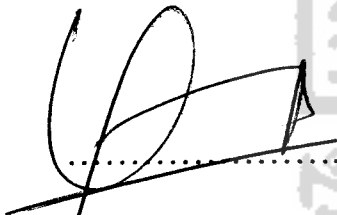
By

R.A. NOVITA RATNASARI

Student Number : 98312057

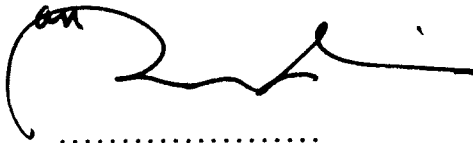
Approved by

Content Advisor,



December 10,2005

Language Advisor,



December 10,2005

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A BACHELOR DEGREE THESIS

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Student Number : 98312057

Defended before the Board of Examiners
On December 30, 2005
And Declared Acceptable

Board of Examiners

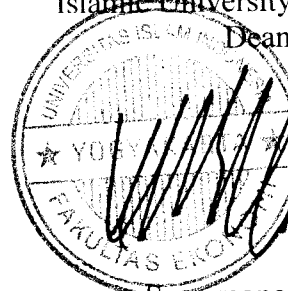
Examiner 1

Samsul hadi, Drs., Ms., Akt

Examiner 2

Yunan Nadjamudin, Drs., MBA., AK

Jogjakarta, December 30, 2005
International Program
Faculty of Economics
Islamic University of Indonesia
Dean



Suwarsono, Drs., MA

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Lily

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ABSTRACT

Compensation system in a company is really important because it relates with reward for its employees. If the used compensation system was not satisfied the SR's, they will be not loyal to the company. But in the other hand, the company is trying to create efficiency.

LUX is using single system of compensation. It pays their SR's based on variable salary of selling products. The fixed salary was given only for the first three months on the training period. Then, the salary is given only based on how many point the SR could collect by selling some unit products.

In the other side, this system is not satisfying SR because there are no reward when will SR cannot come for example they are sick. But if they can sell many products, they will get a big reward too. This company called this system as unlimited salary. According to the researcher analysis, this single system cannot influence the SR to offer the company products actively. It can be proven from the SR's data that there are many SR's joint and so does SR's quit in the company. So, it is better for company to pay the salary for time when SR's cannot come as fixed salary. Even though it is in small amount of money it can create SR's loyalty.

ABSTRAK

Sistem kompensasi dalam suatu perusahaan merupakan masalah yang paling rumit karena menyangkut balas jasa perusahaan kepada pegawainya. Bila sistem kompensasi yang digunakan perusahaan dirasa tidak memuaskan pegawai, mereka tidak akan loyal kepada perusahaan. Padahal disisi lain perusahaan mencoba untuk menekan tingkat efisiensi semaksimal mungkin.

LUX menggunakan sistem kompensasi tunggal yaitu membayar pegawainya (sales representative) dengan gaji tidak tetap berdasarkan banyaknya produk yang dapat mereka jual. Gaji tetap justru diberikan hanya pada masa pelatihan yaitu tiga bulan pertama SR menjadi pegawai diperusahaan selanjutnya pegawai hanya menerima gaji tidak tetap yang dihitung berdasarkan banyaknya point yang dikumpulkan dari penjualan tiap unit produk.

Sistem ini disatu sisi tidak memuaskan pegawainya karena tidak adanya balas jasa untuk waktu dimana mereka tidak dapat bekerja misalnya sakit. Tapi disisi lain bila mereka mampu melakukan penjualan banyak merekapun mendapatkan balas jasa yang besar pula perusahaan menyebut balas jasa ini sebagai penghasilan yang tidak terbatas. Berdasarkan hasil penghitungan yang dilakukan penulis sistem ini tidak mampu mempengaruhi pegawainya dalam bekerja. Hal ini terbukti dari banyaknya pegawai yang keluar masuk dalam perusahaan. Jadi alangkah baiknya bila tiap perusahaan membayarkan upah untuk waktu-waktu dimana pegawai tidak dapat masuk bekerja. Walaupun kecil upah tersebut mampu menciptakan loyalitas pegawai pada perusahaan.

CHAPTER I

INTRODUCTION

1.1. Study Background

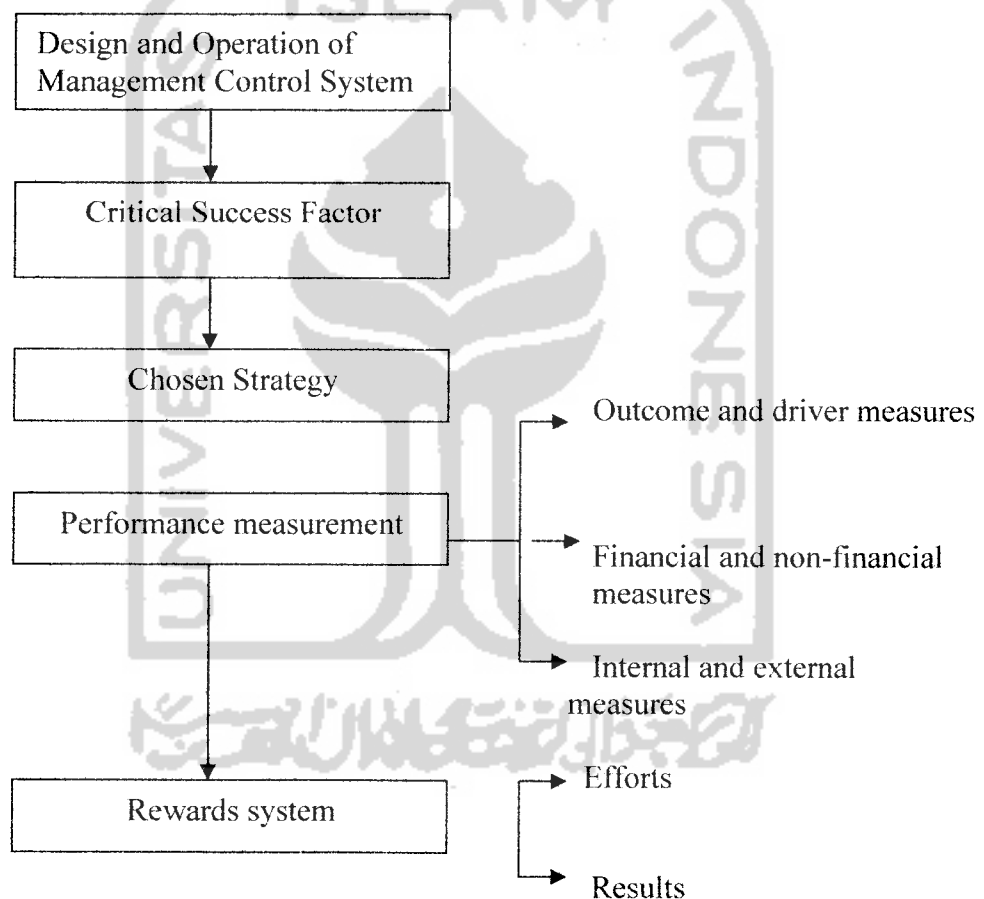
Control system is one of important system used by company to ensure that all company activities run in right way to achieve the company goal with effective and efficient program. The activities of management control are planning, coordinating, communicating, evaluating, deciding and influencing. The control system includes the activities such as strategic planning, budget preparation, program execution and program evaluation. By applying management control system a company can implement the right strategic planning to achieve the company goal because the right strategic can enable the goal be achieve more effectively and efficiently. One of important strategic planning is the compensationsystem, which tries to give rewards to company employee's conform with their contribution for the company goal.

One of the important strategic planning is the compensation system, the compensation system try to give rewards to company employee's conform with their contribution for the company goal.

People learn to say "thank you" for any object, service, or compliment received. In some circumstances, the thank-you is an adequate recompense, in different circumstances the thank-you needs to take on a substantial form, like a payment in kind or money. In work relationship, compensation takes the form of salary and wages a variety of benefits in non-economic rewards such as challenging assignments and praise from supervisor (Rahindra and Manuel, 1992)

Before the researcher talks more about compensation, the researcher tries to make the outline of management control system, performance measurement and relate it to the compensation or rewards system

The Out line Of Performance measurements And Compensation System



(Garry Dessler, p:421) compensation refers to all forms of pay or reward going to employees and arising from their employment, it has two main components:

1. Direct financial payments, wages, salaries, incentives, commissions and bonus.
2. Indirect financial payments in the form of financial benefits like employer paid insurance and vacations.

Generally compensation can be defined as "*the reward*" for employee because of their contribution and participation in achieving company goal. Whether in financial form or non-financial form.

The reward itself comes from two components, efforts and results (William J. Stanton & Rosane Spiro, Management of Sales Force). It can be figured as below:

$$\text{REWARDS} = \text{EFFORTS} + \text{RESULT}$$

Efforts, workers must believe that if they expend greater effort, it will lead to performance improvement. If they believe this, they will be motivated to put forth greater effort. Otherwise, they will not expend that effort regardless of the potential for reward. For example, if the worker believes that introducing products to new customers will lead to improved performance, they may be motivated to introduce the product to many new customers just in one time, but this will not lead to significantly improved performance. That means workers must correctly understand the reasons for their success and failures.

Results also called performance, not only sales value rewards, but workers must also feel that attaining them is conditional upon performance. If the rewards are pretty much the same regardless of how good or bad that

performance is, then the rewards will not be effective motivators. Workers must also understand exactly what must do to get rewards.

Practically, compensation payoff based on results and not efforts. However, it is nice of course if both elements are combined to measured the compensation. Although the key to rewards in most cases is results.

Compensation is what employee receive in exchange for their contribution. When managed correctly, it help the organization achieve its objective and obtain, maintain, and retain a productive workforce. *“Managers (Anthony & govindarajan, 1998) typically put a great deal of effort on activities that are rewarded and less activities that are not rewarded.” Compensation system is one of systems that do not reward the behaviors leading to organizational goals or do reward the behaviors countering the goals.*

Two philosophies on incentive compensation (Anthony and Govindarajan):

Fixed pay

Recruit good people



Pay them well



Expect good performance

Performance-based pay

Recruit good people



Expect good performance



Pay them well if performance is actually good

Compensation is one of control system in organization. With which employees in one organization can be motivated and encouraged to achieve organizational objective. However it is not an easy way for company to decide payment for the employee as high as they want. In one side company wants to pay their employee more then other company to prevent their employee move to their rival company and on the other side, company needs to make the budget for cost in minimum rate. Nowadays many company use compensation system as solution to let the company cost works efficiently. The company decides to pay wages and salary in minimum rate instead they give many rewards for employee participating and contributing to support company program.

Compensation can be classify into two group:

1. Economic rewards

- Cash payments: Base pay, Merit pay, Incentive plans, Cost of Living (COLA)
- Benefits: Income protection program, Reimbursed time off, Services and perquisites

2. Non-Economic rewards

Interpersonal and Personal growth

Compensation system is aimed:

1. To get qualified human resource
2. To retain valued and productive employee

3. To comply with the requirements of pay equity
4. To promote attitudes conducive to loyalty and commitment to the organization, high job involvement, and job satisfaction
5. To stimulate employee growth that enables the employee to accept more challenging positions
6. To comply with the related laws.

Rewards system is considered important in organization management control system, because without adequate compensation, current employee are likely to leave and consequently, the company will have to recruit new employees, a process which is not easy to do.

Compensation very important to employee as individual because the amount of compensation shows the value of employee among others employee, family and society. The fixed compensation rank decide the employee life scale beside that the variable compensation rank show the status and price of them. Because of that if the employee feel unsatisfied with the compensation received their performance, motivate and desire of work can dramatically decrease.

Regarding many consideration about the benefit and useful information from the observation, the researcher takes a research entitle:

**‘THE ANALYSIS OF COMPENSATION SYSTEM, CASE STUDY
ON: PT LUXINDO RAYA’**

1.2 Problem Identification

The research tries to identify the capability of existing compensation system to satisfy both company and their workers.

1.3 Problem Formulation

Based on the study background above, the problems of the research can be formulated as follows:

1. What kind of existing compensation system used by company?
2. Can the compensation system influences sales team to achieve company goal?

1.4 Limitation of research area

1. The compensation system was based on the vision and mission of the company
2. The researcher only consider the compensation system used by PT. LUXINDORAYA jl. P. Mangkubumi no 57

1.5 Research Objective

1. understand and analyze the compensation system use by company
2. How can the compensation satisfied both side, the company and the workers.

1.6. Research Contribution

1. The result of this research will be useful for company to understand the compensation system used already satisfied their worker or not.
2. This result of this research might be useful for others company, they can implement the system if they show it work well in the same business unit.
3. This research will be useful for the researcher in giving her understanding about the compensation system theoretical and practical.
4. This research is considered as a part of academic final assignment for researcher in order to fulfill the academic prerequisite to get the degree of economic bachelor in the faculty of economic, Islamic University of Indonesia.

1.7. Research Method

1. Type of Research Method

The research method conduct in this research is qualitative method. The researcher will be collect the company data that is related with the compensation system and then analyze it.

2. Research Subject

The subject of the research is PT LUXINDO RAYA, jl. P. Mangkubumi No. 57 Yogyakarta

3. The Source of Data

- 1) General Data
 - a) Company profile

- b) Organizational structure and job description
 - c) Other data that relate to this research
 - 2) Specific Data, related to the data needed in accordance with compensation perspective:
 - a) The system used by company
 - b) The procedures of salary and wages paid
 - c) The product or facilities
 - d) The customer
 - e) Other data that related to this research
4. Data Collection Method
 - 1) Literature method: this method is used to get an understanding of compensation system and other theories that related to it.
 - 2) Interview and Discussion

Interview process is done through questions and answers directly with the competent parties. The discussion process is the exchange of knowledge between the researcher and the competent parties of the company. The topic relate in that process are about: working time schedule, salary and wages paid and those related information with compensation given.
5. Technique of data analysis

This research will use the qualitative approach or non-statistical data in analyzing the problems.

After all data are obtained, then I will begin to analyze those data.

The steps that are going to be conduct are:

- 1) Classifying the data obtained for compensation paid. The data must be complete and conform the problem and the purpose of the research.
- 2) Describing the steps for compensation paid by company by using researcher personal idea from literature study to support the explanation.
- 3) Analyze each steps for better understanding
- 4) Analyze the strength and weaknesses of company compensation system.
- 5) After the analysis complete, arranging and writing the report of the analysis will be done. Whether it bring advantages or disadvantages to the users the researcher will give necessary recommendation and suggestion.

1.8. Thesis Contents

The main features for this thesis contents can be described as follows:

Chapter I Introduction

This chapter will discuss about study background, problem Identification, problem formulation, problem limitation, research objective and research benefit.

CHAPTER II

THEORETICAL FRAMEWORK

2.1. Motivation and Reward

Management compensation is an important mechanism that encourages and motivates managers to achieve organizational objectives. Managers typically put forth a great deal of effort on activities that are rewarded and less on activities that are not rewarded. Numerous examples exist of compensation system that do not reward the behaviors leading to organizational goals or do reward the behavior countering the goals.

The solution to the management problem of motivating people to behave in a way that furthers the goals of the organization relies on the relationship of organization incentives to personal goals. Individuals are influenced both by positive and negative incentives. A positive incentive, or “reward,” is an outcome that results in increased satisfaction of individual needs. A negative, or “punishment,” is an outcome that results in a decrease in the satisfaction of personal needs. Reward incentives are inducements to satisfy those needs that individuals cannot obtain without joining the organization. Organizations provide rewards to participants who perform in agreed upon ways. Research on incentives tends to support the following:

- Individual tends to be more strongly motivated by the potential of earning rewards than by the fear of punishment, which suggests that management control systems should be reward-oriented.

- A personal reward is situational. Monetary compensation is an important means of satisfying certain need; beyond a satisfaction level, the amount of compensation is not necessarily as important as nonmonetary rewards.
- If senior management signals by its actions that regards the management control system are important, operating managers will share the same opinion. If senior management pays little attention to the system operate, managers are likely to pay little attention either.
- Individuals are highly motivated when they receive reports (feedback) about their performance. Without such feedback, people are unlikely to obtain a feeling of achievement or self-realization or to sense corrective actions that are needed to meet their objectives.
- An incentives rapidly becomes less effective as the period between an action and the report of it increases. At lower levels in the organization, the optimal frequency of feedback between the action and the feedback may be only hours; for senior management, it may be months.
- Motivation is weakest when the person perceives an incentive as being either unattainable or too easily attainable. Motivation is strong when the objective can be obtained with some effort and when the individual regards its attainment as important in relation to personal needs.
- The incentive provided by budget or other statement of objective is strongest when managers participate actively with their superiors in the process of arriving at the budgeted amounts. Objectives, goals, or standards are likely to provide strong incentives only if the managers perceives them as fair and feels committed to attaining them. The commitment is strongest when it is a matter of

public record-that is, when the manager has explicitly agreed that the budgeted amounts are attainable.

A manager's total compensation package consists of three components:

1. Salary
2. Benefits (principally pension and health benefits, but also perquisites of various types)
3. Incentives compensation

The three components are interdependent, but the third is specifically related to the management control function. The compensation of managers in large companies tends to be higher than compensation in smaller companies, and compensation in one company tends to be competitive with that of other companies in the industry, but few others generalizations can be made about the level of management compensation.

2.2. Incentive Compensation Plans

Incentive compensation plans can be divided into:

1. short-term incentive plans, which are based on performance in the current year. Bonus for manager under this plan usually paid in cash.
2. long-term incentive plans, which relate compensation to the longer-term accomplishments, usually related to the price of the company's common stock. Bonus under this plan is an option to buy company's common stock.

2.2.1. Short-Term Incentive Plans:

The Total Bonus Pool

In a short term incentive plan, shareholders vote on the formula to be used in arriving at the total amount of bonus that can be paid to a qualified group of employees in a given year, which is called the “bonus pool.” This formula usually is related to the overall company profitability in the current year. In deciding on the size of this pool, the overriding issues is to make the total compensation paid to executives competitive.

Some methods using the bonus pool are:

1. Set a percentage of the profits
2. Base the bonus on a percentage of earnings per share after predetermined level of earnings per share has been attained.
3. Bonus is equal to a percent of the profits before taxes and interest on the long-term debt minus a capital charge on the total of shareholder equity plus long-term debt, similar to the Economic Value Added concept.
4. Base the bonus on the increases in profitability over the proceeding year.
5. Base bonus on company profitability relative to industry profitability.

Carryovers

Instead of paying the total amount in the bonus pool, the plan may provide for an annual carryover of a part of the amount determined by the bonus formula. Each year a committee of the board of directors decides

how much to add to the carryover, or how much of the accumulated carryover to use if the bonuses would otherwise be too low.

The advantages of this method are that:

1. it offers more flexibility, since payment is not determined automatically by a formula, and the board of directors can exercise its judgment
2. it can reduce the magnitude of the swings that occur when the bonus payment is based strictly on the formula amount calculated each year.

Deferred Compensation

Although the amount of the bonus is calculated annually, payments to recipients may be spread out over a period of years, usually five. Under this system, executives receive only one-fifth of their bonus in the year in which it was earned. The remaining are paid out equally over the next four years.

The advantages of this method are that:

1. managers can estimate, with reasonable accuracy, their cash income for the coming year.
2. deferred payments smooth the manager's receipt of cash, because the effect of cyclical swings in profits are averaged in the cash payments.
3. a manager who retires will continue to receive payments for a number of years; this only augments retirement income but also usually provides a tax rates after retirement may be lower than rates during working life.

4. the deffered time frame encourages longer-term thinking with regard to decision making.

2.2.2. Long-Term Incentive Plans

Stock Options.

A stock option is a right to buy a number of shares of stock at or after a given time in the future, at a price agreed upon the time the option is granted. The major motivational benefit of stock option plans is that they direct managers energies toward the long-term, as well as the short-term, performance of the company. The motivational impact of such plans is dampened to the extent that factors beyond the control of managers affect stock prices.

Phantom Shares.

A phantom stock plan awards managers a number of shares for bookkeeping purposes only. At the end of a specified period the executive is entitled to receive an award equal to the appreciation in the market value of the stock since the date of award. This award may be in cash, in shares of stock, or both. Unlike a stock option, a phantom stock plan has no transaction costs.

Stock Appreciation Rights.

A stock appreciation right is a right to receive cash payments based on the increase in the value of stock from the time of the award until a specified future date.

Performance Shares

A performance share plan awards a specified number of shares of stock to a manager when specified long-term goals have been met. Usually the goals are to achieve a certain percentage growth in earning per share over a three-to-five year period; therefore, they are not influenced by the price of the stock.

Performance Units

In a performance unit plan, a cash bonus is paid on the attainment of specific long-term targets. This plan, thus, combines aspects of stock appreciation rights and performance shares.

2.3. Incentive for business unit manager

Incentive systems are offered prior to the actual performance. Perhaps the most important distinction is that merit pay usually adds into and permanently increase base pay, whereas incentives are one time payments and do not have a permanent effect on labor costs. When performance declines, incentive pay automatically declines, too.

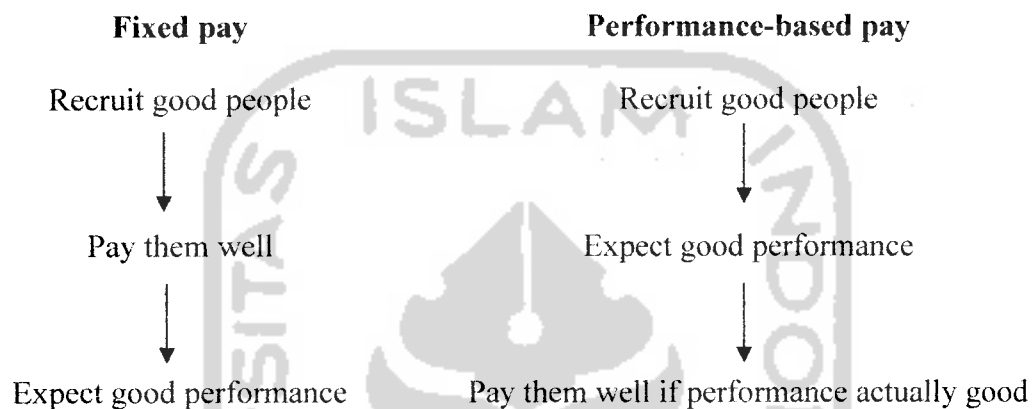
Type of Incentives

1. Financial incentive includes salary increases, bonuses, benefits, and perquisites (automobiles, vacation trips, club membership, and so on).
2. Psychological and social incentive include promotion possibilities, increased responsibilities, increase autonomy, a better geographical location, and

recognition (thropy, participation in executive development program and the like).

Size of Bonus Relative to Salary

Two philosophies on incentives compensation can be describe as:



The difference between the two philosophies, is that under fixed pay, compensation comes first, and performance comes later; while under performance-based pay, performance comes first and compensation comes later. Therefore the motivational implication of both philosophies is different since salary is an assured income, an emphasis on salary may lead to conservatism and complacency. Whereas an emphasis on incentive bonus tends to encourage managers to put forth maximum effort.

Compensation refers to all of financial returns and tangible services and benefits employees receive as part of an employment relationship. People gain satisfaction from their work, but the kinds and the strengths of satisfaction have been difficult to identify, define, and measure with any degree of precision. Furthermore, the individual identifies attains another. Meanwhile, as the individual and the group coordinates their needs and efforts, a third set of the group those who

both receive and offer some form of reward for the service provided by the individual and the group. Employers use their reward system to attract and retain those who not only have the desired knowledge and skills, but also have the interest and are willing to put for the effort needed to link their knowledge and skills to the accomplishment of organizational goals and objectives.

Cutoff Levels

A bonus plan may be constrained at either the end of:

1. the level of performance at which a maximum bonus is reached (upper cutoffs),
or
2. the level below which no bonus awards will be made (lower cutoffs)

Bonus Basis

A business-unit manager's bonus could be based solely on total corporate profits or on business unit profits, or on some mix of the two. The manager's decision and action have more direct impact on the performance of his or her own unit than that of other business unit. This would argue for linking incentive bonus to business unit performance.

Performance Criteria

1. Financial Criteria, Financial criteria is different in each business unit based on the responsibility center. LUX business unit use revenue center as a responsibility center so the financial criteria would be based on sales volume.

2. Adjustment for uncontrollable factors. Companies make adjustments for two types of uncontrollable influences:
 - ❑ Removes expenses that are the result of decisions made by executives above the business unit level.
 - ❑ To eliminate the effects of loss due to "acts of nature" (fires, earthquakes, floods) and accidents not caused by the negligence of the manager.
3. Benefits and Shortcomings of Short Term Financial Target, which link business unit managers' bonus to achieve the desired annual financial targets. It induces managers to search for ways to perform existing operation in different ways and initiate new activities to meet the financial targets.

Bonus Dermination Approach

A bonus award for a business-unit manager can be determined on the basis of either strict formula, such as a percentage of the business unit's operating profit, or purely subjective assessment by the manager's superior, or by some combination of the two.

2.4. Agency Theory

Agency theory explores how contracts and incentives can be written to motivate individuals to achieve goal congruence. It attempts to describe the major factors that should be considered in designing incentive contracts.

An agency relationship exist whenever one party hires another party to perform some service and, in so doing delegates decision-making authority to the agent. In a corporation, shareholders are principals, and the executive officer is their

agent. At lower level, the CEO is the principal, and the business unit managers are the agents. The challenge becomes how to motivate agents so that they get as productive as they would be if they were the owners.

One of the key elements of agency theory is that principals and agents have divergent objectives. The divergent preferences can be reduced through incentive contracts.

Divergent Objectives of Principals and Agents.

1. Agency theory assumes that all individuals act in their own self-interest. Agents are assumed to receive satisfaction not only from financial compensation but also from the perquisites involved in an agency relationship. The perquisites can take the form of generous amounts of leisure time, attractive working conditions, country club membership, and flexibility in working hours. For example, some agents may prefer leisure to hard work (effort). Managers effort increases the value of the firm, while leisure does not.
2. Based on risk preferences, agency theory assumes that managers prefer more wealth to less, but that the marginal utility, or satisfaction, decreases as wealth is accumulated. Agents typically have much of their financial wealth and also of their human capital. Human capital is the value of the manager as perceived by the market; it is influenced by the firm's performance.

The divergence in preferences associated with compensation and perquisites arises whenever the principal cannot easily monitor the agent's, action. The principal has inadequate information about the performance of the agent; therefore the principal can never be certain how the agent's effort contributed to actual firms

results. This situation referred to as information asymmetry. These asymmetries can take on several forms. Without monitoring, only the agent knows whether he or she is working in the principal's best interest. Moreover, the agent may know more about the task referred to as private information. Because of both the divergence of preferences between the principal and agent and the private information of the agent, the agent may misrepresent information to the principal. This misrepresentation is such a general nature that the name moral hazard has been given to the situation where an agent being controlled is motivated to misrepresent private information by the nature of the control system.

Control mechanism

Agency theorists state there are two major ways of dealing with the problem of divergent objectives and information asymmetry, *which are monitoring and Incentives.*

Monitoring

The principal can design control systems that monitor the actions of the agent. The principal design these systems to limit actions that increase the agent's welfare at the expense of principal's interest. Agency theory has attempted to explain why different agency relationships entail different levels of monitoring. For example, the effectiveness of monitoring is increased if the task performed by the agent is well defined and the information used in monitoring is accurate. If the task is not well defined or easily monitored, incentive contracting becomes more

appealing man control device. These alternative monitoring and incentives are not mutually exclusive.

Incentive contracting

The other mechanism that can align the interests of the principal with those of the agent is incentives. The principal attempts to limit divergent preferences by establishing appropriate incentive contract. The more an agent's reward depends on a performance measure, the more incentive there is for the agent to improve that measure. Therefore, the principal should define the performance measure that satisfies him or her. The ability to accomplish this is referred to as goal congruence. A compensation scheme that does not incorporate an incentive contract poses a serious agency problem,

A challenge facing the principal is identifying signals that are correlated both with agent effort and firm value. The agent's effort, along with outside factors like the general economy and natural disasters, is combined to determine performance. The more closely an outcome measure reflects the effort of the manager, the more valuable the measure is in an incentive contract- If the measure of performance is not closely correlated with the agent's effort, there is little incentive for the agent to increase the measure.

Rewarding an individual's innovative efforts and contribution can only be done by subjective assessment. Subjective rewards-relying on the personal judgment of superiors-allow managers to recognize innovative behavior that is difficult to specify in advance and to assess the contribution and effort of individuals in the interactive process. Only subjective rewards provide the flexibility to reward creativity in the face of unanticipated threats and opportunities.

Subjective rewards yield three outcomes that help stimulate organizational learning:

1. Rewarding contribution and effort provides incentives for employee to make their efforts visible to their superiors. To demonstrate their contributions, employees will be motivated to communicate information about emerging problems and opportunities to their bosses, as well as to report how they have responded. In this way, they can demonstrate their competence, creativity, and effort through information sharing, analysis, and action planning. Of course, this upward communication feeds the learning process that can lead to better understanding of competitive markets and potential new action plans.
2. Rewarding contribution and effort, rather than results, reduces information biasing that is a constant concern in diagnostic control system. Because rewards are not mechanically tied to uncontrollable events that could affect performance expectations, employees are more likely to share both good news and bad news.
3. Rewarding contribution subjectively demands that superiors have the ability to calibrate the efforts to subordinates accurately. To do so, superiors must themselves have a sound understanding of the business environment, decision context, array of possible decision alternatives, and potential outcomes of decisions not taken. Without this knowledge, it is impossible to allocate reward fairly. However, superiors can only gain this knowledge from deep understanding of the business and its changing competitive environment. Superiors must, invest a good deal of their own time and attention to really learn about the business and its changing dynamics.

None of the incentive arrangements can ensure complete goal congruence. This is because of the difference in risk preferences between the two parties, the

asymmetry of information, and the costs of monitoring. These differences cause additional costs. Even an efficient system of incentive alignments will still result in some divergence of preferences. This divergence is named the residual loss. The addition of the costs of incentive compensation, the costs of monitoring, and the residual loss are formally titled agency cost. Which inherent in incentive compensation. There are two things considered by a company that pays its CEO a bonus in the form of stock options.

1. One cost is the risk preference differences between the owners and CEO. The agent, already risk averse, incurs additional risks when his or her pay is based on stock price performance. To compensate the CEO for taking on this risk, the contract will have to increase the amount of expected pay. In addition, to minimize the possible downside potential, the agent may not take on high risk/high return projects that the principal may find desirable,
2. The lack of direct causal relationship between agent's effort and the change in stock price. Stock prices are effected by factors outside the control of the agent. If the stock price rises because of factors beyond the control of the agent, the stock price may decrease even if the agent exerts high effort.

CHAPTER III

COMPANY'S PROFILE

3.1. Introduction

In the era of last developing technology, all activities of human life tend to use the modern technology to ease their work. Technology develops in all aspects of human life such as in information, home appliance, etc. One product greatly influenced by the technology is electronic products. In terms of the area of production, electronic companies can be divided into two general groups: National company and International company, National company is a company producing and selling the product in domestic coverage area, while international company produces and sells the product both locally and internationally.

Luxindo Raya is one of the International electronic companies headquartered in Switzerland. Luxindo Raya produces electronic products for home appliances using "LUX" as its brand. As an international company, it has many branches all over the world including in Indonesia. Luxindo is one of a hundred best companies in the world and one of the best companies producing home appliance products. The process of production and material procurement are centered in its headquarters, Switzerland. Branch offices only conduct marketing activities, while product supplies are usually delivered by the headquarters once a month. By using this system, the company tries to maintain the same quality in every country.

In this chapter the researcher attempts to analyze the Luxindo Raya as the case study of this research. This chapter is divided into ten parts. Those are introduction, the history of Luxindo Raya company, organizational structure, job

description. Luxindo Jogjakarta, product and division, target and rewards, vision, mission, core beliefs and principle values, company strategies and operational activities and Luxindo Raya remuneration scheme.

Although Luxindo Raya does not have various kinds of product like their competitor, they can exist until now. The compensation or remuneration system which use by Luxindo no changes at all time to time, just the nominal amount change suitable with the world inflation. Because of that the researcher wants to know more about how this company can exist in today's business competition, with many competitor, various kind of product produce by them and the same, even more qualified product competitor.

The History of Luxindo Raya Company

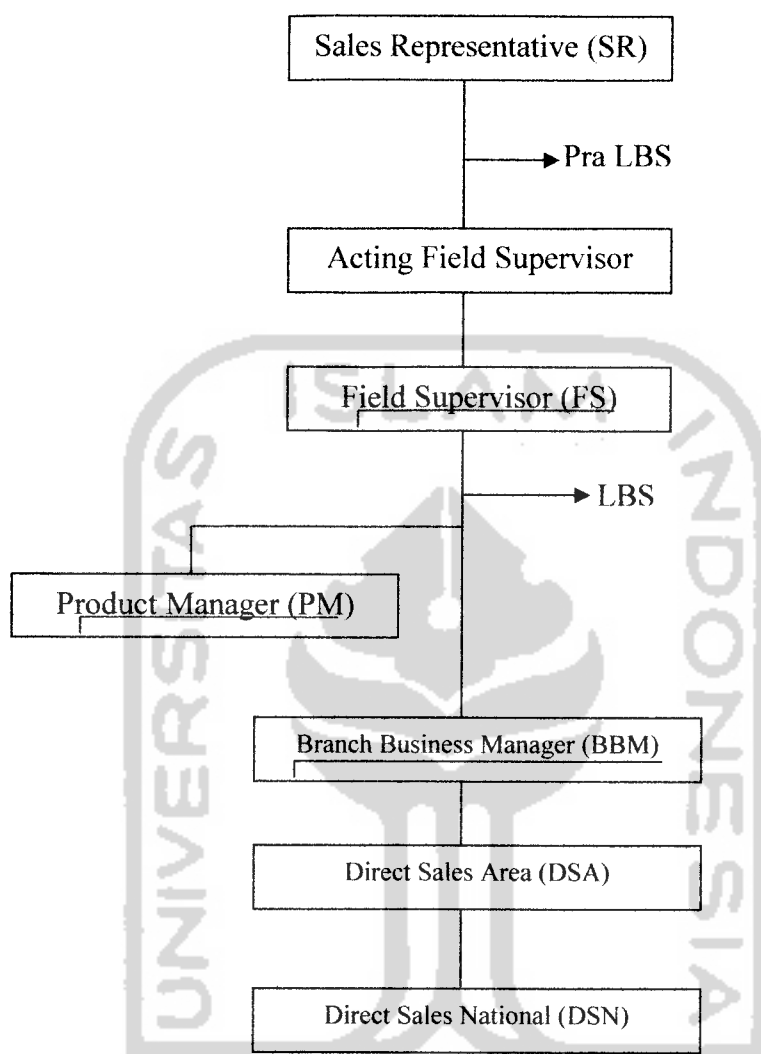
LUX is the historical name in the Electrolux group. Lux was established by Mr. Axel Wenner gren a Sweden on 1901, As a dreamer man, he dreamt everything, including one that he could help his wife to easier her home task like washing the cloths, clean the house, etc. Not just dreaming, he tried to make it real by himself. For the first time he made and sold directly to consumer the street-tamp with LUX brand. Not being satisfied at all, he wanted more than that, until one time, when he saw his wife cleaned their home and tried to clean the carpet from hair and all dust. He got interesting idea to create cleaning tools, so he try to made something and worked hard for it. Then on 1912 his idea became real when he successfully created one tool to clean the house that called "vacuum cleaner". LUX was the first company that invented handy vacuum cleaner, that can be used and kept easily.

The marketing strategy applied by Mr. Axel Wenner Gren was door to door sales, since according to him, this was more efficient strategy. Mr. Axel Wenner Gren became both the owner and general manager. In 1915, the company developed fast for almost all houses had the "LUX" vacuum cleaner. Seeing this fact, Mr. Wenner create a motto that "every house is a LUX house". In 1919 LUX joint another Swiss electronic company, Mechanic Electro, and then changed their brand name to "Electrolux". Electrolux Group company grew fast. Which can be chronologically described as follows:

1913-1920	Electrolux developed fast and spread to all Europe country.
1927	Started to develop outside Europe
1928	Opened branch in France and England
1930	Spread to the Pacific area.
1930-1940	Built branch in America Latin
1964	The group develop their product to be automatic and more flexible useless.
1970-1990	Entered to Asia country

In 1992, because of different management's perspective and strategies, some company owner choose to quit from Electrolux group and produced and sold product under "LUX" brands name. Until now LUX keep and hold their original direct marketing strategy, in others words, they still sell their product door to door.

3.2. ORGANIZATIONAL STRUCTURE



3.3. JOB DESCRIPTION

Sales Representative (SR)

SR is responsible to sell the company products by demonstrating product. The responsibility of Sales Representative are introducing the product function, how to use it, the advantages of using the product, what kind of paying procedures that company offers and eventually persuading the customer to buy the product.

For follow up and evaluation. Sales Representative must join internal meeting every morning in his/her branch lead by Branch Business Manager.

Acting Field Supervisor (AFS)

AFS sell company product by product demo done by Sales Representative who are in team with him or her. Acting Field Supervisor is responsible for the right step done by Sales Representative to demonstrate the product and help new Sales Representative to find place to demonstrate the product.

Acting Field Supervisor evaluate his or her job every morning too, in meeting with sales representative and Branch Business Manager.

Field Supervisor (FS)

FS sell company product and ensure Sales Representative and Acting Field Supervisor achieve their division target. Like Acting Field Supervisor, Field Supervisor must attend the morning meeting to evaluate the previous day sales result and today target.

Product Manager (PM)

PM is for either responsible for either the product quality received from the head office or product input and product output in his/her branch, pricing product received by customer to be exchanged with LUX product is also considered PM,s job.

Branch Business Manager (BBM)

BBM makes sure that target branch can be achieved, communicate the strategies to achieve the target with Sales, Acting Supervisor and Supervisor, recruit the new sales representative, organize training for new sales representative, training for pra LUX Business School. Branch Manager job is evaluated by Direct Sales Area in a meeting once in a month.

Direct Sales Area (DSA)

There are only six Direct Sales Area in Indonesia, Their job is to make sure all Branch under their area achieving the target. The Direct Sales Area arrange the strategies to achieve the target, they can decide what the rewards given if the target achieved by division, just for members of one area not all members of area. For job evaluation, The Direct Sales Area need to attend the meeting once a year with Direct Sales National.

Direct Sales National (DSN)

DSN is The Highest position in one country. He should arrange everything for all of branch in one country, how much target for one area are determined, what kind of strategies should be implemented. What kind of reward given, how many the reward are depends on the sales volume. The reward can be in the form of trip, both local and international. To get international trip, the sales team must reach certain point. Otherwise, it will be transferred to local trip. Moreover for all of those activities, the important thing to do is to make sure that the country can achieve the target set by head office. The rewards beside trip may be different in one area to another, which is determined by DSA.

3.4. LUXINDO JOGJAKARTA

Luxindo entered Indonesia in 1977, which for the first time open their branch in Jakarta as the capital of Indonesia. The result showed that the sales volume in Indonesia is good so that the management opened another branch in Jakarta. Soon after that LUX was developed to all over areas in Indonesia. In 1990, LUX expanded to Jogjakarta and was located in the P. Mangkubumi street as West

Jogjakarta branch, and in 2000 LUX opened another branch in Jogjakarta on Taman siswa street as East Jogjakarta branch. Until 2004, PT. Luxindo Raya in Indonesia have opened 160 branch in all over country. Jogjakarta is one of nineteen branch members of Direct Sales Area (DSA) in Central Java, The researcher conduct a case study on Luxindo branch on west Jogjakarta only.

Company divides the company division based on the product sold in their country because every country sells different product. For instance, washing machine is not sold in European country because the technology there is more developed than other countries. In Indonesia, including Jogjakarta, there are four divisions representing four product offered, One division has several teams but the team from one division is different with others just because it is result by the Branch Business Manager.

3.5. DIVISIONS AND PRODUCT

Divisions	Product	Type of Product	Team
OR Line	Air C leaner	AC-1	1
DD Line	Vacuum Cleaner	VC-1	6
		VC-2	
		VC-3	
		VC-4	
KT Line	Washing Machine	WH-1	3
		WH-2	
		WH-3	
KQ Line	Water Purifyer	WP-1	2

One team includes minimum two or three sales along with one supervisor or one Acting Supervisor. Although employees work as a team, the remuneration give and counted individually, because the team in this company easier the sales to promote and demonstrate the product. But there are any reward for a winner

division, win means one division can achieve the target. Therefore they get individual commission and bonus for team.

The time working in this company is not limited by company because they hold principle not to give limitation for money paid as result of product company sold as many as they can. The area to sell the product is unlimited too, they can sell their product in everywhere eventhough the area has another LUX branch. The company has transportation with driver to facilitate the company members.

3.6. TARGETS AND REWARDS

Every member of this company works based on the target. Target for Indonesia is set by headquarter and than Direct Sales National will set the target for all areas in Indonesia. Every achievement of target have rewards value. The rewards type is different for each other.

Example 1.1

No contest for April month

Month: April 2003	
Division	Target/unit
DR	67
DD	135
KT	81
KQ	30
BBM	293

Example 1.2

Contest “get your own motorcycle” for SR/AFS/FS

Sales Period: 1st may – 30th June 2003

Division	Target		
	SR	AFS	FS
DR	20	30	30
DD	30	42	42
KT	25	37	37
KQ	18	26	26

Example 1,3

Contest “go to Sydney” for SR/AFS/FS/BBM

Sales period: 1st July - 25th September

Division	Target		
	SR	AFS/FS	BBM
DR	30	46	76
DD	45	61	106
KT	32	50	82
KQ	27	43	70
Total			334

3.7. Vision, Mission, Core Beliefs, Principle Values

Company Vision

- *Costumers*: Make every house is LUX house
- *Employee* : Make a real unlimited income

Company Mission

Open the branch in all over the world, and sell product with better quality and better performance of sales team support with Lux Business School and Lux academy.

Core Beliefs

Customer focus

It is believe that taking care of their product after sales period will satisfy their customer. Company not only sells its product but also take care of it, Customers can call the branch office if they need to repair the product periodically or for other problem dealing with product purchased.

Communication

Believe that communication with others members and their boss as good learning and they can take more values and experience from the communication.

Employee

It is believe that employee is the party that has direct relation with customer and is someone who shows the performance of company, therefore company must improve the quality of their employees with education and trainings.

Quality

It is believed that the quality of product will greatly create high sales volume.

Principle Values

- **PRIDE** : Everyone must believe that if there is a desire the success will be achieved. LUX is something they can be proud of because LUX always give rewards for all successful man.
- **EARNING** : more product can be sold, the more money earned by the employees.
- **FUN** : A successful man knows when he should work harder and when he should have fun.

3.8. Company Strategies and Operational Activities

Based on its vision and mission, company implements three core strategies known as **3 FT**:

1. Full effective Time

Employee working time is not limited by company. They can sell anytime and anywhere. However, in the morning there is meeting schedule that must be attended by all of employees, in which they talk about fast day sales and today's planning. After meeting, the effective working time starts until 6 pm because evening is regarded time to rest but if consumer does not mind employee demonstrating their product, they can work at the time arranged with the consumer. Employee working day is every day, there are no off time. Off time can be taken with some requirement and punishment, for example if one employee absence they will not receive some bonus, etc.

2. Full performance Team

Employee works in a team, which includes Sales Representative, one Acting Field Supervisor and/or Field supervisor. One team works in the same place but for different targeted home or consumer, One Sales Representative can come to one house with his AFS/FS and offer product by product demonstration.

3 Full qualified Training

Employee of Lux company are a qualified one as they believe qualified human resources can support company programs. All of company's employees must have skill but they do not need a formal skill or education like university graduate. They have their own school, rules and policies.

3.9. LUX Business School

□ For Sales Representatives (SR)

1. Basic Training

New Sales, will be trained by Branch Business Manager of his branch

2. Re-training

3. Crass- Course

Course for SR who sell nine unit in three month

4. Pra LBS

□ For Supervisor (AFS/FS)

1. Basic Training

Safes, will be trained by Branch Business Manager of his branch

2. Re-training

3. Crass-Course

4. Pra LBS

The different between SR and AFS/FS School is that SR school is located in the branch office only and AFS/FS is located either in Jakarta or the center office of one country.

□ For Branch Business Manager (BBM)

1. BBM 1 for class one, two and three

2. BBM 2 for class one, two and three

3. BBM 3 for class one, two and three

The center of LUX Academy is located in Singapore.

Remuneration Type for SR

Examples for KT Line remuneration are:

- a) Transportation allowance
- b) Commission
- c) Premium for three month
- d) Incentive
- e) Insurance Accident
- f) Carrier

a) Transportation allowance

Company gives transportation funds to every SR in cash, which is given as reimbursement of cost spent by SR to come to the company office and lunch fee. Transportation (cars) and the driver have been provided by company. Transportation fee is divided into two types fixed (field allowance) and variable (transportation allowance).

A. The transportation commission is given to a Sales Representative who has been working for more than two months and new Sales Representative who has successfully sold the product.

Unit/ month	Porterage cost	Transportation
1	Rp. 100,000	-
2	Rp. 145,000	Rp. 200,000

As new SR, company ask them to sell eighteen company product (called target for new SR) in period of six months.

This commission can be canceled if Sales Representative has been absent for four times as rule bellows :

2 x permit : 1 absence

2 x late : 1 absence

B. Field Allowance

New Sales Representative can receive Field Allowance for Rp. 85,000 every ten days in a month based on below regulations:

- ❑ New Sales Representatives have a right to receive field allowance since they passed Basic Training.
- ❑ The field allowance is given directly to sales representative on 11th, 21st and date for commision given.
- ❑ New Sales Representative who has successfully sold in first month still have right to get this Field Allowance

The Field Allowance will be canceled if New Sales Representative is absent one time in ten days period calender.

Wheter or not new SR has successfully sold the product in the first month, if he or she can sell at least a product in the second month, the new SR can get Field Allowance for Rp 225,000 which is paid in all commision due date.

b) Commision

Company provides in cash for every SR and the amount is given based on sales volume of a SR. The commision is counted based on the reward point of a

product type sold by him or her and it will be totalled at the end of month. The description of commission can be drawn at table below:

TYPE	PAID WAYS/point			
	Cash	2 month	6 month	12-18 month
WH-I	17.5	17.5	16.6	15.7

In the last month, the total point receive by sales representative is valued as belows:

<u>Point</u>	<u>Rupiah</u>
8.5 – 15.9	12,000
16 – 27.9	16,000
28 – 39.9	19,000
40 – 51.9	21,000
52 – 63.9	22,000
64 – 75.9	24,000
76 – more	26,000

c) Premium per three month

This reward is also given in cash but the count of this point is based on first three month, second three month and third three month, the company gives this premium still based on sales volume and pick up point on sales product.

3.1. The first three month

To all of Sales Representative who has successfully sold in the first three month can receive premium :

- Rp. 85,000 for 3 – 4 unit
- Rp. 110,000 for 5 – 6 unit
- Rp. 140,000 for 7 – more

3.2. The second three month

To all of Sales Representative who has successfully sold in the second three month can receive premium :

- Rp. 110,000 for 6 – 8 unit
- Rp. 150,000 for 9 – 11 unit
- Rp. 190,000 for 12 – more

3.3. The third three month

To all of Sales Representative who success to sold in the third three month can receive premium :

- Rp. 135,000 for 9 – 11 unit
- Rp. 180,000 for 12 – 14 unit
- Rp. 225,000 for 15 – more

d) Incentive

Company always share their profit to sales team. Incentive is given by company if there are any contests and the measure is on sales volume. Different with transportation allowance, commision, premium per three month incentive is give in some types:

- Holiday tickets for local and abroad including fee, transportations, hotel etc.

- Electronics, like television, VCD, DVD, refrigerator, air conditioner and also motorcycle, etc.
- Scholl. LUX have their own school which is related to the improvement of career of SR in LUX.
- Cash money

e) Company Insurance

Company registers every Sales Representatives in insurance program which are paid by company. It includes:

1. Accident insurance.
2. Death insurance.

Pension insurance is not included because SR is only freelance employee.

f) Career

As a Sales Representative in LUX, every Sales Representative has a chance to develop him or herself to be a skillful Sales Representative and to get much money. After Sales Representative show himself capable (can achieve all target continue in three month), LUX give them more chance to have satisfying career (permanent). In all over the world, LUX have policy to employee skillful labor from their own organization (intern) not extern labor. Career is much related to the sales contest because sales contest can support the sales volume of SR. If a SR wins in sales contest it means SR show a good performance and SR should prove the performance not only for one month but also for three month

continuously then SR can be a permanent employee after joining the employee training.

Remuneration type for AFS/FS

1. Base wages
2. Variable wages
3. Incentive
4. Bonus
5. JAMSQSTEK

1. Base wages

After a SR has joined training to be AFS/FS, they are not a freelance employee anymore. They will receive a fixed pay/base pay Rp. 500,000,- at the end of the month as fixed employee.

2. Variable wages

Variable wages paid by company is based on total point received by supervisor. This point is counted based on their own sales volume, not their downliner's (SR) sales volume.

Total point in a month	Variable wages per unit
21.0 – 25.0	Rp. 4,500,-
25.1 – 32.0	Rp. 8,000,-
32.1 – 50.0	Rp. 10,000,-
> 50.0	Rp. 12,00,-

3. Incentive

Incentive is given by company as a transportation allowance. This transportation is given based on point received in a month as drawn.

Total point in a month	Transportation allowances
> 25.0	Rp. 7,500,- per point
25.1 – 39.0	Rp. 220,000,-
> 39	Rp. 330,000,-

4. Bonus

Supervisor bonus is called as premium productivity. This premium productivity is give based on the following requirements:

- Total division members (SR) in a month must be at least six SR and there should be at least SR are success to sell more than two units.
- If total members in one division are less than six SR, supervisor does not have right to receive the bonus.
- The productivity premium of SR in one division can be formulated as follow:

$$\frac{\text{Total division sales}}{\text{Total SR extract (-) 1}}$$

- Table of amount received

Productivity average of division Members (SR)	Total premium
3.0 – 3.5	Rp. 300,000,-
3.6 – 4.0	Rp. 500,000,-
4.1 – 4.5	Rp. 700,000,-
> 4.5	Rp. 1,000,000,-

CHAPTER IV

DATA ANALYSIS

4.1. Combination Pay Plans

Today, some form of combination pay plan is used to compensate about 75 percent of all sales forces. Broadly speaking, the purpose of any combination plan is to overcome the weaknesses of a single method, while at the same time keeping its strong points. One of the reasons why LUX co. used the combination pay plan depend on single method

Based on what is stated is by Thomas N. Ingram and friends (2001. Sales Management, *analysis and decision making*) "*paying sales people a straight salary (exclusively by a sallary) is uncommon. Such plans are well suited for paying sales support personnel and sales trainees. Sales support personnel, including missionaries and detaiers, are involved in situations in which ii is difficult to determine who really makes the sale. Because they only concerned primarily with dissemination of information rather than direct solicitation of orders, a sallary can equitably compensate for effort. Compensation based on sales results might not be fair*".

Most of the combined pay plans fall within the following categories:

- Salary plus commission and/or bonus.
- Commission with guaranteed drawing account.
- Commission and bonus.

In a combination pay plan, what portion should be incentive and what portion salary? The answer depends on the nature of the selling tasks and the

company's marketing goals. The incentive portion should be larger when a company is trying to increase its sales or gross margin, especially in the short run. The salary element is larger when management emphasizes customer servicing, a fully balanced selling effort, or team selling. However, in LUX there are no fixed salary at all, instead, only field allowance for the first month paid by company to sales representative whether they can sell the company product or not.

4.2. Specific elements of pay plan in LUX

Financial rewards

1. Basic compensation plan
 - a) No fixed salary
 - b) Commissions
 - c) Bonus payments called premium per three month
 - d) Fringe benefits including insurance accident, transportation allowance and field allowances
2. Sales contests in LUX called incentive

Psychological and Social Rewards

1. Recognition awards, such as pins, trophies, certificates
2. Praise and encouragement from management
3. Job enrichment
4. Opportunity for promotion (this may also be a financial reward)

Other elements

1. Sales meetings and conventions
2. Leadership and supervision

3. Sales training programs—induction and continuation
4. Sales mentoring

4.2.1. Financial rewards

1. Basic compensation plan

a) No fixed salary

Although sales in this company work as full time employees (SR work from 7a.m. until 10 pm), they do not receive Fixed salary. *Fixed salary* means amount of money given by company monthly to their employee not based on employee's working time or a unit product could he sold by them, but it is given for employee security.

Referring to the above definition, every new SR joining in LUX company for the first month will receive fixed salary still because although new SR do not sell any unit of product they receive some amount of money. Nevertheless, in the second month and the rest SR will not receive fixed salary anymore. What they receive is only variable salary, which is given to SR depending on how many product could be sold by them. Product and salary are in balance, which means that the more product can be sold the more money can receive by SR.

Fixed salary is only given to supervisor and higher position. Branch manager of LUX said: "...to be a supervisor SR only need show a good performance in three month continuously...". This good performance means that SR can fullfill the product target selling

which is set differently to every SR in different division in this company.

This company's system is actually similar to other companies in that it applies the first three month as probation in which employee will receive fixed income without any commission or bonus. Furthermore, if within the contract time an employee shows a good performance he or she they can be assigned as fixed employee and get either fixed salary or some company allowances. Good performance in this company is shown from the volume of product sales in three month continuously by SR, if a SR reaches the target only in two month, and do not reach the target in the third month, the first two months are no longer put in consideration as good performance. It means that the SR should start again from the beginning. SR do not received fixed salary until they are to be a supervisor. What SR receive is only commissions and bonus.

The advantages of having no fixed salary:

- 1) Less fixed cost
- 2) Company can hire more employee
- 3) Create an active and creative employee

On the other hand, the disadvantages of having no fixed salary:

- 1) It is hard to find skillful employee without any security in work.
- 2) Employee could quite anytime. Company will then need more time just to look for someone interested to join the company. This

makes company loss much time to offer their product if many employees quit. It is regarded unefficient.

b) Commissions

Commissions in LUX is the important as well as interesting part for SR because from this part SR can earn money. LUX never limit the amount of salary that can be received by SR, only SR themselves can limit their income. If SR plans to have higher income, SR should sell more unit of product.

LUX commission plan involves a regular payment for the performance of a unit of work. A commission is related to a unit of accomplishment, in contrast to the salary method, which is a fixed payment for a unit of time. A commission is usually based on factors that are largely controllable by the sales people and consists of three items:

1. *A base* on which performance is measured and payment is made—for example, sales in dollars or units of the product. LUX use base a unit of product
2. *A rate*, which is the amount paid far each unit of accomplishment—for example, LUX value a unit of product based on points set by them.
3. A starting point for the commission payments.

For example.

TYPE	PAID WAYS/point			
	Cash	2 month	6 month	12- 18
WH-1	17.5	17.5	16.6	15-7

In the last month, the total point received by sales representative is than valued using below regulations:

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40 – 51.9	21,000
52 – 63.9	22,000
64 – 75.9	24,000
76 - more	26,000

The advantages of Straight Commission Plans

1. Probably the major advantage of the straight commission method of sales compensation is the terrific incentive it gives to the sales force. Many firms have no ceiling on SR commission earnings, so their income opportunities are unlimited.
2. Commission payments are a strong motivating factor to get the SR to work hard. Typically, a salesperson on commission works more hours each week than one on salary.
3. A commission plan probably is the best type of pay plan for weeding out ineffective sales SR.

4. Another big advantage to the company is that a commission is a direct respond. That is, an expense is incurred only when a sale is made or son other activity is performed.

The disadvantages of the Plans

The limitations of the commission method of sales compensation mentioned most often can be summed up under one point, it is difficult to supervise and direct the activities of salespeople because they tend to think they are in business for themselves.

Often, under the usual commission structure, the salespeople's only concern is to sell more merchandise, without regard for the interests of the company or the customer. SR may concentrate on easy-to-sell items and frequently ignore those that are slow moving. However, it does not happen in LUX because they use other elements called bonus and sales contest which include cash and non cash rewards.

c) Bonus plans

Combination plans introduce a new component namely a bonus. The word bonus is probably the most loosely used word in the compensation vocabulary as a result, it is sometimes difficult to accurately assess the extent to which it is used in pay plans. A bonus is a lump-sum payment for an above-normal performance. Because of its nature, a bonus cannot be used alone, but instead, must always be combined with another element such as a salary or commission.

Strictly speaking, management need not announce in advance either the amount of the bonus or the basis for distributing it.

However, most sales bonuses are intended to stimulate the sales force to perform certain tasks by offering an incentive. Unless the plan is explained fully in advance, management will gain nothing by giving a bonus. The most commonly used basis for paying a bonus is the measure of a salesperson's performance against a quota—typically, a sales volume quota or an expense quota. A SR may get a cash bonus of x dollars for going 10 percent over quota.

In LUX bonus is called premium per three month, which is just like commissions, it is paid by company based on sales volume in the first three months of a year, the second three months and the third three months. Company will then set how much money can be received by SR if they can sell some unit of product. The more SR can sell the product, the more money they get.

Bonus is typically used to direct effort toward relatively short-term objectives such as introducing new product. In general bonus may be offered in the form of cash or income equivalent, such as merchandise or free travel. Although commissions or salary may be the financial compensation base bonuses are used strictly in a supplementary fashion.

In LUX bonus is not only given as supplementary. Bonus or premium per three month in LUX can help SR to promote themselves to be supervisors. As researcher states before, to be a supervisor SR

only needs three month showing good sales. In other words, bonus hold the important part for SR career in LUX company.

d) Fringe benefit

1. Company insurance programs

Insurance for SR includes accident and death insurance without pension plan. Pension plan is provided by company for supervisor and upper level. Premium for all employee including SR is paid by LUX, while pension plan is paid 2% by the company and the rest is paid by employee.

2. Transportation allowances and field allowances

Actually SR should not worry about transportation because company provides corporate along with the driver to help them to do their work. Besides, company also provides transportation allowances to SR. Therefore, transportation allowances given by company is not real for transportation cost because it just to supports SR in doing their job and selling product as many as possible. In other words, if the transportation allowances is similar to the bonus. It can be considered fixed bonus because it is given if SR can sell two or more unit of product then they will similarly get Rp. 200,000,-.

Another allowance is field allowance. For the first month, field allowance is paid three times every ten days, each of period is paid Rp. 85,000,-. For the second and the following month, the allowance is paid at end of the month. Similar to the transportation

allowances, the field one is just a cash money received by SR only to motivate them to sell product, but the difference is that SR just needs one unit sold then they get Rp. 255,000,-

The advantage of using company car is that SR can be on time coming to the office if not they need to go to targeted places with their own transportation and their own cost. Having the discipline, SR can be on time joining a morning meeting with their manager discussing the strength and the weakness action to sold product, so that effective meeting can then be achieved.

2. Sales contests (incentive)

Sales contest in LUX is called incentive. This incentive can be in cash, electronic product, a trip, training, etc. Sales contest can motivate SR to achieve their target of sales volume as well as their career in LUX, since being a permanent employee SR needs to show good sales performance in achieving their target set by company in three month continuously. Sales force contests are short-term incentive programs that use prizes and awards to motivate SR to achieve goals specified by management. Contests are a popular motivational device.

A contest should have a clear-cut, definite purpose, such as something management wants the sales force to do that it is not doing. Contests are best used to achieve such specific goals as getting new accounts, selling specific products, or relieving certain overstocked inventory positions. In planning and conducting a successful contest,

managers must design the contest, select the prizes, and promote the contest.

Contest Design

The contest should be designed so that each person has an equal opportunity to win. If the average or poor SR learn that the top producers win all the prizes, they will silently withdraw from the competition. Opportunity to win may be equalized through the use of quotas or by allowing for differences in territories and selling abilities. The SR who makes the greatest improvement relative to others is the winner. In this way, even the poorest salesperson has a chance to win.

A variation of the design, described above, is an open-ended contest in which there is no limit of the number of people who can win by meeting their preset goals. In this way, people are competing only with them selves. This is in contrast to a closed-ended contest in which there are a limited number of winners.

Another method of broadening the opportunity to win is to use a tiered contest. In this type of program, two or more levels of prizes are awarded. If salespeople perform at or above a certain level, they get a certain prize—say, a trip to Paris. If they achieve at a lower level, they get a different prize—maybe a trip to the Bandung. This can be used in conjunction with an open-ended contest in which everyone can win.

Prizes

Contest success depends to a great extent on the attractiveness of the prizes. Cash prizes, merchandise, and travel are frequently used as incentives. Cash prizes have the advantage of giving the SR the greatest choice in how to use the prize. On the other hand, travel and merchandise are more visible and interesting to promote and publicize. Also, some studies have found these noncash prizes to be more effective for motivating SR.

Promotion

The sales contest and the prizes which will be given should be widely and continually publicized throughout the duration of the contest. At least 10 percent to 15 percent of the budget for the contest should be spent on promotion. The goal is to keep everyone excited.

Objections to Contests

While contests can increase sales and boost morale, they may also have some unintended effects. Frequently, sales contests lead to undesirable selling methods, such as overstocking, overselling, and various pressure tactics. In the short run, such tactics may enable a SR to win the contest, but in the long run they can cause trouble. Many executives object to contests on the grounds that they create morale problems. To some extent, the open-ended and tiered programs can alleviate the possible morale problems.

One of the biggest objections to sales contests is that, almost inevitably, a decline in sales occurs afterward. The sales force cannot keep up the high level of activity indefinitely. Also, some crafty sales zeps stockpile “orders by getting customers to delay orders in the period just before the contest begins”. Many questions have been raised about the long-run benefits of a contest. If a contest has achieved wider distribution and new dealerships, a long-run benefit should occur. However, if the contest has focused mainly on sales volume, its long-range value is questionable. Lack of permanent accomplishment is not necessarily bad, however. For instance, many contests are designed for a such as selling out on overstocked inventory.

Briefly said, contests can be effective motivators, but they must be carefully and thoroughly designed to encourage participation by the greatest number of people.

4.2.2. Psychological And Social Rewards

Managers often assume that financial incentives are the best motivators and that developing a good compensation package is the only thing they must do to motivate their sales force. However, evidence suggests that SR are motivated by both financial and nonfinancial incentives. In fact, there is evidence that money is not always the best motivator. A variety of factors, including job enrichment, recognition, promotion, encouragement, and praise, motivate performance. These factors are discussed below.

1. Recognition and Honor Awards

A fundamental principle of good human relations is to give full recognition to individuals who deserve commendation. Most salespeople enjoy public recognition of their accomplishments. Plaques, pins, or certificates can be used to recognize accomplishment levels it is really difficult to give too much recognition to anyone.

As stated by Joe Rice, a Belden-Stark Brick Corporation sales manager:

"...The last trip I qualified for was a trip to Istanbul to meet the president of our parent company. I can afford a trip to Istanbul on my own, but a chance to be recognized as one of the top American salespeople is something you can't put a price on... "

(William J Stanton and Hasan Spiro, 1999)

These incentive programs are most effective when they recognize approximately half of the salespeople. If too many people receive the awards, they lose their value; if too few receive them, they may be viewed as too hard to achieve. The awards should be publicized and presented in a public ceremony or banquet. Involvement by top management is also important as this adds significance and prestige to the award. Often clubs are developed for outstanding producers or those who meet certain goals. Membership in such clubs usually bestows on high achievers the right to various recreational diversions in addition to the ego-gratifying recognition connected with just being in the select group. The life insurance industry has long had its Million Dollar Round Table to recognize agents who sell that amount of life insurance each year.

2. Encouragement and Praise

The easiest and least expensive form of motivation is personal encouragement and praise from the manager. Small things such as a word of encouragement, a personal note, a pat on the back, or a thank-you for a job well done goes a long way. Most SR like to feel that someone knows and cares about how much extra effort went into heading off the competitive threat to their largest account or how hard they tried, even though they didn't get that new account.

3. Job Enrichment

Salespeople thrive on challenge. One way managers can challenge SR is by giving them greater responsibility, authority, and control over their jobs. Also, most people like to have variety in their job-related tasks. Doing the same things over and over again quickly becomes boring to someone who is seeking challenge. If managers vary some aspects of the sales job, this can provide a stimulus for increased levels of motivation. Finally, like everyone else, salespeople want to feel that they are performing a meaningful task that will make a significant contribution to their companies and/or to those around them. Managers must make sure that each salesperson understands the importance of his or her contribution to the company's performance.

4. Promotions

Title changes can be another source of motivation. Changing a SR title from sales representative to senior sales representative, for example, can be used to recognize different levels of accomplishment. LUX

Company recognizes seven levels of achievement for career salespeople from sales representative to Direct Sales National. Each level entails a major increase in responsibility. Of course the possibility of being promoted into management is a motivating factor for many salespeople.

4.2.3. Other Elements

Purposes of Sales Meetings

Management can use sales meetings to communicate the company's long-term goals and strategic objectives and to explain how important the salesperson's role is in achieving these goals. This instills in the SR a sense of self-esteem and pride in and identification with the company. This kind of communication is particularly important for salespeople, who are so often physically isolated from their companies. Also, many of them rarely see each other except at sales meetings. Thus the meetings enable them to develop friendships and build team spirit and solidarity.

Sales meetings are also used to inform SR about product changes and new products, to explain new advertising and marketing programs, to provide training, and to inspire the sales staff to work harder and smarter. Meetings such as these can help the sales staff understand what is expected, improve their knowledge and skills, and build confidence in their efforts to succeed.

The impact of the company compensation system

Company wants to encourage salespeople to reach and exceed their goals. Thus compensation plans are designed to motivate salespeople to perform. According to a recent survey, most companies do a relatively good job of using the sales compensation plan to motivate their salespeople. Seventy percent of those surveyed reported that their plans were effective or very effective.

LUX goals "to *make all home is LUX home*" means all people use LUX product. Now most companies try to correlate efforts and result with rewards. It is fair enough to make balance between pay off on effort and on result. But it can be very problematic. A person can be work very hard (expanding much effort) but get little reward because the results of that effort are minimal. It could be that the results are minimal due to factors beyond the control of the salesperson. In reverse, with little effort has brought big results and consequently big rewards. But in LUX, sales people still pay off on result, based on selling volume not based on their effort. That is why all salespeople in this company only concern with selling more product and ignore customer satisfaction.

A good pay plan should act as an unseen supervisor of a sales force by enabling management to control and direct the sales activities. This usually means motivating sales people to ensure a fully balanced selling effort. As a business become more customer focused, its salespeople tend to become territorial marketing managers. This in turn means that they must be motivated to do a total selling job. That is the compensation plan must offer

incentives flexible enough to cover such varied tasks as full time selling. LUX very concern about incentive flexibility because most sallary of SR coming from this part depend on others part, which are bonus and premium. Commissions is very flexible, it is based on volume of product sold by SR themselves. Using this system, LUX can build active sales team in that SR may figure out how much money they will get from company as the result of their hard work in selling the product. As the consequence, a SR must serve as supervisor for themselves.

A good compensation plan should assist in attracting the caliber of sales wanted by the company. A sound plan should also help to keep desirable people. LUX pay plan helps to build the quality of sales force that the company wants, however, it will be hard and time consuming to find and create a good sales team. As stated before that a SR should successfully sell the company products for three month respectively so that he can get the payment as compensation. Otherwise, he will not get any compensation although he has worked full days. Based on the fact, it seems hard for Company to maintain its workers without any security (i.e. payment) for them. Therefore, a quick turning over cannot be avoided and consequently, the company should start to recruit again and will miss too much opportunity cost and time in selling tne company product.

From LUX management's point of view, a compensation plan should be economically administered. Furthermore, a firm wants to keep its sales force expenses in line with those of competitors. Otherwise, the firm

will have to increase the price of its product or suffer decreased profit margins.

A compensation plan should be sufficiently flexible to meet the needs of individual territories, products, and salespeople. Not all territories present the same opportunity. A sales representative in a territory where the same method as a SR in a newly entered district. Flexibility is also needed to adjust for differences in products. Some products are staples and can be sold by taking orders for frequent repeat sales. Others are sold one to a customer and much creative selling is needed.

Generally, nobody wants working in one company without any security. If they can choose other company, they will definitely choose company which provides fixed salary although it is not much. firstly because they will feel safe in working, secondly they can be active salesforce if company offers anykind of incentives so that they can also be loyal to the company.

People are usually interest to join this company because the requirements are easy to fulfill, which is only graduate from senior high school or higher, and does not require certain skill and experiences. Every plan should provide regular income, at least at a minimum level. The principle behind this point is that SR should not have to worry about how to meet living expenses if they have a bad month, if they are sick or cannot work for a period, they should have some income. However, this steady income should not be high that it lessens the desire for incentive pay.

CHAPTER V

CONCLUSION AND RECOMMENDATION

5.1. Conclusion

Based on the data analyzes in the compensation system that supported by the information given by the management, the researcher concludes that:

1. LUX use combination method of the compensation system, commision and bonus. They do not put any fixed sallary for all of their SR. sallary and compensation for SR is all in variable form. This system is regarded unfair because SR work fully in a day (working time in LUX from 7 am to 10 pm) with all risk in working field and no security provided by company. The advantages using single system are less fixed cost, company can hire more employee and this system in one side create their SR to be active to offer and sell their products to get much sallary. If this condition happen progressively SR may do their best to get more sallary and therefore increase the selling volume. On the other side , if SR is not always success to sell the product, their motivation will decrease and if this continuously happens SR can quit anytime. It means company needs to find new employee and need more time to train them, and consequently company will loose much time to market the products the other weaknesses are company hard to find skillful employee and they will not care about other sides of their job, like the quality of product or customer satisfaction. What they care is only selling the products as many as they can.
2. company compensation system can not influences sales team to achieve company goal it can be shown from the data that many of sales people quit, it

it means they are not satisfy with company compensation but the decreasing of sales people not influences product sold Another result can be read from the data that wheater many people join this company the product sold must not increase and on the contrary if many of sales people quit from company the product sold must not decrease. It can be prove from the calculation which relate sales people to product sold as parameter

$\alpha = 5\%$ as constant number

N= 24 month data use to each division of company.

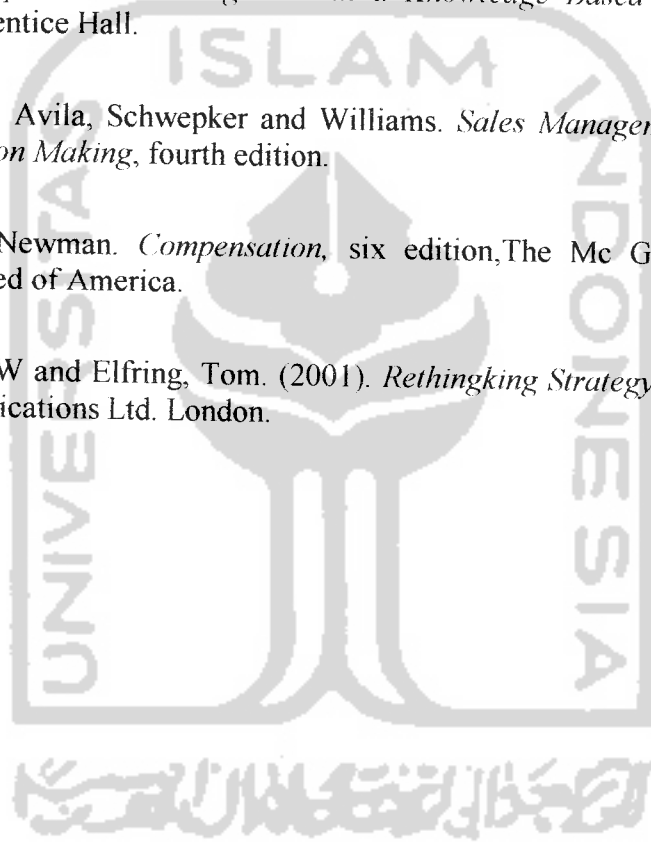
The result is not significant because α from calculation is more than 5% for all division of company. So it can be conclude that how many sales people are in the company not influences at all to the company product sold.

5.2. Recommendation

It is regarded fair enough if company use combination plan of compensation system which are provides fixed sallary for SR although it is just a little aumont and variable sallary, in order to make their SR interested and active to sell more products to get more sallary and other compensation offered by LUX. This combined system can also keep SR working for company and make SR loyal to the company. And it is nice if management not only consider SR performance based on their result but also combine it with all effort done by them, if company just concern about selling the product, their SR will do the same as company treat them. They care only selling product as much as they can, they do not care about customer satisfaction and quality of product.

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**Products sold and amount of SR
2003-2004**

Month Years	Division	SR position				Product sold
		begining	enter	out	end	
2004 January	DD	19	10	9	20	33
	KQ	8	9	8	9	5
	KT	13	-	3	10	27
	DR	-	1	-	1	-
february	DD	20	6	8	18	32
	KQ	9	4	6	7	6
	KT	10	9	3	16	25
	DR	1	-	-	1	-
March		18	8	7	19	27
		7	5	8	4	2
		16	-	3	13	34
		1	-	-	1	-
April		19	2	7	14	15
		4	1	3	2	3
		13	4	1	16	22
		1	-	-	1	-
May		14	11	2	23	34
		2	2	-	4	-
		16	10	1	25	27
		1	-	-	1	1
June		23	10	15	18	52
		4	10	6	8	10
		25	5	12	18	3
		1	-	-	1	-
July		18	2	10	10	31
		8	-	4	4	30
		18	8	6	20	50
		1	-	-	1	-
August		10	10	1	19	34
		4	7	1	10	15
		20	4	4	20	41
		1	-	-	1	-
September		19	10	10	19	28
		10	-	2	8	2
		20	6	9	17	21
		1	-	-	1	-
October		19	4	4	19	48
		8	-	-	8	21
		17	2	3	16	47
		1	-	-	1	1

November		19	3	2	20	53
		8	4	4	8	5
		16	4	4	16	44
		-	1	-	1	1
Desember		20	4	6	18	79
		8	5	8	5	6
		16	6	4	18	
		1	-	-	1	1
2003						
january		31	-	7	24	43
		7	1	2	6	2
		12	-	2	10	15
		-	-	-	-	-
Febuary		24	21	17	28	33
		6	8	6	8	3
		10	8	-	18	20
		-	-	-	-	-
March		28	12	13	27	56
		8	-	7	1	1
		18	1	5	14	21
		-	-	-	-	-
April		27	-	2	25	42
		1	9	-	10	8
		14	4	1	17	25
		-	-	-	-	-
May		25	5	6	24	40
		10	8	8	10	4
		17	3	3	17	56
		-	-	-	-	-
June		24	3	7	20	44
		10	9	5	14	3
		17	2	3	16	30
		-	-	-	-	-
July		20	13	5	28	40
		14	4	10	8	3
		16	10	7	19	20
		-	-	-	-	-
August		28	11	6	33	54
		8	6	5	9	4
		19	4	3	20	22
		-	-	-	-	1
September		33	11	14	30	37
		9	1	3	7	5
		20	5	6	19	22
		-	-	-	-	1
October		30	11	14	27	53

		7	6	3	10	18
		19	16	7	28	45
		-	-	-	-	-
November		27	2	8	21	38
		10	9	6	13	9
		28	2	8	22	53
		-	-	-	-	-
December		21	5	7	19	57
		13	9	8	14	11
		22	2	11	13	45
		-	-	-	-	-

