

WHAT IS COMMISSION AND SHOULD I CONSIDER IT?

WHAT IS COMMISSION?

A commission is a service fee charged by a distributor who makes a sale on behalf of your business. It is usually calculated based on an agreed percentage of the retail price. This method of payment-for-service is commonplace in the sales industry (e.g. brokers, telemarketers and some retailers). Commission is the cost of selling your tourism product (accommodation, tour, experience, activity, attraction) through the tourism distribution system and can be considered a marketing method to capture a customer beyond your reach. It creates an opportunity for an indirect sale through a third-party.

WHAT SERVICE IS PROVIDED WHEN COMMISSION IS CHARGED?

In the tourism industry, a commission is only ever charged when a sale of your product has been made on your behalf. In the lead-up to this sale, the partner will likely have been promoting and marketing your product to their audience, including their ongoing clients, exposing your business and products to a broader or untapped market.

This may include international markets which your business does not have the resources to reach on an ongoing basis, or perhaps where there may be language barrier to overcome.

Some agents will include your business into their brochures and itineraries for promotional activity, while many agents also undertake their own marketing campaigns (e.g. radio, television, online) to draw customers to their retail stores or websites.

WHO RECEIVES COMMISSION?

You can opt to work with a broad range of distribution partners and encourage them to sell a product on your behalf by offering them a commission (or 'discount'). Travel agents, travel wholesale agents, tour operators and some visitor information centres will expect a fee for their service, and this is referred to as the travel distribution system (refer to the *Working with Distribution Partners* fact sheet for more information). These distribution partners each have a different role to play and therefore require different levels of commission.

HOW MUCH COMMISSION DO I NEED TO PAY?

Commission is usually calculated on a percentage off the recommended retail price (or 'rack rate' or 'shelf price'). The amount of commission paid on each sale can vary depending on the type of distribution partner you work through, how many other travel agents /people are involved in the chain of selling your tourism product and the breadth of marketing reach. See below for some examples of how this chain can work and examples of commission structures.

COMMISSION PAID TO SOURCE OF BOOKING			TOURISM OPERATOR PAYS
	DIRECT BOOKING	Customer books direct	0%
	RETAIL TRAVEL AGENT	Customer books through RTA (10-12%)	10-12%
	VISITOR INFORMATION CENTRES	Customer books at VIC (12%)	12%
	ONLINE TRAVEL AGENTS	Customer books through OTA (7-25%)	7-25%
	DOMESTIC WHOLESALE AGENT	Customer books through RTA (10%) → RTA books through domestic wholesaler (10%)	20-30%
	INBOUND TOUR OPERATORS	Customer books through RTA (10%) → RTA books through international wholesaler (10%) → Wholesaler books through ITO (5-10%)	25-30+%

Top Tip

Not all distribution channels operate in the same way, so the above commission percentages are guides only. The distribution method illustrated above is based on traditional Australian markets, however many markets offer wider flexibility in their travel distribution systems.

CAN I AFFORD TO PAY COMMISSION?

Can you afford to turn sales away? If you are booking out your seat/bed capacity without the support of a distribution partner, then you have little to gain; However, if you have spare capacity, then you are potentially missing out on valuable revenue. Making your product available through a distribution partner creates an opportunity to drive sales and cash flow for your business. To ensure you can afford to pay commissions, you will need to have a price strategy, pricing your product appropriately, to ensure your business has the required profit margins. Offering commissions is effectively a form of marketing for your business and is typically much more affordable for small businesses who do not have access to big marketing budgets.

Top Tip

Your retail price should remain the same, no matter the manner in which the customer books. This is called 'Rate Parity' and means that the customer sees **one price** for your tourism product, no matter whether the booking is made directly or indirectly. **Do not add the cost of commission on top of your retail price for each partner;** it is important to have a consistent rate across all sale platforms. This reduces the administrative burden of various price points, provides confidence to the customer that they are receiving the same product or service, and ultimately keeps the 'retail price' of your product consistent.

You can incentivise direct bookings with 'value-add' products (such as a complimentary bottle of wine), but you cannot discount the retail price that you have agreed to with your distribution partner/s. If it is deemed necessary to discount in order to stimulate revenue, offer the discounts to all distribution partners. If you are able to offer the discount early enough, more distribution partners will be able to promote it via their marketing channels.

PRICING YOUR PRODUCT TO INCORPORATE COMMISSION

The recommended retail (or 'market' or 'gross') price of your product is made up of the following cost components:

- **Fixed costs** or overheads required to keep the business open – e.g. electricity, marketing, telephone, admin wages, etc.
- **Variable costs** or the costs associated with supplying the service – e.g. consumables (wine/food), laundry, cleaning, tour hosts, etc.
- **Commission allowance** – the average commission you expect to pay to travel agents (more on this below)
- **Profit margin** or the income that will contribute to your bottom line (e.g. 15-20%)
- **Goods & Services Tax** – should be incorporated into your recommended retail price if you are registered for the GST

Top Tip

Refer to the *Interactive Pricing Calculator* to help you calculate the cost of your product.

WHAT IS AVERAGE COMMISSION?

Your sales are likely to come from a range of sources. Therefore, if you decide to work with Inbound Tour Operators (ITOs), you do not automatically add 25% to your retail price to cover the commissions.

For example, if you make half of your annual sales through ITOs (at 25% commission), but then half of your sales come direct (at 0% commission)- the average commission you pay across all sales is 12.5%. The average commission paid by the South Australian industry, with reliable inbound markets, ranges significantly from approximately 8 to 18%.

You will need to forecast where your sales will be coming from to calculate the average commission you can expect to pay over a year of sales. Generally, it can take more than three years for reliable sales to come through from ITOs. Therefore, if you are just starting out with distribution partners, you can expect that a large proportion of your sales will come direct or through other distribution partners (such as OTAs).

When referring to the example chart below, the operator needs to incorporate an extra 7.9% into their pricing structure. This structure will allow the operator to pay:

- 15% commission on 35% of their sales
- 20% commission on 10% of their sales
- They can even afford to pay 30% on 2% of their annual sales

See the chart below for an example on how to calculate average commission on a year of sales:

A - COMMISSION TYPE	B - PROPORTION OF YOUR ANNUAL SALES	C - WEIGHTED AMOUNT OF COMMISSION
Direct sales @ 0%	53%	0%
OTA @ 15%	35%	3.5%
Wholesaler @ 20%	10%	2%
ITO @ 30%	2%	0.6%
	Total 100%	Total Average Commission = 7.9%

To calculate your average commission:

1. Column B – estimate the proportion of annual sales you will make through each distribution method; the total percentage must equal 100%
2. Multiply each of the commission rates in column A, by the sales proportions in column B. Place the answers in column C.
3. Add each of your answers in Column C to come to your **Total Average Commission** for the year.

Use this chart to calculate the average commission you might expect to pay over a year of sales:

A - COMMISSION TYPE	B - PROPORTION OF YOUR ANNUAL SALES	C - WEIGHTED AMOUNT OF COMMISSION
Direct sales @ 0%	%	%
OTA @ 15%	%	%
Wholesaler @ 20%	%	%
ITO @ 30%	%	%
	Total 100%	Total Average Commission = %

Review your sales record at the end of each year and in order to forecast your average commission for the next year, make adjustments to the above table based on where your sales came from. If you have been undertaking sales or marketing activity towards a certain type of agent, allow for the increase in business expected from that agent type.

Small adjustments do not have a major impact on price, however if a significant proportion of your sales suddenly require commissions you have not allowed for, you may need to readjust your prices or types of distribution partners you are working with sooner.

Top Tip

Note that the tourism trade year operates from April-March. If you are contracted with trade partners, they expect the same prices and rates for the term of the contract, which is usually in line with the tourism year calendar.

HOW DOES COMMISSION IMPACT ON INDIVIDUAL SALES?

It is useful to look at how paying commission can affect the bottom line on a single sale. The following chart compares the impact.

	A - DIRECT	B - RETAIL AGENT	C- WHOLESALER	D -INBOUND TOUR OPERATOR
Commission	0%	10%	20%	30%
Retail Price	\$150	\$150	\$150	\$150
Variable Cost	\$50	\$50	\$50	\$50
= Gross Profit	\$100	\$100	\$100	\$100
Less commission	(\$0)	(\$15)	(\$30)	(\$45)
Money in Your Pocket (to cover Fixed Costs + Profit Margin)	\$100	\$85	\$70	\$55

Each of the above scenarios contributes to your overheads and should add to your profit margin. Even at 30% commission, a sale made through an Inbound Tour Operator supports cashflow and helps to cover fixed costs and keep your business open. In this scenario, paying a commission on a sale is still better than not making a sale at all.

Top Tip

Although there is a cost to selling through distribution partners, resulting in less profit margin, you are still attracting more customers to your business. This creates happy customers who will share their experience through word of mouth – the best form of advertising!

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