CLAP NOW INC

MEMORANDUM

TO: Doug Tyson, VDS President and CEO

FROM: Department of Accountancy---Clap Now Inc.

DATE: February 8, 2006

SUBJECT: Product Data Management (PDM)

This memo contains information regarding the principal-agent relationships, the sources of problems with Product Data Management (PDM) division of Visionary Design Systems, potential solutions and recommendations for changing PDM compensation, potential solutions and recommendations for changing the compensation system for VDS employees, and potential solutions and recommendations for other organizational changes.

PRINCIPAL-AGENT RELATIONSHIPS

The founding fathers are the principals of VDS, and the employees are the agents. Alignment and minimization of the principal and agent's goals and agency problems are due to the principals' option-intensive compensation plan. Agency problems arise as the PDM division reacts differently because the managers have different expectations of the PDM division than the PDM specialists.

SOURCE OF PROBLEMS WITH PDM

The primary source of problems with PDM is that the agents feel that PDM is an investment center, whereas the principals want it to produce profit; consequently, the managers will not fund PDM until revenue justifies it. Most VDS employees and customers poorly understand the PDM market. PDM must spend time to create an infrastructure and customer base. The managers assume that the current option-intensive compensation plan will be an effective motivator for the PDM specialists to be revenue seekers. The managers also want the PDM division to act as part of the VDS team, yet they do not maintain the same communication with them as they do with the other VDS employees. This is partially because the managers are unaware of the PDM industry, and cannot offer the specialists expertise.

POTENTIAL SOLUTIONS AND RECOMMENDATIONS FOR CHANGING PDM COMPENSATION

The PDM division does not currently have an established market or customer base like VDS originally had, so compensation must be based on return on investment (ROI) rather than revenue. In turn, to earn compensation for reaching difficult yet attainable goals, the agents will work harder to grow PDM. Consulting is their profit center; as a result, PDM consulting hours carry more weight in regards to compensation. In addition, VDS's most profitable software deals include PDM software or the future integration of PDM, so PDM software revenue should once again be included in the PDM compensation plan.

POTENTIAL SOLUTIONS AND RECOMMENDATIONS FOR CHANGING THE COMPENSATION SYSTEM FOR VDS EMPLOYEES

Primarily, the new compensation plan must emphasize to employees the importance of PDM software and services sales. More specifically, the sales representatives need a plan that will reward them for selling PDM software and consultation hours to customers. By raising PDM sales quotas and putting more weight on PDM sales in their compensation plans a higher number of sales representatives will sell a larger amount of PDM software.

POTENTIAL SOLUTIONS AND RECOMMENDATIONS FOR OTHER ORGANIZATIONAL CHANGES

Managers need to meet with PDM specialists regularly rather than just twice a year and, because the specialists have specific knowledge, the managers should listen intently and be open to their new ideas. It is crucial that management monitors, and reviews PDM's performance. Furthermore, the managers need to allow the specialists access to capital, and people in order to grow PDM. In specific, the PDM programmers need training so they must work in the PDM division; the sales representatives need to regularly attend PDM sales seminars so the specialists can educate them about PDM software and integration.

CONCLUSION

This memo explains VDS's problems with PDM by examining the sources of problems, potential solutions, and recommendations. VDS's current business philosophy and compensation plan needs modifying because the PDM division is more complex than the rest of VDS. The managers must treat the PDM division as an investment rather than a profit center and suffer temporary losses to experience future revenue.