I

History, Terminology, and Introductory Remarks

One of the world's greatest authors, French philosopher and writer, Voltaire, is known for saying, "If you wish to converse with me, define your terms." This is exactly where we will start our journey, defining affiliate marketing itself, and all of the key terms, participants, and processes. We will also discuss how affiliate marketing fits into your overall marketing mix, how affiliate programs work, and how affiliates differ by the promotion methods they use.

Chapter 1 **Understanding Affiliate Marketing**
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1 Understanding Affiliate Marketing

With its heavy focus on performance, affiliate marketing is a model of advertising that, regardless of its young age, has already gained great popularity among multiple online businesses, including many of the largest brands. It exists at the intersection of all other types of online marketing, and it involves all possible forms of online advertising. In this chapter, I will lay the foundation for your knowledge about affiliate marketing, including looking at its history, its basic terminology, and all its main components.

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What Is Affiliate Marketing?

Affiliate marketing is performance-based marketing, whereby a product or service gets remunerated for every sale, visit, or subscription sent to the merchant. Because of this performance-based component, which is the cornerstone of affiliate marketing, it is also sometimes called *performance marketing*. The payment arrangements used include pay-per-sale (or cost-per-sale), pay-per-lead (or cost-per-lead), pay-per-click (or cost-per-click), pay-per-call (or cost-per-call), and other similar action-dependent compensation patterns. They are also frequently referred to as cost-per-action (CPA) payment models. Cost-per-action means affiliates' compensation is wholly dependent on their performance. CPA is a type of remuneration that essentially says, I'll pay you when there is action. In most cases, advertisers have to choose one of the payment models, but in some cases there is room for more than one type of compensation in one affiliate program. For example, a merchant can use the cost-per-sale (CPS) and cost-per-lead (CPL) models together, paying 10 percent commission on each sale (CPS) as well as $0.50 for each newsletter sign-up (CPL). Or an advertiser may decide to employ both the CPL and pay-per-call (PPCall) models within one program, by paying both for lead-generating forms filled out on their site and for phone calls referred by affiliates.

Origins of Affiliate Marketing

Mainstream affiliate marketing owes its birth to CDNOW.com and Amazon.com. In November 1994, CDNOW started its BuyWeb program, which was the first online marketing program of its kind at that time. Amazon continued this pattern in July 1996 with its associates program. Amazon claims to have more than 1 million associates worldwide as of 2010.

An affiliate (marketing) program is a business arrangement whereby one party (the merchant or advertiser) agrees to pay another party (the affiliate or publisher) a referral fee, bounty, or commission for every occurrence of a desirable (to the advertiser) action. Examples of such actions include sales and leads that occur in the event of the end customer clicking the affiliate link prior to completing the sale/lead. It is important for the advertiser to define what will make the end user's actions qualify for affiliate remuneration. That's where we get the lingo of *valid leads* and *confirmed orders*. You don't want to pay for fake, or fraudulent, "referrals." I will discuss this topic in more detail in the following chapter.

Depending on the merchant's preference, an affiliate program may also be called an associate, commission, revenue-sharing, bounty, or partnership program. The payment pattern is always a pay-for-performance pattern: When there is qualified action, there is payment.

Since most of the traditional scenarios involve compensating affiliates for sales and leads, these will be the main examples used in this book. Also, although there are different terms for affiliates (see the next section), I will stick to the terms *affiliate* for the marketers who get compensated based on performance and *merchant* for the advertiser who the affiliate has their performance marketing relationship with.

Affiliates, Subaffiliates, and Superaffiliates

Now let's turn to three terms you need to be comfortable with as far as different affiliates go: affiliates, subaffiliates, and superaffiliates. It is important to understand what these terms mean, how they differ, and what they have in common.

Affiliates

Sometimes also called *associates* or *publishers*, affiliates are essentially independent marketers who may choose to promote a business and be paid according to one of the previously described performance-based models. They are the sales force for your affiliate program. I like to think of affiliates as dealers or your most valuable partners who promote your brand and your business, investing their own money to sell your product/service.

Affiliates are *independent* marketers who choose what affiliate programs to promote, what programs to drop, what merchants to push more aggressively, and on what merchants to spend less effort. They are self-managed and in the vast majority of cases are not accountable to merchants for performance. All of this makes them very different from the traditional business definition of an affiliate. On the other hand, the freedom that undergirds their very business existence allows affiliates to develop into an extremely self-motivated workforce. I will talk about it more in the following chapters, but at this stage, you should understand that this lack of top-down influence and control does not hurt affiliates' productivity. In fact, the freedom that's embedded in affiliates' hearts helps them achieve heights that would have been otherwise impossible.

What I Don't Mean by *Affiliate*

The term *affiliate* can be easily mistaken for something that it is not. Flipping through literature on business and economics, you will see the following definitions:

- *Compilation of State and Federal Privacy Laws* tells us that the term "means any company that controls, is controlled by, or is under common control with another company" (Privacy Journal, 2002).
- Michael R. Lavin in his *Business Information* points out that the term "can be used as a generic word to indicate either a subsidiary or division" (Oryx Press, 1992).
- Arvind V. Phatak in his *International Dimensions of Management* writes that terms such as *affiliate* and *subsidiary* should be (and are) "used synonymously" (Dame Publishing, 1994).

Continues

What I Don't Mean by *Affiliate* *(Continued)*

- Finally, in their *Security Analysis: Principles and Technique* volume, the infamous Benjamin Graham and David Dodd make an observation that *affiliate* is more indefinite than *subsidiary*. They write that "an affiliate may be a company effectively controlled—perhaps jointly with others—though ownership is less than 50%. Or the relationship may exist through control of both companies by the same owning group or 'parent,' with resultant close commercial or operating ties." Also, "in some cases a company may be called an affiliate although it really is a subsidiary." (McGraw-Hill, 2005)

None of these is even close to what the term *affiliate* means in the context of affiliate marketing. Looking at the mentions of common ownership, control, and "close commercial or operating ties," you can conclude that one *affiliate* can justly be characterized as an *antonym* of the other. Not one of these elements is present in the context of the affiliate-merchant relationship.

Subaffiliates

Subaffiliates are your second-tier affiliates, or affiliates who have joined your program by a referral from an affiliate you already have on board. Some affiliate programs choose to pay both the subaffiliate and the affiliate who sent them to you on a first- and second-tier commission basis. You will learn about the pros and cons of such a setup in the section called "Tuesday: Determine Whether You Need a Two-Tier Program" in Chapter 6, "Week 4: Finalize Payment Models and Cookie Life."

Figure 1.1 reflects a self-description provided by an affiliate who wants to act as a first-tier affiliate, redistributing profit between his subaffiliates. In this case, the merchant does not have a second tier in its program, but the affiliate has set up a system to make this possible. You'll learn more about this later in the book.

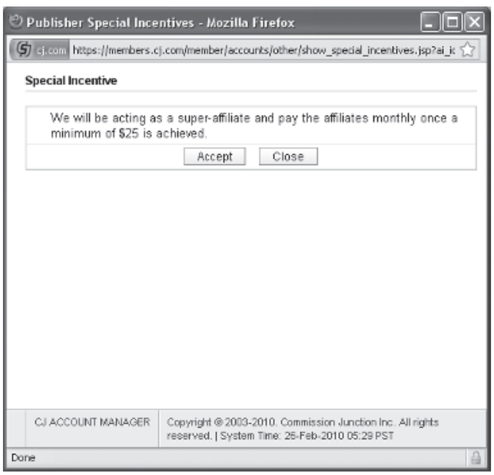

Figure 1.1 Affiliate self-description. They will be considered a first-tier affiliate rather than a subaffiliate.

Superaffiliates

Superaffiliates are affiliates capable of generating a substantial amount of traffic and sales for merchants. I like to define superaffiliates in terms of the following three characteristics, in order of priority:

Maturity Superaffiliates generally manifest high levels of professional and psychological maturity. They are able and confident in what they do.

Potential One such affiliate can turn a whole affiliate program around. From what I have seen in the programs I have managed and also in the statistics reported by other outsourced program managers (OPMs), it is not unusual for one to three such affiliates in the program to drive 50 percent to 70 percent of all affiliate program sales.

Income They are steadily making at least five figures a month in gross profit and are normally involved in affiliate marketing full-time.

Although some people may mention "preferential treatment" as a characteristic of superaffiliates, this factor has no place in the definition. Private offers, co-branded landing pages, and other manifestations of the "preferential treatment" are consequences of superaffiliates being what they are, not determinants.

In addition to the previously mentioned characteristics, it is important to address a topic that I call the "problem of superaffiliate recruitment." One of the questions that is most frequently asked by merchants—both those who have just launched an affiliate program and those who have already been in this business for some time—is, "Where and how can I recruit some of those superaffiliates?"

Superaffiliates are not your easy-to-catch type of fish. It often takes years of relationships development, networking in the right circles, attending the right events, and making contact with the right people before you can recruit a superaffiliate. Additionally, every merchant should be aware of two factors. First, many superaffiliates are often focused on particular niches and do not sign up for programs that are functioning outside their niches of interest. Second, superaffiliates generally partner with affiliate programs that have a proven track record and a solid conversion rate that can be verified through third parties (normally, affiliate networks).

If your affiliate program is new or underdeveloped, you have little to no chance of recruiting an existing superaffiliate. There is, however, a solution.

I believe that any affiliate manager can help a new affiliate grow to a superaffiliate status. If your product/service sells online, it should also sell through the affiliate channel. What you need is either a marketing expert (paid search marketer, SEO specialist, video or mobile marketer, and so on) who would be willing to work with you on a commission basis or a website that already has the traffic you are targeting, and then you need to convince them to try your affiliate program by putting up a link or two on their site. Both of these methods have worked for me in the past. I have seen skilled online marketers, who have never tried an affiliate program before, turn into top affiliate producers, and I have also seen popular content websites that were attracting the same audience as my clients become the best affiliates in the program.

So, even though talking an established superaffiliate into working with your program may be challenging, there is another way, and it's one that successful affiliate program managers have been using for years: A manager can help a newbie become a superaffiliate.

Affiliate Marketing vs. Multilevel Marketing

The amount of business and even e-commerce literature that equates affiliate marketing to multilevel marketing (MLM) is substantial enough for me to address this common misconception in the very first chapter of this book. Paul Ford, for example, in his *Multi-Level Marketing* brochure, states that affiliate marketing is just another term for MLM, a name that appeared because of recent changes in legislation regulating businesses that employ multilevel systems (Real World Real Money, 2010). Shah and Erickson in their *Dictionary of E-Commerce* state that affiliate programs use "a multilevel marketing concept where consumers (affiliates) attract additional consumers" (J.L. Kumar for Anmol, 2003). As explained, affiliates are most often not consumers but marketers and, frequently, professional marketers. Also, the "multilevel marketing concept" is utilized only when a program has the previously described second tier, which allows affiliates either to earn a one-time bounty on every affiliate they refer to the merchant (for example, you may decide to pay your existing affiliates $1 for every new affiliate signup) or be paid a lifetime second-tier commission on all sales generated by the affiliates they refer (for example, a merchant may be paying a 10 percent commission on the first tier and 2 percent on the second tier). It is this last possibility that confuses some people, and it is important to mention that it is extremely unusual for any affiliate program to have more than two commission tiers (most have only one).

In her *Riches in Niches* book, Susan Friedmann warns affiliates about being trapped into MLM type "affiliate" programs, especially those that charge affiliates to join the program (Career Press, 2007). Just as the sign-up fee should immediately raise a red flag in the affiliate's head, so should the presence of multiple tiers.

Another interesting point is being raised by Scott Dacko in *The Advanced Dictionary of Marketing*. Dacko states that the scope of network marketing (also known as *matrix marketing* or *multilevel marketing*) overlaps "with many aspects of affiliate marketing." He writes that the basic approach of both affiliate and MLM is united by "the use of an interconnected system of firms or other individuals outside the organization who essentially act as agents of the firm in facilitating the distribution of the firm's offerings and in securing sales from end customers" (Oxford University Press, 2008). The author is only partially right—both affiliate and MLM use outside people to market a product/service. However, the outside sales force that is "interconnected" in MLM programs is not in any way interlocked in affiliate marketing programs. Additionally, although the primary goal of most MLM schemes is to create (and profit from) pyramids of resellers, the main idea behind affiliate marketing is the creation

Affiliate Marketing vs. Multilevel Marketing (MLM) *(Continued)*

of a direct partnership/affiliation between a merchant and an affiliate, as well as collaborative work toward the achievement of common goals such as creating sales, leads, or other desirable customer actions.

Affiliate marketing is *not* MLM, and a close look/comparison quickly reveals the differences.

Universality of Affiliate Marketing

Affiliate marketing is *universally applicable*, and any online business can be enhanced by running an affiliate program. Since the essence of affiliate marketing is in placing the main emphasis on the actual consumer action that occurred, it is always a no-lose situation for the merchant (unless you pay for clicks, of course). When starting an affiliate program, you may decide to remunerate affiliates for clicks sent to you. This is only one option. In fact, most affiliate programs do *not* do this. Most merchants tie the compensation of affiliates solely to the registered and confirmed sales or leads (fraudulent, duplicate, and other unqualified actions do not count).

If you're hesitant, go to any search engine, and see what your competition is doing. Basic competitive intelligence has never hurt anyone. Chances are that upon querying any major search engine by using a "<your product> affiliate program" key phrase, it will be much easier for you to make your decision.

Another aspect of universality that is important to point out is that affiliate marketing is universal by its very nature. It exists on the crossroads of all other types of online marketing. I frequently underscore that affiliate marketing is not a type or kind of marketing. It is more appropriate to understand it as a special marketing context, the undergirding principle of which is its performance-based remunerating model. This model works with any type of marketing: display, contextual, video, social media, and other types of advertising, as well as search engine marketing (SEM), email marketing, and other methods. The only difference with the pre-affiliate model is that advertisers *post*-pay and do it for the actions of their choice, as opposed to *pre*-paying for the actions of the publisher's choice (for example, you can run an ad on a content publishing network and not pay them by thousands of impressions [CPM] but for the actual conversions that these impressions generate).

Marketing Channels and Types of Affiliates

Since I have touched upon the subject of universality, it seems appropriate to now expand the topic and look at types of affiliates. Successful affiliates seldom exist in a pure form but are more often incorporating several marketing approaches in their strategies. However, for you to better understand how things work, it is helpful to break down the more popular approaches into groups. They all cover an online marketing channel, and I like to split them into the following five groups.

Content Publishing

Affiliates who employ this method build content-saturated websites (as in our example in Figure 1.2) and monetize them by featuring merchants' links on those properties. Links should be understood as all possible types of affiliate links: banners, widgets, text links, video, product links, and so on. The ways in which a content affiliate may advertise a merchant range from in-text links to sidebar ads to separate sections devoted to merchants' banners to even a product selection. Examples of content publishers would include both large portals like Forbes.com and smaller content producers like bloggers.

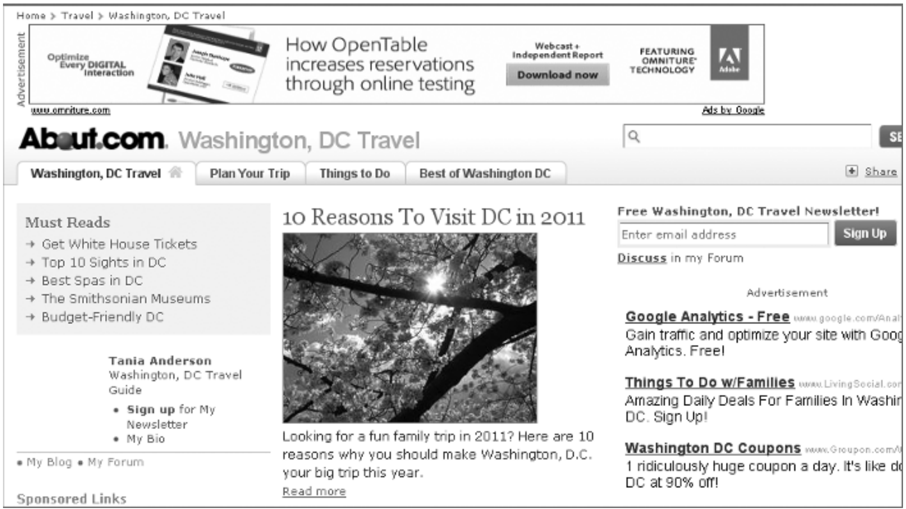

Figure 1.2 About.com is a classic example of a content publisher.

Couponing

Multiple affiliates are already using this method of promotion, and with projections on online coupon use anticipated to increase further, new coupon websites should be expected to spring up. These affiliates play on the human psychology of trying to find a product at a discounted price if possible. To satisfy this demand, these affiliates put together collections of coupons from different merchants (see Figure 1.3). Since the number of coupons gathered "under one roof" can easily exceed several thousand, the key to success is in the convenient categorization of deals. The more successful coupon affiliates segment their coupons by vertical markets, holidays, lowest price markdowns, expiration dates, types of coupons (for example, deal of the day, free shipping, buy two...get third free), and so on.

Figure 1.3 Example of a coupon affiliate website

Data Feeds

A whole segment of affiliates work with merchants' product feeds. They are generally selling products of multiple merchants "under one roof" (see Figure 1.4), importing product information into their websites via the use of data feeds that merchants make available to them.

A subgroup of *comparison shopping affiliates* should definitely be mentioned here. Adding the convenient function of cross-merchant price checking or feature checking to their online engines, they add value by simplifying the product search and comparison process for the end user.

Figure 1.4 Shopzilla is a data feed–driven website

Email Marketing

Any individual or organization that has a mailing list of targeted prospects who have opted in to be contacted can make an excellent email affiliate. Here, just as is the case with any type of affiliate, it is important to emphasize that merchants safeguard their own brand and reputation by partnering with acceptable marketers. It must be made explicitly clear that advertising considered spamming or unsolicited commercial email (UCE) is unacceptable and will be penalized. Let your emailers know they may use mailings to customers and opt-in e-mail lists only so long as the recipients are already customers or subscribers of the affiliate's services or websites and that recipients have the option to remove themselves from future mailings.

Paid Search

Many PPC marketing experts turn to affiliate marketing to monetize their skills and expertise. Such affiliates bid on merchant-specific keywords and key phrases at Google (Figure 1.5), Yahoo!, Bing, and other search engines, and they send the PPC traffic either directly to the merchant's website or via an in-between page of their own (depending on their own goals and the restrictions imposed by the merchant). In multiple situations, paid search affiliates can replace either the merchant's in-house paid search marketing expert or an outsourced solution. As with every affiliate, the main benefit is that the PPC affiliate invests their own resources and costs the merchant only when the desirable action occurs.

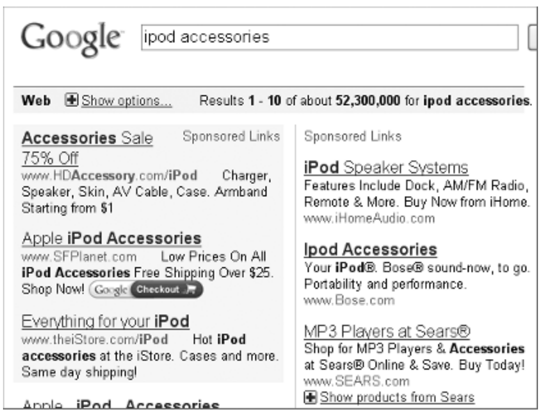

Figure 1.5 Google AdWords ad units

Loyalty Marketing

Loyalty marketing has been around for a while. It became especially popular when airline companies started using it. Airlines would reward their customers with "frequent flyer miles," which are, essentially, points that, once accumulated to a certain threshold, qualify the customer to obtain a free airfare or other product/service. Now, while traditional loyalty marketing aims to "reward loyal customers for making *multiple* purchases" (*Essentials of Marketing*, 2008), loyalty affiliate websites focus on one sale/transaction at a time. Loyalty affiliates (also known as *incentive affiliates*) facilitate the desired user action by offering them an incentive. Cash-back/rebate offers, donations to charitable organizations, and contributions to scholarship funds are by far the most popular forms of incentives used by this type of affiliates (see Figure 1.6). FatWallet.com, BigCrumbs.com, and CashBaq.com are classic examples of incentive affiliate websites. The idea behind such a business model is simple: Share a part of the revenue you receive from the affiliate program with the end consumer.

Figure 1.6 Example of a cash-back affiliate

Many merchants and affiliate program managers do not know what loyalty affiliates are and how they operate. This, in some cases, results in low-quality affiliate program performance, whereas in others, it may bring about unwanted customer activity. To illustrate how it works when it does work for the merchant, look at the following example:

- Merchant A pays 10 percent commission on all orders.
- The incentive affiliate offers its visitors a 5 percent cash-back reward.
- Everyone (customer, merchant, and affiliate) is happy.

However, there are instances when partnerships with incentive affiliates do *not* work (and cannot work) for the advertiser/merchant. I'll model three contexts to illustrate such a situation. If one of the following performance-based payment models describes your current or prospective affiliate program, you want to explain in your program's terms and conditions that you do not work with loyalty affiliates and screen affiliate applications carefully to look for sign-up requests from incentive/loyalty affiliates.

Scenario 1

- Merchant B (hosting company) pays 50 percent or $25 (whichever is greater).
- The incentive affiliate offers $15 cash back on all orders.
- Problem: Customer signs up for only one month of hosting at $6.95.

Scenario 2

- Merchant C (diet supplements merchant) pays $35 per sale (including orders for free trials).
- The incentive affiliate offers $20 cash back on all orders (including free trials).
- Problem: Customer orders a free trial.

Scenario 3

- Merchant D (credit relief company) runs a PPL affiliate program paying $20 per lead.
- The incentive affiliate offers $10 cash back to everyone who fills out the form on the merchant's website.
- Problem: Obvious.

The marketing model used by incentive/loyalty affiliates can work for you when your affiliate program's specifics allow for this type of online marketing. In certain contexts—such as the three scenarios—affiliate program managers should keep the incentive affiliates out of their programs. In essence, the problem in all three cases is in the misalignment of merchant and affiliate interests. Loyalty affiliates can work extremely well in scenarios where merchants are paying a percent of sales rather than a bounty or a per-lead amount.

Additionally, in cases when there is room for a merchant's partnerships with incentive affiliates, affiliate program managers should regularly monitor their behavior. Some incentive/loyalty affiliates are known for using cookie-overwriting toolbars, forcing clicks, and engaging in other unethical behavior. I will discuss these problems later in the book to equip you to police and fight such behaviors.

Partnerships with acceptable incentive affiliates can bring additional sales to your affiliate program. Conversely, partnerships with the wrong types of incentive affiliates can do your program much damage. It will simply not grow beyond the level of sales that a handful of unethical affiliates can refer to you, interfering with the performance of your other online marketing channels; in addition, no decent affiliate will want to work with you. This principle applies not only to this particular type of affiliates but to any rogue affiliate in the program (be they a paid search or a loyalty affiliate).

Social Media

This area is quickly gaining popularity among Internet users, and affiliates are happily leveraging this growing acceptance of forums, microblogs, social networks, and other social media channels. Some affiliates are putting together Facebook apps and monetizing them through affiliate marketing, others are tweeting deals on Twitter (with the help of tools like the one in Figure 1.7), while yet others are creating social shopping engines where users can interact with each other, helping each other shop. The more sophisticated and innovative the method is, the more successful the affiliate generally is. Just as it is with other types of affiliates, make sure you partner with marketers that have ethics on their side and are helping you build your brand.

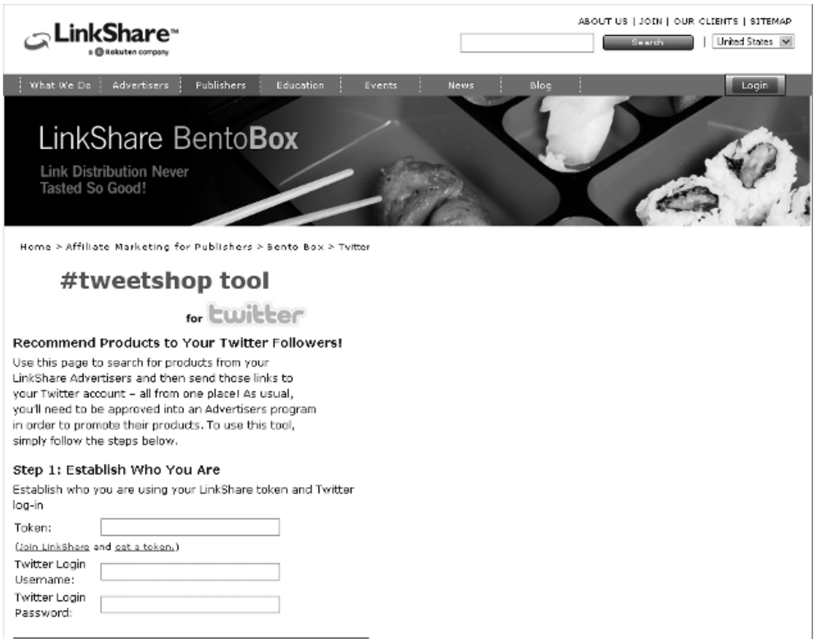

Figure 1.7 TweetShop Tool by LinkShare affiliate network encourages affiliates to market on Twitter.

Video

Online video is a technology that is enthusiastically accepted by end users. However, the number of affiliates using it is still relatively small. If the affiliate program platform allows for it (as in Figure 1.8), you want to provide affiliates with any video creatives (that would track referring clicks and credit commissions when they are due) or allow them to use their own (encouraging them to produce video clips for marketing use). In the least sophisticated scenario, encourage them to at least embed YouTube (or Viddler) videos into the pages of their blogs/websites, complementing the video with search-engine-friendly text and linking it to you through an affiliate link.

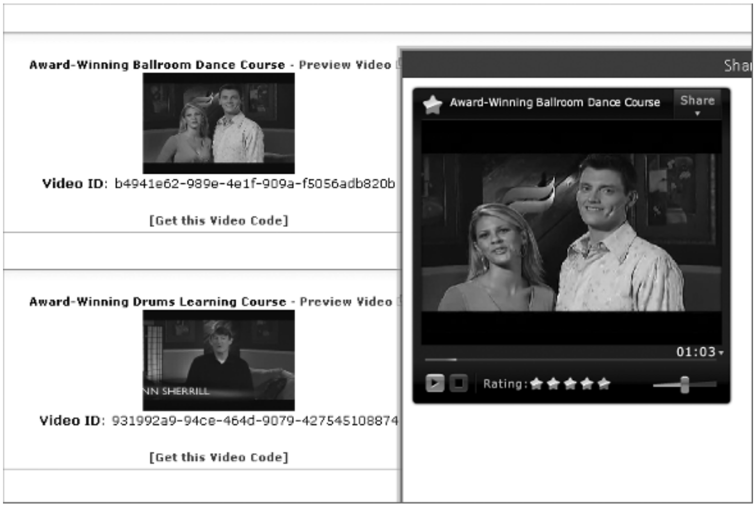

Figure 1.8 Video creatives by Legacy Learning Systems offered through ShareASale affiliate network

Any of these methods can be generic or niche-oriented. When an affiliate chooses to be "niche," they specialize in a particular niche (or niches) only, optimizing their website in such a way that it gets most of that targeted traffic. Examples of popular affiliate niches are apparel, shoes, entertainment, books and magazines, and sports.

Note also that my list does not include those I call wanna-be affiliates (banner farms are the best example). Each of the groups has its superaffiliates. You need to understand the way each group works, what problems and challenges they encounter, what factors they are considering while looking for an affiliate program to join, and what they want you as an affiliate program manager to help them with once they are on board with your program.

The famous Peter the Great was known for striving to learn everything first-hand, from the inside out. With this philosophy in mind and disguised as a common man (even though he was the emperor of Russia), he traveled to the Netherlands and England to study shipbuilding and sailing. This knowledge and experience helped him build Russia's first navy, which was instrumental in his wars against the Ottomans and the Swedes. I always encourage affiliate program managers to follow the emperor's example and start affiliate accounts with all major networks. Take your time to try them yourself in the capacity of PPC affiliate, mall affiliate, coupon affiliate, and so on. Try various affiliate tools provided by the networks and third parties. You will gain invaluable experience in the process. Do not quit those accounts. You'll need them later for ongoing competitive intelligence.

Popularity

Affiliate marketing is one of the most powerful and cost-effective customer acquisition tools available to an online merchant today. You decide what commission to pay and pay only when results (sales, leads, and/or clicks) are obvious.

Remember that unlike with other channels of distribution, affiliate marketing hardly has any advertising and marketing expenses involved yet often shows the best return on investment (ROI). With affiliate marketing, you pay only for the desired performance. With most other advertising, however, you get no performance guarantee, and generally the results aren't as good.

If you are not yet utilizing the affiliate marketing channel, I'm glad you're holding this book in your hands. It will teach you the ins and outs of affiliate program management and help you start and run your own affiliate program. I know you won't regret it.