

Are Agencies Paid Too Much... A Self-Administered Test

Anyone asking that question typically has a motive. Or, think they already have the answer.

If you would have asked me that question when I ran Grey Worldwide or FCB, my answer would have been "NO -- how can you ask me such a thing". But, I am sure most of the client CFO's and Procurement Officers I worked with had a different answer.

So, how about a test? A few questions you can answer in the comfort and privacy of your office about your current agency compensation arrangements. In the end, you can judge for yourself whether you might be paying your agencies too much, or not.

1. Do you pay based on commission or level of spending?

If yes, you must like simplicity. It is the old standard and typically has absolutely no relationship to the work or creative/media output your company or brand needs.

2. Do you pay your agencies on cost plus or man-hours which covers agency salaries, overhead and guarantees them a profit?

If yes, you are not alone, but who and how is staffing determined -- by you or the agency? And, do you have any idea whether that staff is actually working on your business at the contracted percentages? And, what is and isn't in the overhead rates? And, are they truly associated with running your business? Finally, are guaranteed profits no matter what the outcome fair to you?

3. Does your compensation arrangement encourage agency efficiency?

Don't know? Cost plus or commission systems pay based on spending or man-hours. The more of either, makes the agency more money. In fact, the agency is actually incentivized through either system to be inefficient.

4. Do you develop a SOW document with your agency based on the primary brand or company objective(s) and what is needed?

You might, but most SOW documents end up being a project list. What it should be is a blueprint -- a living, breathing document that both the agency and client develop together and refine as the year unfolds. Complexity, creative rounds, number of teams should all be determined in the SOW. "Need" or "output" should be the basis of your compensation arrangement.

5. Waste! Are you limiting or setting any parameters for the work requested on the SOW?

While no one wants to limit creativity, agencies typically like to function with an "open checkbook". Many times they create (or are asked to create) multiple solutions to an assignment without any regard to cost. Unlimited teams, unlimited rounds, waste your money, increases staff hours unnecessarily and many times makes it unprofitable for the agency as well.

6. What happens if marketing conditions change? Does your fee adjust up or down or do you have a fixed compensation arrangement?

Most cost plus man-hour agreements are based on a fixed staffing plan or a set fee. But, marketing is a dynamic ever-changing environment, so if cost cutting is needed, it is very hard to change cost plus agency fee arrangements without reopening agency negotiations each and every time.

7. Do you sit down with your agency and spell out in "measurable terms" what is expected of them?

Agencies are hired to do something! But, most clients don't establish an overall goal that can be measured and evaluated to determine if you are getting what you are paying for in terms of results.

8. Do you pay your agency a bonus? And, is it meaningful?

Most clients do, but if it isn't tied to why the agency was hired in the first place and measurable metrics, why have it? Agencies loves to say, they want "skin in the game". But, most bonuses are so small and written off by agency management they provide little effect on agency behavior.

9. Does your agency get its profits (built-in or guaranteed) no matter what happens?

This is the missing component. In most compensation arrangements, agencies get their 15-20% profit margins no matter what results they achieve. And, are they held accountable for the "marketing partner" label they so frequently use. It is only fair to ask an agency to put all of its profits (not base costs) on the line if the metrics are fair and measurable.

10. Would you pay your agency more than the standard 20% profits for incredible work?

The best clients want to pay their agencies more, not less. But, they also want that agency to help them generate, one way or another, the extra revenue to pay above that profit margin standard. If you want the best work, the best talent, agencies should be paid more than 20% when they hit one out of the park.

So how did you do? My guess based on my experience running agencies and working with many different client organizations, you are probably not optimizing your agency compensation arrangement, and in turn it is costing you money.

According to AdAge, the top ten agency communication groups generated revenue of over \$52 billion in commissions, fees and services to clients (and that is just a part of what clients are spending with agencies today).

That's an enormous amount of money and I will venture to say there is a lot of waste, overpayments and unsuccessful results associated with that \$52 billion. Agencies increase brand value and that is a proven fact. But, clients need to pay for that value only when the work, works without the inefficiencies and waste cost plus man-hour and commission systems encourage.

If you change your compensation arrangement and start paying based on need and success, your agency relationship will change fundamentally, but for the better.

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