Agency Compensation: Where Are We Today? Fiction vs. Reality

Fiction #1: There is a single compensation method that is ideal for all advertising accounts.

- ANA studies provide evidence from analysis of 300+ client-agency relationships, no two agreements were exactly alike.
- Conclusion: Each agency has the opportunity with each account to find a unique compensation method to best serve the client and yield a reasonable profit for the agency.

Fiction #2: The only objective of compensation negotiation is to minimize the agency income.

- Set objectives that infuse negotiation discussions with advertising quality and services issues.
- Make a point to clearly demonstrate the link between the cost of agency service and its value.

Fiction #3: Since advertising agency cost accounting systems are generic, advertising agency services are generic.

- Don't allow cost accounting data to become the dominant basis for compensation negotiation.
  - Use it as a tool for understanding the service requirements.
  - Never forget the value of an idea.
- Take the opportunity to set up performance measures of your own.
  - Let your clients know what you can do for them.
  - If you don't set the standards, your clients will.

Fiction #4: Advertising agency cost accounting data are now used to maximize <u>efficiency</u>.

- But not many agencies use cost accounting data to analyze the cost and profitability of each account.
- Conclusion: Get a handle on it.
  - Be able to unbundle your services:
    - Know where your costs are attributed.
    - Know the manhours needed for various activities; different categories of business.
  - Evaluate economies of scale.
- Avoid subsidizing small accounts through large ones.
  - Reassess your smaller accounts and make them self-sufficient.
  - Resign accounts that are perennial losers.
- Investment spend
  - Put manhours to work on spec.
  - Nurture – not milk – long-term relationships.

Fiction #5: The longer you put off discussing compensation with a client, the better off you're going to be.

- It's asking for trouble.
- Put your cards on the table – let everyone know where they stand from the outset.

Fiction #6: Compensation is the exclusive domain of the agency CFO and CEO.

- Senior people, both account and creative, need to know your compensation philosophy.
  - Train managers in pricing strategies.
  - Examine internal approval processes for pricing contracts.
- Conclusion: Exude conviction that your clients receive outstanding value for the money they pay.

Fiction #7: The best offence in compensation discussions is a solid defense.

- Be more forthcoming
    1. Compete on the basis of how big your ideas are, rather than how little you will charge for your work.
    2. For each of your clients, find a compensation system that exactly fits your needs and the needs of your client.
    3. Work to understand the relation of your costs to the excellence of your product.
    4. Give your organization knowledge of, and confidence in, the way you price the product you sell.
    5. Be positive and constructive in compensation discussions, rather than reactive and reclusive.

Reality: What Agencies Can Do In The Future

- Unbundle services and charge realistic prices or fees for each service.
    - Don't do small budget assignments for free.
    - Don't give away ancillary services unless it's an "investment spend" situation.
- Be more innovative with your compensation plans.
    - Study how other service organizations get paid.
    - Value your ideas, not the labor involved.
- Change your perspective from being <u>billings-oriented</u> to being <u>profit-oriented</u>.
    - Concern must be aimed at margins and absolute profit enhancements, not unit growth.
- Know that you're in the driver's seat.
- Restructure your thinking about costs.
    - Find a relevant organizational mechanism for reducing hierarchies and managing the service mix in an integrated fashion. The "team" approach.
- Develop more powerful arguments for what is cost and what is profit.
- Push for bonuses for superior performance.
    - If you do a great job – you deserve to make more money.