Truth in advertising: Achieving transparency with media rebates to fuel growth

Advertisers can build more transparent, partnerlike relationships with their media agencies by taking four steps.

Sarah Armstrong, Joe Regenbogen, Rachael Schaffner, and Robert Tas

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“We’re at an interesting point—CMOs can achieve more success now by showing growth versus cost cutting.” This quote comes from the former CMO of a leading global brand and reflects a broad desire in businesses to turn marketing into a bona fide engine for growth. An important way to make that happen is to free up dollars and funnel them into high-growth opportunities.

However, finding those dollars can be challenging when it comes to media spend. This is because many companies don’t have a clear view of where their dollars are going and what impact they are having. This lack of clarity means that a significant portion of media spend—in the form of fees or rebates—isn’t recouped by the marketer. In our experience, marketers can address this issue and fuel growth by increasing transparency between advertisers and media agencies, which decide where consumers should see marketing messages, and then purchase the needed ad space from broadcasters and digital platforms.

Transparency is a hot topic in the advertising world today. Many large advertisers have long felt a lack of clarity in their relationships with media agencies. Companies that make sizable media buys often find themselves asking: What are we paying for? Are we getting all we are entitled to from our spend?

Advertisers currently have concerns about agency transparency—or the lack thereof—in three primary areas: media rebates, programmatic fees, and data and tech sharing/ownership.

Media rebates. Agencies often don’t disclose or pass along to their clients rebates (also known as agency volume bonuses, or AVBs) they receive from media companies.

Programmatic fees. Programmatic digital-media buys often carry difficult-to-understand and at times opaque agency fees whose face value is small—pennies per activation—but can add up when the numbers involved reach into the millions.

Data and tech sharing/ownership. Agencies typically share only the data generated by ad tech platforms, which may not provide an optimal view for clients. They are also sometimes in charge of parts of a client’s tech stack, even though advertisers can achieve more data transparency and greater control by running the stack in-house.

This article focuses on how advertisers can drive the changes that ensure greater transparency in connection with media rebates/AVBs. It is informed by more than 100 engagements with marketing organizations over the past two years, as well as a series of interviews with industry executives, including many CMOs at global advertisers.

Marketing organizations that tackle this issue effectively can get access to rebates they are entitled to receive—which can amount to millions of dollars, or even tens of millions at the largest advertisers—and reinvest them in growth. They can also put their relationships with media agencies on a sounder, more trusting footing, where both parties can work together, in partnership, to achieve win-win outcomes.

Rebates today and how the industry views them

Rebates paid by media companies to agencies—and often not passed on to advertisers—have long been a fact of life. Rebates are lowest for traditional media, such as television and radio, where they can total up to 5 percent of overall spend with a given TV or radio supplier. Even though this isn’t large on a percentage basis, when advertisers invest a major portion of their budget in traditional media, rebates can amount to very large sums. Rebates for out-of-home advertising are typically larger, as much as 15 percent. In digital media, rebates are the largest, estimated at 20 to 35 percent, when both cash and noncash AVBs are included.

The rebates question had been brewing for a while, but it became a top-of-mind issue after the 2016 release of a study sponsored by the Association of National Advertisers (ANA). The study suggested that media companies commonly pay cash rebates or offer free inventory to agencies in return for volume buys, but agencies typically don't pass along these rebates to their clients. As a sign of the unease advertisers have been feeling about rebates, since 2015 more than 500 advertisers have issued RFPs for media agencies, including some of the largest U.S. advertisers. [1]

In interviews, executives at leading advertisers and other industry professionals were critical of the way media agencies handle rebates. They particularly noted how large a role rebates play in the industry (see sidebar "Media-agency practices").

While it's difficult to attribute financial impact directly to these recent criticisms, most of the major agency holding companies have seen flattening or declining revenues since 2016—the year the ANA report was released.

Additionally, the stock market—a forward-looking indicator—has not been kind to the agency holding companies of late. As of early spring 2018, share prices for four of the leading holding companies had experienced double-digit declines since mid-2016.

The size of rebates doesn't seem to be a big factor in advertisers' budget decisions. Programmatic spend, the area where rebates are highest, is estimated to have grown 30 to 50 percent in North America since 2015.

Interviews surfaced mixed views on whether the recent focus on rebates has damaged advertiser-agency ties (see sidebar "Current state of advertiser-agency relationships"). Some observers believe these relationships have been harmed irreparably, while others are hopeful they can be salvaged.

Media-agency practices

"Some agencies built a bankrupt business model and thought they would never be found out. . . now it's a vicious cycle, competing on price in a race to the bottom."

—*Media auditing-firm executive*

"Confusion is a strategy" (referring to how media agencies seek to obfuscate what is really going on with rebates).

—*Former media-agency head*

"It's in the media agency's interest to keep things ill-defined."

—*Former CMO of a global financial-services company*

"There are ways agencies make them [AVBs] hard to track."

—*Media auditing-firm executive*

Current state of advertiser-agency relationships

"There's a whole generation of CMOs who will never trust agencies . . . and vet every buy."

—*Media auditing-firm executive*

"Working with agencies can be done with a generous spirit. . . . I want my agencies to make money and attract top talent. . . . I just want it to be clear and transparent how they make it."

—*Former CMO*

The recent focus on rebates has led some advertisers to renegotiate their agency contracts. It isn't clear, however, that this has led to increased transparency. In the face of advertisers' push for more transparency, some agencies have continued former practices and others have figured out how to continue receiving the equivalent of rebates, but under a different name and structure (see sidebar "The more things change").

In the current environment, even trusting advertisers are seeking to verify that their agency relationships are on the up-and-up: an executive at a leading third-party auditing firm reported that his business has increased threefold since 2015.

There is a better way. By working to achieve greater transparency, advertisers can move toward sounder relationships with their media agencies, based on clear and straightforward rules of engagement.

Four steps to greater transparency

Advertisers can build more transparent, partnerlike relationships with their media agencies by taking four steps.

1. Build accountability by engaging senior leaders

The initial step is for the advertiser to appoint an executive—perhaps the CMO or head of media—who is responsible for ensuring that relationships with media agencies are transparent. A key job for this person is to engage in an open, partnerlike manner with a counterpart who is a senior executive at the agency. As a former agency head said, "Only a small inner circle at the media agency has the full view of how the money from rebates is flowing: Global CEO, CFO, or local CEO/CFO."

The executive who takes the lead at the advertiser also needs someone whose job is to ensure that the full value of rebates is received on an annual basis. For more on how this gets done, see step 3, which describes the annual governance process.

The more things change

"[The ANA report] set off a nuclear weapon in an enclosed space . . . but it feels like we're back to business as usual in the industry."

—*Executive involved with ANA study*

"Agencies can sell a piece of research to a media vendor for millions, even if its true cost is very low, as a way of receiving hidden undisclosed revenue . . . this practice is like selling a $20 million pencil."

—*Media auditing-firm executive*

"An agency might get a kickback from a TV network for doing a piece of research . . . often receiving tens of millions of dollars."

—*Former media-agency head*

Another important role for the person who oversees transparency for an advertiser is to educate a select group of the company's own senior executives, including the CEO and CFO, about rebates. Once C-level leaders understand the importance of rebates, they typically provide the dedicated resources needed to track them and are willing to engage in a discussion with agencies about the importance of transparency when necessary.

2. Embed transparency in contracts and pay fair compensation to agencies

A second key to ensuring transparency is making sure the contracts in place call for the advertiser to receive the full value of any rebates/AVBs. These should include both cash payments and any free advertising space agencies receive. It may not be an easy process. As an executive at a media analytics/benchmarking firm said, "This not only requires tough conversations but heavy lifting to ensure the overall approach is reflected in the details of the contract." Since the marketing domain is evolving so rapidly, any contract with a media agency should also be reviewed at least every two years, to make sure it is up to date.

Rebates are not the only issue at play in the relationship between advertiser and agencies. It is also important to have a clear agreement and common expectations around agency compensation. In fee negotiations, it can often be counterproductive for advertisers to press their agencies too hard. Some agencies, we fear, now rely on rebates to become whole after advertisers have pushed them aggressively on fees and rates. One CMO noted, "In fee negotiations, clients should negotiate price in the context of an explicit level of service but be cautious about the 'water-balloon effect.' When pushed, agencies will find different and creative ways to maintain margins."

The goal should be to compensate agencies fairly while also motivating them to achieve outcomes that generate value for the advertiser. We have found that an effective approach is to provide a base fee paired with a substantial upside in the form of a pay-for-performance bonus based on clearly defined metrics.

Progressive advertisers are not afraid to pay generous and motivating performance incentives, as long as they are tied to outcomes that create mutual value. A mutually beneficial arrangement like this can allow for win-win relationships that endure over the long haul. We have found that some media agencies, in response to pressure from clients, are themselves calling for a shift to compensation structures that embody this kind of model. If advertisers prefer to stay with a more traditional compensation model, they should ensure that a fair margin is built into the fee, so their agencies don't look for other sources of revenue.

3. Institute an annual governance process

Some advertisers think they can check the box and claim they have a transparent relationship with their media agency once they update contracts. In many respects, though, the work is only beginning. Ensuring adherence to the transparency provisions in the formal agreement may require resetting norms.

Putting in place an annual governance process to check whether rebates that are due have been returned to the advertiser is key to following through on adherence to contract terms. This means having the agency provide a detailed summary of the rebates that have been returned, itemized market-by-market and across all media and suppliers.

The rebates governance process should be an annual management routine, so that media agencies know it isn't a one-off. This is a basic business discipline.

It forces advertisers to conduct due diligence and ensures they get the rebates to which they are entitled on an annual basis.

To undertake this annual review, the advertiser needs to have the relevant data readily at hand. This isn't complicated, nor does it require high-end marketing technology; some companies do it with Excel spreadsheets. It can be tedious, though, due to the amount of information to be reviewed, and some companies have benefited by automating aspects of the process. The larger point, however, is that assembling the data necessary to track rebates isn't a complex technical challenge. The objective is simply to access the information needed for the annual review and to complete the review like clockwork each year.

4. Bring in the right auditors when needed

Advertisers sometimes lack the knowledge, skills, and discipline to track rebates effectively, and it's not feasible to establish such a capability overnight. For companies in this situation, a media audit focused on rebates can play a critical role. This is typically an add-on to the financial-compliance audits done every year. While it adds another item to the cost line, a rebate audit can more than pay for itself, especially for companies new to this realm. Even when the needed skills exist in house, audit firms can be a useful resource to triangulate what the advertiser can observe. A former CMO reinforced this perspective by saying, "Media audit firms are essential . . . [they] help with fraud but [are] also just good hygiene for leaders to know where the money is."

The best way to use an audit firm is to have experts at the auditor highlight where and how rebates are being taken by agencies from suppliers. It is also important to note that not all auditors are created equal. Advertisers should be careful to engage an auditing firm with the right experience, ideally one that has former media-buying directors.

Moving toward a transparent advertising industry

The four steps outlined above apply to any advertiser. To get moving on building transparency around rebates, a marketing organization must prioritize the issue. Ensuring transparency requires a long-term effort and will demand ongoing attention and management, though there can also be early wins that can fund future activities and maintain momentum.

The largest companies, with the biggest budgets and a leadership position, can also play an important industrywide role. Several CMOs mentioned that a group of leading advertisers could create a coalition of peers. Members could compare notes and define a vision of the new, transparent future toward which they want the industry to migrate. A group of influential players could have the clout to drive the needed changes.

Media agencies also have a stake in greater transparency. By engaging advertisers in an open, straightforward way, they can restore trust and build true partnerships with their clients. Greater transparency can also boost the reputations of the media agencies, which have suffered in recent years.

Further, in the face of the changes roiling the industry, agencies may not be able to maintain the status quo. A former agency head noted that the industry's business model is based on rebates: "Most media-agency profitability is driven by nonclient revenue . . . we would not have a [media buying] business if we didn't have rebates." With clients now pushing back, agencies that fail to move toward more transparent practices could well find themselves at a competitive disadvantage. Some smaller, independent media agencies are already winning business by making a pitch based on their "integrity and transparency."[2]

Insisting on transparency in rebates will require a significant effort by advertisers, but the potential rewards make it worthwhile. As the CMO at a large global company said, "There's real money in this—and taking money back that we are leaving on the table will allow us to fuel growth." ■

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[1] 4A's, *Accounts in Review*, 2015-17.

[2] Barry Dudley, "The perfect storm that's blowing up in media," *The Drum*, February 16, 2018.

Sarah Armstrong is a partner in McKinsey's Atlanta office, **Joe Regenbogen** is a consultant in the Seattle office, **Rachael Schaffner** is a senior knowledge expert in the Washington, DC, office, and **Robert Tas** is an associate partner in the New York office.

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