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Pioneering Agency ROI Solutions For Marketers Worldwide

## “The Fiction of Hourly Rates for PR Agencies – A Road Map for Marketing and Procurement”

By Arthur Anderson

### A Morgan Anderson “Best Practice” Series

This is one in a series of Morgan Anderson papers devoted to best practices for compensating agencies and other professional services firms. In this paper, we take issue with the “fiction” of PR agency hourly rates and **discuss case examples using fact-based knowledge and actual assignments from marketers** – rather than using agency surveys and trend analyses. We intend this paper to enable clients to negotiate fact-based PR agency compensation where transparency and benchmarking are part of the solution and agency cost containment and performance results are objectives.

#### BACKGROUND

PR agency compensation has been a challenge for marketing and procurement executives given **a)** the lack of transparency, and **b)** the misconceptions that are inextricably linked to the inexpert PR hourly rate syndrome. Recent developments now resolve this. Among them, are new types of Annual Scopes of Work and the de-construction and benchmarking of PR staffing plans and agency costs and economics. **When using them, cost reduction over a 12 to 18 month period can range from 10% to 20% of annual agency fee paid.** Such efficiencies can then fund additional client programs, drop to the bottom line, or provide funds for implementing agency incentive programs to drive PR results and value contributed by the agency.

This is necessitated by the increasingly huge sums spent on Public Relations as PR becomes a full partner in a client’s marketing communications arsenal and an important marketing tool. Morgan Anderson estimates Global PR agency revenues to be \$12 Billion in 2010, and we expect this to double by 2016 to \$24 Billion.

Here are questions clients ask:

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- **Hourly Rates:** *“Are the hourly rates charged by our PR agencies reasonable and competitive compared to comparable agencies and industry benchmarks?”*
- **Transparency:** *“How do we get transparency from our PR agencies that is fair and reasonable ... and does it work for both parties to the relationship?”*
- **Productivity/Containment:** *“What opportunities are there for productivity and fee containment with our agencies?”*
- **Fee Methodology:** *“Is the hourly rate methodology (or labor-based fee for that matter) used by our PR agency the best and right one given our needs and objectives?”*
- **Agency Performance:** *“How should we best assess and increase agency performance and value ... and also link this to agency compensation?”*
- **Benchmarking:** *“How should we benchmark our agency’s Scope of Work, staffing plan, and its costs and economics so we are assured they are reasonable and relate to industry benchmarks?”*

## CHALLENGES

**Problem: PR Fee compensation proposed by agencies often lacks transparency, is rooted in fiction, and not linked to benchmarks**

Not only is the annual investment in PR fees huge, but, also, there are special problems when hourly rates are used for compensating PR agencies. **However, when assessed and resolved, there is a range of 10% to 20% in cost-containment opportunities embedded in PR fees, or an industry total of \$1 Billion to \$2 Billion in PR fee cost containment.**

Reasons why PR rates baffle clients:

- PR agencies did not spring from general advertising agencies who provide full disclosure and transparency to clients, but rather developed as independent, entrepreneurial agencies
- PR agency use of hourly rates established a superficial level of confidence in clients, but, in fact, suffer from lack of transparency and defined terms
- PR hourly rates are not transparent or benchmarked and clients assume (incorrectly) that **an hourly rate at one agency is the same as the same rate at another agency when, in fact, they are not**
- PR contract compliance audits rarely assess how hourly rates are developed and how their components compare to other agencies and industry benchmarks

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## SOLUTIONS

Non-transparent hourly rates present a special problem. These are an agency's "ask" whereas few clients, until recently, had knowledge bases they could use to present an "offer". Solutions such as best practice Scope of Work (below), defined staffing plans, and agency cost/economic analyses are now in the client's toolbox to use. There are also sophisticated metrics (below) that can be used for hourly-rate and labor-based fees to shine the light on PR agency compensation. This paper discusses two solutions:

### 1) Protocols by client and agency in the development of a best-practice PR Scope of Work

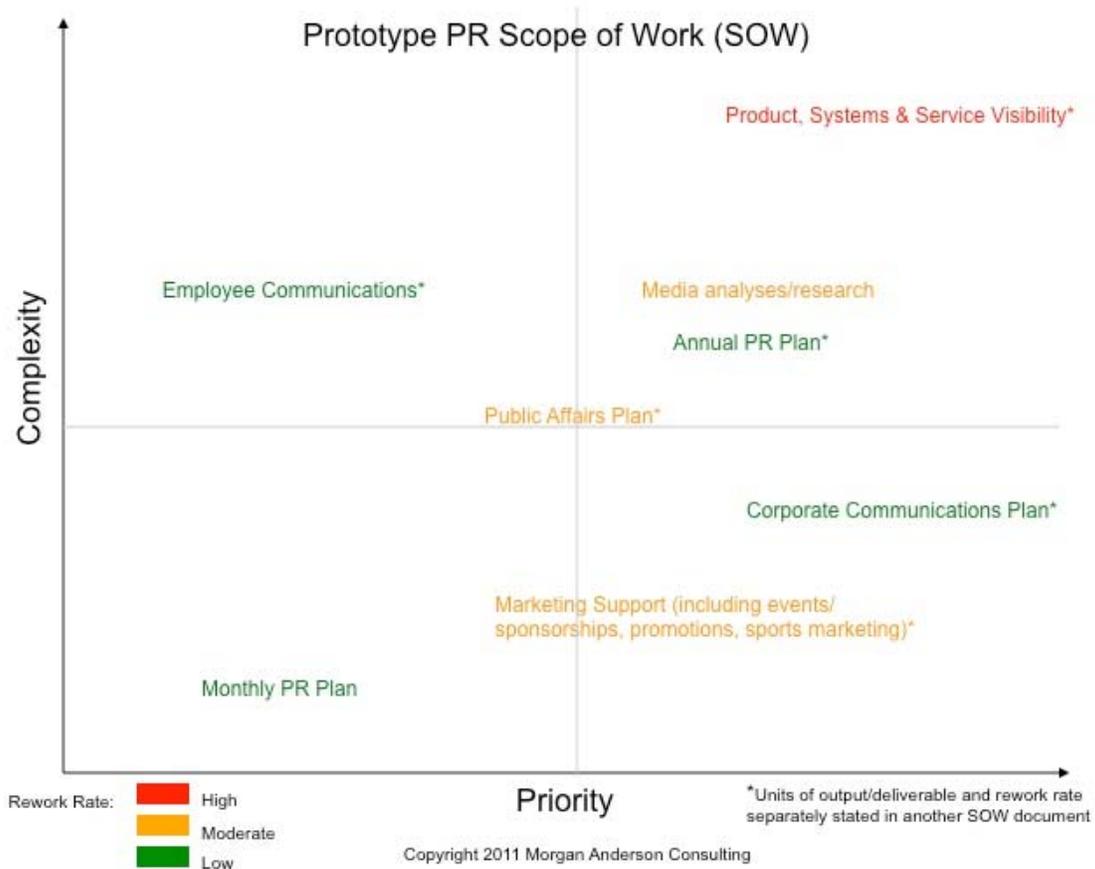
### 2) De-constructing and benchmarking PR agency hourly rates.

#### 1. Developing a Best-Practice PR Scope of Work

The following is a best-practice Scope of Work case study in graphic form. Morgan Anderson emphasizes carefully defined development of a client's SOW document. It **is the foundation for the agency's staffing and economics**. If it is merely a laundry list of tasks and activities, absent of any codification, then it cannot be used as an **effective negotiation and agency management tool**. We advise that clients provide more detail in their SOW to enable a clear understanding between client and agency of the needs, expectations, and absolute requirements in the work ahead.

Due to space limitations, the following is not the actual SOW, but, rather, an abbreviated version of an assignment involving multiple, comparable PR agencies where the client applied factors of **Complexity, Priority, and Re-work Rates**, as well as, PR goals, units of output, activities and deliverables, to designate what the PR agencies were to do for their annual SOW. SOW variables will, of course, differ depending on specific client objectives, the brand/business unit, and category. With multiple PR agencies and brands in particular, a schematic grid, such as the following, can be very useful to practical application of the factors and variables listed above. Again, the SOW is a living document – not a précis or detailed list of tasks – to be used as a "tool" for dialogue, negotiation, and improved client management of its agency, as well as, enhanced productivity from its agency.

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## 2. De-Constructing/Benchmarking PR Hourly Rates

Agency transparency and benchmarking analyses are key drivers to this process. As the chart below shows, the range between seemingly comparable PR agencies is huge, and actual variances present opportunities for understanding negotiating PR agency compensation.

There are three elements needed for de-constructing PR hourly rates: 1) a best practice Scope of Work (see above), 2) a defined Staffing Plan, and 3) disclosure of agency economics per a structured methodology, utilizing real-time benchmarks. These open the door to informed PR agency fee negotiations and achieving cost-containment objectives. The structured methodology can be used to de-construct and benchmark labor-based fees as well as hourly-rate based fees.

The following is from Morgan Anderson assignments where comparable PR agencies were assessed. The big surprise here is the very large variances between similar PR agencies in how they report information to clients. All data below is using the same methodology and

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definitions for a similar Scope of Work. The culprit, in the case of **hourly-rate based compensation**, is that hourly rates suffer from the lack of transparency and, until recently, independent industry benchmarking.

The foregoing variances, though they may appear extreme, are indeed fact-based and selected from actual assignments for marketers using an identical, comparative approach. When taking a fact-base approach the opportunities are advantageous:

- Client Efficiencies
- Accountability of the parties to each other
- Cost Containment
- Transparency
- Fact-based dialogue between client and agency, and
- Improved client-agency relationship

<b>Agency Metrics</b>	<b>Agency 1</b>	<b>Agency 2</b>	<b>Variance*</b>
<b>Blended Hourly Rates</b>	\$99	\$142	+43%
<b>Base Rate Card Hourly Rates</b>	\$80	\$116	+45%
<b>Fee \$ Per FTE (Actual SOW)</b>	\$177,000	\$273,000	+54%
<b>Fee \$ Per FTE (Prototype SOW)</b>	\$195,000	\$330,000	+69%
<b>Overhead Ratio</b>	101%	284%	+181%
<b>Profit</b>	5%	17%	+240%
<b>Multiplier</b>	2.41	4.57	+90%
<b>Agency “Standard Year” Hours</b>	1500	1950	+30%

\* Variance = (Agency 2 – Agency 1)/Agency 1

Note – information in this chart is not comparable to other data sets unless the identical assessment methodology and definitions are used.

### OUTCOMES/BENEFITS

The outcomes and benefits of this approach enable marketers to negotiate fact-based hourly-rate compensation for their PR agencies, as well as activity-based fees, using standard methods and benchmarking when stewardship, efficiency, transparency, cost containment, and business results are objectives.

In the past, hourly rates proposed by agencies presented impediments to achieving this, but as demonstrated here, recent approaches now overcome the impediments. And, worth repeating

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is that fee cost containment over a 12 to 18 month period can range from 10% to 20%, and in some instance 25%, of PR fees paid under traditional hourly rate methodologies.

Other outcome/benefits in these studies were:

- Best-practice contract provisions including definitions of transparency and full disclosure
- Value-based (incentive) fee compensation
- Possible PR agency consolidation to those best-in-class
- Assessment of Out-Of-Pocket reimbursements — reimbursements in this study ranged from a Low of 2% of fee-paid to a High of 28% of fee-paid, presenting other opportunities for cost containment

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Should you wish specifics of the study or to learn more, please email Lee Anne Morgan at [lamorgan@morgananderson.com](mailto:lamorgan@morgananderson.com) or Arthur Anderson at [aanderson@morgananderson.com](mailto:aanderson@morgananderson.com).

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