4A's Client Audit Guidance

A Guidance Directive from the American Association of Advertising Agencies

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Overview

For many marketers, the investment that they make in advertising and promotional support for their brands is one of the most strategically important and financially significant elements of their business model. Given the importance of a marketer's advertising activities, many advertisers want to ensure that their marketing investment is properly calibrated, expertly managed and carefully monitored.

Agencies recognize the importance of fostering positive relationships with their marketer clients, relationships that are built on a bedrock of mutual respect and trust. Agencies also recognize, however, that given the size of a marketer's media and production budgets, having an agreed framework mechanism to impartially assess an Agency's compliance with its financial and media stewardship obligations plays a critical role in ensuring the continued health of the relationship. It is through the process of jointly establishing an appropriate framework, at the earliest possible time, that the Agency and Marketer can best demonstrate and confirm their mutual commitments to building a close relationship. Ultimately, the framework established should serve to best ensure, in an efficient way, mutual and clear understanding in the handling and stewardship of the account.

Marketer audit and review programs (Stewardship Programs) can feature a broad range of activities, including contract compliance verification, financial controls and disbursement audits, media audits (which are more comprehensive than a traditional contract compliance audit because media auditing requires knowledge of media planning and buying dynamics as well as access, subject to third-party rights, to audience measurement information and processing systems), as well as a range of other review, benchmarking and effectiveness-assessment activities.

This publication has been developed by a multidisciplinary task group comprised of senior agency management, finance, legal and commercial practices representatives of the 4A's community. The "4A's Client Audit Guidance" white paper is intended to provide agencies with important information, including principles, best-practice guidance and illustrative tools which will help facilitate an effective and efficient stewardship framework for both the agency and the advertiser. This guidance primarily relates to client contract compliance verification audits associated with media transactions and agency financial activity. It should be noted that a client-agency Master Service Agreements (MSA) might include other types of verification or audit provisions that are not within the scope of this guidance paper, for example: verification of compliance with client policies, compliance with laws (HIPAA, Foreign Corrupt Practices, etc.), data security audits, etc.

Stewardship Framework

Comprehensive stewardship of a client's marketing investment should ideally feature coordination between the marketer and their agencies. Furthermore, given the increased complexity of marketer and agency operations, coordination of stewardship activities should begin with collaboration on stewardship framework. For example:

1. Joint discussion between the agency and client on stewardship goals, expectations and responsibilities.
2. Words like stewardship, verification and audit mean different things to different people. In order to avoid confusion and misunderstanding, there should be precise agreement on stewardship process, scope and rules of conduct. Furthermore if third parties (auditors, consultants, benchmarkers, etc.) are engaged by the client, the third party's role and scope must be agreed upon by agency and client.
3. There should be clarity on the elements of marketing spend and agency operations that will be involved in stewardship review.
4. Marketer and agency should discuss the involvement of appropriate, knowledgeable and objective resources in the stewardship process in order to facilitate successful outcomes.

In order to facilitate consistent and reliable implementation of an advertiser-agency stewardship framework, it is helpful to establish the principles that will guide stewardship activities and it is important to understand industry best practices.

Guiding Principles

There are five key guiding principles that will help the advertiser, agency and if applicable, any third-party intermediaries evolve effective and efficient stewardship arrangements.

1. Stewardship activities should be directly correlated with agency service activities and the agency-client Master Service Agreements (MSA) provisions.
2. Jointly clarify steward expectations, definitions and scope of each stewardship activity. Financial audits, MSA compliance verification and other types of due diligence activities entail distinctly different objectives and process. There should be mutual agreement

between the advertiser and agency on due diligence expectations and scope, for example, benchmarking exercises which are intended to assess the relative effectiveness and efficiency of a client's marketing activity can be controversial, even when conducted in a fair and balanced manner, if they are inaccurately identified as an audit or a contract compliance verification activity.

3. Effective stewardship activities are timely, efficient, focused and reiterative. Stewardship of a client's marketing investment is not a one-and-done competition. Stewardship is an ongoing collaboration. Agency and client are well served to jointly evolve continuity of due diligence activities and collaboratively consider going-forward enhancements that recognize changing marketplace conditions and technology advances.
4. Selection of any third-party auditors or consultants should be mutually agreed upon. There are many different types of auditors (The Big 4, Certified Public Accounting firms, client internal auditors and agency internal auditors). Auditors should remain completely objective and professional in all its dealings with agency personnel. There are also many different types of consultants that conduct process, media efficiency, agency compensation, production, benchmarking and other marketing review activities. Consultants are not auditors, and auditors are not consultants. Mutual agreement on the involvement of appropriate, knowledgeable and objective resources is essential to a successful stewardship process.
5. Effective stewardship need not and must not jeopardize the protection of intellectual property and confidential information of the client, agency or third parties, including other agency clients, media suppliers or data licensors.

Agency Best Practices

In the course of 4A's community discussions related to marketing stewardship and client audit activities, a range of agency best practices were identified. The association's task group has developed best practice suggestions that should help agencies foster effective and efficient stewardship arrangements with clients.

1. Develop and broadly communicate your firm's client audit policy. Your audit policy should reflect your firm's operations structures, service activities, internal control framework and business philosophy. Agency internal finance and management leadership should be aligned on audit policy elements and implications for agency operations. The agency audit policy provides an important framework for discussion with clients when negotiating MSA provisions and collaborating on stewardship arrangements.

2. Confidentiality requirements related to agency, employee, client and third-party proprietary information should be detailed in your firm's confidentiality policy and coordinated with your agency's client audit policy.
3. The agency should execute Non-Disclosure Agreements (NDAs) directly with all auditors and consultants in a form that is satisfactory to the agency. The consultant and auditor NDAs should establish parameters related to access to and use of confidential information. The consultant or auditor agreement should acknowledge that they will not ask for agency confidential information that is expressly prohibited in the agency-client contract (for example salary data). The consultant or auditor NDA should confirm the auditor and consultant will apply the terms of the NDA and be responsible for all parties that they utilize to provide services, including their employees, officers, subcontractors and affiliates, whether owned by them or not. Agencies should not rely on an NDA with an auditor and consultant that they are not a party to, for example, an NDA between the client and their auditor or consultant, as this does not give the agency the right to seek a remedy for a breach of the terms of the respective NDA against the auditor and consultant and also does not recognize that the information is confidential and/or proprietary to the agency/advertiser.

   Many clients, and virtually all agencies and media companies, do not want confidential rate data included in third-party databases unless specifically agreed to in advance by all parties. Consequently, agencies normally prohibit use of agency and client information beyond the scope of the specific engagement and prohibit use of confidential information in consultant databases. It should be noted that many clients do not want their data, even if aggregated or anonymous, included in consultant databases because such disclosure could erode a client's strategic or scale-buying advantage.
4. The client-agency Master Service Agreement (MSA) should establish the framework for conducting stewardship activities.

   The MSA should specify due diligence ground rules and parameters, i.e., why, what, how and who:

   - *Why*. The goals and objectives of discrete stewardship initiatives.
   - *What. S*pecifications of what activities can be reviewed as well as which relationship components are not subject to review. The client MSA should make it clear that any audit must be directly related to: (1) the services provided by the agency to the client (2) the method of compensation agreed to by the parties and (3) jointly agreed-upon policies and practices.
   - *How.* Outline procedures for establishing the scope, process, timing and reporting of due-diligence activities.

- *Who*. Establish ground rules related to the involvement of subject matter experts who should be considered for different types of stewardship activities.

The MSA should also cover appropriate rules and limitations related to access to and use of information.

For reference, the Appendix provides examples of clauses relating to media stewardship that should be considered for inclusion in an MSA. Each agency-client MSA should specify stewardship parameters that relate to the agency's servicing arrangement for that client's business.

5. Auditors are not consultants. Consultants are not auditors.
   The agency agreement with the client should specify that the client cannot choose as an auditor any person who, or the division of any firm that, is engaged in the business of providing consulting services to businesses in the advertising industry. The auditor's motivation to upsell and cross-sell their own firm's other services would significantly impair their perceived ability to undertake an objective audit.

   The agency-client MSA should:

   - Specify mutually acceptable auditors for contract compliance and financial audits. Many agencies specify the internationally recognized general audit practice group of "Big 4" global audit firms who are approved by recognized supervisory bodies to undertake company audits, are members of professional bodies that promote knowledge, skills and professional standards and employ professionally qualified personnel.
   - Separately specify mutually acceptable, qualified and independent consultants for benchmarking, media activity and fee-compensation reviews.

6. Distinguish between verification and disclosure.
   Independent auditors are appointed by clients not only because of their audit expertise, professionalism and adherence to best practices but also because the agency may permit them a greater level of access to relevant agency confidential information for the purpose of verification than what the agency would provide to a client. The involvement of independent auditors permits the agency to protect both the confidential information of the agency and the agency's other clients. Financial audits and audits involving sensitive agency confidential information should be conducted by the audit group of a "Big 4" or credible independent Certified Public Accounting (CPA) firm via a process that provides the CPA firm with the opportunity to view the information for purposes of verification through an agreed-upon procedure. A verification audit allows the auditor to verify the correctness of the agency's information while protecting the agency's confidential information. Consequently, the agency's non-disclosure

agreement with the auditor restricts the auditor from disclosing the agency's confidential information to the client.

7. Client, agency and auditor should agree on the scope of the audit, process and information requirements in the MSA and in advance of the start of the audit. Agreements between the parties should prohibit unauthorized "audit scope creep." Furthermore, agency should clarify any information access and audit limitations or restrictions.

   It is common practice to limit audit or restrict access to the following:
   - Individual payroll records and personnel files
   - Expenditure or information of other clients
   - Agency overhead cost and non-billable expenses
   - Agency trading desk, programmatic buying and other non-disclosed media sales financial records
   - Confidential supplier information, for example, media supplier or data licensed information
   - IT and HR systems raw data, agency data centers or server rooms and agency network access logs
   - Transactions outside the scope of services provided to the client

8. Contingency consultants and contingency auditors have an inherent conflict of interest and should be prohibited.

   Auditors or a consultant whose compensation is in whole or in part derived from analysis of advertising industry audit findings have an inherent conflict of interest. The agency-client MSA should prohibit contingency arrangements and eliminate the involvement of contingency practitioners. Fee arrangements based on share of findings tend not to form collaborative working relationships between the client and the agency as the contingency nature of the fee motivates the auditor to focus solely on how they can maximize their own fee and not on making recommendations that improve how financial stewardship for both client and agency is managed. In practice, these fee arrangements result in several consequences, including excessively large audit sample sizes with the resulting onerous agency resource requirements to manage the audit, a focus on areas that both agency and client would consider inappropriate, and/or measuring against metrics that have neither been agreed between the agency-advertiser nor established as an "industry standard," for the sole purpose of looking for additional audit areas to maximize the fee paid by the client and also an agency concern that auditors may subsequently use audit findings to sell services in to other agency clients.

9. Specify client right to audit parameters.
   Agency policies and client MSAs should establish the parameters related to the client's right to audit, including:
   - Auditor qualifications and mutual agreement on auditor selection
   - Audit duration, frequency and time limitations
   - Audit cost responsibility
   - Auditor personnel should not be involved on any engagement if they have any actual or perceived conflicts of interest based on their relationships, history, associations or work performed at agency to be audited or the agencies key management.

10. Auditors and consultants should be required to provide the agency with a draft report of findings prior to the report being delivered to the client to ensure the report is both factually correct and communicated in appropriate context. The requirement that the agency receive the draft audit report prior to the client receiving the information should be codified in your agency's policies as well as the agency's agreements with clients and auditors.

    The purpose of an audit is to confirm the agency has complied with specific terms of the client/agency agreement. The audit and subsequent draft report should be reviewed by the agency to ensure the auditor remains within the boundaries of their auditor role and does not overstep the mark into consulting territory, e.g., providing "consulting opinion" on what market practice is or isn't or suggesting changes to contract language, unless otherwise agreed with the agency, or advise clients on compensation rates or fee structures with or without "benchmark data."

Summary Conclusions

Agencies and clients should collaboratively work together to design effective and efficient controls and verification procedures related to significant marketing expenditures. Comprehensive client-agency stewardship arrangements entail alignment on expenditure policies, clarity on internal control responsibilities, agreement on appropriate transparency and relevant scope of verification.

Well-crafted stewardship activities can and do provide reassurance and foster confidence in the agency-client relationship.

Supplemental Information

In order to help the agency community with implementation of stewardship and audit best practices, this document includes an Appendix that contains supplemental information.

The Appendix includes:

- 4A's Media Audit Guidelines:
  4A's Guidelines for Digital Media Audits
  4As Guidelines Local Radio Media Audits
  4A's Guidelines for Local TV Media Audits
  4A's Guidelines to National TV Buying and Stewardship Audits

- Media Stewardship Parameters MSA Examples

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Media Stewardship Parameters MSA Examples

The agency-client MSA should specify stewardship parameters that relate to the agency's servicing arrangement for that client's business. Examples of media stewardship clauses that should be considered for inclusion in an MSA:

1. Methodology for post buys
2. Disclosure and advance mutual agreement on all client buying guidelines
3. Acknowledgement of industry standard for Television post buys GRP delivery (e.g., +/- 10%)
4. Clarity and mutual agreement on posting organization for assessing post buys (the agency or third-party auditor if client utilizes third-party media audit firm).
5. Agreement on potential third-party audit scenarios in the future, along with contract language that protects each party's business interests. Language should require agreement of agency and client to align on approach, methods, conclusions and proposed actions resulting from a media buying audit. This should include agency compensation impact as well.