collective szabo wisdom®

MEDIA COLLECTION PROFESSIONALS

SZABO ASSOCIATES, INC. VOLUME 36, ISSUE 3, SEPTEMBER 30, 2021

MORE is better than less.

Dear Friends:

In any economy, getting paid in a timely manner is a priority. With the current economic uncertainties, it is essential to work closely with your customers and their advertising agencies and understand the terms of payment in all your contracts. The liability clause landscape remains unsettled after 30 years with media companies' adoption of Joint and Several and advertising agencies' adoption of Sequential. This issue's feature offers some steps that media companies can take to reduce their risk when faced with accepting Sequential. Proactive communications is key, along with a plan to implement in the event of late payments.

Our Quality Awards banquet on August 23 at Maggiano's in Buckhead was great fun. 2021 Quality Award recipients were: Krissy Chea, David Grieco, and Kenya Johnson, and Pat Robinson received the President's Award for her outstanding contributions.

Our fall events include the Media Outlook 2022 virtual conference October 19-20, followed by the Georgia Association of Broadcasters Annual Convention, October 22-23 in Atlanta. Szabo will be the after-party sponsor for the GAB's Gabby Awards on October 23.

Best wishes for a fine fall season.

Robin Szabo, President
Szabo Associates, Inc.

Sequential Liability . . . 30 Years and Counting!

Thirty years ago, there was a seismic shift in the way media companies were paid for advertising. In February 1991, the American Association of Advertising Agencies (the 4A's) issued its groundbreaking statement defining Sequential Liability. "The Agency shall be solely liable for payment of all media invoices if the agency has been paid for those invoices by the advertiser. Prior to payment to the agency, the advertiser shall be solely liable."

Sequential liability was intended to protect agencies from being held responsible for payment in the event that their advertising clients failed to pay them, due to bankruptcy or any other reason. For the 60 years prior to the 4A's statement, the standard practice was one of sole liability, where the agency booked the advertising and was solely responsible for payment. As recently as 1988, this practice was upheld by the court systems. An October 1988 California Court of Appeals ruling established "custom in the industry," stating that an advertising agency is responsible for payment of any advertising orders it placed (See *Collective Wisdom,* from March 31, 1989). Further, it is the agency's responsibility to screen its own customers' credit and to bill and collect from their customers.

This lawsuit had referenced the liability clause of the 4A's, which stated, "Station agrees to hold agency solely liable for payments to be made under this contract, except that where Agency is not an advertising agency, the person, firm or corporation which authorizes Agency to contract for television time hereunder shall be liable in the event of default by Agency." Later in 1988, the 4A's dropped that liability clause from its standard contract.

Enter Joint and Several. In response to the 4A's introduction of sequential liability, the BCFM/BCCA (now MFM/BCCA) encouraged media to adopt a position of "joint and several" or "dual" liability, holding both the advertising agency and the advertiser liable for payment until the media source received payment in full. Neither side has moved far from its position over the last three decades. Most media companies adopted joint and several liability, but have faced stiff resistance from advertising agencies.

Agencies, having weathered some downturns in the market that resulted in even some large, well-established customers declaring bankruptcy, want to share that risk with media companies. Media companies are under increasing pressure to offer new and innovative advertising programs to win and keep customers. Both rely on advertisers for revenue.

The unfortunate reality is that the ball is often in the advertiser's court. Large customers have learned that they can make demands that both agencies and media companies are forced to accept, rather than risk losing much-needed revenue.

Sequential liability works fairly

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30 Years & Counting —

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well when advertisers and agencies remain solvent and all parties deliver the products and services as promised. But what can – and should – be done when one of the parties fails to pay in a timely manner? Media clients are owed needed revenue and left with the difficult decision of whether to pursue the agency, the advertiser, or both in order to get paid.

While media companies may feel perpetually behind the eight ball with regard to payment liability, there are numerous measures credit managers can take to keep payments flowing and solve payment problems before they age to the point of being uncollectible.

Foster Cooperation.
If faced with accepting sequential liability and for it to work well, all three parties must be engaged in the media buy. This requires agreement between the agency, advertiser, and media company. This cooperative effort begins with all three parties recognizing the importance and benefits of working together. Everyone should receive copies of all documents involved: contracts, terms of payment, bills, and receipts.

Advertisers should understand that it is in their best interests for media to be acquainted with their businesses and their agreements with ad agencies. When they keep up-to-date records and pay their agencies on time in accordance with their agreements, they are reducing their liability should the agency fail to pay. The media outlet will know that the problem lies with the agency and can pursue payment from it. In the event that the advertiser fails to pay the agency, the media company may be a willing ally to the agency in efforts to collect from the advertiser.

Since the agency is the party with whom the advertiser contracted, the agency should be the primary source of information on the advertiser. The agency is responsible for running a thorough credit check and sharing those results with the media company.

Sequential liability contracts with advertising agencies typically leave media properties vulnerable to losing money if an advertiser goes under and does not pay its agency bill. This is particularly an issue with start-up tech companies without a lot of assets. For this reason, media needs more information on the financial stability of both the advertiser and the agency.

Ask about the terms of payment. Agencies, in some cases, are accepting longer payment terms with advertisers, and media outlets are caught unaware of these terms until their own invoices become delinquent. What about those advertisers with questionable creditworthiness? Is the agency willing to demand payment in advance for these customers? By knowing the agency's timetable and its payment terms with the advertiser, the media outlet can know when to expect payment and when to take action when an invoice becomes delinquent.

What if the agency itself is not considered creditworthy, or there is a lack of agreement between the media company and the agency concerning payment liability? A media company needs set policies and procedures for these circumstances as well.

Similar to situations when the advertiser is not deemed creditworthy, options include refusing to grant credit or requiring advance payment. Additionally, include the ability to place a credit hold on an agency until past-due payments are brought current or to an acceptable level. When necessary, the collection process should alert the agency's client if the agency delays payment.

Forge Personal Relationships.
In years past, contracts were agreed to in person and sealed with a handshake. In today's digital world, everything is done electronically and even phone conversations are becoming rare – until there is a problem.

The advertising buy starts with the media salesperson, whether they are approached by an agency or they reach out directly to an agency or their client in hopes of making a sale. Successful salespeople learn about their clients' markets and share news of interest and new opportunities to promote their products. Communication should not end with the order.

Clearly explain your policies and procedures to everyone involved in the transaction. In-person communication works best for this step. When that is not possible, a Zoom-style video call is the next best option. Keep in contact – by text, email, video call, phone call or whatever means the customer prefers – while everything is going well. Check to see if they are satisfied with the ad placement and are getting good results. Be responsive to their concerns and issues and cultivate a partnership-style relationship. That way, they are more likely to reach out and work toward a solution when they have cashflow problems.

Also, keep the advertiser in the loop if the agency is slow to pay. Advertisers that are true partners are more likely to "police" their agencies to make sure the media portion is paid on a timely basis.

Manage Disputes.
Of course, the best possible outcome is where everyone gets paid right on schedule. The account pays the advertising agency, the advertising agency pays the media outlet, and the media salesperson gets their commission.

Hope for the best and prepare for the worst. Develop a clear policy for resolution of disputes. Decide ahead of time what you will do and when you will do it if either the agency or advertiser fails to pay.

If the agency refuses to pay, will you inform it that you intend to notify the advertiser of the nonpayment? If the agency claims it has not been paid by the advertiser, will you contact the advertiser? If so, when?

Involve sales personnel. Enlist the sales representative's participation in procuring a completed credit application, resolving disputes, and assisting in the initial collection process should a delinquency occur. After all, they need those commissions.

Seek input from your legal

counsel. Carefully review insertion orders and contracts for any changes in language. Proactively notify your legal counsel of any alterations in an agency's liability position, and enlist its help in evaluating options and developing procedures.

Mitigate Bankruptcy Fallout.
A worst-case scenario: An ad agency unexpectedly files for bankruptcy, leaving media hanging as unsecured creditors. If the advertiser has not paid the agency, the sequential language, while inferior to joint and several, still allows the media provider to pursue the advertiser for payment.

A commonly held myth is that the ad agency has a fiduciary responsibility to pay the media outlet if the agency has been paid by its client. In reality, agencies treat advertiser payments as "comingled funds" rather than segregated funds held in trust for individual advertisers. Agencies can do as they please with the payments they receive and, in fact, can even pledge accounts receivable as collateral.

Agency of Record (AOR) documents can clarify the roles the agency and advertiser play in the media buying process and further protect media in the event of an agency bankruptcy. This document, which you can develop in-house, specifies the authorities that have been granted to the agency to act on behalf of the advertiser in purchasing space or time, including the agency's authority to contract in the advertiser's name and to bind the advertiser to the agreement's terms and conditions. Additionally, the form should include a statement that, if the advertiser entrusts the agency with money to pay the media provider, the advertiser will remain liable if the agency fails to pay.

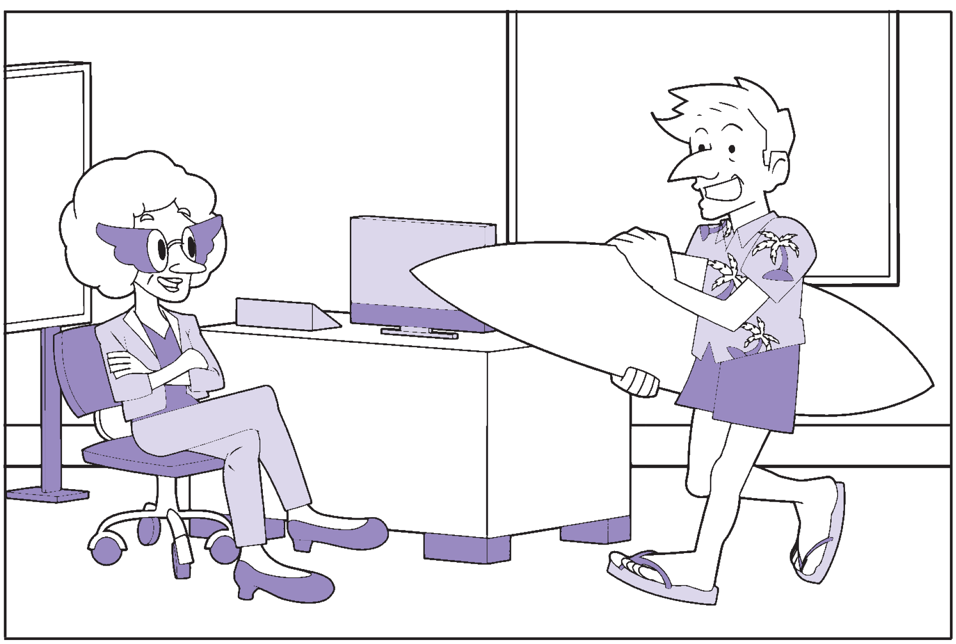
Reality Check for Digital.
Folio's mid-2020 decision to discontinue regular reporting on the print magazine publishing industry is indicative of media's shift from print to digital. Many traditional print publications are either stopping print issues entirely or adding digital issues alongside their print titles. One large business-to-business publisher, long known for industry-specific magazines, now estimates that print generates less than 40 percent of its total revenue. This acceleration toward digital has pretty much codified sequential liability's predominance, with digital buys following the authoritative Interactive Advertising Bureau's (IAB's) terms and conditions.

The payment liability language promoted by the IAB can be found on its website, www.iab.com. The main takeaway, simply stated, is that media are to hold agencies liable for payments only to the extent that proceeds have cleared from the advertiser to the agency for the ads described in the insertion order. For uncleared sums, media must hold the advertiser solely liable. Additionally, nonpayment to the agency by an advertiser does not preclude other of the agency's advertiser clients from buying advertising through the agency. In other words, if a specific customer fails to pay the agency, the agency is not liable for that payment and can still place ads on behalf of other clients.

New Risks.
No one questions that 2020 was a rough year, with most businesses suffering financially from the COVID-19 pandemic. Advertising and marketing budgets were slashed and quite a few went under and/or were forced to declare bankruptcy.

There is optimism this year as businesses have re-opened and consumer spending has increased. Three prominent global ad agencies, IPG's Magna, Publicis' Zenith and WPP's Group M, are predicting increases between 3.2 percent and 6.2 percent in advertising spending for 2021, according to *Forbes* magazine. Digital advertising is expected to account for more than half of all ad buys, with estimated growth between 8 percent and 14.1 percent. There are, however, some new risks on the horizon.

Agencies seem to be doubling down on sequential liability, citing increasing risk and liability of doing business with big digital media platforms. A recent example: Group M, Facebook's media-buying agency since 2014, has withdrawn from its global media services account review. Group M did not state a reason for its decision, but the editorial board of *The Wall Street Journal* implied the withdrawal had to do with terms of the review's contract, which would have



Guess this means that you finally broke through the payment liability deadlock on that big account. Cowabunga!

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shifted more risk and liability to the media agency.

These large digital media platforms have historically treated ad agencies as principals, not agents, in terms of their clients' media buys with them, giving them sole liability for those ad commitments. Thus, those agencies were left liable for payment when the pandemic led to clients declaring bankruptcy.

Why, then, did these digital media platforms diverge from the industry-standard of sequential liability? A *MediaPost* article in July by Joe Mandese puts some of the blame on agencies themselves, citing an "even more insidious practice that evolved during the early days of digital media-buying, when in order to benefit from rebates, commissions and discounts paid back to the agency, many of Madison Avenue's biggest shops agreed to be treated as principals, not agents, for the ad buys." Decades later, these deals are no longer so advantageous for agencies, some of which are trying to renegotiate terms with their big digital media suppliers to be treated as agents rather than principals, according to Mandese.

Looking Forward.

While media companies can push for joint and several liability and other protections, more often than not, they cannot demand it.

So what can be done? There are no easy answers, only steps that media companies should take to reduce the risk of nonpayment. All parties – the advertiser, the agency and the media company – need to work together and share information for the good of all three. Knowing who is responsible for payment, confirming all communications in writing, copying all parties involved in the transaction, and possibly obtaining a signed AOR from the advertiser or personal guarantees in borderline cases can substantially lower your risks. It is indeed the age of sequential liability, for which there seems to be no end in sight. ♦