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ARTICLE

Service level agreements (SLAs) are one of the most critical components of an outsourcing arrangement. When properly designed and executed, SLAs drive desired behaviors, monitor performance and guide the governance of contractually agreed objectives. Numerous other factors can also contribute to the ultimate success of the outsourcing relationship. For example, consider the importance of establishing clearly defined business goals, or the critical importance of effective communications and contract management. The ultimate success or failure of an outsourcing arrangement cannot be attributed to a single element; but as we will soon see, service level agreements can have a significant impact on desired outcomes.

The problems (and perhaps, ultimately, the failures) associated with outsourcing relationships are varied. Improper business alignment, poor execution, and failure to realize stated levels of improvement are among various contributors. In most cases, causes of failure can be tied directly or indirectly to the fact that service level arrangements and supporting measures were not properly established. A recent Cutter Consortium ongoing outsourcing survey asked respondents what problems they have faced in current or past supplier relationships. According to the survey results, the following responses were among the top 10 (percentage represents the percent to total number of respondents).

Expectations Not Met (48%)
Service Level Agreements Not Clear (38%)
Poor Quality of Service (38%)
No Measurable Evaluation Criteria (31%)
Outsourcing Agreement Not Well Written (22%)

We can see a pattern emerging in these results. As we take a closer look at these issues, we see that service level agreements and measures play a key role.

- **Expectations Not Met.** This may be the result of poorly conceived performance targets.
- **No Measurable Evaluation Criteria.** Perhaps the service levels don't provide quantifiable measures of performance
- **SLAs Not Clear.** This could be the result of inadequate scope definition.

While not conclusive, we can surmise that the majority of these problems can be linked directly or indirectly to service level management.

The subject of service level agreements covers a wide variety of topics. Some of the more important aspects that will be presented in this Executive Update include the SLA Framework, Identifying Service Level Measures, Measuring Levels of Service and Monitoring Performance.

The SLA Framework

Properly framing the service level agreement does not guarantee success, but the process of defining levels of service and creating the proper measures of those services is an opportunity to effectively position expectations of the desired outcomes.

The successful outsourcing arrangement typically has followed a well thought out framework for establishing and monitoring SLAs. A basic service level agreement framework includes:

- **Planning:** identifying service level measures and performance targets;
- **Executing:** collecting data, analyzing results and reporting; and
- **Governance:** monitoring performance and making adjustments.

During the planning phase, efforts are made to identify service-level measures that support the business objectives of an organization and provide meaningful indicators as to the level of service. At this time, baseline data is collected and analyzed, which reflects current levels of performance. Based upon these levels of performance and in consideration of business goals and objectives, service level measures are established. At the same time, the required infrastructure to support future activities that are necessary to support the capture and reporting of service level data is defined. Finally, a detailed implementation plan is developed, preparing the organization for executing the SLAs and measuring performance..

The execution phase begins when the contract is in place and services are being provided. This phase includes the collection of all necessary service level measures. Checks and balances must be in place to ensure data integrity and accuracy. As data is collected and stored in a secured repository the results are analyzed and reports are produced. Ideally, the proper distribution of reports was identified during the planning phase and the various management groups that use these results are now receiving the critical information they need to govern the contract.

Governance is the ongoing process of reviewing performance measures and contrasting those results to the stated goals and targets. It's also a standard procedure to conduct periodic audits on the service level data to ensure consistency, accuracy and completeness. During the life of the contract, it will most likely be necessary to adjust the service level measures. Business opportunities may change or more realistic targets and goals may come to light. So, it's important to incorporate procedures for making changes to the service levels in the outsourcing agreement.

Identifying Service Level Measures

As I mentioned earlier, identifying the proper service level measures during the planning phase requires knowledge about the strategic direction of the business. In addition, it is important to consider the depth and breadth of various categories that may need to be considered. For example, in an outsourcing arrangement that supports the Application Development and Maintenance (AD/M) of an IT shop, there may be several ways in which service levels are to be evaluated. Measures that support the business may include time to market and product quality. Customer-oriented measures related to levels of satisfaction comprise another typical SLA category. From the technical view of the service delivery proposition, response time and day-to-day performance measures may be included. And finally, from a process performance perspective, issues such as compliance and effective communication may well round out a general outline of service level measures in an AD/M outsourcing arrangement.

Properly framing the service level agreements and the supporting service level measures requires the setting of reasonable and appropriate performance targets for the customer. Once the service level measures are identified, the next step is to establish performance thresholds by asking such questions as: What is the proper level of service that can be expected? What is the appropriate level of improved performance that can be expected year after year?

These are the fundamental questions that must be properly answered in order to have a reasonable expectation of performance yields.

Measuring Levels of Service

The answers to these questions come from baseline performance data that reflects the customer organization's current performance level. Performance targets that represent achievable results and best fit customer requirements are established. Ideally, performance targets are established based upon a baseline period that covers a period 12 to 18 months prior to the final contract. When these targets are established prior to final negotiation of the contract, they can become part of the contractual agreement. Unfortunately, baselines are often developed during the first year of an outsourcing contract, which is not necessarily the ideal time to baseline an organization since it takes 12 to 18 months for a new contract to "settle in," and performance levels tend to be lower during this period.

The ideal baseline scenario requires a pre-contract activity that includes both a quantitative and qualitative analysis of current practices and performance levels. The quantitative element measures the level of performance and may express this performance in dollars, defects, units of work, etc. The qualitative element, meanwhile, includes an assessment of the current practices that have contributed to high or low yields of performance. This is used to determine current areas requiring improvement, where you can set improvement expectations

Once established, performance levels provide for contractually defined service levels that will monitor service performance trends over time. For example, if we have identified the need to measure a cost per unit of work and reduce our costs over time, we need to set reasonable reduction targets based on current costs. A contract is sure to fail if unrealistic performance levels are established.

By using industry-accepted measures such as function points, organizations can access and incorporate industry-standard performance levels and/or best-practice performance levels. These industry benchmarks can be used for establishing annual performance targets, or to compare best-practice levels of performance. They bring a sense of reasonable expectations regarding performance levels to both the customer and the provider.

Monitoring Performance

The reporting of performance levels of service is scheduled on a periodic, pre-defined basis. It's intended to provide a status of performance and used to identify unacceptable variances from the stated standards. This reporting also serves as the basis for initiating changes, which will improve service level performance.

Typically, senior management receives a high-level, scorecard-like summary of performance results. The information on a performance scorecard may contain information relating to each service level measure, including the baseline performance level, the annual target or goal, the current performance level, a trend indicator and, perhaps, information relating to industry best practices performance levels.

As results are reported and assessed, it may be necessary to adjust the service level agreements. Procedures for making adjustments should be noted in the contract. Reasons for possible adjustments include scope changes, service level performance changes or procedural changes. When changes occur, it may be necessary to establish new baseline measures and keep customer expectations in line with current performance trends. Finally, an annual audit is always key in keeping SLAs on track. Both parties should agree on audit criteria and include it in the contract. Audit criteria may include such topics as data collection integrity, data storage and security, reporting accuracy, and compliance with procedures. A reasonable check on these variables will be particularly helpful during the first year of a contract.

Key Points to Remember

Outsourcing agreements are negotiated with good intentions and high hopes. But once the contract is signed and service delivery begins, it is the service level agreements that govern the success of the outsourcing arrangement. They help to set expectations and they are critical to the proper monitoring and governing of the contract. It is important to remember:

- SLAs should follow a proper and well planned framework
- Service level measures should focus on the strategic direction of the business and drive desired behaviors
- An adequate baseline period should allow for both quantitative and qualitative performance measures
- The accuracy and integrity of the service level measurement data is key to the monitoring of performance
- Plan for reasonable and fair adjustments

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