DEFINING STANDARDS WITH SERVICE-LEVEL AGREEMENTS

INSIDEOPS: Insights for operations leaders in asset management

BACK-OFFICE CONVERSION

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Functionalized operations and business process outsourcing are becoming increasingly popular options among asset managers. The potential benefits of both are significant, but the risks to operations and efficiency are equally great if proper governance is not established up front.

Functionalized operations can lead to multiple handoffs within a process that require different business units to complete certain deliverables at a certain level of quality by a certain deadline. In the case of operations outsourcing, an organization depends on an external service provider to hit the same targets. Without a strong governance structure, there are many opportunities for missed deadlines or poor-quality deliverables.

THE VALUE OF SERVICE-LEVEL AGREEMENTS

A sound operational governance model relies on well-defined processes and expectations. This can be achieved through service-level agreements (SLAs). SLAs are formal or informal contracts between two parties that define the scope of work and the key responsibilities of each party. An SLA may be a contractually binding agreement between a client and external service provider, or an internal service agreement between two business units within a company.

SLAs are used to define service standards, and identify and correct service-level issues to mitigate their impact on operations. Agreement between parties on the service-level standard, how that standard will be measured, and the penalties or remediation measures that will apply if the standard is not met is important for a constructive service relationship. For service recipients, SLAs help define service standard expectations and incentivize desired behaviors. For service providers, SLAs help define each party's roles and responsibilities, provide transparency regarding service assessment and establish mutual accountability where client dependencies exist.

DEVELOPING SERVICE-LEVEL AGREEMENTS

The development of any effective SLA begins with an inventory of in-scope processes. An effort should be made to fully understand the steps required to complete each process and the various points at which SLAs are necessary. If up-to-date process flow or procedure documentation is available, that's an ideal starting point for this analysis. If not, the documentation will need to be created from scratch.

Once documentation is obtained or developed, it should be reviewed to determine key risk areas, identify handoffs and dependencies, and establish timing requirements. Each of these parameters will help isolate the areas where SLAs are required. A typical inventory will include a complete list of all handoffs or deliverables, and their owners. It will also identify when deliverables must be completed and indicate the level of quality expected.

Once an inventory has been created, it is important to validate the accuracy of the SLAs with all interested parties. Since SLAs correspond to handoffs between teams, each SLA should be two-sided, with provisions for both the provider and the recipient. Both sides should agree on the parameters and ensure they meet their requirements to effectively complete the process.

It is important for SLAs to be realistic to ensure that the quality of deliverables is not compromised. Unrealistic SLAs can incentivize undesirable provider behaviors, including the modification of standard reviews and controls to meet overly aggressive timelines. This scenario often occurs in outsourcing relationships where the client's demands cannot always be fulfilled in a controlled manner. Even when the client-service provider relationship is strong and effective, defining realistic SLAs based on the workflow and its dependencies is key to helping achieve the desired outcomes.

USING SERVICE-LEVEL AGREEMENTS

Effective SLAs are measurable and enforceable. Before implementing an SLA, key metrics or evaluation criteria need to be defined and tracking tools should be implemented.

When it comes to monitoring performance, transparency, oversight and accountability are critical. Consistent reporting can help the party providing the service understand how it's performing relative to expectations and either correct service-level issues immediately upon identification or prevent them altogether. In advanced environments, fully automated SLA reporting is ideal. Workflow or dashboard tools that track the status of deliverables offer a robust and auditable way to evaluate SLA performance in real time.

In outsourcing relationships, it is also important to identify which SLAs, if missed, would constitute minor or major service-level violations and to define the appropriate consequences of those violations.

A minor SLA violation may warrant service or fee credits, while a major SLA violation may constitute a breach of contract. Both parties must review possible scenarios, clearly define each scenario's penalty and consider the potential ramifications of those penalties.

In cases where the SLA is between two units within a company, the penalties may be different, but consequences should still exist. Management reporting can be used to highlight issues as they occur and force delinquent business units to take action—whether that means developing a plan to improve performance, re-evaluating resourcing or changing leadership.

CONCLUSION

As asset managers increasingly turn to functionalized operations and outsourcing, strong governance models will be essential for ensuring the efficiency and efficacy of operations. Meaningful SLAs can help ensure that quality and timeliness standards are maintained, while providing useful insights into operational processes.

For an SLA to be effective, both parties must work towards its success. SLAs should be realistic; any demands for quality and timeliness must be within each partner's reach. They should also be measurable and enforceable, with performance metrics and measurement tools established at the outset. At the end of the day, both sides have an interest in reducing firm-wide risk and increasing the potential benefits of the relationship in the most efficient way possible.

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