SLA VS KPI: WHAT'S THE DIFFERENCE?



In the pre-cloud computing era, application management strategies involved a simple selection of Service Level Agreement (SLA) contract items and Key Performance Indicator (KPI) metrics.

A narrow set of IT solutions, interfaces, and services were deployed on premise to perform a variety of business related tasks. Cloud computing has transformed the strategic options in application management and IT service delivery to an extent that IT professionals and business executives struggle to extract business value from otherwise promising enterprise IT solutions.

This article explores the terms SLA and KPIs, and provides the guidelines necessary to improve service levels and business performance:

What is a Service Level Agreement (SLA)?

An SLA is a written agreement that qualitatively and quantitatively specifies the service committed by a vendor to a customer. It identifies:

- The metrics used to measure the level of service provided
- Remedies or penalties resulting from failure to meet the promised service level expectations

An SLA is needed to support the performance of operations that depend upon the underlying services provided by the vendor. Various levels of service may be offered at different pricing ranges and customers often make an optimal trade off between service level and cost.

By setting the SLA contractual obligations, vendors manage expectations across their customer-base. The measured metrics and performance indicators also allow both the vendor and customer to identify, track, report and evaluate the true measures defining real-world business needs and performance.

In addition to the service-related components, an SLA also contains provisions about:

- Payment
- Exchange of confidential information
- Work product ownership
- Warranties
- Liability limits
- Termination terms
- Insurance
- Force majeure clauses

SLAs should be seen as targets for the measured metrics instead of contractual obligations holding provisions for legal and financial penalties upon failure to meet service levels. For instance, a datacenter downtime on average costs around $9,000 per minute according to a 2016 Ponemon Institute research report. Under an SLA agreement, most vendors of cloud-based datacenter services would only reimburse credits charged for the underserved SLA metrics.

SLA should be seen as a process to improve the service qualities that impact business performance. In the age of cloud computing, when business organizations scale their operations proactively in response to market circumstances, SLA metrics and contractual obligations should be seen as a process to improve service quality and meeting evolving business requirements. The following key principles can help organizations devise and seek optimal SLA terms for their business needs:

- **Future-proof service levels without breaking the bank.** Setting the service level bar too low and meeting current business needs at the lowest possible cost may be counter-productive due to the lacking roadmap for cost-effectively improving service levels in the future.
- **Measure the business outcome of various SLA metrics.** Some metrics may not promise adequate business value despite the high cost of service level provided, while other metrics may define the business impact but not adequately considered for evaluation.
- **Understand the vendor performance history with service levels.** Fails to sustainably remediate recurring issues often defines the ability to meet service levels in the future.
- **Service levels and agreements are bound to change in response to changing business circumstances.** Follow a realistic plan to implement service level changes toward a preferred end-state without compromising cost-effectiveness, business growth and scalability.
- **Incentivize continuous improvements in service levels.** Negotiate high cost penalty upon recurring failure to meet service levels. This can prevent vendors from using service credit reimbursements as an alternative to investing in otherwise expensive root cause resolution.

What is a Key Performance Indicator (KPI)?

Key Performance Indicator (KPI) is a measure that defines the progress with respect to a strategic goal. A KPI provides an analytical basis to evaluate progress toward stated objectives. KPIs can be devised for:

- Specific business processes, technologies, components or resources
- The overall business performance in terms of growth, revenue generation, ROI, or other decision making criteria

KPIs are designed to reduce the complexity in evaluating prior decisions and the resulting impact and consequences. KPIs provide a manageable and holistic visibility into business performance from a variety of angles, allowing decision-makers to adapt strategies for optimum results. It is therefore critical to identify, monitor, report and evaluate the most impactful metrics that indicate the true performance of the associated business component. The following guiding principles can be adopted in identifying the correct KPI metrics:

- **KPIs must be selected based on the strategic link with the business performance.** Select KPIs that decision-makers use to manage the business. For instance, if a team is managing customer experience, financial KPIs may not offer a full correlation to customer satisfaction.
- **There's no specific number of KPIs that must be used.** Multiple KPIs may be required to aggregate across diverse selection groups to communicate the complete picture regarding prior decisions impacting present and future business performance.
- **KPIs that are relevant today may not be useful tomorrow.** Decision makers are expected to evolve how they select, measure and report KPIs in response to changing market and business circumstances. A framework to proactively perform this transition can further simplify the task of reporting and understanding KPIs.
- **Limitations and assumptions should be well-considered in evaluating KPIs.** For instance, some KPIs do not measure tangible data points but relative performance or perception mapped onto quantifiable information. Any discrepancy in inferring absolute performance of the metrics must be considered before guiding decisions.

What's the difference?

Both the Service Level metrics and KPIs provide useful information. Service Level metrics provide information on the baseline performance expectations. An agreement toward meeting those expectations is regarded as an SLA term.

KPIs provide information on the efficiency and success in meeting organizational goals or expectations. While SLAs are used to ensure that service level metrics don't fall below certain metrics criteria, KPIs help ensure that specific performance improvements and results are met adequately or exceedingly. In order to improve service level performance, the engaged service provider, internal or external, is expected to adopt appropriate actions.

For performance improvements on specific metrics and KPIs, organizations need to take appropriate actions internally to meet the strategic objectives.

Related reading

- BMC Service Management Blog
- 6 SLA Best Practices for Service Management Success
- IT Organization Metrics & KPIs: A Well-Rounded Approach
- Digital Transformation Metrics & KPIs for Measuring Success