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# MANAGED SERVICES: A LEGAL ANALYSIS AND TEMPLATE CONTRACT

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# Managed Services Contracts



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# Agenda – the Managed Services contract Lifecycle

- Pre-contract - tender process and supplier due diligence
- Transition phase
- (Transformation)
- Operational phase
  - service level and credit regime
  - Contracts tools for ensuring flexibility and ‘value for money’
- Termination and exit

# What *are* “Managed Services”?

- From a legal perspective what matters is:
  - The service provider is taking over an entire function (eg the entire telecoms infrastructure) on an “end-to-end” basis
  - It is then a type of outsourcing – over an extended period (3-5 years typically)
  - The customer is not buying software or hardware – they are buying a *service*. This will be highly bespoke – specific to the particular customer.
  - Customers might expect the underlying technology to change / improve during the life of the contract.
  - Often at an all-inclusive price determined in advance.
- Contrast with another outsourcing trend – “multi-sourcing”
  - In multi-sourcing the customer chooses several suppliers who are each responsible for separate (but related) aspects
  - One recent example – application support and IT infrastructure

# The Template

- Aims to be reasonably even-handed – but has a (slight) pro-supplier bias
- Contemplates two phases:
  - “Set-Up” or due diligence; and
  - post-acceptance service provision
- Assumes transfer of assets and contracts but not of staff
- Transition but no transformation
- Ideally Customers would separate these two and use the first step to generate a detailed plan for putting second step out to tender

# The RfP Process – Some Tips

- Attach a draft contract if possible
- Chosen supplier to warrant that all representations made in their response to the RfP are true, accurate and not misleading

# Pre-contract phase: supplier due diligence

- Access to equipment, third party contracts, existing service level data, customer staff
- Supplier validation of cost and delivery assumptions; identification of risks
- Ideally prior to contract – but resourcing constraints
  - Impacts on contractual protection given – and received – by customer
    - warranties, service level verification period, variation of charges
- Dependent on co-operation of outgoing supplier (if there is one)
  - address in termination/exit management provisions

# Transition phase

- Asset transfer arrangements
  - people, equipment and third party contracts
- Third party contracts
  - Novation, termination, assignment or agency
  - cross-indemnities pre/post-transfer
- Customer warranties re suitability/quality of assets
  - quality of due diligence process
  - bargaining power
- Freeze on changes to existing processes and tools?
- Service level verification (“baseline”) and/or service credit holiday period
- Exit management plan & procedures manual
  - consider incentives for completion
  - update obligations throughout life of agreement

# Transformation

- When transition is complete service levels kick-in
- Then, possibly, transformation:
  - to reduce costs, improve service levels – by specific measures (eg move data centre, adopt virtualised desktop)
- Contract typically to contain detailed transformation plan (not to be confused with a transition plan)
  - milestones, liquidated damages
  - specified improvements in service levels (“ratchet”)
- Also “continuous improvement”
  - Reports on new tech, sharing of benefits
  - Often this is the main motivation for the customer.

# Service level and credit regime

- The SLA should be:
  - clear
  - properly integrated to the main terms and conditions;
  - flexible
  - **measurable**
- Types of service level:
  - continuous e.g. system/application availability
  - event-based e.g. calls answered within agreed timeframes
  - sample e.g. accuracy of forms/completed letters sent out (BPO)
- Basic principles:
  - measure what's important, not what's easy
    - impact on customer's business
  - avoid over-measurement
  - avoid incentivising wrong behaviour
  - allow for service level improvement

# The SLA - example

KPI		SLA	
		Mean Value	Maximum Value
1	Network Availability	99.98%	-
2	Time to Repair Critical Situations	120 min	210 min
		180 min	300 min
3	Time to Repair Urgent Situations	240 min	480 min
4	Time to Repair Non-Urgent Situations	24 h	72 h
		-	4 d
		-	30 d
		-	180 d
5	Network Operations	-	1 d
		-	4 d
		-	10 d
6	Circuit Activation	-	1 d
		-	4 d
		-	10 d
7	Analysis and Diagnose Network Quality	1 d	3 d
		3 d	5 d
		5 d	8 d

- KPI 2s and 4: split according to importance of the node
- KPIs 5 and 6: split according to the priority of the work order
- KIP 7: split according to customer impact.

Service credits payable for failure to hit these.

# Service level and credit regime

- Avoiding SLAs which incentivise wrong behaviour
  - E.g. application support outsourcing – 95% of P2 faults resolved within 4 hours means no incentive to resolve faults where SLA has already failed
  - Addressed through compounding service levels:
    - 95% of P2 faults resolved within 4 hours
    - 100% within 8 hours
  - This is also the idea behind the “mean” and the “maximum”
- Points-based regimes
  - “points” allocated based on business impact of SLA
  - service credits triggered if points threshold reached
  - multiplier for repeated failure – penalty risk
- Resist “sole and exclusive” – or at least allow other remedies once max reached
- “Earn back” for over-performance?
  - May be appropriate, but only if the customer gets a benefit from over-performance (eg cf voice quality & availability)

# Flexibility and Change

- Benchmarking
  - May be very difficult to do in practice for Managed Services – which are often very highly tailored to a specific customer
  - Can be difficult to compare prices but you can benchmark service levels against other suppliers
    - Definition of “Good Quality” (or “Good Value”) is important
  - *All* the service or specific elements? How often?
  - Consequences of the report finding the service is *not* good acceptable? Retrospective price reduction? Termination?
    - *C&W v IBM* – IBM offered *retrospective* compensation
    - Template suggests – on price, Supplier must make a new offer, which *is* “Good Value”, with a new Initial Term

# Flexibility and Change

- Change Control
  - Mechanism for parties to agree scope and charging impact of a particular change (whether contract amendment or service change)
  - Usually the procedure can't force an agreement – but you *can* have a mechanism allowing an immediate change with price consequences to be agreed later.
    - One example (not in the template) – the “Nike” (“just do it”) clause. (Can also be used in context of fault prioritisation)

# Flexibility and Change

- Governance
  - Often underestimated but very important for maintaining solid working relationship
  - Programme of regular meetings: monthly (even weekly), quarterly, annual
  - Contract to be clear on who attends, how minutes taken, agenda items

# Exit management and assistance

- Exit assistance for extend beyond termination date
- Exit Management Plan (EMP)
  - To be updated during life of contract
  - contract deals with exit principles, EMP deals with operational aspects and mechanics
- Transfer back of data, contracts, equipment
  - if non-exclusive contracts, assistance in sourcing alternatives
  - pricing and transfer/assignment charges
- TUPE transfer of staff

# Conclusion

- Unlike with many other types of contracts, a managed service contract entails a long term commitment between the parties
- Relationship must be flexible enough to cope with change over time
- The contract / SLA can provide mechanisms for this
- BUT – the key lies in the management of the relationship between the parties – at all levels. The contract / SLA is just a tool to help achieve this

# Questions

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