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Service Providers: Align Deal Constructs to Buyer Expectations

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Initiatives: Lead a Profitable Tech Services Practice

Services buyers evaluate multiple commercial constructs beyond pricing to optimally align contracts to their business needs. Tech services leaders can use this research to identify how buyers expect to pay for services today and in the future.

Overview

Key Findings

- Digital business services buyers utilize a fairly even spread of five commercial models when contracting services from suppliers, and they expect to continue doing so.
- Buyers expect contracts with a fees-at-risk component to rise from an average of roughly a third of contracts today to 40% by 2027 as they seek to align the benefits they receive from services with their spend.
- Business and blended IT-business buyers are more likely than IT buyers to use fees-at-risk components in contracts today, with nearly 35% of contracts including this component. However, by 2027, IT buyers expect to increase use of this at-risk contracting mechanism from 30% to 38% of contracts.
- “Indecisive” buyers tend to utilize time-and-materials (T&M) contracts more than “confident” buyers (using Gartner’s Enterprise Technology Adoption segments), perhaps reflecting varying maturity in pricing deals.
- Emerging use of accelerators, assets and new generative AI (GenAI) assistants during service delivery offers promise of greater services speed and scale, but also adds complexity to commercial constructs.

Recommendations

Technology service leaders structuring commercial constructs into contracts should:

- Align services commercial constructs to buyers' preferences, by configuring time and materials, fixed price, fixed price per milestone, outcome-based and consumption-based models that optimize for simplicity, value capture and longer-term client retention.
- Use fees-at-risk components in competitive contracts and to demonstrate a commitment to delivering both contractual obligations and broader client benefits.
- Understand buyer context, including business-IT role orientation, to anticipate and structure at-risk components and triggers according to buyer preferences.
- Tailor fixed price and T&M contracts appropriately to relevant buying centers by using Gartner data and Enterprise Technology Adoption profiles.
- Anticipate and respond to buyer pressure for commercial models that account for potential services productivity gains from asset-enabled services by pricing assets by value delivered.

Digital Business Services Buyers Use at Least Five Commercial Models for Contracting With Suppliers

Buyers use at least five commercial constructs across their supplier contracts today: time and materials, fixed price, fixed price per milestone, usage/per unit and outcome-based (see the Background and Context section below for definitions).

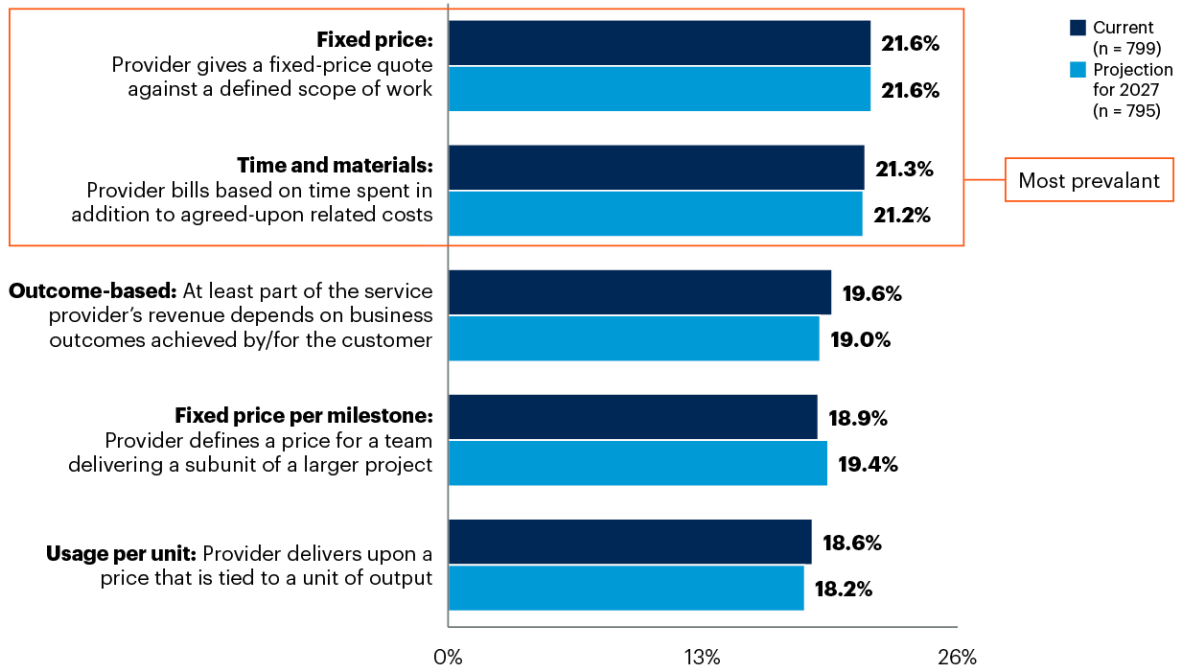
While no model is dominant, buyers are more likely to use fixed price and time and materials, according to the 2024 Gartner Digital Business Buying Drivers Survey (see Figure 1). Both of these are familiar to buyers and adapt well to differences in labor and overhead costs across customer and supplier markets.

Looking forward, buyers do not expect their mix of contracting models to change substantially by 2027, with the exception of a slight decline in outcome-based models and a slight increase in fixed price per milestone models. The expected slight decline in outcome-based contracts may reflect an acknowledgment that these contracts are the most challenging to design and execute, making them a better fit for large transformation programs that include a program-level value assurance workstream.

Figure 1: Percentage of Services Contracts With Various Commercial Models

Percentage of Services Contracts With Various Commercial Models

Mean percentage



n varies; all services buyers, excluding "not sure"

Q. Currently, what percentage of your organization's services contracts include the following attributes, and what is your projection for 2027?

Source: 2024 Gartner Digital Business Buying Drivers Survey
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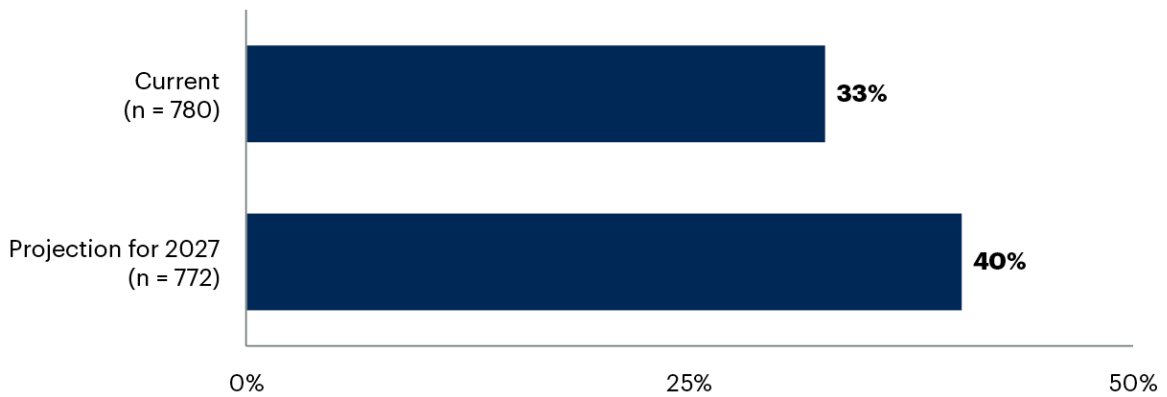
Fees-at-Risk Contract Arrangements Are Poised to Grow Substantially by 2027

Fees at risk, or those contracts that include certain performance-based payment triggers (such as satisfaction holdbacks, milestone delivery or financial hurdles) are expected to grow in use. At-risk arrangements are included in 33% of contracts today, on average, and are expected to rise to over 40% of contracts by 2027, according to the most recent 2024 Gartner Digital Business Buying Drivers Survey (see Figure 2). This fact broadly aligns with buyers' ambitions to contract with suppliers for business outcomes – enabling them to reduce or increase payment based on predefined payment triggers.

Figure 2: Percentage of Services Agreements With Fees-at-Risk Component

Percentage of Services Agreements With Fees-at-Risk Component

Mean percentage



n varies; all services buyers, excluding “not sure”

Q. Approximately, what percentage of the services agreements within your entire organization (and to the extent that you know) currently include a fees-at-risk component, and what do you project this percentage to be in 2027?

Source: 2024 Gartner Digital Business Buying Drivers Survey

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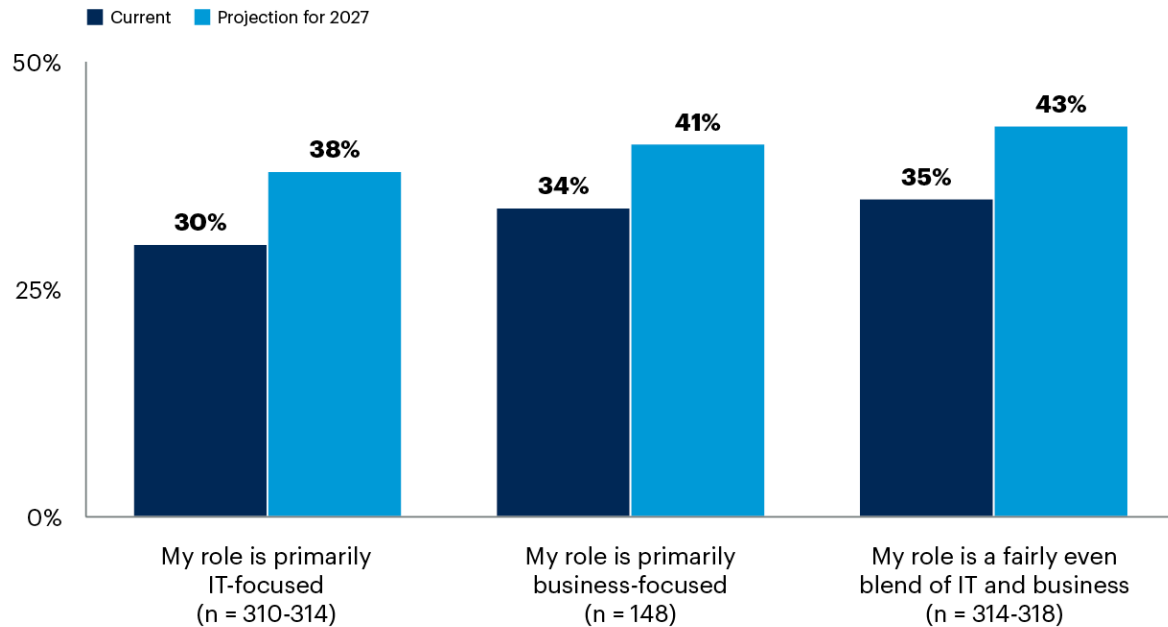


Notably, respondents who describe their role as a blend of business and IT have a larger share of contracts with an at-risk component than IT buyers, with 35% of contracts currently including this mechanism (see Figure 3). These blended roles say almost 43% of contracts will include an at-risk component by 2027. Buyers whose role is primarily IT-focused said that, on average, 30% of their contracts include at-risk components currently, and they expect to see this feature in 38% of contracts by 2027.

Figure 3: Percentage of Services Contracts With At-Risk Components by Decision-Maker Role

Percentage of Services Contracts With At-Risk Components by Decision-Maker Role

Mean percentage



n varies; all services buyers, excluding “not sure”

Q. Approximately, what percentage of the services agreements within your entire organization currently include a fees-at-risk component, and what do you project this percentage to be in 2027?

Source: 2024 Gartner Digital Business Buying Drivers Survey
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“Indecisive” Buyers Favor Time and Materials Over Fixed Price Contracts, While the Opposite Is True for “Confident” Buyers

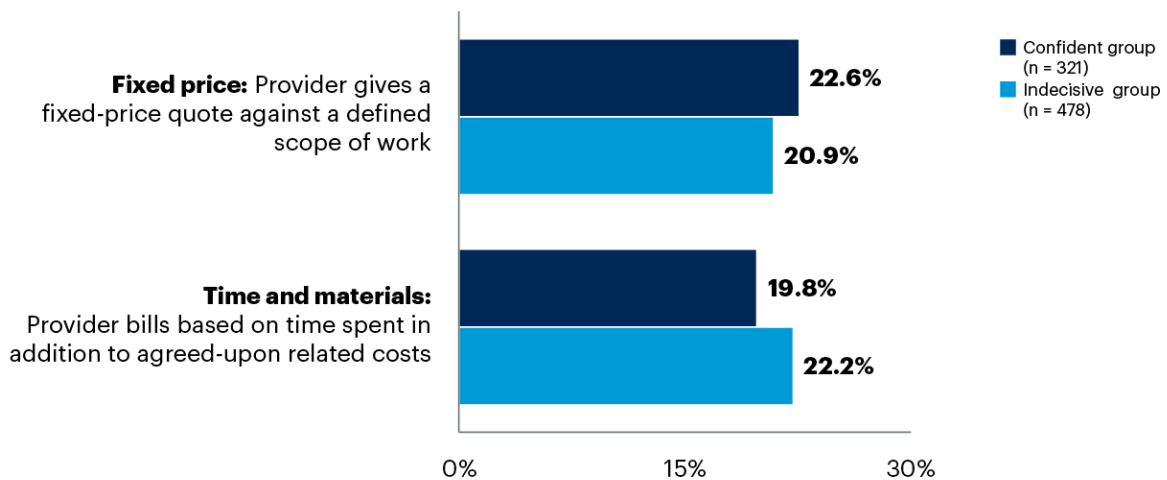
Prevalence of commercial models also differed slightly by Enterprise Technology Adoption profile. Gartner uses its own proprietary Enterprise Technology Adoption Profile Framework, developed across a variety of research studies for the past 10 years, to better understand firm-level enterprise technology adoption attitudes and behaviors (See Enterprise Technology Adoption Profile Self-Assessment).

In this study, the confident group (characterized as Ambitious Leaders, Agile Leaders, Fast Followers and Disciplined Followers), tended to use fixed-price services slightly more than the indecisive group (characterized as Reluctant Followers, Conflicted Laggards or Disinterested Laggards). Conversely, the indecisive group uses time and materials significantly more than the confident group (see Figure 4). This may be a reflection of these buying segments’ level of risk tolerance and/or proficiency in estimating overall deal pricing.

Figure 4: Percentage of Services Contracts With Various Commercial Models – Confident vs. Indecisive

Percentage of Services Contracts With Various Commercial Models – Confident vs. Indecisive

Mean percentage



n varies; all services buyers, excluding “not sure”

Q. Currently, what percentage of your organization’s services contracts include the following attributes?

Source: 2024 Gartner Digital Business Buying Drivers Survey

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What to Expect From Commercial Contracting Models Going Forward

With the obvious exception of at-risk arrangements, buyers appear to expect more of the same from providers’ services contracting models in the coming years. However, three trends may impact these perceptions.

- **Increasing deal complexity.** Services deals themselves increasingly include business consultants and technology experts, solution accelerator assets, and a mix of proprietary and off-the-shelf software and analytics models. These types of projects require more sophisticated pricing, commercial constructs, and strong governance over discounts across labor and nonlabor components included in the deal.
- **Use of assets for accelerating services execution.** Pricing for assets, particularly for tools and accelerators used during service delivery, remains a quandary for most service providers. As asset R&D and delivery costs have risen (and become more variable) for accelerators, service providers will be compelled to find effective ways to, at minimum, recover these costs from customers to avoid services margin compression. Ideally, asset pricing and commercial constructs will be accretive to revenue, margin and overall enterprise value.
- **Increased use of specialized AI and GenAI assistants for services delivery.** Gartner expects service providers will increasingly augment their expert delivery resources with GenAI assistants (for example, IBM Consulting Advantage Assistants and Microsoft 365 Copilot). While these assistants offer the promise of speedier service delivery and increased scalability, they also come with material, highly variable operating costs for compute. At worst, providers may be forced to use alternative commercial models to cover these costs. At best, providers will find ways to monetize the accelerators as time goes down and materials costs go up.

Analysis

Background and Context

Technology and business services providers offer a variety of different commercial models to buyers. Buyers demand this flexibility in order to align service provider fees to the timing and magnitude of financial ROI or operational impact they expect to see from the services they purchase. Suppliers use their commercial structures to remain competitive, align with customer expectations, and optimally, to sustain or grow margins.

The predominant services models in use today include:

- **Time and materials:** Provider charges a customer fees based on time spent by billable resources in addition to agreed-upon related expenses (e.g., tools, travel).
- **Fixed price:** Provider gives a fixed-price quote against a defined scope of work.
- **Fixed price per milestone:** Provider defines a price for a team delivering a subunit of a larger project (e.g., a sprint) and bills the client when the milestone is completed.

- Usage/Per unit: Provider charges a price that is tied to a unit of output or consumption (predefined per standard service work unit, per user, desktop, server terabyte or ticket).
- Outcome-based: At least part of the service provider's revenue is dependent on business outcomes achieved by/for the customer (for example, reducing customer acquisition cost [CAC] by 15%).

Fees-at-risk arrangements are those that contain language that makes customer payments contingent on one or more triggers. Triggers can include a wide variety of measures, including but not limited to quality or outcomes such as overall satisfaction, responsiveness, adherence to time or budget, financial or operational results, and levels of technology adoption.

Conclusion

Commercial constructs have become an important lever for reducing deal friction, competing effectively in the services market and derisking deals for services buyers and providers alike. Increasing buyer expectations for at-risk fee arrangements may well be a signal that this construct is a simpler way to align buyer and seller interests than more complex models like business-outcome-based. Given buyers' expectations for more of the same in the coming years, technology service leaders should seek to optimize the deal constructs that balance simplicity, value capture and longer-term client retention.

Evidence

2024 Gartner Digital Business Buying Drivers Survey. This survey sought to understand the behavior of services buyers to support their digital business – including what they are buying, the use cases for technology, delivery model preferences, how far they have progressed on their digital transformation journey and what lies ahead. The survey was conducted online from February through April 2024. In total, 880 respondents from organizations with annual revenue of at least \$50 million or equivalent from Asia/Pacific (31%), North America (30%), Western Europe (27%), and Southern Europe (12%) participated. Industries represented included banking and securities, manufacturing, natural resources, communications, media and services, government, retail, wholesale trade, insurance, utilities, transportation, healthcare providers and education. Qualified respondents were decision makers or decision influencers at the director level or higher involved in the selection or evaluation of at least one of the following consulting or outsourcing services within the past two years: business consulting, technology consulting, application implementation, application managed services, infrastructure implementation, infrastructure managed services, infrastructure as a service, business process services, digital product engineering, and marketing, experience, content and image services. Disclaimer: Results of this survey do not represent global findings or the market as a whole, but reflect the sentiments of the respondents and companies surveyed.

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