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MEMORANDUM FOR CHIEF ACQUISITION OFFICERS
SENIOR PROCUREMENT EXECUTIVES

FROM: Anne E. Rung
Administrator

SUBJECT: Effective Use of Reverse Auctions

This past December, the Office of Federal Procurement Policy (OFPP) issued guidance directing that agencies take a series of actions to foster innovation, increase savings, and improve performance in the acquisition process.¹ For commonly purchased goods and services, these goals will be pursued through category management and a broad set of supporting strategies to achieve better results. Reverse auctions are one of the tools agencies have used in recent years to acquire certain common needs, such as commercial off-the-shelf information technology (IT) hardware and software. In a report published December 9, 2013, the Government Accountability Office (GAO) noted the increased use of reverse auctions at a number of agencies and recommended that OFPP issue guidance to help ensure agencies capture savings and other benefits of this tool.² This memorandum reviews the benefits of reverse auctions, offers a set of reminders to help contracting offices maximize the value of this tool, and asks agencies to work with OFPP in identifying and collecting data that can be used to evaluate and improve results.

The value of reverse auctions

A reverse auction is a process for pricing contracts supported by an electronic tool where offerors bid down, as opposed to the traditional auction which requires buyers to submit sequentially higher bids, the main goal of which is to drive prices downward. Offerors are given the opportunity to continually revise their prices during the bidding process until the auction closes. Multiple benefits have been identified in connection with the use of reverse auctions, including the following:

Price reductions. When properly used in combination with other source selection principles, reverse auctions can yield noteworthy savings. GAO notes that the four agencies it studied (Army, Department of Homeland Security (DHS), Department of the Interior, and the

¹ See *Transforming the Marketplace: Simplifying Federal Procurement to Improve Performance, Drive Innovation, and Increase Savings* (December 4, 2014), available at <http://www.whitehouse.gov/sites/default/files/omb/procurement/memo/simplifying-federal-procurement-to-improve-performance-drive-innovation-increase-savings.pdf>.

² See REVERSE AUCTIONS: Guidance Is Needed to Maximize Competition and Achieve Cost Savings (GAO-14-108), <http://www.gao.gov/products/GAO-14-108>.

Department of Veterans Affairs (VA)) reported approximately 12% in savings from purchases totaling more than \$800 million during fiscal year (FY) 2012 for a range of commercial items, including IT, laboratory equipment, furniture, and detection and radiation equipment. The Department of Energy separately reported seeing an average savings of about 14% per contract awarded to provide core supplies and services for its National laboratories. These savings were generally calculated by comparing the agency's independent government cost estimate to the closing price of the reverse auction.

Savings have been reported both through open market purchases (e.g., often for purchase orders awarded under the simplified acquisition threshold (SAT)) and by leveraging existing multiple award contracts. The latter include the Federal Supply Schedules managed by the General Services Administration (GSA) and government-wide acquisition contracts (GWACs), such as the Department of Health and Human Services' Electronic Commodities Store GWAC and DHS's FirstSource contract for IT commodities, which is a total small business set-aside. GSA reports that agencies who conducted reverse auctions against Schedule contracts using its electronic platform, which launched in FY 2013, achieved savings of 19% and more than 23% in FY13 and FY14, respectively.

Enhanced competition. Reverse auctions offer the ability to conduct robust, real-time price competitions. They allow for multiple "rounds of bidding" for continued price reduction. This type of interactive bidding, when it occurs, strengthens competition.

Significant small business participation. GAO reported that 80% of the dollars awarded through the reverse auctions it reviewed from FY 2012 were made to small businesses. A number of agencies have reported continued success in driving dollars to small businesses. For example, agencies have awarded 85% of auctions to small businesses using GSA's reverse auction tool since it was launched in July 2013.

Getting the best results from reverse auctions

As with all procurement tools, effective use of reverse auctions requires careful planning and execution. Contracting officers should consider the following issues to help optimize the results achieved from reverse auctions:

Is the requirement suited for a reverse auction? Reverse auctions are not a one-size-fits-all tool. Reverse auctions are likely to be most effective in a highly competitive marketplace when requirements are steady and relatively simple and might otherwise be acquired using either a sealed bid or achieving best value through "low price technically acceptable" source selection criteria, and result in fixed price agreements. These circumstances would typically exist in acquisitions for commercial items and simple services that often fall under the SAT. As with any procurement, market research must be conducted to understand the marketplace and to determine if it is reasonable to assume that the potential benefits of a reverse auction can be achieved.

Is the agency capturing and reviewing data from prior reverse auctions? A number of reverse auction tools capture prices paid information, as well as offered prices made during the auction. This information has a number of important benefits. In particular, this information can help agencies formulate more accurate government cost estimates, which, in turn, helps to ensure fair and reasonable pricing. Outside of reverse auctions, this cost information (used in conjunction with relevant non-cost information) may help an agency as it looks for more competitive prices for similar items on existing contracts, and reduce overall contract duplication.

GSA's reverse auction tool, which can be used in conjunction with its Schedule contracts, VA's Schedule contracts, Federal Strategic Sourcing Blanket Purchase Agreements (BPAs), agency BPAs against GSA Schedules, and other agencies' contracts (e.g., DHS First Source II), captures detailed (level III) prices paid spending data from past reverse auctions. Agencies can access prices paid information through the Common Acquisition Platform,³ a tool that GSA has launched to help agencies identify best-in-class contracts issued by GSA and other agencies, best practices, and other information agencies need to reduce the proliferation of duplicative contract vehicles and deliver the best value possible to federal customers and the American people.

To ensure the competition benefits of reverse auctions are being appropriately leveraged, agencies should review any available data on offers received and consider questions such as the following: Is the agency getting more bidders? If the agency is getting a similar number of bidders as it did without using a reverse auction, is it getting interactive bidding? If not, is the transparency of the bids helping to generate lower prices than the government was getting previously? If the agency has previously used a reverse auction and gotten only one bid, has it taken steps that it believes will increase interest in the auction to justify any fees it may be paying to a third party provider?

Is the agency promoting small business participation to the maximum extent practicable? Agencies remain fully responsible for adhering to all applicable small business contracting policies when using reverse auctions. In general, agencies are required to automatically set-aside work for small businesses when the anticipated dollar value is below the SAT. If a determination is made that a small business set-aside is inappropriate, contracting officers must document the reason. For acquisitions above the SAT, contracting officers must set-aside for small businesses when there is a reasonable expectation that offers will be obtained from at least two responsible small business concerns and an award will be made at fair market prices.⁴

When a requirement is set-aside for small business, this information must be conveyed in the solicitation and notice for a reverse auction so that participation in the auction is appropriately limited. In both set-aside and non-set-aside solicitations, the contracting officer must take reasonable steps to ensure that the offerors have access to information regarding the process and any expectations when utilizing reverse auctions, including contact information of the contracting official who will answer questions about the solicitation.⁵

³ <https://hallways.cap.gsa.gov>

⁴ See FAR 19.502-2 Total small business set-asides.

⁵ See FAR 5.102(c)(2).

Has the agency sought feedback from the vendor? While use of reverse auctions in federal contracting has increased in recent years, agency experience with this tool is likely to be more limited than with many other more established practices. Vendor feedback may be particularly helpful as agencies build experience and work to generate robust competition. Accordingly, agencies are encouraged to elicit feedback from auction participants, including experiences with a third party contractor, if one was used to facilitate the competition.⁶

Have the appropriate internal controls been followed? An agency should ensure its contracting staff is carrying out its statutory and regulatory responsibilities, irrespective of whether a third party contractor is used to support the effort. This includes making sure that the contract file is documented⁷ with market research results, an independent government cost estimate, vendor quotes, brand name justifications (where applicable), a price reasonableness determination, and documentation that the vendor is a responsible source.

Has the workforce been provided tools, guidance, and/or training? Agencies must ensure that members of the acquisition workforce are trained and are familiar with any agency-specific policies and procedures that govern the use of reverse auctions. Online continuous learning modules, CLC 031 – Reverse Auctioning and FAC 052 – The GSA Reverse Auction Platform, are available from the Defense Acquisition University (DAU) and the Federal Acquisition Institute (FAI).⁸ These courses provides a basic introduction to the process of using reverse auctions.

Does the agency regularly review its reverse auction practices and policies? Like other acquisition tools, agencies should be evaluating their experiences with reverse auctions and the effectiveness of existing practices and policies as part of its procurement management reviews so that refinements can be made as necessary. To support these efforts, OFPP intends to convene a working group to review needs for standardized data collection and other matters (see next steps below).

Additional considerations when using a third party contractor

When agencies decide to contract with a vendor to conduct reverse auctions (hereinafter referred to as a “third party contractor,”) agencies must consider the following additional issues:

Fees. Contracting officers should negotiate a fee structure with a private sector service provider that provides the best value to the government. There are multiple ways in which fees might be charged when a third party contractor is used. The cost to conduct a reverse auction may be a percentage of the transaction, a percentage of the savings, or a flat fee. Whatever the arrangement, agencies must make a determination before awarding a contract with a third party contractor that the fee structure represents a fair and reasonable cost for the reverse auction

⁶ For general guidance on the use of vendor feedback surveys to target opportunities for improved acquisition practices, agencies may wish to consider *Acquisition 360-Improving the Acquisition Process through Timely Feedback from External and Internal Stakeholders* (March 18, 2015) available at <https://www.whitehouse.gov/sites/default/files/omb/procurement/memo/acquisition-360-improving-acquisition-process-timely-feedback-external-internal-stakeholders.pdf>.

⁷ See, FAR Subpart 4.8.

⁸ http://icatalog.dau.mil/onlinecatalog/courses.aspx?crs_id=440

service. In addition, fees should be considered in evaluating whether the price of the product or service (including any additional fees for use of another agency's existing contract) is fair and reasonable. Anticipated cost savings should be taken into account in determining the reasonableness of the fee.

In order to maximize competition and small business participation, agencies are encouraged to cover the costs of vendor participation and avoid fee arrangements where vendors must pay to participate in the agency's reverse auction.

Government contracting official responsibilities. Agencies must take additional steps to ensure that the selected third party contractor provides a "seller-neutral" marketplace. The agency remains ultimately responsible for ensuring that third party contractors do not perform inherently governmental functions and that processes are compliant with all procurement laws and regulations, including those associated with protecting the integrity of competition, reviewing past performance, providing appropriate notice of the reverse auction, establishing terms of participation and the basis for source selection, securing proprietary vendor information, and facilitating communications between the agency and vendors during the course of an auction. Agencies should ensure that no contractors are excluded from bidding in an auction by a third party contractor. Only an agency official may exclude a bidder from participating in an auction.

Contract data information. Any information used in a reverse auction conducted by a third party contractor is the property of the Federal Government and should be provided to the agency on a regular basis based on the agreement between the agency and the third party contractor. These data will be used in support of government-wide efforts to reduce duplication and create further savings.

Next steps

To maximize the value of reverse auctions and ensure practices are effective and meeting their intended purposes, OFPP seeks to work with agencies to identify the essential management data points (e.g., price paid for item, fees paid (if any), number of bidders, and level of interactive bidding) and mechanisms for collecting and aggregating information in a manner that leverages technology and avoids the need for manual collection. As explained above, electronic reverse auction tools typically allow agencies to maintain documentation of each auction online, creating a virtual library of prices paid data that is a key component of category management and can be useful in developing better price estimates and purchasing strategies for future requirements. Similarly, terms and conditions can be stored in an easily reusable format for recurring requirements, saving valuable time.

Accordingly, agencies that have used reverse auction tools (either directly or with the assistance of a third party contractor) are asked to provide points of contact to Susan Minson (e-mail: sminson@omb.eop.gov or 202-395-6810) no later than July 10, 2015. As part of this process, OFPP will work with agencies to review methodologies for calculating savings.

Please remind your acquisition workforce of the points and best practices outlined in this memorandum and encourage them to take the online training accessible through FAI and DAU. For your awareness, as a further step, the Federal Acquisition Regulatory Council will open a case to develop coverage on the use of reverse auctions in the Federal Acquisition Regulation and will address the guidance in this memorandum, as appropriate.

Any questions should be directed to Ms. Minson. Thank you for your attention to this guidance.