CONTRACTING AWAY ACCOUNTABILITY - REVERSE AUCTIONS IN FEDERAL AGENCY ACQUISITIONS

JOINT HEARING
with
Small Business Committee Subcommittee on Contracting and Workforce

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON VETERANS' AFFAIRS
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CONTRACTING AWAY ACCOUNTABILITY - REVERSE AUCTIONS IN FEDERAL AGENCY ACQUISITIONS

Wednesday, December 11, 2013

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON VETERANS' AFFAIRS,
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS,
Washington, D.C.

The Subcommittees met, pursuant to notice, at 10:11 a.m., in Room 334, Cannon House Office Building, Hon. Richard Hanna [Chairman of the Subcommittee on Contracting and Workforce] presiding.

Present from Subcommittee on Oversight and Investigations: Representatives Coffman, Roe, Kirkpatrick, O'Rourke, and Walz.

Present from Subcommittee on Contracting and Workforce: Representatives Hanna, Bentivolio, Meng, and Chu.

OPENING STATEMENT OF HON. RICHARD HANNA

Mr. HANNA. I will call this to order this morning. Thank you all for being here. Obviously I am not Mr. Coffman. He is tied up in a Budget meeting and hopefully he will be here as soon as he possibly can. And I am going to read my own opening statement and then we will introduce our witnesses and go from there.

This morning we are here to talk about reverse auctions, specifically when they make sense for taxpayers as well as when they do not. Reverse auctions can be a way to facilitate competition and increase small business participation, or they can be a barrier to entry for small businesses and a ways of evading meaningful competition.

As I have said before no one type of contracting methodology is inherent good or bad. It is how government uses these tools that matter. In May my Subcommittee held a hearing that looked at the use of reverse auctions for construction services and the testimony we received convinced me that reverse auctions do not work for these contracts. Therefore, I introduced H.R. 2751, the Common Sense Construction Contracting Act of 2013, to restrict the use of reverse auctions for construction services. However, 90 percent of reverse auctions are for goods, not services. And today we are going to look at the other uses of reverse auctions.

On Monday the Government Accountability Office released a report that suggests that reverse auctions are not being used properly for other types of goods and services. The GAO found that last year over one-third of reverse auctions conducted for agencies had no interactive bidding, the hallmark of reverse auctions. Yet agencies paid $3.9 million in fees for these auctions. Furthermore, they

found that 24 percent of all reverse auctions were not awarded to the lowest vendor. And in 27 percent of the cases there was only one vendor bidding.

This raises very serious questions about who is conducting reverse auctions, how they are conducted, and for what goods and services they are being used. Despite the fact that reverse auctions accounted for nearly $1 billion in contracts in year 2012, there is no Federal law or regulation that addresses that procurement methods. It seems we are making it up as we go along, and often it seems detrimental to small businesses. While 95 percent of reverse auctions are less than $150,000, the amount of small business act reserves exclusively for small business only reaches 86 percent of reverse auction awards. This has become so problematic that the Small Business Administration's chief counsel for advocacy has requested that the administration at a minimum provide a clear policy statement to the acquisition community that reverse auctions must comply with and the requirements that contracts within this simplified acquisition threshold are to be reserved exclusively for small businesses.

I am hoping our witnesses today will help us understand the scope of the problem and what actions we need to take to ensure that reverse auctions are used in a responsible manner. Our procurement systems should be efficient, transparent, and promote competition. That includes small business.

I continue to believe that part of the solution to our fiscal crisis is finding ways to improve competition, thereby reducing costs. Small businesses are crucial to being part of that solution since their participation increases competition, creates jobs, and encourages innovation. I look forward to your testimony today, and again I thank you for being here. And I yield to the Ranking Member Ms. Kirkpatrick.

[THE PREPARED STATEMENT OF HON. RICHARD HANNA APPEARS IN THE APPENDIX]

OPENING STATEMENT OF HON. ANN KIRKPATRICK

Mrs. KIRKPATRICK. Thank you, Mr. Chairman, for holding this hearing today. And I appreciate your vigilance on the matter that we are examining, the reverse auction process. It is important to provide oversight on programs and processes at the Department of Veterans Affairs to ensure the funding Congress makes available is being spent efficiently and effectively.

I understand that the Government Accountability Office has recently released a report on reverse auctions where they looked at what agencies are buying, how agencies are conducting reverse auctions, and the extent to which the potential benefits of reverse auctions are being maximized. GAO generally found that agencies were not always aware of how fees are paid; agencies do not track the fees; competition and savings are not always maximized; interactive bidding was absent in over one-third of fiscal year 2012 reverse auctions; and there is a general lack of guidance and training on the reverse auction process.

Mr. Chairman, I am concerned with the findings of the GAO. I am sure you would agree that lack of guidance, training, and over-

sight are very common themes that run throughout the majority of the report regardless of what GAO is looking at.

While VA's testimony addresses some of the concerns, I am most interested to hear how they plan to move forward with reverse auctions and ensure that the process is efficient and effective. According to the VA the use of reverse auctions has increased from $78 million in fiscal year 2011 to $305 million in fiscal year 2012. Because of that increase over a short period of time, they need to get this right. Veterans expect VA to do better.

Thank you, Mr. Chairman, for this opportunity, and I yield back the balance of my time.

[THE PREPARED STATEMENT OF HON. ANN KIRKPATRICK APPEARS IN THE APPENDIX]

Mr. HANNA. And I yield to Grace Meng, the Ranking Member of the Small Business Committee.

OPENING STATEMENT OF HON. GRACE MENG

Ms. MENG. Thank you, Mr. Chairman. As the buyer of more than $500 million in goods and services each year, the U.S. government represents a major market for small businesses. For these firms obtaining a Federal contract can take a company to the next level, allowing it to grow stronger in experience and add more employees. By having more options to purchase from agencies can also benefit in terms of quality and price. As a result, it is critical that small businesses are not left behind when it comes to Federal contracts.

Over the years a wide range of initiatives have been enacted to accomplish this. Goals have been established to measure agencies' small business contracting efforts while the SBA operates an array of programs to channel contracts to smaller companies. Among these are initiatives targeted at increasing opportunities for veterans, women, and minorities, which together have helped to direct more than $90 million in total contracting dollars to small firms.

While this sounds like progress, more needs to be done. One such area that needs greater attention and oversight is emerging procurement methods. These techniques, such as multiple award contracts, web-based buying platforms, and strategic sourcing, are becoming more prevalent, and small businesses risk being left out.

Today we are going to explore another such method, reverse auctions, and how agencies are using them, and whether or not they are benefiting the taxpayer and small firms. Reverse auctions seem to focus competitive forces on behalf of the taxpayer. By doing so, prices can be forced lower. Last year agencies reviewed in the GAO report we will be discussing today used this method to procure more than $800 million of goods and services, nearly double their amount from 2008.

However, in part given to the rapid growth concerns have been raised across a wide range of issues, calling into question whether reverse auctions are saving money and providing opportunities for small firms. One such issue was raised during a hearing held earlier this year in this Small Business Subcommittee. By driving prices down these auctions may not be suitable for service contracts, such as construction, which often depend on overall value. Unfortunately service contracts continue to be awarded through

this method, potentially shortchanging taxpayers and causing small contractors to miss out on opportunities.

In its report, GAO has recently brought to light other issues. This includes a finding that more than one-third of auctions had only one bidder. One has to question the need for an auction when there are no competing bidders.

Further concerns were raised that over half of auctions were used to procure items from preexisting contracts. In many cases this caused the government to pay fees, one to use the original contract and another for the reverse auction.

I hope today's auction can shed further light on how these fee structures operate and if agencies are paying more than they should be. In theory reverse auctions have the potential to achieve real savings for the taxpayers, but in practice we are not there yet. A first step would be incorporating regulations in the FAR and issuing government-wide guidance as the GAO has recommended. This could help address many of the concerns that we will hear about today and help ensure that reverse auctions maximize the government's value while allowing small firms to fully participate.

Like other sectors the procurement sector is evolving. Our job today is to oversee this change and make sure that it is not doing more hard than good. I want to thank all of the witnesses who have traveled here today for both their participation and insights into this very important topic.

I would also like to submit a statement on the record from the Quality Construction Alliance.

[The statement of Quality Construction Alliance appears on p.]

Ms. MENG. Thank you, and I yield back.

[THE PREPARED STATEMENT OF HON. GRACE MENG APPEARS IN THE APPENDIX]

Mr. HANNA. Thank you, Ms. Meng. We have two witnesses on our first panel today. Mr. Nigel Cary, President of Cox Construction Company on behalf of the Association of General Contractors. Just quickly, you have five minutes. We will be a little lenient. When you see the yellow light go on you have a minute left. So thank you, you may begin, Mr. Cary.

STATEMENTS OF MR. NIGEL CARY, PRESIDENT, COX CONSTRUCTION COMPANY; AND MR. LOUIS J. CELLI, JR., DIRECTOR, LEGISLATIVE DIVISION, THE AMERICAN LEGION

STATEMENT OF NIGEL CARY

Mr. CARY. Thank you for inviting the Associated General Contractors of America, AGC, of which I am a member, to testify. AGC represents over 25,000 construction contractors, suppliers, and service providers across the Nation.

As you stated, my name is Nigel Cary. I am employed at Cox Construction Company and was President of the firm for 20 years. We are a Federal small business construction contracting firm based in Southern California that specializes in work for government agencies.

Since Cox's founding in 1979 we have been awarded over 150 public projects ranging in size from $25,000 to $30 million. For our work we have won Construction Contractor of the Year awards

from the U.S. Army Corps of Engineers four times. This success begins with the need to submit accurate and complete bids.

Today I will discuss why my company and many other construction companies, both small and large businesses, do not participate in reverse auction procurements. Reverse auctions are a cost only competition suitable for the procurement of established manufactured goods that have little if any variation in their design, manufacture, or use. This definition is confirmed by GSA on their reverse auction Web site. Frequently asked question number one states GSA reverse auction is an efficient and cost effective platform for buying non-complex commodities and simple services.

Construction, however, is a complex service that is project specific and inherently variable. Each contract is subject to unique requirements and conditions. No two construction projects are ever identical in their scope or execution. Thus from the outset construction services do not belong in the intended or stated use of Federal reverse auctions.

Furthermore, contrary to their intended use reverse auctions do not guarantee the lowest price. Each bidder recognizes that they can provide successively lower bids as the auction progresses. As a result, a bidder has no incentive to reveal and subsequently may never offer its best and lowest price.

Reverse auctions create an environment in which bid discipline is critical but difficult to maintain. As prices are lowered a construction contractor could be faced with having to seek better pricing from subcontractors and suppliers for 20 or more components of the project. With smaller staffs and resources, a small business may not be able to keep up with the fast pace of rapidly changing prices and may inadvertently underbid a project.

The risk of pricing and judgment errors in the compressed auction timeframe is huge. For this reason my company, despite over 30 years of experience, will not participate in any reverse auction. Many other construction companies take the same position, that the risk does not justify participating. Thus the government is receiving bids from a reduced number of companies, limiting competition to the detriment of the Federal government and taxpayers.

This should not be news to Federal agencies. Following a 2003 pilot study and report the U.S. Army Corps of Engineers, the largest and most experienced Federal construction agency, does not procure constructions services through reverse auctions.

We find it unfortunate and misguided that each Federal agency learns the mistake of reverse auction procurement for construction on its own. This neither benefits the construction industry, small business, or the American taxpayer. As such, AGC holds that the only solution is for Congress to enact law that prohibits reverse auction procurement of construction services. AGC therefore supports H.R. 2751, the Common Sense Contracting Act of 2013, since this bill would prohibit Federal agencies from using reverse auctions for construction contracts suitable for award to small businesses.

Thank you for this opportunity to provide the views of the construction industry in this important matter.

[THE PREPARED STATEMENT OF NIGEL CARY APPEARS IN THE APPENDIX]

Mr. HANNA. Thank you, sir. Mr. Louis Celli, Director of Legislative Division of the American Legion. Thank you for your service and thank you for being here, sir.

STATEMENT OF LOUIS CELLI, JR.

Mr. CELLI. Thank you. As noted in all the opening remarks the American Legion also recognized that in 2012 more than one-third of the reverse auctions conducted by FedBid had no interactive bidding. Seventy-six percent of all auctions went to the lowest bidder. Government wide, 23 percent of reverse auction contracts were either the same price or more expensive than the established GSA price, and for the Veterans Health Administration that number was as high as 35 percent. In a significant amount of auctions there was only one bid and the agency still had to pay the three percent on top of the cost of the procurement, at a total cost to the government of $4 million for these one off awards which are becoming increasingly of concern to the Federal government.

Chairman Hanna, Chairman Coffman, Ranking Member Kirkpatrick, Ranking Member Meng, and distinguished Members of these Committees, on behalf of Commander Dellinger and the 2.5 million members of the American Legion, I thank you for holding this hearing and thank you for inviting the American Legion to share our views and research with you regarding the government's use of reverse auctions. My complete testimony has been submitted for the record so I will briefly highlight some of our findings for you now.

World War II veterans are known as the Greatest Generation. Not because of what they did during the War, but because of what they were able to accomplish after the War was over when they came home. As these veterans came home there were few jobs and even fewer opportunities. Companies that grew large from war production were impossible to compete with and were winning all post-War government contracts. Which is why Congress introduced the Small Business Act.

The Small Business Act regulates how government interacts with and protects small businesses. Coming off the Great Depression of the thirties, the Small Business Act helped the United States get back on her feet and become the strongest economic superpower on the planet. Reverse auctions are not in the Federal acquisition regulation. They were not part of the Small Business Act. And as a matter of fact, all of the pending legislation considered before this Congress seeks to restrict the use of reverse auctions.

The reasons for this are numerous. Yet the only real argument for using them is to drive down prices. Since small business accounts for almost 90 percent of all reverse auction bidders, it is the small businesses who are suffering the most. Reverse auction advocates claim that reverse auctions save contracting officers time by as much as eight hours per procurement. The American Legion is having a difficult time reconciling those numbers and those claims based on the work that is involved in purchasing a procurement off the GSA schedule with a credit card versus going through the reverse auction process to purchase that same GSA schedule, product, or service.

The American Legion works with hundreds of veteran business owners and has consistently received negative reports regarding the reverse auction process. The most common comment we hear is that the process is unfair, deceptive, and fraught with cheaters. This is not a characterization by the American Legion as to the quality of reverse auction services, it is only offered as a perspective of what the overwhelming opinion is regarding reverse auctions in the veteran community. From our research we found that the number one problem with the reverse auction system is that it poises the Federal government to be a predatory position without highly skilled and highly ethical oversight mechanisms in place to ensure that the government is not being wrongly enriched by creating an overbearing procurement process, then places reverse auctions in a continued recipe for disaster.

Another concern we have is the possibility of misappropriation of slush funded tax dollars. Congress appropriates money for specific purchases based on forecasts submitted by the administration and agencies. If these purchases are then procured below what is appropriated then any saved dollars should immediately be returned to the Treasury and not reprogrammed for wish list items that Congress did not appropriate funds for in the first place. When these processes boast savings, what actually happens to that money? If it does not go back into the Treasury then the American people are not benefiting from those savings and the professed savings are not ever actually realized. The only way to make sure that the process is fair, to guarantee that the Federal government is statutorily prohibited from purchasing goods or services through reverse auction process below what is deemed to be fair market value. It is up to you to protect small business. It is up to you to help this country wrest itself from the greatest economic depression since the 1930's. And it is up to you whether or not you decide to take charge and turn this generation of returning veterans into a generation that the Greatest Generation would be proud of. What are you going to do?

Thank you again for inviting the American Legion to participate in this hearing, and I look forward to answering your questions.

[THE PREPARED STATEMENT OF LOUIS CELLI, JR. APPEARS IN THE APPENDIX]

Mr. HANNA. Thank you. Thank you very much. Mr. Celli, thank you. What I get from both of your testimonies is basically there is no purpose, no good purpose in reverse auctions. We had somehow assumed that it might work with items that are commonplace, that are more or less commodities. But even with what you just said, even in that case, just to reiterate, we found that even items that there was a price listed, that oftentimes we are paying more than that in the reverse auction process. And in fact, just so I can hear it twice, we are actually paying a fee to do that, to accompany. That is your understanding, too?

Mr. CELLI. That is correct. In the extremely limited circumstances under which reverse auctions might be appropriate, is it worth supporting an entire procurement system based on those few circumstances?

Mr. HANNA. I understand. And is there an overall benefit? And you think not?

Mr. CELLI. We think not.

Mr. HANNA. Mr. Cary, what you said was very clear to me, having been in construction for 30 years myself. But in your case, I mean it is effectively, if I could sum it up, you view this as a race to the bottom in terms of the way the process unfolds because there are so many elements to bidding on a construction process that you simply cannot click away at a computer and lower your own price. You wind up with perhaps the least qualified, that company that is most desperate, or looking for cash flow, or whatever it is. The time and the way the whole process engages, contractors, you are not able to get, almost by definition, you are unable to get a qualified response every time there is a new bid. Do you want to speak to that, if you consider that accurate?

Mr. CARY. Yes, that would be accurate. You know, the way the construction industry works, as a general contractor we are reliant on a large number of subcontractors and suppliers who have to provide pricing for every project, project specific pricing. To be trying to reach out to, and I picked a number of 20, suppliers or subcontractors, you know, even on a small job, it is just virtually impossible. Because they are all going to start at their highest price. They are not going to give you their best price straight out knowing that they have an opportunity to get more than their best price.

Mr. HANNA. So this is kind of an example of something that looks good, sort of smells okay, but just in the real world it is not practical?

Mr. CARY. Exactly. In the real world this would not work and is just not practical.

Mr. HANNA. Mm-hmm. You may have subcontractors of 20 or 30 different trades, electricians, plumbers, whatever they are, and they are not sitting in that room with you lowering your price to compete with someone from another state, perhaps another country, I do not know, probably not, who may not know what they are doing. Or may not be——

Mr. CARY. That is correct. So the opportunity for making mistakes, or for somebody to, you know, underbid a project on the false pretense that, well, Company A can do it so I can do it for $1,000 less.

Mr. HANNA. So there can be a fundamental disconnect between value, outcome, and the process?

Mr. CARY. Well the reverse auction process totally ignores value, which is where most Federal procurement is now looking at, is best value procurement. Which is a combination of price and prior experience, or specific experience that you bring to the table for that project. Reverse auction process would completely ignore that.

Mr. HANNA. I am going to yield to Ranking Member Kirkpatrick. Thank you.

Mrs. KIRKPATRICK. Thank you, Mr. Chairman. Mr. Cary, it is clear that you do not think the reverse auction process should be used for construction. Do you see a place for it in other procurement process outside of construction?

Mr. CARY. I thought I did until I started reading these reports, yes. I really cannot speak to that. I am only familiar with the con-

struction industry and our processes. And yes, certainly on the face of it it seems like a great idea. But as I read the reports that have been put out here, there is a lot of problems. And I think it was probably time to put a hold on this process until it can be thought through and really managed properly if it is to continue.

Mrs. KIRKPATRICK. I am curious about a statement in your written testimony. On page five you say that the process is detrimental to the relationship between the buyer and the supplier. Can you elaborate a little bit on that? What you see happening there?

Mr. CARY. Yes. That is referring back to the best value proposition of construction. Where, you know, federally, on the Federal side and pretty much exclusively in the private sector a construction contract is awarded on the basis of best value, where the contractor brings his services, his team, his experience as well as his price. And it may not necessarily be the best price that provides the best value to the customer, in this case the government agency who is buying that service.

Mrs. KIRKPATRICK. When did you first interact with the VISN, with the VA Integrated Services Division? And can you describe what your experience was with them?

Mr. CARY. I am speaking for AGC, yeah.

Mrs. KIRKPATRICK. Yes.

Mr. CARY. We have not been able to really interact with the VISN. We are talking to their headquarters of procurement for the VA here in Washington, and they are receptive to talking to us, and we are trying to arrange a meeting with them in January to follow up. But it is unclear to us at this point how much control they have over the VISNs and whether their policy would get down to that level or those regional offices.

Mrs. KIRKPATRICK. Okay, thank you.

Mr. CARY. We hope to resolve that.

Mrs. KIRKPATRICK. Okay, thank you. Thank you. I hope you will keep the Committee posted on that progress. Mr. Celli, does the American Legion have an official position on reverse auction process?

Mr. CELLI. While we do not have a specific resolution that specifically addresses reverse auctions, we do have a position with regard to the way veteran contractors are treated in the marketplace, which completely covers the scope and dynamic aspect of reverse auctions, in which we are opposed.

Mrs. KIRKPATRICK. Would it be possible for you to provide that to the Committee?

Mr. CELLI. It is mentioned in my written testimony and there is a link in my testimony which will take you right to that as well.

Mrs. KIRKPATRICK. Okay. To that process?

Mr. CELLI. But I can send a copy over as well.

Mrs. KIRKPATRICK. Okay. Thank you. You know, the VA has suspended the use of the reverse auction process. What do you think is the best next step for the VA to take?

Mr. CELLI. Me?

Mrs. KIRKPATRICK. Yes, Mr. Celli, yes.

Mr. CELLI. No problem. Well just suspending the process to begin with is the right step to take. If they do plan to reinstitute the reverse auction process I think there is an extremely large amount

of oversight that needs to happen. And it needs to be done with a focus on being fair to the small business and not being in an overbearing manner, squeezing them down to their last dime. And it also needs to reflect upon established pricing models that are already accepted throughout GSA.

Mrs. KIRKPATRICK. Would your opinion about reverse auctions change if as Ranking Member Meng talked about there was a standard or something put in the FAR that would give guidance on how they are to be used?

Mr. CELLI. You know, I just think that we are putting too much effort behind a procurement vehicle that really is not necessary. I think that GSA was primarily established to provide the best possible price to the government and fair market value. So if you already have that program in place, what would be the need then to institute yet another tool to try to accomplish that same goal? And in addition use the GSA vehicle as a means to use that new tool? It does not really make a lot of sense.

Mrs. KIRKPATRICK. Okay. I thank the panel for being here and I yield back.

Mr. HANNA. I yield to Chairman Coffman.

Mr. COFFMAN. Thank you, Mr. Chairman. And I just want to thank you for your leadership on this issue, Mr. Chairman, and Ranking Member as well from both the Small Business Committee as well as the Veterans' Committee. Mr. Cary, how has the fact that OFPP has not provided any guidance on reverse auctions affected how they are implemented?

Mr. CARY. We see that as a big problem. Because agencies as you get down regionally, you know, to the smaller levels are going out, seeing no guidance on this, and really nothing from stopping them to do it, using reverse auctions in situations where they are just not appropriate, and for complex services that they do not fit the definition of reverse auctions to begin with and they create something that is very difficult for people to propose on and compete in.

Mr. COFFMAN. Do you think that in terms of VA's procurement is there anything that they do in terms of procurement that would fit this current reverse auction system?

Mr. CARY. Speaking outside my expertise, I would assume simply procurement of materials, supplies would fit. But again, that is not my expertise. So I am looking at that from the outside thinking that that is what would work.

Mr. COFFMAN. Okay. Mr. Celli, how does the Legion's Small Business Task Force view reverse auctions?

Mr. CELLI. Overwhelmingly the American Legion Small Business Task Force is against small auctions and extreme——

Mr. COFFMAN. Reverse auctions?

Mr. CELLI. Reverse auctions, sorry. And extremely distraught by them. Overwhelmingly, without fail. We could not find one business owner who thought that reverse auctions, even business owners that are in our Small Business Task Force that have been successful using them do not think that they are a good use of their time, their effort, their money, or a good value for the government.

Mr. COFFMAN. Okay. Thank you, Mr. Chairman. I yield back.

Mr. HANNA. I yield to Ms. Meng.

Ms. MENG. Thank you. Mr. Cary, each construction offers its own unique set of factors that will help determine the cost of each project. For example, a company constructing a building in my district in New York will not face the same conditions as a firm that has a project in Florida. Do you believe that the reverse auction process allows the agencies to consider the variables that construction projects face?

Mr. CARY. No, we do not. Again, being purely price based it does not take into consideration the experience of the company proposing and the team that it would bring to that project. And those are really vital components in the award of an overall best value award for any construction project.

Ms. MENG. Thank you. Mr. Celli, with the unemployment rate still hovering around seven percent, it is vital that we use tool that spur job creation. In your testimony you discuss concern that reverse auctions will lead to decreased employment opportunities for veterans. Can you please explain why this would occur?

Mr. CELLI. We would be happy to. The reverse auction process is probably perfect for that single entrepreneur sitting in the basement in front of a computer passing goods and services from the distributor directly to the Federal government. That does not promote any type of overhead. So the businesses that thrive are the businesses that are able to hire more personnel, hire more veterans, and grow their businesses to such a degree that they can offer a greater scope of products. So if the government is going to continue to try to beat small businesses down to their last dollar the result is not going to be small business growth. It is going to be decline and therefore they are going to hire less veterans.

Ms. MENG. What are some examples or procurement methods you believe would allow small businesses to grow and hire more veterans?

Mr. CELLI. You know, the procurement processes that are in place. And make no mistake about it, there is no simple way to procure goods and services for the Federal government. You know, it is an extremely legally difficult process. But those businesses that are able to get through those hurdles to get a GSA schedule, to successfully bid on a project, those are businesses that have been proven that they have a strong business and a good handle on the procurement process and an understanding of the way the laws of the Federal government work, specifically with regard to the Federal Acquisition Regulation. So you know, the Federal government already has some very successful tools that they are using. We have not found the reverse auction process promotes that. As a matter of fact what it does is it then opens up competition to businesses that have not been tested, that have not been through that process. And it possibly opens up the Federal government to businesses that cannot perform.

Ms. MENG. In your opinion what is the number one challenge and example of problems that your members are personally facing when it comes to the process?

Mr. CELLI. The reverse auction process?

Ms. MENG. Yes.

Mr. CELLI. Specifically that the reverse auction process can when it is a common item drive the final winning price to below market

value, and in many cases to below the actual cost of the item for that vendor. That is the single most, the single largest complaint that we receive and the single largest challenge. And we see that in many cases disrupting the relationship between the distributor and the manufacturer. If it is an open competition and I am a distributor for XYZ Corp. and I am an authorized reseller, I buy it from the manufacturer at $10, I have to sell it at at least $10.01 in order to make a profit. But if the manufacturer is able to compete in that same process they can easily sell it for $9.99, at which point I cannot even compete. And if I do, if I compete at the thought process that I am going to use this as loss leader just to get some government attention and maybe sell consumables that support that product later at a higher price, it really becomes a shell game.

Ms. MENG. Thank you. I yield back.

Mr. HANNA. I yield to Mr. Roe.

Mr. ROE. I thank the Chairman for yielding. I apologize for being a couple of minutes late. We got some bad intel and started off in the Rayburn Building this morning hunting for this meeting, so I apologize for that. And Mr. Chairman, I would like to submit for the record the statement of the National Electrical Contractors Association, if I could.

Mr. HANNA. Without objection.

Mr. ROE. I thank the Chairman.

[The statement of National Electrical Contractors Association appears on p.]

Mr. ROE. Let me I guess help understand for me a little bit better. I love Ebay. And I am trying to understand, and I love buying guitars. So I will bid on some guitars and sometimes you will see one out there that the price is not right and you will get no bids. And what I am trying to figure out, and I do understand there are products out there that you purchase that have almost no margin, I get that, and that is a tough business to be in when you are in a very low margin business. And I guess what I am trying to understand is, in FedBid the concept I like because it allows you to find the, as you pointed out, the best product at the lowest price which is what we should be trying to do. But it is not working. A third of the bids, when I read the material this morning, only are a single source bidder, just one bidder. And Ebay you can turn down if you do not meet a certain value, and I am trying to understand what we can do. If you do not hit the price that the seller is willing to sell it for, I mean, obviously you could buy a $4,000 guitar for $2, I would buy as many of them as I could get. But the seller is going to say, "This is worth that, and I am not selling it below that." Is that something you could do in FedBid?

And just for you all, Mr. Cary you also, how, why is this not working? Because my instincts tell me, shoot, it works phenomenal on Ebay. You can find out around the world what something is worth. You can get the value of it. It might not be what the seller thinks the value is worth but what the market will pay for that particular item. Why is that not working?

Mr. CELLI. Well Dr. Roe, I think that you brought up an excellent analogy. And Ebay, if you remember, those of us who were around when Ebay first started, it became almost a fever to bid.

And at the beginning of Ebay what you ended up with was a lot of folks who overbid for products that they ended up overspending for because they got involved in that emotional fever bid. So——

Mr. ROE. I have a wife, though. And that usually reduces that fever a little bit.

Mr. CELLI. There are, you know, Ebay has over the years now become a much more commonplace to purchase new and used goods. But with Ebay there are safeguards in place because the seller, as you mentioned, can start a bid at a particular price, or mention that they will not go below a certain price. And with the reverse auction process that same, it is new, it looks like a window of opportunity for businesses that were not previously in the Federal procurement arena. They may not completely understand what their responsibilities are once they win that procurement. There, as Mr. Cary points out, the more complex procurements are much more difficult to put into the reverse auction process because there are far more nuances that may need to be discussed before the winning bid is selected. And if you were buying only ballpoint pens it might be easier, but then there is already a mechanism to do that.

Mr. ROE. Is the sealed, what I am familiar with as a public official, as a local official, is the sealed bid process. Where you go in, you see what the specification, just like in the contracting business, Mr. Cary I know you are. You see the specifications in any particular, whether you are building a bridge or a building or whatever. And the lowest bidder who meets those specifications wins the bid. And you do, as you all have pointed out, you do learn who the good people are. Pretty soon you figure out who the good people are, and the people who meet those specifications time after time after time. And I have not necessarily always accepted the lowest bid, but the best bid. So sometimes the lowest bid, I mean, you know, the old adage would you like to go into space on the lowest bid? I think a lot of times we do not do that and we do it for a reason, because our experience tells us that the lowest bid may not be the best bid. Is that a process that could work? Where you just have a sealed bid, Friday afternoon at 1:00, you open the bids, the lowest bidder that meets the specifications gets the contract?

Mr. CARY. That would be the traditional way of procuring construction services, yes. It has worked for years. Today it has evolved more to best value. Most agencies are now using best value, where it is either a combination of your price and your experience for the project, or technically acceptable low price. Where the bidders are in a word screened, if they reach a certain technical bar then those bids are considered and the low price of the bidders who were deemed above that bar is accepted. Those work very well. Agencies use them. You know, over the last ten to 20 years litigation in construction has vastly decreased. And I think the government is receiving a lot better value for its construction today than it used to. So there are established processes that work, yes.

Mr. ROE. Okay, thank you. I yield back.

Mr. HANNA. Ms. Chu?

Ms. CHU. Yes, thank you. Mr. Cary, you talked about specific examples of where the reverse auction does not work. In particular types of contracts where it just does not come down to a simple commodity, commercial item, or maintenance. You talked about the

VA Northern California Healthcare Systems and the Carl Vinson VA Medical Center in Dublin, Georgia. Could you elaborate on those examples to show how it does not work?

Mr. CARY. Yes, certainly. You know, not having bid on the projects I cannot get into all the details. But looking at the description and knowing what is involved in a construction project, those were clearly major projects, renovations in existing, working hospital facilities, that require a large number of services provided by subcontractors and suppliers. Technically complex procurements where the experience of the proposers, you know, needs to be considered alongside the price. You do not want the low price coming in, as was stated, building a rocket to go to the moon. You know, you are going to look at the experience of that contractor. You want someone who is familiar with infectious disease control, safety requirements inside a working medical facility. There is a lot more to it than just the low price.

Ms. CHU. In fact you said for the VA medical center it was supposed to be a simple repair or alteration of structure but it was a complete roof replacement.

Mr. CARY. There is a big problem that I did not mention in my oral testimony today of misinterpretation, yes. And this, when you look at the GSA schedule also they have a Schedule 56 that allows some construction services. The big problem is that when you get down to the regional or the local level, those services can be easily misinterpreted and expanded to what is really a full on construction project, not a simple supply or service.

Ms. CHU. Right. Mr. Celli, you did a survey of your members regarding reverse auctions and they were overwhelmingly negative. Can you say who participated in the survey and what was the overwhelming kind of specific thing that they had to say?

Mr. CELLI. I can. I do not have the names right here in front of me but I can certainly provide that to your staff afterward because the businesses have agreed to share their stories with you, so we are happy to do that. And with all the members, as a matter of fact.

Overwhelmingly again, you know, there is a huge mistrust in the system. They do not know who they are bidding against or if they are even bidding against a person. We find out later that the FedBid system in particular is specifically designed in such a way that it can be programmed to bid against nobody. It can be programmed by the buyer to automatically lower the bid until it gets to a certain level, which is a little big disingenuous in the bid process. There are some other concerns about legal bidders, bidders who are providing gray market products versus authentic products. So there are a lot of question within the community about the legitimacy of the bid process.

Ms. CHU. You also had some recommendations for government if it is going to continue to use reverse auctions. What are some of those recommendations?

Mr. CELLI. Well first and foremost there needs to be a safety mechanism in place that does not allow government to purchase an item or a service below market value. There is really no justification for that. It is a slippery slope for a small business to get into. They may be willing to risk it at the cost or in the hopes that they

will ultimately get more business from the Federal government later, but it is not a good practice for the Federal government to prey on small businesses in that way. So the first safeguard I would say is to make sure that good market research is being conducted to establish what the minimal acceptable price would be. The other would be to just completely get rid of the leader lag indicators, as mentioned by Mr. Cary a few minutes ago, almost as a sealed bid process. If that is going to be your bid, then that is your bid. And professionals who are in this arena know what they can afford to bid and that is what their bid is going to be. More outreach training, I think that if they do plan to continue this more outreach training for small businesses I think is critical. And collect the fees directly from the buyer, not the seller. That is another disingenuous practice. When you tack three percent onto the final price from the buyer, show the buyer a three percent increased price, deliver those funds then to the small business when it is the buyer's responsibility to pay that fee and then go to collect that three percent from the small business. Why does a small business have to be burdened with paying the fees of the buyer if it is the buyer's responsibility to pay the fees?

Ms. CHU. Thank you. I yield back.

Mr. HANNA. Mr. Bentivolio?

Mr. BENTIVOLIO. Thank you, Mr. Chairman. I am going over this and it, you know, I represent a constituency that likes to pay less. They want spending cuts. And it seems to me that a way to do it is take the lowest bidder. And market value really is based on the market. If the market is willing to sell it at one price, I am willing to buy it at that price, that creates the market, right? Do we agree?

Mr. CELLI. No, I actually do not agree. Not necessarily.

Mr. BENTIVOLIO. Okay.

Mr. CELLI. And the reason that I disagree is because when you throw outliers into the equation you then distort and warp what the true market value actually for most people when you have one or two that are willing to subvert their own pricing structures simply to get into the market. And again, it poises the Federal government as a more overbearing monopolistic type of buyer. And that is not the responsibility of government.

Mr. BENTIVOLIO. Okay. And I understand and I agree with you. So how does, Mr. Cary, can you elaborate on how the private sector deals with this? Because they want to maximize profits, but at the same time they also want performance, right?

Mr. CARY. Yes.

Mr. BENTIVOLIO. And that is the big question. Because in my district, you know, I have people who are, they can build a better product, or the same product, meeting government regulations or specifications, but are not necessarily getting the contract. And then it is that contract in some cases is going to the lowest bidder, who cannot perform. And subsequently comes back to the original bidder that can make the product at a fair price and make a fair profit, and the government now has to pay more for it because they have to expedite and pay a, what do you want to call it? Extra fee for having it done in quicker time. So how does the private sector deal with those kind of issues?

Mr. CARY. Well actually addressing the Federal side of it on the construction business, again, the established procurement methods of best value or technical acceptable low price screen the contractors who are bidding on the project and take those factors into consideration. There are other factors, their experience, their capabilities for this project, their likelihood of success. One of the screens that the Corps of Engineers and the Navy both frequently use is called your likelihood of success, and where they rank those contractors. They then either weigh that with the price or put those contractors into a pool of acceptable contractors and take the low price.

But again to your other point, the contractors also present their best price one time. You are not hedging that against where other people are pricing their product. You get those best prices the first time around. And the government knows it has got the best prices. Under the reverse auction process we do not see where that best price is necessarily ever reached.

Mr. BENTIVOLIO. Because they keep underbidding? Do I understand——

Mr. CARY. Or they never bid down to the best price. The opposite problem of what seems to be happening more on the manufactured goods side of the table, in construction everybody is going to give you the price they would love to get so they can retire next year. But, and if nobody else comes down to the price that they could really do it for, you know, and make a fair small profit, they are going to take it for the higher price.

Mr. BENTIVOLIO. Very good. Thank you.

Mr. CARY. Does that make sense? We see often, and it has been related to me by companies who have participated in reverse auctions, that their winning bid or their winning price was not the price that they would have bid it if it had been a sealed bid. It was higher because the price never came down to their best price.

Mr. BENTIVOLIO. Very good. Thank you very much, I appreciate it. I yield back.

Mr. CARY. Sorry for the long explanation.

Mr. BENTIVOLIO. No, that's fine. Great. You did great. Thanks.

Mr. HANNA. Thank you both. If there are no other questions for this panel, I want to thank you for your time and your testimony and for traveling such long distances. And I invite our second panel to be seated.

Thank you. We will hear in a moment from Ms. Michelle Mackin, Director, Acquisition and Sourcing Management, Government Accountability Office; Mr. William Sisk, Deputy Commissioner, Federal Acquisition Service, General Services Administration; and Mr. Major Clark, Assistance Chief Counsel for Procurement Policy, Office of Advocacy, Small Business Administration. Ms. Mackin, you may begin.

STATEMENTS OF MS. MICHELLE MACKIN, DIRECTOR, ACQUISITION AND SOURCING MANAGEMENT, GOVERNMENT ACCOUNTABILITY OFFICE; MR. WILLIAM SISK, DEPUTY COMMISSIONER, FEDERAL ACQUISITION SERVICE, GENERAL SERVICES ADMINISTRATION; AND MR. MAJOR L. CLARK, III, ASSISTANT CHIEF COUNSEL FOR PROCUREMENT, OFFICE OF ADVOCACY, SMALL BUSINESS ADMINISTRATION

STATEMENT OF MICHELLE MACKIN

Ms. MACKIN. Chairmen Coffman and Hanna, Ranking Members Kirkpatrick and Meng, and Members of the Subcommittees, thank you for having me here this morning to discuss reverse auctions. My statement today is based on a report we issued just two days ago and our work focused on the four agencies that had about 70 percent of the reverse auction activity in 2012. These were the Departments of Veterans Affairs, Homeland Security, the Interior, and the Army.

First I would like to discuss trends. And you will see from the chart that clearly trends are on the rise here.

[Chart.]

Ms. MACKIN. Over the past five years there has been 175 percent increase in use of reverse auctions for these four agencies, with over $800 million in contract awards in 2012. In general reverse auctions are used for simpler supplies and services, predominantly IT and medical products and equipment. Importantly, however, some agencies are planning to use reverse auctions for more complex items and more complex contracts that can last up to five years.

Secondly, I will address some areas of confusion we found regarding how reverse auctions work. There is a perception that the auctions always go to the lowest bidder. But we found that almost a quarter of the 2012 auctions did not go to the lowest bidder. Another concern we had was about the extent to which small businesses are getting reverse auction awards. And we found that most of the contracts did go to small businesses. They received over 80 percent of the dollars in 2012.

And then regarding fees. A company called FedBid ran almost all of the government reverse auctions in 2012. FedBid's fee for conducting the auctions is capped at three percent of the winning bid and it cannot exceed $10,000. As you will see in the chart as an example of how the fee works, in this case the winning vendor's lowest bid was $10,000. FedBid added its three percent fee and the government paid the final contract award price that included the fee. The vendor then remits the fee back to FedBid.

In some cases we found that FedBid received no fee and this happened about 20 percent of the time for the 2012 auctions. We also found cases where agencies are paying two sets of fees, one to FedBid to conduct the auction and another to use an existing contract such a GSA or VA schedule contract. But our main source of concern was that agencies were simply not aware of the fees they are paying to use these auctions.

And finally I would like to turn to the two key intents of reverse auctions, competition and savings. Regarding competition we found two main buckets. What we call interactive bidding where multiple

vendors are bidding against one another and this happened about 65 percent of the time. However, there is also what we call ineffective competition where only one vendor submitted a bid or multiple vendors submitted only one bid each. This happened about 35 percent of the time and clearly there are concerns here about if the benefits of competition are being realized.

And finally FedBid calculates the savings for the agencies based on the delta between the government's cost estimate, or the target price, and the final contract price, which of course includes FedBid's fee. In this example the agency's target price or government estimate was $11,000 and the calculated savings on this particular auction was $185 after accounting for FedBid's fee. In total FedBid calculated $98 million in savings for the four agencies in 2012 but we have questions about the accuracy of these savings. For example, if there was no interactive bidding perhaps agencies could have gotten a better price using other mechanisms. Also the target price or government estimate may not be sound. For example, we found over 1,000 cases where the winning bid actually exceeded the government's estimate even with interactive bidding.

In conclusion, as we discuss in our report we believe government-wide guidance and regulations are needed to help ensure that reverse auctions achieve the intended benefits. We made recommendations along these lines to the Office of Federal Procurement Policy and they did agree with the recommendations. Mr. Chairmen, Ranking Members, this concludes my statement and I would be happy to answer any questions.

[THE PREPARED STATEMENT OF MICHELLE MACKIN APPEARS IN THE APPENDIX]

Mr. HANNA. Thank you. Mr. Sisk, you may begin.

STATEMENT OF WILLIAM SISK

Mr. SISK. Good morning Chairman Coffman, Chairman Hanna, Ranking Member Kirkpatrick, Ranking Member Meng, and Members of the Subcommittees for Veterans' Affairs Oversight and Investigations and Small Business Contracting and Workforce, my name is Bill Sisk and I am the Deputy Commissioner of the General Services Administration's Federal Acquisition Service. I appreciate the opportunity to appear here today to discuss GSA's recently launched reverse auction platform. This effort is one of a continuing series of actions that the Federal Acquisition Service has undertaken in support of GSA's mission to deliver the best value in acquisition and technology services to government and the American people.

Based on data since its inception, GSA's reverse auction platform is one tool that with proper training and use can provide savings to agencies, help them achieve small business goals, and provide visibility into spending data that over time can help agencies make better acquisition decisions. GSA's reverse auction platform was put into operation July 1, 2013 and is designed to be an efficient and cost effective platform for buying non-complex commodities and simple services. This initiative's focus is to drive down the total cost of acquisitions and increase savings to customers and taxpayers.

GSA's reverse auction platform is an e-tool available to our government partners to use to facilitate the requests for and submission of quotes or offers for products and services through GSA multiple award schedules and blanket purchase agreements, or BPAs, Veterans Administration schedules, and Department of Navy BPAs against GSA schedule contracts. GSA leveraged existing eBuy and GSA auctions.gov IT infrastructure resources, which reduced development costs and provides users a familiar look and feel when using the reverse auction Web site. The GSA reverse auction tool is non-mandatory and available to agencies to consider as they develop acquisition strategies.

Additionally, by leveraging GSA schedule contracts and their unique ability to provide a broader array of vendors and small business set aside capability, GSA's reverse auction platform improves the government's ability to maintain small business participation through broad competitions and set asides to promote agencies' meeting small business goals in a cost effective way.

There are a variety of potential benefits to agencies of this platform, including that it displays realtime pricing, provides customers with level three spend data or historical pricing data, interfaces with existing systems to verify that contracts are still valid under the GSA multiple award schedules program, assist in meeting small business goals, and facilitates compliance with competition requirements. While agencies may realize these benefits, it is also important that the reverse auction platform be used appropriately. GSA provides training on the reverse auction platform regularly to both the buyer and vendor communities. GSA offers on average four training sessions per week in a variety of forums. To date over 50 sessions have been conducted and over 2,000 individuals trained on the platform. Additionally, frequently asked questions and answers are available on the site as a resource for users.

The data so far has demonstrated savings in price, good competition from vendors, and support for small businesses. To date, several Federal agencies, including GSA, have utilized the platform for 485 auctions, realizing about 6.7 percent savings on average, with an average of three vendors participating per auction. 85.53 percent of the total awards and 87.18 percent of the total value of all contracts have been made to small businesses.

As the GSA reverse auction platform continues to mature and evolve with more training and education provided, GSA predicts an increase in the use of the platform based on the initial interest in the platform and the overall interest by agencies in using reverse auction procurement solutions. Additionally we predict future spend data may provide insight for potential strategic sourcing opportunities. As we move forward we welcome insights from Congress, from industry, and from other partners, Federal agencies, on additional ways to improve the platform and ensure it is used appropriately. During this time of continued budget uncertainty and ongoing fiscal pressure, GSA has launched the reverse auction platform in the hopes that it will be used by our partners to maximize savings in terms of both driving competition among vendors to achieve cost savings and by cutting processing times so that agencies can achieve resource savings as well. This tool is one offering

by GSA to deliver better value and savings to our partners and ultimately the American taxpayer.

Thank you again for the opportunity to testify and I am happy to answer any questions you may have.

[THE PREPARED STATEMENT OF WILLIAM SISK APPEARS IN THE APPENDIX]

Mr. HANNA. Thank you, Mr. Sisk. Major Clark?

STATEMENT OF MAJOR L. CLARK, III

Mr. CLARK. Good morning, Chairman Hanna, Ranking Member Meng, Members of the Small Business Contracting and Workforce Subcommittee, as well as Chairman Coffman and Ranking Kirkpatrick and Members of the Veterans' Affairs Subcommittee on Oversight and Investigations. I am honored to be here today to present testimony to you on behalf of the Office of Advocacy of the U.S. Small Business Administration, more specifically on behalf of Chief Counsel Dr. Winslow Sargeant. Dr. Sargeant would like me to thank you for the support that you have provided this office and looks forward to a continued partnership with you as we mutually strive to improve the economic climate for our small business stakeholders.

Let me make it very clear that the Office of Advocacy is not in opposition to reverse auctions in the Federal marketplace. Today we are advocating for clear reverse auction guidance from the Office of Federal Procurement Policy.

Mr. Chairman, my name is Major Clark. I am the Assistant Chief Counsel for Procurement Policy for the Office of Advocacy. And while my professional career includes both public and private sector experience, I previously served as the staff director for the House Small Business Committee under the chairmanship of the Hon. Parren J. Mitchell of Maryland. So thank you for having me back for this session.

I ask that this written testimony and two attachments be included as part of the official transcript of this hearing.

Just as a brief segue, in 1976 Congress created the Office of Advocacy pursuant to Public Law 94–305 to represent the views of small entities. Advocacy advances the interests and concerns of small businesses before you, the Congress, the White House, Federal agencies, Federal courts, and policy makers. The Office of Advocacy is an independent office within the Small Business Administration. So the views expressed by our office do not necessarily reflect the views of SBA or the administration. We work with Federal agencies in the rule making process to implement the requirements of the Regulatory Flexibility Act. The RFA requires Federal agencies to consider the effects of their proposed rules on small businesses and other small entities, including small governments and small nonprofits. And it is really pursuant to the above statutory authority that the Office of Advocacy has been involved in the monitoring of reverse auction activities in the Federal marketplace since 2006.

There are actually two letters that I asked to be included as part of the written testimony. The first one is on February 27, 2008 the Office of Advocacy sent a letter to Administrator Denett of the Of-

fice of Federal Procurement Policy with the recommendation from small stakeholders to better define the reverse auction process. And again, I ask that that attachment be included as part of the record for this proceeding.

The second attachment is a more recent letter to Administrator Lesley Field of the Office of Federal Procurement Policy dated January 21, 2012 and this letter is from Dr. Sargeant of the Office of Advocacy. And again this letter expresses the concerns as conveyed to us regarding some of the negative impacts of reverse auctions on small businesses and asking that the Office of Federal Procurement Policy come out with clearer more defined guidelines so that our small business stakeholders would clearly be able to understand the process as they attempt to play in the Federal acquisition marketplace.

Now in addition to those two letters, the Office of Advocacy held a procurement round table in Seattle, Washington in which a small business stakeholder very vividly expressed to us the problems she experienced with the reverse auction process. And some of those things are stated in the testimony. And in addition to that we also have been part of a process with the Office of Federal Procurement Policy in which small business stakeholders have presented their concerns to this office. So we are concerned with clear guidance. We think the guidance should clearly place a definition on what constitutes reverse auction. We think the guidance should also include a very clear understanding of how FAR Part 19 applies to these particular parts. And we also think that the guidance should include a very clear understanding of the cost parameters that small businesses incur with this particular process. And these are the concerns that have been expressed to us by our small business stakeholders.

Mr. Chairman, this concludes the testimony. I would be happy to answer any questions that you may have.

[THE PREPARED STATEMENT OF MAJOR L. CLARK, III APPEARS IN THE APPENDIX]

Mr. HANNA. Thank you. Without objection everything you mentioned will be added to the record.

Ms. Mackin, in your testimony you mention that non-complex procurements, assuming for the moment that that might be a construction contract or something like that, do not necessarily work well. Would you like to elaborate on that? Because as you know that is what we heard from the previous testimony.

Ms. MACKIN. Actually it is the, a lot of what we found that was bought in 2012 was IT products, specific types of medical equipment and so forth. And traditionally that has kind of been considered appropriate, if you will, for a reverse auction. I did look at our data and for VA specifically about five percent of their reverse auction activity was for construction related contracts in 2012. And as you know there is a whole range of codes that can relate to construction. So from alterations, and so forth, to perhaps more complex items.

Mr. HANNA. Well actually I mentioned that wrong, incorrectly. It is complex do not work well, but thank you for answering the question. Do you, FedBid earned $13.4 million in fees in 2012 for re-

verse auction work by the four agencies GAO reviewed. I understand that GAO found cases where agencies were paid fees even though there were no savings. Clearly FedBid, you could argue, did their work. But what about that and the fact that there are many cases where they actually paid more than the posted or GAO quoted price? How can you rationalize that? And why do averages matter, as Mr. Sisk said when you get three or four bidders, when we know that there was only one bidder, there may have been only one bidder on a whole host of projects, hundreds as we know. And so averages do not, are not really relevant in my mind. I guess the question is how do you justify paying three percent out when you actually end up paying more at the end, and do you?

Ms. MACKIN. Frankly we have concerns about some of these scenarios. If agencies paid FedBid's fee but got no savings from that particular reverse auction, that is a concern. And the scenario where that happens is for example the agency contracting officer establishes the government estimate for example, picks a schedule price for a certain vendor. That vendor submits a bid and actually gives the government a discount. But that discount is eaten away because the agency still pays FedBid's three percent fee. So that is not a good situation in our view.

The other main concern we would have is the one bid scenarios, which happened, as was mentioned, over a third of the time. In those cases we really think going straight to the schedules or using other mechanisms would probably result in a better price.

Mr. HANNA. Mm-hmm. So you would agree with Major Clark that rules that, rules need to be much better defined, or defined at all in this case?

Ms. MACKIN. Absolutely. We think there need to be cross references in the FAR so contracting officers know how to use these reverse auctions. And so the vendor community can be clear as well about how they should be working.

Mr. HANNA. I think we are about to put a slide up. Thank you.

[Slide.]

Mr. HANNA. This is the Web site. It shows that FedBid is a contracting office of the Department of the Army. It is confusing at best, but we can all agree that that is not accurate? This is from Fed Biz Ops. So maybe it is just a technical thing that needs to be corrected but clearly it is not part of the Department of the Army.

Ms. MACKIN. It is not part of the Department of the Army.

Mr. HANNA. You may want to look at that. I am going to yield to Ranking Member Fitzpatrick, thank you.

Mrs. KIRKPATRICK. Kirkpatrick.

Mr. HANNA. Kirkpatrick.

Mrs. KIRKPATRICK. Thank you. Ms. Mackin, you heard Mr. Cary in the first panel say that he did not think that reverse auctions were appropriate for construction services. But you say that they were only used five percent of the time. Can you tell the Committee what your opinion would be going forward in terms of using reverse auctions for construction services?

Ms. MACKIN. I think it really goes back to the requirements, which of course come from the buying agency. And this I believe would not apply only to construction but for anything that could be

considered more complex. If the requirements are not clearly stated and represented to the vendor community you cannot be sure you are going to get what you paid for. I know there is a lot of concern about construction per se, and maybe that is something that OFPP could address when they issue the guidance that we have recommended.

Mrs. KIRKPATRICK. It seems that getting the target price is really essential to the savings. What recommendations do you have about what would fine tune that process so we can get a better target price?

Ms. MACKIN. Well as I mentioned the target price is the contracting officer's government cost estimate. And you know, it is not just the reverse auction issue. This is more of a general contracting concern we see in a lot of our work across the Federal government, is how sound is the market research? How robust is the market research? If they are just contacting one vendor and getting a quote and using that as the target price, that may not be adequate depending on what is being procured.

Mrs. KIRKPATRICK. Do you think guidelines addressing the target price should be included in whatever guidelines are generated to improve the reverse auction process?

Ms. MACKIN. I think that would be very helpful. And you know, probably the main concern I would have is what do you do when you only get one bid in a reverse auction? Do you proceed as we saw and just award the contract at that price? Or do you maybe reconsider that maybe a reverse auction is not the best bet here for various reasons?

Mrs. KIRKPATRICK. I have a concern that in your testimony that the agencies are not tracking this process. What needs to be put in place so that they can track? Why is that happening?

Ms. MACKIN. Yes, we were frankly a bit surprised to find that agencies did not know how much they were paying FedBid in fees. They did not know much in duplicative fees, for lack of a better word, they were paying when they were using a schedule contract, for example, through a reverse auction. And so some agencies, and VA is one of them, have taken steps to get that information. So now on a case by case situation contracting officers at VA are documenting how much they paid in fees. And sometimes it is a loss, if you will, when the target price is exceeded. But at least they are getting that information. I do not think any agency, however, is looking at it from a macro point of view, in total how much are we paying to use reverse auctions and is it always the best way to go?

Mrs. KIRKPATRICK. So maybe that is also something that should be put into the guidelines. We saw that they were doing that at the macro level. Would you agree with that?

Ms. MACKIN. Yes, absolutely.

Mrs. KIRKPATRICK. Now if you had to prioritize your top three next steps for the Committee, what would that be?

Ms. MACKIN. Well I think, you know, the key thing here is putting something into the FAR, and obviously the VAR, and all the different agency regulations. And OFPP has taken some steps to do so over the past ten years, but it has never actually materialized into the regulation. So I think that is critical.

But even before that happens, because that could take some time, some government wide guidance, best practices, when does this make sense, when does it not make sense, I think would be very helpful. Each agency has guidance but they are not always the same and I think that is part of the concern from the vendor community.

Mrs. KIRKPATRICK. Major Clark, would you agree with Ms. Mackin's top priorities in terms of making this process better?

Mr. CLARK. In general, I would agree. I am not necessarily sure at this point in time as to whether or not the guidance needs to actually be put into the FAR. I do think that the Office of Federal Procurement Policy needs to come out with some very clear guide points, guidelines for the acquisition community. I am still not totally convinced that they need to be put into the FAR at this point because the whole process of reverse auction as an acquisition tool is continuing to evolve. Much of the testimony here this morning, including the very recent GAO report, as well as the testimony from GSA, clearly indicates to me that there is this evolution which has been occurring since 2006, when we first got involved in the Office of Advocacy. So I am not totally convinced that it needs to be put into the FAR at this point in time. But clearly yes, I agree that there needs to be clear guidelines coming out of Office Federal Procurement Policy.

Mrs. KIRKPATRICK. Thank you, panel, for answering my questions. And I yield back.

Mr. HANNA. Thank you. Chairman Coffman?

Mr. COFFMAN. Thank you, Mr. Chairman. I want to ask you all to comment on this. It seems to me maybe under the narrowest of circumstances the reverse auction process would work. But I remember when I was State Treasurer for Colorado and I initiated a program where I would sell these tax and revenue anticipation notes, and you know, we would do it electronically, and everybody could see the bid process as it was ongoing, the window that it would be open. And so the objective was clearly to get the lowest rate we could in those for the benefit of the taxpayers of Colorado. But that was, I mean, it was so simple that, you know, there were no variables other than the interest rate. But the amount of money was the amount of money that we were going to put out in these tax and revenue anticipation notes.

And so here you have a lot of variables in terms of certainly you know what the quantity is but there's a lot of qualitative measures. How do you account for those in a reverse auction process? Ms. Mackin, why do we not start with you?

Ms. MACKIN. Well I think again it goes back to the agency contracting officer. They are really the lynchpin to making sure this works properly. And so in their solicitation, in their requirements which are then posted on the reverse auction site, they need to make those variables very clear. And if it does not seem appropriate for a reverse auction because it does seem like it is getting too complex, maybe they need to reconsider. That is one concern we have. Some agencies are perhaps not mandating use but strongly encouraging reverse auctions to be used. And I think it needs to be more considered depending on what is being procured.

Mr. COFFMAN. Yes?

Mr. SISK. Ultimately I think it is up to the warranted contracting officer that makes the decision. Our objective at GSA is to provide an e-tool that gives them the option for commodities and very simple services to go out to the vendor community that is available through multiple award schedules to get the best price for the taxpayers. But ultimately it is up to the warranted contracting officer to make the decision.

Mr. COFFMAN. Mr. Clark?

Mr. CLARK. I would agree that it is up to the warranted contracting officer to make that decision. I would however continue to place a caveat that that decision has to be couched within the context of the existing FAR and statutory provisions that deal with small business. And again, I am specifically referring to FAR Part 19 that deals with awarding and reserving contracts for small businesses at certain dollar thresholds. And I would hope that the warranted contracting officer would actually take this into consideration when that decision is being made. But that is the benchmark of everything as we see it, and that is, you know, how are they complying with the various small business provisions?

Mr. COFFMAN. Okay. Ms. Mackin, on March 5, 2012, FedBid informed O and I that they trained, they had trained 2,100 VHA contracting personnel in the use of reverse auctions. In lieu of OFPP's lack of guidance, does this concern GAO?

Ms. MACKIN. We did hear from different agencies that FedBid was doing training, and that that did increase in the fourth quarter when of course spending tends to go up. It depends on what the training was. If it is just the mechanics of how to use this reverse auction tool, that is one thing. But I think that, again to avoid crossing into that inherently governmental realm, the agency contracting officer needs to be completely in charge of writing the solicitation, determining the pool of vendors that will compete for the reverse auction, and making the final award determination.

Mr. COFFMAN. Ms. Mackin, according to VHA Health News article a government employee brought the reverse auction process, "with her when she transferred to VA from another agency." According to her, "it is free to the government. Everybody wins." Is that an accurate statement?

Ms. MACKIN. I would not characterize it as free to the government. As was discussed in some cases the government is paying a fee and not getting any savings as a result. So again, it really goes back to the government agencies tracking this information and knowing what they are paying and what the cost benefits are of using this tool.

Mr. COFFMAN. Thank you, Mr. Chairman. I yield back.

Mr. HANNA. Thank you. Ms. Chu? Meng? I'm sorry.

Ms. MENG. Thank you. A question for Mr. Sisk, GSA schedule contracts are negotiated with the intent of achieving the contractor's most favored customer pricing, the vendor's best possible price for the goods or services. However, schedule holders routinely offer lower prices than their contract price when competing in reverse auctions. How are vendors allowed to offer conflicting prices?

Mr. SISK. Well the multiple award schedule price that has been determined to be fair and reasonable, you can always negotiate

down from there. And so that is permissible within the multiple awards schedule program, for vendors to offer a cheaper price.

Ms. MENG. Do you think it should raise a red flag as to the ability of the vendors to fulfill a requirement when their bid is below the most favored customer pricing?

Mr. SISK. Our mission is to always get the best price that we can for the government. Sometimes vendors get a better price from their distributor. Sometimes they have been able to lower their overhead. And so the schedules price that is established when we negotiate that contract initially is that the price is fair and reasonable to put sort of a ceiling price in place. But again, if we have competition amongst the schedules holders and we can get a better price for the government, then that is our goal.

Ms. MENG. And your agency recently unveiled its own system for conducting reverse auctions. There are those that have voiced concerns about the current systems out there and the ability of vendors to use them. How does it compare to those that are available through private sector contractors?

Mr. SISK. A couple of things that are a little bit different about our program. First, it is run by a government agency so we have government contracting officers looking at what is available through that program. It is also based on the platforms that we have available for our E–Buy system, which is a system for government contracting officers to go out and get quotes from schedule holders. So they can use their same sign in information to get into our reverse auctions platform as well. So it is another tool that is available for them. In addition to that we also have visibility over all the prices paid through the system and so we hope that that information can help us educate government contracting officers in a better way going forward to get the best price for the taxpayers.

Ms. MENG. Mr. Clark, in recent legislation Congress added a type of bid listing protection in limited circumstances for subcontractors who are used by prime contractors in their bid proposal. What the language does, it requires that the name subcontractor cannot be replaced with the contracting officer's approval. And if it does happen subcontractor's who are replaced without cause can now complain to the contracting officer. Do you agree that it would be good to implement major subcontractor bid listings for all Federal contracts if it would protect subcontractors from post-award substitution without cause?

Mr. CLARK. Would you mind repeating that for me, please?

Ms. MENG. Do you agree that it would be helpful to implement major subcontractor bid listings for all Federal contracts if it would protect subcontractors from post-award substitutions without cause?

Mr. CLARK. The answer to your question is yes, the Office of Advocacy has over a period of years expressed concern with the process in which small business subcontractors have had to endure in the Federal marketplace. So if this provision actually provides that level of protection, just one more level of protection that our small businesses need, that type of protection is much needed.

Ms. MENG. Thank you. I yield back.

Mr. HANNA. Dr. Roe?

Mr. ROE. I thank the Chairman for yielding. And also, I failed to mention thank you for holding this hearing today. Also, just a couple of quick questions. One, do you think that the FedBid reverse auction should continue in its current form? And if not, what would you replace it with?

Ms. MACKIN. I guess from our point of view there is not a problem per se with how FedBid is conducting these auctions. The issue is really with how the government agencies are using them and what information they have, and more importantly do not have, about competition, about the fees they are paying, and about what is appropriate to go through an auction.

Mr. ROE. I think the, and Ms. Mackin I am going to stay with you for just a second, and Mr. Sisk, I want him to chime in also on that question. But I think you made a very important point and so did Mr. Clark about the simplicity. In other words if you are bidding out, with my medical background, tape, IV solutions, gauze, you know, those kinds of things, splints, whatever, that's pretty simple stuff. I mean, you know what it is, you know you have got to have it, and you want to get the lowest price. It makes absolute sense. But when you are bidding out complex, like a construction project, that seems an inappropriate use to, for me, for a reverse, let me give you just an example of what happened yesterday with the VA. And the question is why would the VA award a contract for autopsy services December 10th on a reverse auction. I mean, I do not guess at that point it matters to the patient but it might to the information you get that you get the best, most qualified person. To me that is a very complex problem to deal with, would you agree with that?

Ms. MACKIN. I would agree it sounds complex. I would just add that 90 percent of the auctions in 2012 were for products, but ten percent were for services. And I think when you get into the realm of services it can get complex fairly quickly.

Mr. ROE. I think maybe that is something, and I think basically Mr. Clark pointed out the parameters should be really narrow. And I think Mr. Sisk also what you have done, is you have some very narrow parameters in what you are using reverse auction for. But I can certainly see where it would work. But when you then expand it to something as complex as an autopsy, that does not seem appropriate to me. Mr. Sisk?

Mr. SISK. Thank you. Certainly when we set up or tool it was envisioned to be for commodities and for very simple services, for multiple award schedule vendors to compete for the business. And we set the system up with our existing resources based, you know, funded out of our industrial funding fee. But it is for, you know, commodities and very simple services, yes.

Mr. ROE. I yield back, Mr. Chairman.

Mr. HANNA. Thank you. Thank you for your testimony today. I appreciate your time and energy, and the travel, although most of your are local folks, I assume. And I invite Mr. Coffman to take his place as Chairman, and he will introduce the third panel.

Mr. COFFMAN. [Presiding.] I thank the panel for stepping forward. On this panel is Mr. Jan Frye, Deputy Assistant Secretary, Office of Acquisition and Logistics, Department of Veterans Affairs. Mr. Frye is accompanied today by Mr. Philip Matkovsky, Assistant

Deputy Under Secretary for Health for Administrative Operations, Veterans Health Administration. Mr. Frye, you are now recognized for five minutes.

STATEMENT OF MR. JAN FRYE, DEPUTY ASSISTANT SECRETARY, OFFICE OF ACQUISITIONS AND LOGISTICS, DEPARTMENT OF VETERANS' AFFAIRS; ACCOMPANIED BY MR. PHILIP MATKOVSKY, ASSISTANT DEPUTY UNDER SECRETARY FOR HEALTH FOR ADMINISTRATION OPERATIONS, VETERANS HEALTH ADMINISTRATION

STATEMENT OF JAN FRYE

Mr. FRYE. Good morning, Chairman Coffman, Chairman Hanna, Ranking Member Kirkpatrick, and Ranking Member Meng, and distinguished Members of the Committees, we are pleased to appear here this morning to discuss VA's process for establishing and maintaining accountability in its use of reverse auctions. I am accompanied today by Mr. Philip Matkovsky, Assistant Deputy Under Secretary for Health for Administrative Operations.

Reverse auctions currently represent less than five percent of VA's simplified acquisition transactions. VA supports the use of reverse auction tools when appropriate. When used properly they can result in both time and dollar savings, benefiting both the department and the American taxpayers.

As the senior procurement executive I have policy and oversight responsibilities for the department's procurement activities. My office has issued policy outlining appropriate use of reverse auction tools and performed compliance reviews on reverse auction transactions. Since VA's procurement activities operate under a decentralized organization structure, implementation and executive of reverse auctions falls to the heads of contracting activities for the various administrations and staff offices.

VHA's HCA has also conducted oversight reviews of reverse auction transactions, which resulted in similar findings to those performed by my office. The non-compliant issues identified in these reviews are the same as those found when reviewing other contracting methods.

With a few years of experience behind us and the data associated with these transactions available for analysis, VA is evaluating the value proposing of reverse auctions. Specifically VHA is crunching the numbers in an effort to evaluate whether the dollar, time, and process efficiencies estimated by the advocates of these tools are being realized. Efficiencies alone cannot be the only measure of value. The reverse auction process is also being evaluated to ensure compliance with regulation and policy.

VA is aware of the concerns voiced by some small businesses about reverse auction service providers. Meeting small business goals are a priority for the department. This is evidence in the results. In fiscal year 2012 VA conducted 7,587 reverse auctions representing approximately $305 million in total dollar volume. Seventy-nine percent of that total went to small businesses. The department has exceeded goals for small businesses since fiscal year 2010 with the total reaching from 35 to 37 percent of total obliga-

tions. In fiscal year 2013 alone over $6.5 billion was committed to small business.

VA continues to monitor the efficacy of reverse auctions and adjust our policies and processes to be in line with the results of our reviews and business outcomes. Through this monitoring process VA will refine its use of reverse auctions and enable it to identify when to use it more effectively. As a result of these actions VA established and is maintaining a culture of accountability with regard to the reverse auction process.

I appreciate the opportunity to testify today and I am happy to answer any questions the Committee may have.

[THE PREPARED STATEMENT OF JAN FRYE APPEARS IN THE APPENDIX]

Mr. COFFMAN. Thank you, Mr. Frye. Mr. Matkovsky, are you and VHA required to follow the reverse auction policies and guidance released by Jan Frye as VA's senior procurement executive?

Mr. MATKOVSKY. Yes sir, we are.

Mr. COFFMAN. Okay. Mr. Matkovsky, the employee who brought the reverse auction process to VA stated in an email that VA pays nothing for reverse auctions. But, "a fee of up to three percent is paid by the firm winning the bid and is included in their bid price." Now does that not indicate that up to three percent will be added to the contract and therefore VA pays up to three percent for the use of reverse auctions?

Mr. MATKOVSKY. I think it is a two-part answer, sir, if I may. The annual fee we pay to the firm that hosts that reverse auctions is $1. The reverse auction process itself, as I understand it, the bidders will have a published price. Contained in that price is the fee to the reverse auction contractor. So when in effect we find that final price it contains the fee. To say that we do not pay a price for that is technically inaccurate. The price for that reverse auction is built into the price we see.

Mr. COFFMAN. All right. Mr. Frye, did anyone ever bother to validate reverse auctions when they were introduced to VA?

Mr. FRYE. Could you repeat that again? I am sorry.

Mr. COFFMAN. Did anyone ever bother to validate reverse auctions when they were introduced to VA?

Mr. FRYE. With regard to prices paid, savings?

Mr. COFFMAN. Savings.

Mr. FRYE. One of the things that we noticed in 2012 when we put a moratorium in place, in March of 2012 to be exact, was that the prices that were touted as savings, or the savings values, were being provided by the reverse auction firm, FedBid. We did not think that was probably the way to go and so one of the things that we required as we put a new policy in place and promulgated that policy was that for VA or specifically VHA contracting officers were then required to calculate the savings and to document the file with regard to those savings.

Mr. COFFMAN. Okay. Why does VHA not take advantage of reverse auctions conducted by VA, like those of the technology acquisition center?

Mr. FRYE. Well first of all, Chairman, the technology acquisition center has run very few reverse auctions. They have run several and the reports that I have received are that they have saved some

money, there have been some cost avoidances. But they have done it on a very small basis, very small scale. VHA made the conscious decision to use a third-party provider. They could have gone another route but it was their decision to use a third-party provider to assist them instead of running in house reverse auctions.

Mr. COFFMAN. So Mr. Matkovsky, let me refer back to you again, to explain to me why you went with FedBid? It does not make sense.

Mr. MATKOVSKY. At the time we did not have another alternative, and believe a competitive procurement was initiated. There were four invitations to submit, I think there were two bidders, and there were a couple of different models available at the time. One of them was a purchase outright of the licenses and would involve a large capital expense on the front end. Another alternative, as Mr. Frye alludes, would be to have an in house capability to set up that infrastructure. We did not have that at the time in VA. And then there was software as a service, which was the offer from FedBid. It offered very small capital outlays, one dollar. And effectively you are using a service that is hosted externally. It appeared risk averse at the time.

Mr. COFFMAN. Three percent seems excessive, at this point.

Mr. MATKOVSKY. Correct. So that is one of the things I think has been alluded. We have done an internal review again, based on some of the internal reviews, we saw the GAO report. And one of the things we looked at was can we quantify the nature of the return, and does that three percent make it unattractive for us to use this? And until we can feel comfortable with that, we have asked to pause these. There are some existing procurements that will be completed. We have asked to add no new ones to our reverse auction process.

Mr. COFFMAN. Mr. Hanna?

Mr. HANNA. So FedBid, no one bids against FedBid, they are out there three percent, you either hire them or you do not. And Mr. Frye, it seems patently obvious, what you said is that it does not necessarily make sense. And that you may not always earn their money and you may not always need them, if that is fair.

You have heard the testimony up to this point from everyone. Most of it has been fairly negative overall. Do you believe either of you that you are capable of doing what was done through Fedbid on your own, by yourselves?

Mr. FRYE. Well I think we are. Maybe not at the scale that FedBid is able to offer. If we were to do it at the scale that is currently being used, for instance by VHA, we would have to build that capability within our workforce. But it could be done. It would not be done at no cost at all. There would be some overhead cost, and there would be some stand up cost, and perhaps some costs for software licensing and that type of thing. But it could certainly be done and it could be scaled, but it would cost something to scale it.

Mr. HANNA. And you are using them currently for construction services?

Mr. MATKOVSKY. Before I answer the question sir, Mr. Chairman, on the construction, on additional item. We use reverse auctions with the General Services Administration as well for our en-

ergy procurements. So natural gas, electricity, etcetera, we use other than FedBid for some of our reverse auction purchases. I just wanted to clarify that.

For construction we use them for what we consider our local, not complex construction services. Those would be typically roof repair, replacement of flooring, etcetera. But not where you would consider a design/build contract for a stand alone facility, for an operating room, or something of that sort.

Mr. HANNA. So for commodities, oil, gas, electricity, it works okay for you, even with the three percent you say. And for simple, basic construction repair, maintenance, those kinds of things, it has worked okay for you?

Mr. MATKOVSKY. Reasonably okay. I mean, the few examples we have, we have a starting price that we estimated a target of roughly $700,000. Starting bids came in at over $1 million, and the final award price was under $250,000.

I would actually agree with some of the prior testimony and feedback from some of the panel. That you want to make sure that you have a pool of qualified contractors for construction. And in some areas where we have used it, it has been where you have a multiple award contract already in place, so you have taken care of the technical competency and you are using the auction process to drive down price.

Mr. HANNA. And have you seen circumstances where you have one or none——

Mr. MATKOVSKY. We have.

Mr. HANNA. And how do you approach that? What do you say when you see a single bidder on a project that you may know there are many providers that did not apply through this program?

Mr. MATKOVSKY. Well even in the case of some of the utility contracts, we will see a single bidder come in, but the price per unit of energy that we are purchasing is lower than our initial estimate. And we find it to be nonetheless a fair and reasonable price.

Mr. HANNA. Do you feel comfortable rejecting a price that you think is not fair and reasonable if there is only a single bidder?

Mr. MATKOVSKY. I believe the contracting officer is comfortable rejecting the price if they get a single and only one bidder. If they are starting sometimes from an existing contract, they may know the schedule price and see the reduction in the as quoted price.

Mr. HANNA. And so part of the take away of what I hear from you is that in complex cases it is not practical? Unless maybe as you said you have an existing overriding general contractor or something like that?

Mr. MATKOVSKY. Personal opinion, as a general rule, I think that this is less appropriate for highly complex technical proposals where you have to do considerable trade off analyses.

Mr. HANNA. Thank you. I yield back.

Mr. COFFMAN. Ranking Member Ann Kirkpatrick, Arizona?

Mrs. KIRKPATRICK. Thank you, Mr. Chairman. Thank you, Mr. Frye, for your testimony and your appearance today before the Committee. My first line of inquiry is back to construction. I know that has only been five percent of your use of the reverse auctions. But it appears to me there was a significant use increase from fiscal year 2011 to fiscal year 2012. Can you explain that increase?

Mr. FRYE. Actually, I will defer to Mr. Matkovsky on that since it is an operational question.

Mrs. KIRKPATRICK. Okay.

Mr. MATKOVSKY. It had only started in fiscal year 2011 as a pilot process. And then in fiscal year 2012, it had extended use into most of our operating locations. That is really the driver behind that change.

Mrs. KIRKPATRICK. You heard our first panel. Mr. Cary said that he does not think that reverse auctions should be used at all in procuring construction services. Would you agree with that?

Mr. MATKOVSKY. Once again, I think that if you are able to establish the technical competency of the bidder pool, and it is for lower complexity items, I think it can make sense. I would agree with Mr. Cary, that for higher complexity, major construction projects, it does not make sense. Price, lowest price, technically acceptable, is not the evaluation factor you want to apply to a major complex construction project.

Mrs. KIRKPATRICK. Thank you. And back to you, Mr. Frye. What prompted the 2012 moratorium on the use of the reverse auctions? Was that an internal decision?

Mr. FRYE. That was an internal decision. There were a number of issues. Perhaps you have seen the issues that I enumerated in my memo to the procurement workforce. Amongst those were perturbations in our supply chain. We have a supply chain in the VA. The underlying principle is a just in time system. This just in time system is supported by large strategic contracts. Using open market contracts, in this thousands of them, is perpendicular to that system. We want to continue to use, and as a matter of fact we have been directed by the Secretary, to expand the use of these large strategic contracts. So that was one of the factors that prompted us to put a moratorium in place and halt so that we could recalibrate. There were other issues as well. Frankly, and I think it was brought up today in some of the testimony, we really want to look at our suppliers. We want the best and brightest to serve the VA. We serve veterans. We provide health care. And we want the best suppliers there. Naturally we want the best value, we want a good price. We do not want to beat our suppliers down to the point where they cannot sustain low margins. And we were getting some input from a number of suppliers, especially small businesses, telling us that we were beating them down to the point where they could not make an appropriate profit. I do not believe that there are many firms that will survive in the long run if they do not operate where marginal cost equals marginal revenue. In other words, I do not think there are firms out there that are going to offer a price below their break even point and stay in business. So I am not sure that happened. But we did hear on many occasions that we were effectively beating them down. And for that reason some of our better suppliers were departing and did not wish to serve the VA. So that was a concern as well.

Mrs. KIRKPATRICK. Thank you very much, and I yield back.

Mr. COFFMAN. Thank you. Congresswoman Meng?

Ms. MENG. Thank you. When setting a target price in a reverse auction contracting officers base the number on the government's cost estimate or market research. Are purchases made through the

reverse auction process being used to set market research pricing standards for future purchases of like items? If so, how does that conflict with schedule holders of similar items?

Mr. FRYE. Well let me make sure, and I think I understand your question. It is absolutely incumbent upon the contracting officer working with the requiring activity, the organization that needs the product, to develop a target price or an independent government estimate. And that independent government estimate is of course critical when you purport savings. And in many cases we find that we have faulty independent government estimates. That is a function of time in many cases. The requiring activity or the contracting officer in many cases are rushed to get requirements in place and probably do not do, as a matter of fact do not do in many cases, a sufficient job in developing the government's estimate. I think in the future we have to get better at that. We have been working in that not only in the VA but across the government for many, many years. You will see in non-complex buys, buys for commodities, that we sometimes do not hit the mark for the independent government. And you will see in complex buys we often do not hit the mark for the independent government estimate. So someone said earlier in testimony here that the independent government estimate is the key because that is the baseline we use to declare whether we have saved any money or not. So if we have got a faulty baseline, our declared savings are not accurate.

Ms. MENG. And in general the lack of guidance in the reverse auction process has caused some to question the fairness of the system. Vendors are especially concerned with the fact that even after they go through the process the contracting officer is not required to select the lowest bidder for award. How are your agencies ensuring that the process is fair and transparent?

Mr. FRYE. I would respond to that by saying that the contracting officer is always responsible for source selection, except in major, high dollar programs. But in everything we do using reverse auctions the contracting officer is the source selection authority. They are required to determine the winner. They are required to declare a fair and reasonable price. They are declared to document the file accordingly. So I have heard these allegations that this third party, in this case FedBid, was actually awarding the contracts. That is not the case because the contracting officer is the person who executes the contract, signs the face of the contract, and obligates the government.

Ms. MENG. Thank you. I yield back.

Mr. COFFMAN. Thank you. Our thanks to the panel. You are now excused. I would like to recognize Chairman Hanna for his closing remarks.

Mr. HANNA. Thank you, Chairman Coffman, and thank you to all our witnesses today. As we have heard, the way reverse auctions are currently structured does not promote competition as we intend and would like within the Federal procurement area. My bill, H.R. 2751, takes a critical step to solve some of these unfair competitive issues. I look forward to working with my colleagues on the Veterans' Affairs Committee on ways to further develop and expand this bill. And again, I thank you all for being here, and yield back.

Mr. COFFMAN. Thank you, Mr. Hanna. It is important to note that this hearing was the product of a lengthy investigation into the inappropriate use of reverse auctions by Federal agencies. We referred to a reverse auction provider named FedBid throughout the hearing due to its use by many Federal agencies and repeated reference in the GAO report. But our focus was entirely on problems within the government, not with the operations of a private contractor.

VA has begun reconsidering the circumstances in which it conducts reverse auctions. In March, 2012 Jan Frye, VA Deputy Assistant Secretary for the Office of Acquisition and Logistics, suspended all use of FedBid due to a "groundswell of complaints from VA suppliers, at least one protest potentially increased cost, small business programs anomalies, and violations of our VA contract hierarchy." The suspension in 2012 lasted only one month because use of reverse auctions was reinstated due to significant political pressure. We have been notified today that VA's use of reverse auctions again has been suspended.

Clearly the use of reverse auctions is a matter of procurement policy sorely in need of additional guidance. GAO has made recommendations in this regard, and OMB has indicated agreement. However, follow through is necessary. Unfortunately given VA's persistent failure to independently validate the use of reverse auctions, I hope that VA does not do anything to make matters worse.

I ask unanimous consent that all Members have five legislative days to revise and extend their remarks and include extraneous material. Without objection, so ordered.

I would like to once again thank all of our witnesses and audience members for joining in today's conversation. With that, this meeting is adjourned.

[Whereupon, at 12:10 p.m., the Subcommittees were adjourned.]

APPENDIX

Prepared Statement of Hon. Mike Coffman, Chairman

Good morning. I would like to welcome everyone to today's joint hearing titled "Contracting Away Accountability – Reverse Auctions in Federal Agency Acquisitions."

I am pleased to host Chairman Richard Hanna and his fellow Members of the Subcommittee on Contracting and Workforce for the House Committee on Small Business, for this joint hearing.

Reverse auctions are a contracting process used by the Federal government since the late 1990s theoretically to promote competition in the acquisition of goods and services. In a reverse auction, a buyer solicits bids from multiple sellers, in contrast to a standard auction where a seller solicits bids from multiple bidders.

Over the course of a two year investigation by my Subcommittee, it became readily apparent that the use of reverse auctions by the VA has been problematic casting doubt on the extent of competition and the claims of cost savings. In a report issued two days ago, the Government Accountability Office (GAO) substantiated deficiencies with reverse auctions as used by VA. The House Committee on Small Business Subcommittee on Contracting and Workforce has similar issues more broadly with reverse auctions as a procurement method at other Federal agencies.

It is important to note that this hearing is the product of a lengthy investigation into the inappropriate use of reverse auctions by Federal agencies. We will refer to a reverse auction provider named FedBid throughout the hearing due to its use by many Federal agencies and repeated reference in the GAO report, but our focus will be entirely on problems within the government, not with the operations of a private contractor.

VA's sole reverse auction contractor is FedBid. In choosing FedBid to conduct its reverse auctions, VA did not solicit offers from any other contractors, contradicting the spirit of the Competition in Contracting Act of 1984, which requires that agencies fully compete contracts except in limited circumstances. Of the $828 million in Federal agency reverse auctions awarded in FY2012, GAO reported that 99% were conducted by the same contractor, FedBid, and VA awarded the greatest dollar value of these – over $200 million.

VA has signed three contracts with FedBid, each contract containing an action obligation of just one dollar. FedBid's real compensation comes from the fee (up to 3 percent) it adds onto the final award price of vendor contracts. Accordingly, some advocates have concluded from this arrangement that FedBid's service is free to the government. However, it is obvious that when FedBid's fee is tacked onto the final award price of a contract, the seller is effectively passing on the fee to the government.

Of the $1.7 billion in Federal and commercial auctions conducted by FedBid in FY2013, FedBid claims to have saved its customers $159 million – savings of about 8.5 percent, including fees. GAO has cautioned that all information related to fees and savings is provided by FedBid itself. According to FedBid, it calculates its savings against the government's estimated target price. Unfortunately, this calculation assumes the government is thoroughly researching its cost estimates, when for commercial items, the government frequently just reviews list prices. As such, for commercial items, simply relying on published list prices is unlikely to result in the best price since volume discounts are frequently available. Significantly, until April 2012, VA did not attempt any independent assessment of those savings, although guidance issued by VA now requires independent confirmation.

In theory, reverse auctions are intended to promote competition. However, in practice, this competition is too often absent. According to GAO, in FY2012, over one-third of reverse auctions conducted by FedBid for Federal agencies had no interactive bidding, where vendors engage in multiple rounds of bidding against each other to drive prices lower. In 27 percent of auctions, there was only one bidder. Further, in eight percent there were multiple bidders but only one round of offers.

Agencies paid $3.9 million in fees for these procurement services. Perhaps even more problematic is the fact that for over 3,600 reverse auctions, $1.7 million in fees was paid even though only one offer was received from one bidder – thus the government paid extra to award a sole source contract.

Another issue raised is whether VA contract specialists have delegated inherently governmental functions to FedBid. According to the FAR, an action should be undertaken only by a Federal employee if it could "[b]ind the United States to take or not to take some action by contract," "[d]etermine, protect, and advance United States . . . interests by contract management," or "[e]xert ultimate control over the acquisition, use, or disposition" of property or funds. While FedBid does not itself award contracts, it is in a position of exerting significant influence on who gets the award. For example, some vendors have complained that when they have posed a question to a VA contract specialist, they are being refused and referred to FedBid instead. In this regard, it is also significant that FedBid keeps independent past performance records on vendors which it shares with the government, including information regarding the creditworthiness of vendors, but does not share this information with the vendors. In some cases, it appears that the only function of the VA contractor is to sign off on an actual award.

VA has begun reconsidering the circumstances in which it conducts reverse auction. In fact, in March 2012, Jan Frye, VA Deputy Assistant Secretary for the Office of Acquisitions and Logistics, suspended all use of FedBid due to a "'ground swell' of complaints from VA suppliers, . . . at least one protest, potential increased costs, small-business program anomalies, and 'violations of our VA contract hierarchy." The suspension in 2012 lasted only one month, because use of reverse auctions was reinstated due to significant political pressure. We have just been notified that VA's use of reverse auctions again has been suspended.

Clearly, the use of reverse auctions is a matter of procurement policy sorely in need of additional guidance. GAO has made recommendations in this regard that OMB has indicated agreement. However, follow through is necessary.

Two additional points should be included. Reverse auctions may be appropriate for best price but not best value contract awards. Second, the Army Corps of Engineers has repeatedly found the use of reverse auctions for construction-related contracts and services to be improper. Given the VA's horrible track record with regard to major construction projects, I wholeheartedly agree that VA should not do anything to make matters worse.

Prepared Statement of Nigel Cary

Chairmen Coffman and Hanna, Ranking Members Kirkpatrick and Meng, and members of the Subcommittees, thank you for inviting the Associated General Contractors of America (AGC) to testify on federal agency use of reverse auctions to procure construction services. AGC represents over 25,000 construction contractors, suppliers and service providers across the nation.

My name is Nigel Cary. I have been a member of AGC for over 30 years and currently serve as vice-chair of the Federal & Heavy Construction Division. I have worked at Cox Construction Co., since 1981 and was president of the firm from 1991 to 2011. We are a federal small business construction contracting firm based in San Diego County, California that specializes in work for government agencies. Since the Cox Construction's founding in 1979, we have constructed over 150 public projects, ranging in size from $25 thousand to $30 million. Cox Construction has bid or proposed on hundreds of projects for federal agencies and completed projects for the U.S. Army Corps of Engineers (USACE), Naval Facilities Engineering Command (NAVFAC), the Air Force Civil Engineer Center (AFCEC), and United States Postal Service (USPS), among others. For our work, we have won Contractor of the Year accolades from USACE four times—in 1991, 1998, 2007 and 2008.

Today, I will discuss:

I. Why my company and many other construction companies—both small and non-small businesses—**do not participate in reverse auction procurements;**

II. Why the U.S. Army Corps of Engineers—the largest and most experienced federal construction agency—**no longer procures construction services through reverse auctions;**

III. How the Department of Veterans Affairs and General Services Administration, among other agencies, continue to use and to push reverse auctions for construction services; and

IV. Why Congress should enact measures prohibiting reverse auctions for federal construction services contracts, like H.R. 2751, the Commonsense Contracting Act of 2013.

I. The Problems with Reverse Auctions for Construction Services Contracts and How Reverse Auctions Limit Competition

AGC strongly supports full and open competition for contracts necessary to construct improvements to real property. This includes competition among general contractors, specialty contractors, suppliers and service providers. Over the years, it has been established that such competition energizes and improves the construction industry to the benefit of the industry and the nation as a whole, especially taxpayers. As Congress considers the changing the federal procurement landscape, we offer the following points for consideration during your evaluation of reverse auctions.

a. *Reverse Auctions Do Not Provide Benefits Comparable to Currently Recognized Selection Procedures for Construction Contractors*

Vendors promoting online reverse auctions are selling technology for which there may be legitimate economic justifications for some types of procurements. However, those vendors have yet to present persuasive evidence that reverse auctions will generate real savings in the procurement of construction or will provide benefits of "best value" comparable to currently recognized selection procedures for construction contractors, which have been carefully and specifically tailored for all types of construction. Manufactured goods are commodities subject to little or no variability or change in manufacture or application. In comparison, construction services are project-specific and inherently variable. Each construction services contract is subject to the unique demands of the project, including: the geography—including but not limited to site conditions, the seasonality of certain construction activities, project proximity to major suppliers, and site ingress and egress in conjunction with other landowners—the needs, requirements, personnel and budgetary criteria of the owner, specific and unique design features, construction requirements and parameters, and the composition of the project team.

Federal procurement laws recognize that construction stands apart from commodities or manufactured goods. AGC contends that vendors that promote reverse auctions for construction services misuse a procurement process originally designed for commodities. It ignores the unique nature of construction. Construction contractors, specialty contractors, subcontractors and suppliers offer and provide a mix of services, materials and systems. They do not "manufacture" buildings, highways, or other facilities. In fact, the construction process is fundamentally different from the manufacturing process.

b. *Reverse Auctions Do Not Guarantee Lowest Price*

In the context of construction, AGC believes that most of the claims of savings are unproven and that reverse auction processes may not lower the ultimate cost of construction. For example, "winning" bids may simply be an established increment below the second lowest bid not the lowest responsible and responsive price. Moreover, in reverse auctions, each bidder recognizes that he or she will have the option to provide successively lower bids as the auction progresses. As a result, a bidder has no incentive to offer its best price and subsequently may never offer its lowest price—as opposed to during low price technically acceptable procurements and other contracting approaches. In addition, savings from reverse auctions can be one time occurrences.

c. *Reverse Auctions May Encourage Imprudent Bidding*

Reverse auctions create an environment in which bid discipline is critical yet difficult to maintain. The competitors have to deal with multiple rounds of bidding, all in quick succession.

The process may move too quickly for competitors to accurately reassess either their costs or the way they would actually do the work. If competitors act rashly and bid imprudently, the results may be detrimental to everyone, including the owner. There are even reported cases in which owners actually step in to keep an overzealous supplier from obtaining an order that would potentially jeopardized the business viability of the supplier. Absent such steps, imprudent bidding may lead to performance and financial problems for owners and successful bidders, which may have the effect of increasing the ultimate cost of construction as well as the cost of operating and maintaining the facility.

During reverse auctions, small construction businesses are most likely to fall victim to such imprudent bidding and experience the greatest harm. Small construc-

tion businesses have less cash flow and reduced ability to handle risk than non-small construction businesses. Federal construction spending is down over 20 percent since August 2011 according to the U.S. Census Bureau. And, the outlook for public construction remains grim as agencies at all levels of government continue to cut construction spending. Given this reality, small business contractors may simply bid a job below cost to maintain some form of cash flow to remain in businesses. Additionally, some may fall victim to the auction's time restraints and consequent knowledge gap. Under pressure to win the job, a small business may unwittingly underbid, thinking that the subcontractors it has lined up would perform at that low of a price. Unable to have subcontractors perform the work, the prime small business may not have the capability to actually perform all of the work on its own and default. And, to add insult to injury, the federal government can even file a claim against the contractor when it underbids a contract under the False Claims Act. [1]

d. *Reverse Auctions Do Not Allow Thorough Evaluation of Value, Unlike Negotiated Procurements*

Where price is not the sole determinant, federal owners increasingly have utilized processes focused on negotiation to expand communication between the owner and prospective contractors for the purpose of discussing selection criteria such as costs, past performance and unique project needs. These processes recognize the value and quality of project relationships that share expertise to promote greater collaboration among the owner and project team members. These processes also consider quality, safety, system performance, time to complete and overall value that can, in fact, outweigh the lowest price to arrive at the best value for the owner. Such an approach also offers both the owner and contractor the opportunity to discuss and to clarify performance requirements of the project.

On the other hand, reverse auctions do not promote communication between the owner and bidders. Rather, they promote a dynamic in which bidders repeatedly attempt to best each other's prices. In fact, reverse auctions between buyers and suppliers often have a deleterious effect on the relationship between buyer and seller. Non-price factors of consequence to the owner, such as quality of relationship, past performance, scheduling, long-term maintenance and unique needs, are deemphasized in the auction. As a result, reverse auctions do not offer owners an opportunity to evaluate non-price factors.

e. *Sealed Bidding Assures that the Successful Bidder is Responsive and Responsible*

Where price is the sole determinant, the sealed bid procurement process is well-established to ensure integrity in the award of construction contracts. Under sealed bid procurement each proposer offers its best price and bids are evaluated through the use of objective criteria that measure responsiveness of the bid to the owner's articulated requirements and the responsibility of the bidder. In this manner, sealed bidding ensures fairness and value for the federal owner. On the other hand, reverse auctions ignore this tradition. The pressure and pace of the auction environment removes any assurance that initial and subsequent bids are responsive and material to the federal owner's articulated requirements. These auctions expose federal owners to the real possibility that they may award contracts to what would otherwise be non-responsive bidders. In addition, reverse auctions ignore the protections of the sealed bid procurement's laws, regulations and years of precedent that address critical factors and ensure the integrity of the process.

f. *Reverse Auctions Limit Competition*

My company—as well as many AGC members of all sizes—choose not to participate in reverse auctions for all of their risks and faults articulated above. Again, AGC strongly supports full and open competition for contracts necessary to construct improvements to real property. We contend that reverse auctions create an environment where competition is unnecessarily limited to the detriment of the federal government and taxpayers. In fact, we contend that no objective public or private study, including a U.S. Army Corps of Engineers (USACE) study on the issue,

[1] In the case of *Hooper v. Lockheed Martin Corp.,* the U.S. Court of Appeals for the Ninth Circuit ruled for the first time that underbidding or making false estimates in bids or proposals submitted in response to federal government solicitations may constitute violations of the False Claims Act. In a situation where a bidder needs a contract to maintain cash flow, the reverse auction can serve as an easy way for some contractors to do that. However, as this case reflects, there can now be legal liability for doing so that could further endanger the company. For more information see *http://www.mckennalong.com/media/site—files/1979—FCA%20Article.pdf*

has provided persuasive evidence that reverse auctions generate the best cost, or best value for the procurement of construction services.

II. Federal Agency—USACE—Report, Experience and Policy on Reverse Auctions

We have reviewed the findings of a federal agency—USACE—study, published in 2004 entitled "Final Report Regarding the U.S. Army Corps of Engineers Pilot Program on Reverse Auctioning" (see enclosure). The report determined that although reverse auctioning had potential in the purchase of "simple commodities" where variability is exceedingly small or nil (identical products under identical conditions), its use for the purchase of construction services where the dynamics and variables are just too diverse "should be the very rare exception and not the rule – if used at all." The USACE report further states that on the rare occasion reverse auctioning may be considered as an acquisition method, such consideration should only be made after sealed bidding has failed.

On March 6, 2008, Major General Ronald L. Johnson, former Deputy Commanding General of USACE, testified before the House Committee on Small Business on this very issue. MG Johnson testified that "[t]he Corps, through our pilot study, found no basis to claim that reverse auctioning provided any significant or marginal savings over a traditional contracting process for construction or construction services." MG Johnson also testified that "[w]hile this tool may be appropriate and beneficial in more repetitive types of acquisition, we did not find it to be a useful tool for our construction program and do not currently utilize it today to any great extent."

Most recently, on May 23, 2013, USACE Engineering and Construction Chief James C. Dalton, P.E., also testified before the House Committee on Small Business on a similar topic. Mr. Dalton noted that reverse auction procurement "provides a benefit when commodities or manufactured goods procured are of a controlled and consistent nature with little or no variability. Construction is not a commodity." He went on to state that "procuring construction by reverse auction neither ensures a fair and reasonable price nor a selection of the most qualified contractors." As a result of its experiences, USACE does not procure construction services using reverse auction procurement.

Furthermore, the federal government has elsewhere acknowledged that construction services stand apart from commodities or manufactured goods. In a July 3, 2003 memorandum from Office of Federal Procurement Policy Administrator Angela Styles, the government states that "[n]ew construction projects and complex alteration and repair, in particular, involve a high degree of variability, including innumerable combinations of site requirements, weather and physical conditions, labor availability, and schedules." This memorandum was sent to all federal procurement executives to encourage them not to treat construction as a commodity for government procurement purposes.

III. Reverse Auctions in the Department of Veterans Affairs and the General Services Administration

Over the years since USACE's first-hand insight on reverse auction procurement of construction services, AGC has found that some agencies—including the Department of Veterans Affairs (VA) and the General Services Administration (GSA)—continue to use or push this acquisition tool for construction. By no means are these two agencies alone. AGC has also brought the inappropriate use of reverse auctions to the attention of the National Parks Service and other agencies within the Department of Interior. For the purposes of today's hearing, we will address our concerns with the VA and GSA.

a. *Department of Veterans Affairs*

The VA construction program separates into two appropriation accounts: (1) minor construction, for projects of $10 million or less; and (2) major construction, for projects over $10 million. Similarly, the VA structures its construction program into two organizations, one where the 22 regional Veterans Integrated Services Network (VISNs) offices procure minor construction contracts and the other in the Office of Construction and Facilities Management (CFM) that handles major construction contracts.

In AGC's experience, the inappropriate use of reverse auction rests with the VISNs and not with CFM. AGC has tried to reach out to VISNs that utilize this acquisition tool to inform them of prior federal agency experience and the inherent risks they bring. However, they have not been responsive. As such, AGC recently reached out to CFM about minor construction project awards procured through the

reverse auction process since 2011. Those awards included the following 14 examples:

1. VA261–13–B-0854, Renovation Support – Facility Space Realignment, San Francisco VA Medical Center, California; Award: $888,508.80

2. VA247–13–R-1355, Floor Maintenance and Repair, Central Alabama Veterans Health Care System (CAVHCS), Montgomery and Tuskegee, Alabama; Award: $727,924.10

3. VA247–13–Q-1567, Place Ductwork and Equipment, Atlanta VA Medical Center, Decatur, Georgia; Award: $283,250.00

4. VA247–13–B-1655, Auditorium Upgrades, Ralph H. Johnson VA Medical Center, Charleston, South Carolina; Award: $224,540.00

5. VA2417–13–R-0228, Stairwell Repairs, Carl Vinson VA Medical Center, Dublin, Georgia; Award: $208,352.52

6. VA247–13–R-1560, Fall Protection Installation, Atlanta VA Medical Center, Decatur, Georgia; Award: $101,053.30

7. VA262–12–Q-0950, Construct Concrete Slab Parking Pad with Security Fence, VA Medical Center, North Las Vegas, Nevada; Award: $86,700.66

8. VA262–13–Q-0514, Install/Replace Flooring, VA Medical Center, North Las Vegas, Nevada; Award: $82,297

9. VA247–12–R-1390, Floor Restoration Building 802, Charlie Norwood VA Medical Center in Augusta, Georgia; Award: $81,267.00

10. 542–11–4-5306–0076, Retaining Wall Repair, VA Medical Center, Coatesville, Pennsylvania; Award: $75,639.08

11. VA247–12–R-1396, Floor Restoration, Charlie Norwood VA Medical Center in Augusta, Georgia; Award: $52,009.85

12. VA247–13–Q-1348, Medical Air Compressor Installation, VA Medical Center, Fort McPherson, Georgia; Award: $51,685.40

13. 561–13–4-503–0021, Remodel of Homeless Services Domiciliary, Lyons, New Jersey; Award: $47,728.71

14. VA247–13–Q-0604–01, Roof Repairs, Carl Vinson VA Medical Center, Dublin, Georgia; Award: $25,000

All of the solicitations previously mentioned were small business set-aside projects, many of which were for Service-Disabled, Veteran-Owned small businesses. AGC holds that the VA should not jeopardize the financial stability of these veteran small businesses, whose development and well-being is within the VA's mission, for a short-sighted and unproven construction services procurement method already abandoned by the largest federal construction agency.

Additionally, these VA contract awards were for the procurement of professional construction services and not for the purchase of a simple commodity, commercial item or mere maintenance. AGC holds that the VA misclassified these contracts, often as some form of simple maintenance rather than as professional construction services. For example, the VA Northern California Health Care System awarded a nearly $900,000 contract (VA261–13–B-0854) for "numerous interior renovations throughout multiple buildings at the San Francisco VA Medical Center. . . [for which] [t]he contractor shall provide all labor, materials, and equipment."

Here, the VA sought to solicit construction services under the guise of simple maintenance of structures and facilities. However, under no circumstance were the tasks equivalent to cleaning bathrooms. In fact, the solicitation called for over 20 rooms to be renovated in some fashion, including but not limited to work on flooring, plumbing, mechanical and electrical installation. The solicitation also included construction services calling for the use of fire-stopping construction practices and construction operations occurring during business hours in a hospital facility. Additionally construction services contractors were responsible for worksite safety for the contractor workforce and the VA facilities employees and patients.

For another example, the Carl Vinson VA Medical Center in Dublin, Georgia, awarded a $25,000 "roof repair" contract (VA247–13–Q-0604–01) as a simple "repair or alteration of structures and facilities." However, this project was not merely a roof repair; it appears to be a complete roof replacement. Roof replacement is a complex construction service. It should not be procured through a game-like, online reverse auction process in which price is the only factor.

Whatever the cost of the total project, construction requires professional expertise. It is subject to, among other things, weather conditions, rapidly changing diesel fuel and material prices, as well as conditions that introduce an extreme degree of variability to construction, like changing labor supply, workforce safety, and equipment costs and time. Additionally, construction projects can include unforeseen site issues, such as the existence and necessary safe removal of hazardous materials that were not disclosed to the contractor or known to the owner.

The complexities of these processes simply do not compare to the purchase of an off-the-shelf commercial item or mere maintenance. The reverse auction process ignores the expertise of the contractor or the unique nature of construction. Construction contractors, specialty contractors, subcontractors and suppliers offer and provide a mix of services, materials and systems. Again, they do not "manufacture" buildings, highways, or other facilities.

b. *General Services Administration*

Earlier this year, GSA launched an online reverse auction platform (*http://reverseauctions.gsa.gov/*) that enables any federal agency to procure construction services through a reverse auction. AGC notified GSA that it should remove from its Reverse Auction Platform the construction services options outlined in Schedule 56—noted below.

Specifically, the Reverse Auction Platform enables federal agencies to procure "Buildings and Building Materials, Industrial Services & Supplies" through Schedule 56. Schedule 56 includes "Ancillary Repair and Alteration requiring minor construction (includes Davis Bacon and construction clauses); and Installation and Site Preparation requiring Construction, which is necessary for Roof Repair or Replacement, to install a Pre-Engineered or Prefabricated Building or Structure, to install an Above Ground Storage Tank or to Install Alternative Energy and Power Distribution Solutions (includes Davis Bacon and construction clauses) " and construction of foundations.[2]

While GSA may intend for the procurement of what is misclassified as "simple," "ancillary" or "preparatory" construction services through a reverse auction, in practice, such undefined terms could allow for federal agency misuse of the Reverse Auction Platform, costing the federal government—and tax-payers—more in the long run. Determining which contractor is the most qualified at the lowest price to clear and improve land for construction, construct a building foundation, install prefabricated buildings, and repair roofs, among other things in Schedule 56, demands that a procurement agency evaluates a host of source selection factors together, which reverse auctions do not consider. For example, installation of prefabricated buildings can require a degree of design-build project delivery expertise that varies among contractors. However, a reverse auction only evaluates price, whereas established federal procurement practices allow for the consideration of this expertise.

To GSA's credit, it met with AGC in September on this issue. At the meeting, GSA showed its willingness to consider AGC's input as to why specific construction services items in Schedule 56 should not be procured through reverse auctions. In addition the agency was open to feedback on how to prevent contract misclassification.

IV. Congress Should Prohibit the Use of Reverse Auctions for Construction Services Contracts and Support Measures Like H.R. 2751.

As our testimony and the record evidence, the experiences of one federal agency do not necessarily mean another federal agency will learn from them. Rather, we find that each federal agency learns the mistake of construction services reverse auction procurement on its own. This will neither benefit competition and the construction industry—especially small businesses—nor the American taxpayer.[3]

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[2] General Services Administration, "Buildings and Building Materials, Industrial Services and Supplies Schedule 56: Frequently Asked Questions (FAQs)," available at: *http://www.gsa.gov/graphics/fas/FAQs-Buildings-Schedule56.pdf*

[3] As noted previously noted, the federal construction marketplace has retracted by over 20 percent since August 2011. This has come as a direct result of budget cuts—including sequestration—and the prevalence of continuing resolutions that prohibit necessary new project starts, which push back projects to outlying years. Some contractors have, in part, shifted resources towards competing on more private contracts, as that market has slowly improved, than they did previously. As such, competition for federal construction projects may decrease, impacting the price to the government. And, in relation to reverse auctions, those contractors that depend on federal work may become more desperate to win awards and imprudently bid on reverse auctions. Again, as previously noted, this can lead to possible contract defaults that cost federal agencies and taxpayers precious time and resources. In addition, such imprudent bidding can

Continued

As such, AGC holds that the only solution is for Congress to enact a law that prohibits reverse auction procurement of construction services. To the credit of Chairmen Graves, Hanna and Ranking Member Meng, they recently introduced H.R. 2751, the Commonsense Contracting Act of 2013. This bill would prohibit federal agencies from bidding construction contracts suitable for award to a small business through reverse auctions.

AGC previously testified in support of such a measure earlier this year and echoes its support for H.R. 2751 today. However, this bill will not completely prevent federal agencies from using reverse auctions to procure all construction services contracts. Consequently, AGC would support additional legislative efforts to prohibit reverse auctions for all construction services federal contracts.

Thank you for this opportunity to provide the views of the construction contractor industry in this important matter.

Prepared Statement of Louis J. Celli, Jr.

To "aid, counsel, assist and protect, insofar as is possible, the interests of small business concerns"[1] *(Original charter of the U.S. Small Business Administration)*

In 1953 the Small Business Act was signed into law, and created the Small Business Administration (SBA) we know today. The act was created to encourage and promote small business growth, and foster free market competition. In 1945 and 1946 millions of Americans took off their uniforms after WWII and came home to a job market that was shrinking because the war no longer provided economic stimuli. True to their very nature, American patriots turned to entrepreneurship. Still, large firms which grew powerful as a result of war production had a tremendous advantage over smaller, and start-up companies, so Congress created the SBA to help level the playing field.

The Small Business Act applies government wide, not just to the SBA. Government has a fiduciary responsibility and legal obligation to treat small business fairly, and to not take advantage of its buying power and become predatory, or act as a monopolistic powerbroker.

Over the past 10 years The American Legion has worked closely with hundreds of small business owners, and has established a Small Business Taskforce that is comprised of successful small and medium sized veteran owned businesses. Additionally, we have thoroughly researched numerous reports and articles both extolling the benefits of the reverse auction, and the disadvantages of them. Much of the research we reviewed was gathered from the Reverse Auction Research Center which is located in the Department of Management at Southeastern Louisiana University, and through senior leadership at Fed Bid, one of the major online reverse auction services used by the federal government.

The American Legion appreciates the goal of the government contracting community to lower federal exposure through competitive contracting initiatives, but is concerned that misuse of extra-governmental tools that have not suffered the scrutiny of the appropriations process, is putting veteran owned small businesses at risk and could also be serving to undermine the entire procurement process.

According to the Institute for Supply Management, reverse auctions are "a type of e-auction that is conducted online, in real-time, between a single buying organization and pre-qualified suppliers. Suppliers compete in presenting bids to the buyer for the supply of goods or services whose specifications for design, quantity, quality, delivery, and related terms and conditions have been clearly defined"; and David C. Wyld, Executive Director of the Reverse Auction Research Center reports in his 2011 report, Reverse Auctioning: Saving Money and Increasing Transparency, "The reverse auction acquisition tool is not appropriate for all spending categories. In fact, there are "sweet spots" for the use of reverse auctioning, namely in the areas of commodity-type buys of goods and services and in goods that are readily specifiable."[2]

The American Legion also notes that all of the evidence, both for and against reverse auctions consistently use the term "when used correctly, reverse auctions can

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cause desperate prime contractors to put undue pressure on subcontractors, jeopardizing their businesses.

[1] 15 U.S.C. § 631 : US Code - Section 631: Declaration of policy - See more at: *http://codes.lp.findlaw.com/uscode/15/14A/631#sthash.y4mlz3Oa.dpuf*

[2] See David C. Wyld, "Reverse Auctioning: Saving Money and Increasing Transparency" (July 2012), available at *www.businessofgovernment.org/report/reverse-auctioning-saving-money-andincreasing-transparency.*

be an effective purchasing tool". However, "when used correctly" turns out to be the default phrase that places the responsibility for proper use squarely on the customer, in this case – the federal government. Contracting officers who are not formerly trained to use these tools have ended up taking unfair advantage of small businesses, and because these tools are not government tools, the oversight for structure and use lacks proper implementation.

Wyld's article also discusses a 2004 memo from Robert A. Burton, then the associate administrator of the Office of Federal Procurement Policy (OFPP), The OFPP urged each federal agency, in the interest of "maximizing productivity gains from technology ...to explore increasing the use of commercially available online procurement services". One tool specifically mentioned in the Burton memo was reverse auctions, and the OFPP noted at the time that: "If used correctly, the reverse auction approach can ensure that the government receives competitive prices".[3]

Reverse auctions are not necessarily bad, any more than firearms are bad, when used properly by trained professionals. But while largely unregulated and improperly utilized, reverse auctions pervert the federal procurement system and skew the economic marketplace by encouraging awards made through an unnatural procurement process that ultimately preys on weak businesses, rather than promote strong businesses. This process ends up giving a false valuation of fair market product pricing, and will eventually create a disparity between more thorough procurement vehicle processes where value is made part of the decision matrix, and the reverse auction where value or added value is often omitted from bid consideration. Further, reverse auctions appear to undermine the Government Services Administration's (GSA) application process that requires the government be offered the best possible price in the first place. If that is true, then how can GSA contract holders consistently compete in the reverse auction process at offers lower than their established GSA contract?

An example of added value would be a printer and copier vendor that, through their negotiated license agreement with the manufacturer, is required to provide training and technical support on the products they sell. This added value increases the market price of the product, but may not be reflected in the sterile environment of the reverse auction bid process. Reverse auctions create a disproportionate disparity in the federal procurement industry while American Legion resolution 321[4] specifically calls for equal parity in federal procurement, and according to the Federal Acquisition Regulation (FAR); ""Fair market price" means a price based on reasonable costs under normal competitive conditions and not on lowest possible cost".[5] Further, Fair Market Price is mentioned in nearly every part of the FAR and that exact term can be found more than 30 times.

In the FAR we also find FAR part 19 §807 giving a definition of Estimating Fair Market Price;

"(c) In estimating a fair market price for a repeat purchase, the contracting officer shall consider recent award prices for the same items or work if there is comparability in quantities, conditions, terms, and performance times. The estimated price should be adjusted to reflect differences in specifications, plans, transportation costs, packaging and packing costs, and other circumstances. Price indices may be used as guides to determine the changes in labor and material costs. Comparison of commercial prices for similar items may also be used."

And FAR part 15 §404–1 discusses proper Proposal Analysis Techniques;

"(a) General. The objective of proposal analysis is to ensure that the final agreed-to price is fair and reasonable."[6]

And finally FAR part 19.1405 outlines Service-Disabled Veteran-Owned Small Business Set-Aside Procedures;

"(b)(2) Award will be made at a fair market price."[7]

While reverse auctions may have a place in federal procurement, in a limited capacity, The American Legion believes that the federal contracting office has the primary responsibility to ensure that every product that the government spends tax

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[3] Ibid

[4] Resolution No. 321: Support reasonable set-aside of federal procurements and contracts for business owned and operated by veterans, American Legion. National Convention August 2012 *http://archive.legion.org/handle/123456789/2190*

[5] Federal Acquisition Regulation, March 2005, *http://www.acquisition.gov/far/current/pdf/FAR.pdf*

[6] Ibid

[7] Ibid

payer dollars on, is purchased at fair market value. This assurance protects the tax payer, the small business, and the market.

Generally, reverse auctions are not popular in the commercial marketplace because the buyer doesn't always know what they are getting. Another example of reverse auctions is the online travel auction site Priceline. In these auctions the buyer knowingly understands that they are probably going to sacrifice comfort, convenience and quality for a lower price. Our federal government is not authorized to and should not be willing to forfeit those necessities, and congress does not fund government with the understanding that they must purchase marginally acceptable equipment and services, just as there is no pending legislation requiring federal travelers to use Priceline for their travel needs in an effort to save money. Also, Congress appropriates funds through an analytical process based on funding projections. If the government under spends the appropriated amount because they are thwarting the procurement process, then they should be mandated to immediately return the unobligated funds to the treasury, not obligate them for another purpose.

The American Legion is extremely concerned that reverse auctions will lead to decreased quality and decreased employment opportunities for veterans, which is in direct violation of American Legion resolution number 50 [8] that supports more hiring opportunities for veterans. Reverse actions will encourage vendors to learn how to provide the cheapest product and service in order to maintain profit margins, and government will be stuck purchasing poor quality because they will have no ability to shop for best value, only best price. These types of business models favor home-based business that primarily operate online and have no other employees than the owner, and no customer support. Businesses of this type end up relying solely on federal procurement as their only source of income, and this type of business model severely disadvantages businesses that hire veterans because businesses that hire employees have increased overhead expenses.

Businesses that have used reverse auctions successfully include very large businesses like Wal-Mart, Target, and Home Depot, who are in business for the sole purpose of making a profit. Purchasing at the lowest possible price is a core tenet for businesses like this as they have no legal, civic responsibility to protect small business like the federal government does, which is probably one reason our military isn't outfitted with products from Wal-Mart.

An article in Contract Management magazine points out a case study, conducted on The Department of State, reveals reverse auctions are already losing market share and have dropped 30 percent between 2007 and 2010, despite an increase in bid notifications of more than 225 percent. [9]

There will be plenty of testimony presented today that will offer evidence of billions of dollars in savings – but at what cost? The American Legion has been able to find no evidence that this process contributes to business innovation, economic growth, or positive partner relationships between government and industry. The American Legion has found reverse auctions fosters resentment between sellers and buyers and leaves the seller with the attitude of not wanting to provide anything more than exactly what was paid for, thus obliterating any harmonious relationship that should be developed between buyer and seller.

Guy Frankling, e-sourcing and implementation manager at Royal Dutch Shell, argues that specificity is key across all procurement methods. "If you are not clear on your specification, you won't be successful doing it (procuring the good or service) either manually or electronically". [10]

The American Legion also learned that businesses answering solicitations for services find that customers rarely, if ever, include all necessary requirements in the original solicitation. What is wanted versus what was asked for continues to be a source of frustration between contractors and vendors. The American Legion has received numerous complaints from veteran business owners who routinely argue that their customer is dissatisfied based not on the work that was performed, but more importantly, based on the work that wasn't preformed because it wasn't specified in the original solicitation.

The American Legion has worked with businesses that have gotten into trouble with reverse auction wins. In some cases they fail to realize the true expense required to deliver on a bid and have sold at such slim margins that they weren't able

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[8] Resolution No. 50: Support legislation that bolsters the hiring of veterans in the public and private sectors, American Legion. National Convention, August 2012 *http://archive.legion.org/bitstream/handle/123456789/2212/2012N050.pdf?sequence=1*

[9] Contract management Magazine, Reverse Auctions: Turning Winners into Losers, October 2012 *http://www.nxtbook.com/nxtbooks/ncma/cm—201210/index.php#/4*

[10] Reverse Auctioning: Saving Money and Increasing Transparency, 2011, *http://www.businessofgovernment.org/sites/default/files/Reverse%20Auctioning.pdf*

to sustain a viable business model – In other cases they bid based on agreements from other manufacturers or vendors, who, after the bid was won, chose not to perform on the agreement because the profit margins were too low and they subsequently diverted their manufacturing efforts to more profitable projects.

A survey of our members found that opinions regarding reverse auctions were overwhelmingly negative. Some of the more common complaints included;

- Lack of trust in the system – not knowing who they are bidding against, no idea if automated systems are in place of live bidders.
- Lack of federal compliance oversight
- Federal government's use of a commercial service that has not been properly competed through the procurement process, or gone through the federal design build process.
- Buyer funded fees that are charged to the buyer, but paid by the seller. This creates a false sense of inflated receipts and places unnecessary burdens and expenses on the seller.
- Fear of grey market products being sold illegally
- Promotes direct competition between manufacturer and authorized reseller
- Creates unreasonable pressure on small businesses to engage in loss leader pricing strategies
- Quality is unsustainable as this process subverts a healthy and profitable industrial base
- Ultimately, higher quality and more successful businesses are going to walk away from the reverse auction vehicle, leaving only bottom feeders

If the government is to continue to use reverse auctions, The American Legion recommends;

1. More outreach training for small veteran owned businesses.

2. Eliminate the LEAD or LAG indicators. This creates an unrealistic stressor for the seller and can be extremely detrimental for the nascent business.

3. Collect fees directly from customer (buyer).

4. Build a fair market price list into the process for commonly purchased items, and prevent sellers from going below the established fair market price.

5. Make buyers attest that they have conducted proper and adequate market research to determine fair market price.

6. Eliminate the ability of the buyer to set a minimally acceptable price, or clearly state to the seller what the starting price is.

7. Requests for debrief, protests, and any other dispute resulting between the seller and the federal government needs to be handled directly by the federal government, not handled through a civilian commercial company who has no authority to represent the federal government.

8. Exact Match Bids need to be more interactive. Government has unique needs and requirements, and even items issued under the same National Stock Numbers provide variation that can cause end user difficulties.

The Honorable Mike Coffman, Chairman
Subcommittee on Oversight and Investigations
House Veterans Affairs Committee
335 Cannon House Office Building
Washington, D.C. 20510

The Honorable Richard Hanna, Chairman
Subcommittee on Contracting and Workforce
House Committee on Small Business
2361 Rayburn House Office Building (RHOB)
Washington, D.C. 20515

December 9, 2013

Dear, Chairman Coffman, and Chairman Hanna;

Neither The American Legion nor I have received any federal grants or contracts, during this year or in the last two years, from any agency or program relevant to the December 11, 2013, Subcommittee on Oversight and Investigations House Veterans Affairs Committee and the Subcommittee on Contracting and Workforce House Committee on Small Business hearing on the Contracting Away Accountability Reverse Auctions In Federal Agency Acquisitions.

Sincerely.

Louis J. Celli Jr.

Prepared Statement of Michele Mackin, Director

Chairmen Coffman and Hanna, Ranking Members Kirkpatrick and Meng, and Members of the Subcommittees:

I am pleased to be here this morning to discuss the federal government's use of reverse auctions. In recent years, federal agencies have been using this mechanism—in which sellers compete against each other in an online venue to sell their products or services—as a tool to reduce the price they pay for certain types of items. In theory, a reverse auction leverages competition, enabling agencies to obtain lower prices and reduce acquisition costs. We found that government agencies were increasingly using reverse auctions as a means to drive down prices but without adequate guidance to ensure that the potential benefits were maximized.

My remarks today are primarily based on our recently issued report on agencies' use of reverse auctions. Accordingly, this testimony addresses (1) what agencies are buying through reverse auctions and trends in their use; (2) how agencies are conducting reverse auctions; and (3) the extent to which the potential benefits of reverse auctions are being maximized.[1] My testimony today will summarize our findings from that report.

To conduct our work, we used fiscal year 2012 contract award information from Federal Business Opportunities (FedBizOpps.gov) to identify the Departments of the Army (Army), Homeland Security (DHS), the Interior (DOI), and Veterans Affairs VA) as the primary users of reverse auctions, representing approximately 70 percent of the activity. Because the agencies did not maintain the level of detailed information needed for our review, we obtained reverse auction data from FedBid, Inc., the company that conducted almost all of the government's reverse auctions in fiscal year 2012, according to FedBizOpps.

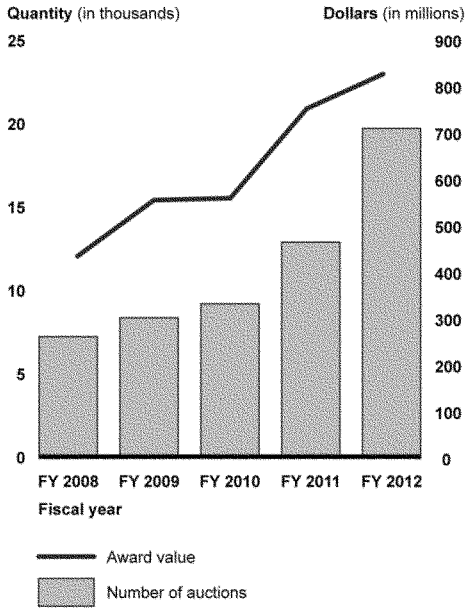
In addition, we reviewed, where applicable, government-wide and agency policies and guidance regarding reverse auctions at these agencies; interviewed government acquisition officials and officials from the Office of Management and Budget's Office of Federal Procurement Policy (OFPP); spoke with organizations representing government contractors; and reviewed a sample of contract files where a reverse auction was used. This work was performed in accordance with generally accepted government auditing standards. Our report provides further details on our scope and methodology.

Reverse Auctions Have Increased and Have Been Used Primarily to Buy Commercial Products and Services

Across the four agencies representing the bulk of reverse auction activity in fiscal year 2012, use of reverse auctions increased almost 175 percent between fiscal years 2008 and 2012. Figure 1 summarizes the growth in use of reverse auctions in dollars and number of auctions.

[1] GAO, *Reverse Auctions: Guidance Is Needed to Maximize Competition and Achieve Cost Savings,* GAO-14-108 (Washington D.C.: Dec. 9, 2013).

Figure 1: Number and Value of Reverse Auctions across the Selected Agencies from Fiscal Years 2008 to 2012



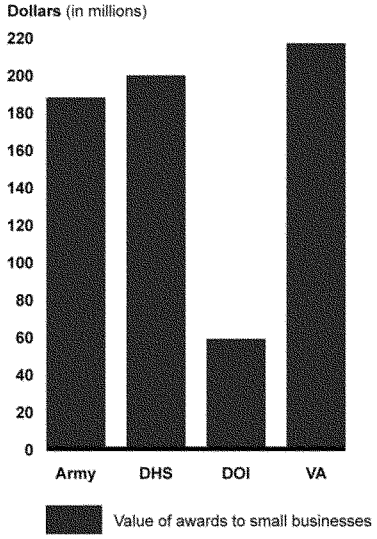
Source: GAO analysis of FedBid data.

Of the $828 million in fiscal year 2012 contracting actions that resulted from reverse auctions at these agencies, $746 million—or 90 percent—was for products. Services, in contrast, constituted about 10 percent. Reverse auctions were used to purchase a variety of commercial products, primarily for information technology (IT) and medical equipment and supplies. While to date most reverse auctions have been used for commercial products, some agency officials told us that the use of reverse auctions to acquire services is increasing and that they are also being used for more complex contracts.

Our analysis of the data also identified some common characteristics among contract awards resulting from reverse auctions. We found the following:

- About 95 percent of the reverse auctions resulted in awards of $150,000 or less.
- About 86 percent of the reverse auction awards—representing 80 percent of the dollars—went to small businesses. Figure 2 shows a breakdown of small business dollars among the four agencies.

Figure 2: Value of Small Business Awards Resulting from the Use of Reverse Auctions across the Selected Agencies, Fiscal Year 2012



Source: GAO analysis of FedBid data.

- Further, almost 50 percent of the reverse auctions were conducted to place orders under existing contracts. In some cases, the use of these contract vehicles includes a fee that the ordering agency must pay.
- And we also found that almost 60 percent of reverse auction awards were in the last quarter of the fiscal year. Agency officials told us this can occur due to the timing of when funds are released and that reverse auctions can facilitate the timely award of contracts late in the fiscal year.

Agencies Use the Same Fee-Based Contractor and Are to Follow Established Contracting Procedures to Conduct Their Reverse Auctions

All four agencies contracted with FedBid, a fee-based contractor, to conduct their reverse auctions during fiscal year 2012. Agency officials stated that contracting officers are required to follow established contracting procedures and rules. The contracting officer must also establish the basis for award. For example, the contracting officer can make the award to the lowest bidder or make the award based on a cost/technical trade-off process where it is in the best interest of the government to consider other than the lowest price. In fact, on the basis of our analysis of a random sample of auctions, we estimate that 24 percent of all reverse auction contracts awarded by the four agencies in fiscal year 2012 were not awarded to the lowest bidding vendor.[2]

Contracting officers can determine reverse auction features, such as the length of an auction, the amount of information available to bidders about each other's bids, and whether to set a target price, which may be based on a government cost estimate or market research. If a target price is in effect, or "active," a vendor must bid below that price and have submitted the lowest bid in order to be identified as the leading vendor. The leading vendor has the lowest price (below the target price) at any given time during an auction. However, a contracting officer can still award a contract even if no submitted bids meet the target price, that is, when no vendors were identified as the leading vendor. These strategies or features can affect the competitive environment of the auction and affect the magnitude of cost savings.

Vendors must register with FedBid and agree to the requirements established by the contracting officer before submitting a bid in an auction. Vendors can use FedBid's system to submit questions about requirements during the auction, and the system notifies the contracting officer via e-mail. It is up to the contracting offi-

[2] This estimate has a 95 percent confidence interval that extends from 17 to 33 percent.

cer to decide whether to answer them. Several vendors stated that FedBid's interface creates an additional layer between the vendor and the end user that can inhibit their efforts to clarify details in the solicitation—such as the type of material an agency requires—that are important in setting a bid price.

As part of our review, we gained an understanding of how reverse auction fees are paid. When a vendor submits a bid, FedBid automatically adds its fee and ranks the adjusted bid (i.e., the vendor's bid plus the fee) against adjusted bids submitted by other vendors. When the reverse auction ends and the contracting officer receives the results, the bids, which already include FedBid's fee, are ranked from lowest to highest. Then, when the agency receives the goods or services, it pays the entire bid amount to the selected vendor, including the fee. FedBid then sends an invoice to the selected vendor, who remits the fee to FedBid directly.

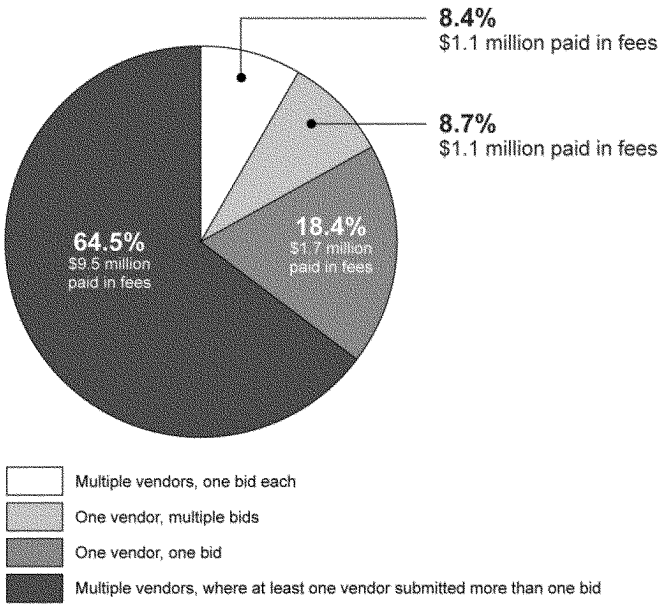
Agency officials and some vendors were confused about FedBid's fees. What we found is that FedBid caps its fee at 3 percent of the winning vendor's bid (though the fee is not to exceed $10,000), but the fee may be less depending on the specifics of FedBid's contract with the agency. In addition, FedBid may reduce its fee or charge no fee in specific circumstances. In fact, we found that FedBid received no fees in 20 percent of fiscal year 2012 reverse auctions.

In July 2013, the General Services Administration (GSA) launched its own reverse auction tool to allow agencies to use reverse auctions with the GSA Schedule without using a separate contractor to conduct the auctions. GSA does not intend to charge a reverse auction fee for awards made to GSA Schedule holders, but agencies would still pay the 0.75 percent GSA Schedule fee. We did not conduct a detailed review of GSA's reverse auction tool.

Competition and Savings Are Not Always Maximized, in Part Due to Lack of Comprehensive Guidance

Competition and savings—two of the key benefits of reverse auctions cited by the agencies we reviewed—are not always being maximized. Both have been limited because not all reverse auctions involve what we refer to as interactive bidding, where vendors engage in multiple rounds of bids against each other to drive prices lower. We found that over a third of the fiscal year 2012 reverse auctions had no interactive bidding—and agencies paid $3.9 million in fees for these auctions. Figure 3 shows the percentage of FedBid's fiscal year 2012 auctions for the agencies in our review that had interactive bidding among multiple vendors, versus those that did not, and the fees the agencies paid to FedBid.

Figure 3: Fees Paid by Selected Agencies Based on Number of Vendors and Bids, Fiscal Year 2012



Source: GAO analysis of FedBid data.

In addition, agencies cite savings as one of the benefits of reverse auctions. Although the agencies in our review stated that they do not publicly report the savings, they use the information—provided by FedBid—to assess the potential costs and benefits of reverse auctions. Using FedBid's approach of calculating savings based on the delta between the agency's target price and the winning bid, savings from fiscal year 2012 reverse auctions for the selected agencies totaled about $98 million.

However, it is unclear whether these savings are accurate. We found that

- the $98 million in estimated savings may be too high since it includes $24 million in savings from auctions without interactive bidding, which in theory would help drive prices lower, and
- 1,111 auctions that had interactive bidding resulted in an award price higher than the agency's target price, which may indicate that the contracting officer set the target price too low.

We also found that agencies

- rely on FedBid to identify their reverse auction activity,
- generally do not track how much they pay in reverse auction fees,[3] and
- sometimes pay two sets of fees when using an existing contract vehicle in conjunction with a reverse auction. For example, 47 percent of acquisitions using reverse auctions were ordered under pre-existing contracts. Agencies paid $6.5 million in fees to FedBid in these cases in addition to paying a separate fee to use some of the existing contracts..

However, we found that VA in particular has taken steps to gain greater insight into its use of reverse auctions. In 2012, the agency's senior procurement executive temporarily halted use of reverse auctions while an assessment was made of their effect on VA acquisitions. The reverse auctions were subsequently resumed, requir-

[3] While agencies generally do not track the reverse auction fees they pay, pursuant to FedBid's GSA Schedule contract, federal agency buyers utilizing FedBid's reverse auction services reserve the right to pay the transactional fee directly to FedBid. We found that the VA in some instances asked FedBid for information regarding the fees paid on specific reverse auctions.

ing collection of savings and fee calculations, which we found evidence of in the contract files we reviewed.

The Federal Acquisition Regulation (FAR) does not specifically address reverse auctions. Agencies have developed their own guidance, though most do not provide information on what to do in certain situations—for example, when only one vendor submits a bid. In our discussions with agency officials and vendors, we found they were uncertain about how reverse auction fees are paid and that confusion exists about how reverse auctions are managed. We believe that the lack of government-wide guidance addressing the use of reverse auctions and the confusion within the vendor community about the process may limit the potential benefits of reverse auctions.

GAO Recommends that Office of Federal Procurement Policy Take Actions to Address the Use of Reverse Auctions

Given the clear trends showing that reverse auctions are on the rise and the lack of government-wide guidance on their use, we made several recommendations in our report. We recommended that the FAR be amended to address reverse auctions from a regulatory standpoint, and also recommended that the Office of Management and Budget (OMB) issue guidance addressing competition and fees and to share agency best practices.

OMB generally agreed with our recommendations.

Chairmen Coffman and Hanna, Ranking Members Kirkpatrick and Meng, and Members of the Subcommittees, this concludes my prepared statement. I would be pleased to respond to any questions that you may have at this time.

Contacts and Acknowledgments

If you or your staff have any questions about this statement, please contact Michele Mackin at (202) 512–4841 or MackinM@gao.gov. In addition, contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals who made key contributions to this testimony are Katherine Trimble, Assistant Director; Russ Reiter; Carl Barden; Virginia (Jenny) Chanley; Dayna Foster; Kristine Hassinger; Georgeann Higgins; Julia Kennon; Kenneth Patton; Roxanna Sun; Bob Swierczek; and Jocelyn Yin.

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Prepared Statement of Bill Sisk

Good morning, Chairman Coffman, Chairman Hanna, Ranking Member Kirkpatrick , Ranking Member Meng, and members of the Subcommittees for Veterans' Affairs Oversight and Investigations and Small Business Contracting and the Workforce. My name is Bill Sisk and I am the Deputy Commissioner of the General Services Administration's Federal Acquisition Service.

I have spent over twenty years at GSA. I started in GSA's Regional office in Atlanta in 1990 and have served in numerous management positions including Assistant Regional Administrator and Regional Commissioner. In my capacity as Regional Commissioner, I represented GSA's Assisted Acquisition Services, Network Services, and Personal Property. I have also served as Assistant Commissioner in the Office of General Supplies and Services within the Federal Acquisition Service and was appointed to the U.S. AbilityOne Commission which is a unique program that provides employment opportunities for individuals who are blind or have other significant disabilities.

I appreciate the opportunity to appear here today to discuss GSA's recently launched Reverse Auction Platform. This effort is one of a continuing series of actions the Federal Acquisition Service has undertaken in support of GSA's mission to deliver the best value in acquisition and technology services to government and American people. Based on data since its inception, GSA's Reverse Auction Platform is one tool that, with proper training and use, can provide savings to agencies, help them achieve small business goals, and provide visibility into spending data that, over time, can help agencies make better acquisition decisions.

GSA's Reverse Auction Platform was put into operation July 1st, 2013 and is designed to be an efficient and cost effective platform for buying non-complex commodities and simple services. This initiative's focus is to drive down the total cost of acquisitions and increase savings to customers and taxpayers. GSA's Reverse Auction Platform is an eTool available to our government partners to use to facilitate the request for and submission of quotes or offers for products and services through GSA Multiple Award Schedules and Blanket Purchase agreements (BPAs), Veterans Administration's schedules, and Department of Navy BPAs against GSA schedule contracts. GSA leveraged existing e-Buy and GSAAuctions.gov IT infrastructure resources which reduced development costs and provides users a familiar look and feel when using the Reverse Auction website. The GSA Reverse Auction tool is non-mandatory and available to agencies to consider as they develop acquisition strategies.

Additionally, by leveraging GSA Schedule contracts and their unique ability to provide a broad array of vendors and small business set-aside capability, GSA's Reverse Auction Platform improves the government's ability to maintain small business participation through broad competitions and set-asides to promote agencies' meeting small business goals in a cost effective way.

There are a variety of potential benefits to agencies of this platform, including that it:

- Displays real-time pricing
- Provides customers with level III spend data (historical pricing data)

- Interfaces with existing systems, i.e., eBuy / eLibrary enabling vendor authentication to verify that contracts are still valid under the GSA Multiple Award Schedules program
- Assists in meeting small business goals
- Facilitates compliance with competition requirements

While agencies may realize these benefits, it is also important that the Reverse Auction Platform be used appropriately. GSA provides training on the Reverse Auction platform regularly to both the buyer and vendor communities. GSA offers on average four training sessions per week in a variety of forums. To date, over 50 sessions have been conducted and over 2000 individuals trained on the platform. Additionally, frequently asked questions and answers are available on the site as a resource for users.

The data so far has demonstrated savings in price, good competition from vendors, and support for small businesses. To date, several Federal Agencies, including GSA, have utilized the platform for 485 auctions, realizing about 6.7 percent savings on average with an average of three vendors participating per auction. 85.53 percent of the total awards and 87.18 percent of the total value of all contracts have been made to small businesses.

As the GSA Reverse Auction Platform continues to mature and evolve with more training and education provided, GSA predicts an increase in the use of the platform based on the initial interest in the platform and the overall interest by agencies in utilizing reverse auction procurement solutions. Additionally, we predict future spend data may provide insights for potential strategic sourcing opportunities. As we move forward, we welcome insights from Congress, from industry, and from partner Federal agencies on additional ways to improve the platform and ensure it is used appropriately.

During this time of continued budget uncertainty and ongoing fiscal pressure, GSA has launched the Reverse Auction platform in the hopes that it will be used by our partners to maximize savings in terms of both driving competition among vendors to achieve cost savings and by cutting processing times so that agencies achieve resource savings as well. This tool is one offering by GSA to deliver better value and savings to our partners and ultimately the American taxpayer.

Thank you again for the opportunity to testify and I am happy to answer any questions you may have.

Prepared Statement of Major L. Clark, III

Chairman Hanna, Ranking Member Meng, Members of the Small Business Contracting and Workforce Subcommittee as well as Chairman Coffman and Ranking Member Kirkpatrick and Members of the Veterans' Affairs Subcommittee on Oversight and Investigations, I am honored to be here today to present testimony to you on behalf of the Office of Advocacy of the U. S. Small Business Administration and more specifically, on behalf of Chief Counsel Dr. Winslow Sargeant.

Dr. Sargeant would like me to thank you for the support that you have provided this office, and he looks forward to a continued partnership with you as we mutually strive to improve the economic climate for our small business stakeholders.

The Office of Advocacy is not in opposition to reverse auctions in the federal marketplace. Today, we are advocating for clear reverse auction guidance from the Office of Federal Procurement Policy.

My name is Major L. Clark, III, and I am the Assistant Chief Counsel for Procurement Policy for the Office of Advocacy. While my professional career includes both public and private sector experience, I previously served as the Staff Director for the House Small Business Committee under the chairmanship of the Honorable Parren J. Mitchell of Maryland so thank you for having me back.

I ask that this written testimony and two attachments be included as part of the official transcript of this hearing.

In 1976, the Office of Advocacy was established pursuant to Public Law 94–305 to represent the views of small entities. Advocacy advances the interests and concerns of small business before Congress, the White House, federal agencies, federal courts, and policymakers. The Office of Advocacy is an independent office within the Small Business Administration, so the views expressed by this office do not necessarily reflect the views of SBA or the Administration. We work with federal agencies in the rulemaking process to implement the requirements of the Regulatory Flexibility Act (RFA). The RFA requires federal agencies to consider the effects of their proposed rules on small businesses and other small entities, including small governments and small nonprofits.

Pursuant to the above statutory authority, the Office of Advocacy has been involved in the monitoring of reverse auction activities at the federal level since around 2006.

On February 27, 2008, the Office of Advocacy sent a letter to Administrator Paul Denett of the Office of Federal Procurement Policy with a recommendation from small business stakeholders to better define the reverse auction process. I have submitted this document as Attachment one.

Attachment two is a more recent letter to Acting Administrator Lesley Field of the Office of Federal Procurement Policy dated January 21, 2012 from Dr. Sargeant of the Office of Advocacy. This letter expresses additional concerns regarding the negative impact of reverse auctions on small businesses.

In the fall of 2012, we held a procurement roundtable in Seattle, Washington. During this roundtable, we heard from a woman-owned small business. The owner explained her recent experience with the reverse auction process where she lost an important contract. Moreover, when she tried to understand why she lost the contract, she could not receive a clear explanation for losing her bid. As a result, the inability of the contracting officer to explain clearly why she lost the auction was as frustrating to her as losing the bid. After our listening session, Advocacy conveyed this experience to the Office of Federal Procurement Policy.

In response to Advocacy's concerns, the Office of Federal Procurement Policy convened a small business stakeholder session in Washington, D.C. in which the attendees conveyed their concerns with the reverse auction process. Some of the concerns included a lack of clear guidance to agencies, conflicts with Federal Acquisition Regulation Part 19, the role and responsibilities of the third party providers, and finally, the fees required to participate in the reverse auction process.

More recently, small business associations that represent small architectural, engineering and surveying companies have reached out to the Office of Advocacy about reverse auctions with the same concerns as other small business stakeholders. It would appear that some agencies are attempting to use reverse auctions for these types of services.

In conclusion, Chief Counsel Sargeant would like to make it perfectly clear that the Office of Advocacy is not in opposition to reverse auctions in the federal marketplace. The intent of this office is to make sure that our small business stakeholders have a voice. We are advocating for clear reverse auction guidance from the Office of Federal Procurement Policy.

Thank you and I look forward to your questions.

Attachment One of Major L. Clark III's Testimony:

February 27, 2008
The Honorable Paul A. Denett
Administrator
Office of Federal Procurement Policy New Executive Office Building
Washington, DC 20501

Subject: "Two Existing FAR Rules/Policies" on Advocacy 's 2008 r3 Top 10 List

Dear Administrator Denett:

The Office of Advocacy is charged with monitoring compliance with the Regulatory Flexibility Act (RFA) and works with federal agencies to ensure that they analyze the impact of their proposed regulations on small business. Under the RFA, agencies are required not just to review proposed rules, but to review existing rules -as mandated by section 61 0 of the RFA. In an effort to increase compliance with section 610 and to ensure that agencies conduct transparent reviews in general, the Office of Advocacy developed the Regulatory Review and Reform (r3) initiative.

This r3 initiative was designed to identify and address existing federal rules that should be reviewed and may need reforming. r3 is a tool for small business stakeholders to suggest needed reforms to regulations that are outdated, ineffective, duplicative, or otherwise in n need of review. After a call for nominations, over 80 existing rules were submitted by small businesses and their stakeholders identifying potential rules ready for review and reform. Following significant review and analysis of those nominations. I have selected the 2008 Top l0 rules for Review and Reform .

The purpose of this letter is to inform you that your office has two regulatory initiatives that appear on our 2008 r3 Top 10 list. This first is a rule on Retainage for Fix Priced A&E contracts and the other item is the OFPP initiative on reverse auctions. Advocacy will be announcing the 2008 r3 Top 10 Rules for Review and reform and releasing its annual report on agency compliance with the RFA on Thursday, February 28, 2008 at the National Press Club. A list of the r3 Top 10 rules

can be found in the attached summary report. Additional information on the r3 initiative is available on our website: www .sba.gov/advo/r3. In addition, a six-month status report will be placed on our website to update the public regarding Advocacy and agency progress on the r3 Top 10 Rules for Review and Reform.

Advocacy has been working with staff in your office on these regulatory initiatives and we see this Top 10 list as an opportunity for both of our offices to accomplish burden reduction for small business and to be responsive to the regulated public.

We look forward to working with your office on these important reviews. If you have any questions or concerns, please do not hesitate to contact me or Major L. Clark, III on my staff at 202–205–7150 or major.clark@sba.gov.

Sincerely,

Thomas M. Sullivan
Chief Counsel for Advocacy

Enclosure

Attachment Two of Major L. Clark III's Testimony:

January 21, 2012
Lesley Field
Acting Administrator
Office of Federal Procurement Policy
New Executive Office Building Washington, DC 20501

Re: Impact of Reverse Auctions on Small Businesses

Dear Administrator Field:

The Office of Advocacy (Advocacy) of the U.S. Small Business Administration submits this request for a review of current acquisition policies and practices regarding the acquisition tool of reverse auctions and the impact of such policies and practices on small businesses.

Office of Advocacy

Advocacy was established pursuant to Pub. L. 94–3051 to represent the views of small entities before federal agencies and Congress. Advocacy is an independent office within the U.S. Small Business Administration (SBA), so the views expressed by Advocacy do not necessarily reflect the views of the SBA or the Administration.

Background

In 1997, the Federal Acquisition Regulations (FAR) were changed to allow for reverse auctions in the acquisition process. In Fiscal Year 2006, the National Defense Authorization Act required the Office of Management and Budget to study and develop a report on all types of commercially available online procurement services, including reverse auctions. In response to this request from Congress, the Office of Federal Procurement Policy established an inter-agency working group to review regulations, policies, and business considerations related to the use of online procurement services. The Office of Advocacy participated in many of the discussions of the working group.

On February 27, 2008, the Office of Advocacy submitted to Administrator Dennett of the Office of Federal Procurement Policy a recommendation from small business stakeholders regarding the need for better policies and/or regulations on the use of reverse auctions. This recommendation for action came as a result of this office seeking input from small business stakeholders across the country on regulations and policies that were negatively impacting their ability to obtain a level playing field in Federal acquisitions. A copy of the letter to Administrator Dennett is *Attachment 1.*

New Developments

On July 15, 2010 former OFPP Administrator Daniel Gordon testified before the Committee on the Budget of the United States Senate that reverse auctions have had some positive impacts on improving the Federal acquisition process and in this regard, some small businesses have been beneficiaries of multi-million dollar awards. We commend these results.

Notwithstanding these successful uses of reverse auctions, the Office of Advocacy continues to receive concerns from small business stakeholders regarding the lack of clarity in the application of reverse auctions from agency to agency. In this regard there is a current protest before GAO in which the small business alleges that the Army used the reverse auction acquisition tool but did not comply with the Small Business Act, (15 USC644). This case is: GAO PROTEST B–406329. SBA has filed

a letter in support of the small business. A copy of the SBA letter is *Attachment 2.*

We believe this case raises concerns that some Federal agencies using reverse auctions may not be complying with the simplified acquisition threshold requirements for contracts to be reserved for small businesses. The Small Business Act (15 USC 644) states, "simplified acquisitions shall be reserved exclusively for small business concerns."

Recommendations

Small businesses have stated that because of a lack of uniform clarity in policy or regulations they find an uneven hand in the application of reverse auctions to micro purchases. We recommend:

1. That the Office of Procurement Policy at a minimum provide a clear policy statement to the acquisition community that reverse auctions must comply with the requirements that contracts within the simplified acquisition threshold are to be reserved exclusively for small businesses.

2. That the Office of Federal Procurement Policy make a clear policy statement that reverse auctions are best when used for commodity acquisitions and not for service contracts.

Conclusion

We commend the efforts of the Federal acquisition community in its commitment of a level playing field for small businesses. We believe that the type of clarity being requested above will be of tremendous assistance to the federal acquisition workforce as it continues to meet the acquisition mission of their agencies. Thank you for your prompt consideration of this request.

Please contact me or my Assistant Chief Counsel *Major Clark* at 202–205–7150 should you have any questions.

Best regards,

Winslow Sargeant
Chief Counsel for Advocacy

Major Clark III
Assistant Chief Counsel for Advocacy

Cc: The Honorable Cass Sunstein, Administrator, Office of Information and Regulatory Affairs

Footnote:

1. 5 U.S.C.§ 601 et seq. [1]

1 Attachment 1: Letter of Chief Counsel for Advocacy Thomas M. Sullivan to The Hon. Paul A. Dennett, February 27, 2008

Attachment 2: Letter of SBA Associate General Counsel John W. Klein to Pedro Briones, Esq., January 5, 2012

Prepared Statement of Jan Frye

Chairman Coffman, Chairman Hanna, Ranking Member Kirkpatrick, Ranking Member Meng, and distinguished Members of the Committees, we are pleased to appear here this morning to discuss VA's process for establishing and maintaining accountability in its use of reverse auctions. I am accompanied here today by Philip Matkovsky, Associate Deputy Under Secretary for Health for Administrative Operations.

Reverse auctions is a type of electronic tool in which the roles of buyer and seller are reversed. Unlike the traditional auction in which the seller accepts the highest price, reverse auctions result in the buyer accepting the lowest price. VA issued guidance in 2003 on the use of this electronic tool.

Since 2004, the Office of Management and Budget (OMB) Office of Federal Procurement Policy (OFPP) encouraged increased use of commercially available online procurement tools, including reverse auctions. In a September 2010 memorandum, OMB's Federal Chief Performance Officer encouraged senior executives to reform contracting through the continued implementation of innovative procurement methods such as the use of Web-based electronic reverse auctions.

VA supports the use of reverse auction as an acquisition tool. Use of this tool was primarily limited to contractor support for VHA. However, early in fiscal year (FY)

2012, concerns surfaced regarding management of the reverse auction process. As a result VA senior procurement executives made the decision to invoke a moratorium and conduct a comprehensive evaluation of VA's current compliance with policy and regulations. The moratorium was put in place on March 3, 2012. VA analyzed randomly selected files and determined that some contracting actions did not fully comply with VA policy and procedures. Since procuring activities had alternatives for obtaining the required supplies and services, invoking the moratorium had no effect on VA's delivery of health care to Veterans.

The Senior Procurement Executive released the new policy and rescinded the moratorium on the use of reverse auctions on April 3, 2012. The VA policy provides specific guidance for VA warranted contracting officers regarding the use of reverse auctions. It directs each Head of Contracting Activity (HCA) to develop internal controls including mandatory training, file documentation and reviews, and standard operating procedures to establish oversight of reverse auction procurements. It further directs that each HCA ensure the savings realized through using reverse auction techniques are auditable and transparent, independent of any reverse auction service provider. Further, each award file must be documented with the savings realized through the use of reverse auction techniques as well as the reverse auction fee paid. VA oversees the procurement process, including reverse auctions through its compliance review process.

VHA leadership requested an internal quality assurance group to conduct a focused review of select procurements that employed reverse auctions as the vendor solicitation method. Results of these internal reviews were briefed to VHA senior management, and based on these reviews, VA is pausing further utilization of our reverse auction tool.

We are assessing the degree to which we can ensure a consistent application of this solicitation method, which includes thorough documentation, and conforms to all aspects of VA policy. The Department will continue to procure products and services through other procurement methods.

The Department conducted 2,261 reverse auctions in FY 2011 representing over $78 million in total dollar volume; 60 percent went to small business. In FY 2012, VA conducted 7,587 reverse auctions representing approximately $305 million in total dollar volume; 79 percent of that total went to small business.

The Department has exceeded goals for small business since FY 2010. The Department's small business accomplishments have ranged from 35–37 percent against goals of 33–34 percent.

Conclusion:

The Department continues to monitor the efficacy of reverse auctions and adjust our policies and processes to be in line with the results of our reviews and business outcomes. I appreciate the opportunity to testify today and am happy to answer any questions the Committees may have.

Statements For The Record

FedBid, Inc.

Chairman Coffman, Chairman Hanna, Ranking Member Kirkpatrick, Ranking Member Meng, and Members of the committees, thank you for the opportunity to provide written testimony on the topic of reverse auction use within the Federal Government and provide commentary regarding the recently published Government Accountability Office (GAO) report GAO–14–108 on reverse auctions (GAO Report).

1. INTRODUCTION

What is a reverse auction? A reverse auction is a competitive process in which a buyer solicits bids from sellers during a period of time set by the buyer. During the reverse auction, sellers have the opportunity to submit a single bid or multiple bids that decrease in price. Unlike a forward auction, like eBay®, in which a seller is selling a product or service and buyers submit competing bids, thereby driving the price up, a reverse auction involves sellers submitting competing bids and driving the price down. An online or electronic reverse auction creates considerable process efficiencies, as seller bids and rebids can be submitted quickly, with real-time information provided to sellers regarding their relative competitive position. In the case of FedBid, sellers are notified whether they 'lead' or 'lag' to the low bid or buyer target price, and are not shown the identity or pricing of competitors.

It is important to note that, in the case of FedBid, buyers are not required to make award to the lowest bid or even to make award at all. If they have opted to

apply best value award criteria, buyers can make award to any seller whose bid, based on the stated award criteria (which can include past performance, technical capability, delivery, etc. in addition to price) provides the most advantageous terms. In addition, at the close of any buy, the buyer can decide to make award, cancel the buy, or repost the buy with different requirements or under a different acquisition scenario.

Although reverse auctioning currently addresses only a very small percentage of Federal spending, it provides an important alternative to traditional procurement methods. With the continuing contraction of the Federal procurement workforce and ongoing budgetary pressures, many agencies have come to realize that traditional means of sourcing, competing and procuring everyday goods and simple services needed to support agency operations just do not work well enough.

How groundbreaking is the government's use of reverse auctioning? As a commercial best practice used by almost all Fortune 500 companies, online reverse auctioning has been around for decades. The Federal government finally removed its prohibition on reverse auctioning as part of the 1997 Federal Acquisition Regulation (FAR) re-write, and then, in 2004, Office of Management and Budget's Office of Federal Procurement Policy (OFPP) issued a memorandum asking Federal agencies to "explore increasing the use of commercially available online procurement services", including reverse auctions. In 2005, both the GAO (MTB Group, Inc., B–295463 (February 23, 2005)) and the Court of Federal Claims (MTB Group, Inc. v. United States, 65 Fed. Cl. 516, 523–24 (2005)) determined that reverse auctions are permissible methods of procurement. To date, agencies have used online reverse auctions to purchase billions of dollars worth of commercial goods and services, from IT products to tattoo removal machines and from lawn care to lab rats.

In fact, when looking at the overall process of online reverse auctioning in comparison with the traditional buying process, the dramatic differences occur in the process and data automation and NOT within the procurement process itself. As with traditional acquisition methods, the agency buyer using reverse auctions works within established contracting procedures and maintains complete control over the purchasing process, including what to compete, which acquisition scenario to use, which award criteria to use (including other than low price technically acceptable, or LPTA) and to which seller to make award. When using FedBid to conduct reverse auctions, agencies typically use simplified acquisition procedures, as the vast majority of auctions on FedBid are for requirements below the simplified acquisition threshold (SAT) of $150,000.

What makes reverse auctioning so attractive as an alternative procurement method? Because of the high degree of process automation, information access and uniformity and ease of use inherent in this form of electronic commerce, reverse auctions provide a number of advantages over traditional procurement methods for firm-fixed price purchases of commercial item goods and simple services. These advantages include cost savings, operational efficiencies, increased small business utilization, and better transparency, accountability and control over agency spend.

2. SAVINGS

a. Cost Savings through Dynamic Competition

The aspect of reverse auctions that seems to attract the most attention is cost savings, and promoting competition is universally regarded as the key to driving high-quality purchasing results, including lower cost. The FAR recognizes this dynamic, providing as one if the guiding principles for the Federal Acquisition System to "Satisfy the customer in terms of cost quality, and timeliness of the delivered product or service, by, for example . . . [p]romoting competition" (FAR 1.102(b)). It also cites promoting competition in the acquisition process as a means of satisfying the customer in terms of cost, quality, and timeliness of the delivered product or service as a "performance standard" within the Federal Acquisition System (FAR 1.102–2).

As a commercial best practice, reverse auctioning is particularly effective in promoting competition through the concept of dynamic bidding, which enables sellers to not only submit an initial bid, but also to submit multiple re-bids – either through an automated re-bidding function or manually – based on some indicator of relative pricing. In FedBid, sellers can re-bid manually or use an automatic rebidding feature that enables them to establish a bid range, including a minimum bid price. The system does not display competitor names or pricing, but simply indicates relative price positioning through a 'lead' or 'lag' notification, enabling a seller to rebid if it lags to another seller or the buyer's target price. The relative pricing indicator approach helps protects against collusion and "winner's curse" situations by encouraging sellers to rebid, but to do so by reviewing their own pricing structure rather than that of another party.

Even with the built-in competition aspect of reverse auctioning, the process in and of itself certainly does not guarantee competition in every circumstance. Rather, the nature of the purchase must provide a reasonable expectation of competitiveness, or the reverse auction process will have minimal, if any, impact on cost of the purchased item. For example, if the purchase is for a specific brand name product, there must be multiple manufacturers or authorized resellers. If a buyer is purchasing a product manufactured by one company and a direct sales model, there will be no competition, regardless of the acquisition method employed. As another example, specific to the Federal market, if the purchase is being made through a certain contract vehicle, there must be multiple suppliers under that contract that actually sell the required item as opposed to just being in the general item category. Not infrequently, a contract may include multiple sellers in a product category but provide little overlap of specific products. As yet another example, if a particular brand of product is being purchased through a contract vehicle using an economic set-aside, the combination of multiple limiting factors may easily restrict competition to a single supplier.

Although the average Federal buy on the FedBid marketplace during FY13 resulted in push notifications to 3,447 sellers with profiles matching the buy requirements, the appropriate seller community is determined by each buyer. Depending on the characteristics of the buy, the size of that seller community can be reduced or expanded accordingly. The GAO Report mentions an example of a Department of Homeland Security contracting officer using multiple successive acquisition scenarios to increase the number of potential bidders in an auction. In that example, the buyer's first posting of auction solicited from among a small group of multiple award contract holders; the first repost of the auction increased the potential pool to GSA Schedule holders; and the second repost broadened the potential pool still further to include all sellers eligible for Federal award. The result of this approach was increasingly robust competition, which ultimately provided the best price after 21 bidders submitted 74 bids. The advantage of using an online reverse auction tool in this case was that the buyer was able to quickly and easily repost the buy to broaden the eligible seller community after evaluating the results of the prior posting, literally with a couple of clicks of the mouse.

b. The Role of the FedBid Fee in Achieving Savings

FedBid's 100% performance-based transactional fee structure plays a key role in validating buy results, including savings. FedBid receives a transactional fee, consisting of not more than 3% of the transaction, but only if the buyer: 1) determines that the reverse auction has met the competition, savings and other buyer generated criteria for the procurement and 2) selects a winning seller. Once the buyer selects a seller, it issues an order to the selected seller for delivery of the commodity or service. When the buyer receives the procured items or services, it pays to the selected seller the total bid amount, which includes the transactional fee. FedBid then collects from the selected seller the transactional fee. There are no fees for buyers or sellers to register, view, or post/bid on an auction, and sellers incur no out-of-pocket costs to use FedBid.

FedBid's 0–3% fee structure enables FedBid to adjust its fee downward to address situations in which the buyer has met its competition and other procurement goals through FedBid but the fee has caused the selected seller's bid to exceed a target price based on an actual market research quote or official published contract price. In such cases, FedBid reserves the right to reduce or remove its fee so that the awarded price will not exceed the target price. Accordingly, the fee can be as low as 0% on a given transaction. Because FedBid is only paid upon award and the buyer can cancel the buy or repost at any time, FedBid's fee model is risk-free for the buyer – effectively guaranteeing that the buyer will not pay more using FedBid than if they purchase offline. In addition, FedBid limits fee cost to Federal agencies, capping fees per auction at $10,000, so that fee is never a primary factor in considering whether to use reverse auctioning – even for larger procurements.

The GAO Report raises an issue of a transaction being subject to two fees if an agency uses FedBid in conjunction with, for example, Schedule contracts. However, FedBid's performance-based fee structure means that no fee is incurred unless the agency realizes true value in using the reverse auction process. As part of the FedBid Terms of Use, FedBid specifically guarantees that it will reduce or remove its fee if it is notified that the fee causes the total price to exceed the seller's published contract price. Government-wide FedBid receives no fee on approximately 20% of all awarded buys. In the Veterans Health Administration (VHA), which employs a more restrictive competitive approach through its contract hierarchy, FedBid receives no fee on approximately 35% of actions, regardless of cost savings or com-

petition. In fact, for the average GSA/Federal Supply Schedules (FSS) buy, FedBid collects a $414 fee, but yields an average of $5,072 in savings, providing a 12x return on investment. Overall, FedBid helps Federal agencies save nearly 10%, including $121 million in FY12 and $160 million in FY13.

Finally, it is important to emphasize that the FedBid fee is the only way FedBid gets paid on Federal purchases. Because it is 100% performance-based, FedBid does not get paid on canceled, reposted or zero fee buys, even though it has performed all services required to compete the buy on FedBid. Those services include provision, operation and management of the FedBid online marketplace and its reverse auction and related functionality; buyer training (in-person, remote and online) and on-site and remote support; seller sourcing, recruitment, training (in-person, remote and online) and support; market support; helpdesk services; quality assurance; reporting; marketplace application feature development and site enhancements; system development, operations, maintenance and upgrades; and, applicable customer system interface development. In other words, FedBid doesn't just promise results; it delivers.

c. Operational Efficiencies through Managed Automation

The GAO Report mentions that "agency officials stated that using reverse auctions reduced some of the time that would otherwise be spent on the acquisition"[1] and that "[a]gency acquisition officials told us that using a contractor for their reverse auctions reduced some of their administrative duties and allowed senior contracting officers to spend more time on complex acquisitions."[2] This aspect of savings – operational savings through improved process efficiencies – in fact, is often a major driver of agency use of reverse auctions, and the FedBid marketplace in particular. Studies conducted by Department of State, Navy, and Customs and Border Protection (CBP) have all validated both the direct impact on time savings for procurements conducted through FedBid as well as secondary impact of improving operations by being able to utilize that time savings to better negotiate complex procurements, perform contract due diligence and closeout, or conduct training. The study conducted by CBP found that, on average, buyers could save approximately 8 hours per buy competed through the FedBid marketplace. This time savings is particularly critical during the fourth quarter of the government's fiscal year, when most procurement is conducted. As mentioned in the GAO Report, "According to agency officials, reverse auctions, which can take as little as an hour for uncomplicated purchases, can facilitate the timely award of contracts at the end of the year."[3]

Why does reverse auctioning through FedBid save so much time? The platform effectively automates the communication and competition and documentation aspects of the procurement process through an intuitive web-based interface. Accordingly, buyers across the government can process thousands of auctions simultaneously, each involving multiple sellers submitting multiple bids on multiple items. Buyers simply perform market research as usual, post requirements according to the acquisition scenario of their choice, then review bid results, perform due diligence and make award. Buyers can access all of their reverse auction activity 24 hours a day, without any practical limitation on the number of requirements posted on the site or the number of auctions running through the site, and all marketplace data is reportable to the buying agency. In addition to the automation, FedBid provides comprehensive support services to both buyers and sellers and complete management of the marketplace.

3. SMALL BUSINESS UTILIZATION

Although the FAR requires a fair and open procurement process that encourages maximum participation by sellers, traditional procurement techniques available to the government buyer make that a difficult standard for buyers to achieve and maintain. Actively notifying sellers of appropriate opportunities and ensuring that minimum response goals are met is time consuming, and traditional offline bid and proposal processes are cumbersome. In fact, even with the advent of FedBizOpps, which serves as the online publication site (or governmentwide point of entry) for Federal procurements, access issues remain. Publication to FedBizOpps is generally not required for awards under FSS or other authorized multiple award contracts, and while the site provides static notification, sellers must still actively search the site for opportunities corresponding with their offerings.

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[1] GAO Report at 18.
[2] *Id.* at 12.
[3] *Id.*

Traditional process limitations and inefficiencies, coupled with an increasing workload and decreasing numbers of procurement personnel, typically mean that most competitive commodity procurements involve a relatively small number of sellers. It also means that sellers who would like to participate in those procurements have a more difficult time tracking them and competing for award. For small businesses, with limited sales and marketing budgets, participation in Federal acquisitions is even more difficult. Thus, even in spite of the government's ambitious set-aside programs and small business utilization mandates, Federal agencies continue to fall short of their goals to increase small business participation.

a. FedBid's Impact on Small Business Utilization

FedBid helps buyers meet the challenge of finding and engaging small businesses, with instant access to thousands of small businesses across every socio-economic, product and service category. The GAO Report finds that reverse auctions provide "high rate of awards to small businesses."[4] In fact, about 86% of FY12 acquisitions using reverse auctions—16,906 of 19,688—went to small businesses, in keeping with the FAR requirement that acquisitions of supplies or services with expected values of more than $3,000 but not over $150,000 are reserved for small businesses, with some exceptions.[5] These acquisitions accounted for $661 million (80%) of the dollar value of all reverse auction awards."[6] During FY12, Federal agencies awarded $1.03 billion to small businesses through FedBid, with 18% ($240 million) to VOSBs, including 14% ($181 million) to SDVOSBs. During FY13, the small business award volume number grew to $1.25 billion, with 27% ($333 million) to VOSBs, including 21% ($259 million) to SDVOSBs.

These statistics have been remarkably consistent year-over-year for more than a decade. FedBid attributes this to three primary attributes of the marketplace: i) relatively low dollar size of the buys, including an average buy size of $44,825 during the study timeframe of FY12, which means more reseller participation and reduced need for commercial financing; ii) ease of access – the opportunities are readily available and simply aggregated without access costs; and iii) ease of use – the marketplace is relatively simple and efficient to use.

FedBid is completely free for sellers to register and use and provides a central location for businesses to filter, search and bid on tens of thousands of solicitations from Federal, state and local and commercial buyers. Federal buyers are able to automatically post combined synopsis/solicitations to FedBizOpps as required by regulation, and FedBid proactively contacts sellers when opportunities arise, using seller-selected profile criteria to communicate complete, detailed information for each procurement. This approach minimizes seller resources required to pursue each opportunity and compete for business, increasing opportunity awareness while lowering sales costs. In addition, because the services are web-based, there is no software to load, and sellers need only Internet access and a browser to participate. Automated bidding and other time-saving features enable sellers to compete on multiple simultaneous opportunities with fewer resources and fewer costs.

b. FedBid's Impact on VHA's Small Business Utilization

As today's hearing focuses on use of reverse auctions by the VHA, it is notable that FedBid has had a materially positive impact on VHA's utilization of small businesses – particularly with respect to VHA purchases below the SAT of $150,000, which makes up the vast majority of VHA's purchases through FedBid. The chart, below, compares all VHA awards for purchases below the SAT with VHA awards for purchases below the SAT made using FedBid during FY12, which was the time period under review by GAO. The data shows that VHA's use of FedBid resulted in:

- A higher share of awards and dollars to small businesses, including VOSBs and SDVOSBs;
- Greater FSS utilization pursuant to agency policy; and
- Broader supplier utilization, with most awards to other than top 5% of suppliers.

Incidentally, the data for FY13 shows very similar results, albeit with a higher comparative percentage of awards and dollar volume through FedBid

[4] *Id.* at 5.

[5] FAR § 19.502–2(a) states each acquisition of supplies or services that has an anticipated dollar value exceeding $3,000, but not over $150,000 is reserved for small business concerns and shall be set aside for small business unless the contracting officer determines there is not a reasonable expectation of obtaining offers from two or more responsible small business concerns that are competitive in terms of market prices, quality, and delivery.

[6] GAO Report at 9.

FY12 Purchases by VHA $3,000-$150,000

Metric	All VHA Purchases as Reported in FPDS [7]	VHA Purchases Using FedBid
Total Number of Awards	**136,043**	**6,994**
Total Amount of Awards	**$2,747,165,200**	**$171,817,992**
Awards to top 5% of Suppliers (%)	**$1.73B (63%)**	**$81.83M (48%)**
FSS Contract Utilization (%)	**$854.6M (31%)**	**$78.80M (46%)**
• Large Business Volume (%)	$405.6M (47%)	$18.74M (24%)
• Small Business Volume (%)	$449.0M (55%)	$60.05M (76%)
• VOSB Volume (%)	$128.6M (15%)	$18.35M (23%)
• SDVOSB Volume (%)	$80.80M (10%)	12.15M (15%)
Non-FSS Contract Utilization (%)	**$1.89B (69%)**	**$93.02M (54%)**
• Large Business Volume (%)	$1.015B (54%)	$10.15M (11%)
• Small Business Volume (%)	$876.9M (46%)	$82.87M (89%)
• VOSB Volume (%)	$361.9M (19%)	$30.97M (33%)
• SDVOSB Volume (%)	$285.4M (15%)	$25.63M (28%)

[7] The Federal Procurement Data System (FPDS) data also includes purchases conducted using FedBid.

4. TRANSPARENCY, ACCOUNTABILITY AND CONTROL

Beyond the benefits of the reverse auction process, reverse auction platforms are data rich tools that can provide agencies with real-time controls over the purchasing process and comprehensive data that can be used to manage their organizations better and make smarter procurement decisions.

With respect to tactical operations, FedBid provides agency contracting officials and management with real-time access to all procurements utilizing the marketplace. Through the Supervisor Dashboard, agency management can review and manage each step of the purchasing process for every buy – before the buy is posted to the marketplace for competition, during the competitive process, after the buy closes but before award, and after award. The dashboard enables them to review and comment on, transfer, or take direct control of the buy. If there are policies related to contract hierarchies, set-aside preferences or other acquisition strategies, management can confirm that those are followed for each buy.

Whereas platform features help improve operations on the individual buy level, it is the data that can provide a significant impact on agency acquisition strategy. Not surprisingly, the basis for the GAO Report on use of reverse auctions is data provided by the reverse auction services provider, FedBid. In fact, the breadth and depth of the procurement data processed and provided through FedBid to agency customers provides those organizations with a tremendous resource by which they can analyze their spend – what they are buying, when and how they are buying it, from whom, for how much – down to the unit pricing of each line item. This type of centrally accessible granular information regarding agency spend is available nowhere else in government procurement. Notably, the GAO Report mentions that another agency using a different reverse auction platform was unable to provide the data necessary for reviewing its reverse auction activity because "the agency collected only summary level information . . . providing the data for each auction would require them to review all contract files to determine whether a reverse auction had

been used."[8] This lack of data access and reporting capability is not limited to a single agency and a specific platform; it simply reflects the normal state of informational limitations within the typical agency procurement environment.

In contrast, FedBid prepares and electronically distributes to customers weekly, monthly and/or annual reports summarizing and detailing procurement activities for the previous desired time period, including, but not limited to, all posted, awarded, and cancelled procurements with the date of action, total dollar amount, name of buyer including buying division, and for awarded buys, the name of selected seller, business size, contract vehicle utilized, and percentage savings based on a total target price set by the buyer. An example of a reporting deliverable is an Agency Operations Report, which provides a detailed purchase history (monthly, annual, and multi-year) of the purchasing activity of the agency, division and/or individual buyers. Standard data fields include: FedBid ID Number, Description, Contract Type, Internal Reference Number, Start Date, End Date, Target Price, Final Price, Selected Seller, Number of Bidders, Number of Bids, Number of No Bids, Socio-economic data, and Savings. FedBid also provides buyers with all acquisition related data necessary for addressing seller issues and disputes, including those involving bid protests, alternative dispute resolution or other legal action.

Reports themselves can be customized at the agency request, or agencies can consume raw data from FedBid and create their own reports. In either case, the available data can help agencies perform valuable analysis to determine the most effective acquisition scenarios for specific item types, the most advantageous timing for purchasing certain goods and services, whether the agency is meeting its socio-economic utilization goals, or whether a contract vehicle provides adequate competition for particular goods and/or services. That information can then inform agency action to adjust purchase timing, increase or adjust use of set-asides, or award additional contracts under a contract vehicle.

5. CONCLUSION

Reverse auctioning is not a cure-all for government procurement; rather, it is proven method for purchasing the types of commercial goods and simple services that Federal agencies use every day to support their operations. Its effectiveness as a procurement method is dependent on the circumstances of each purchase, and it should be approached with the same care and professionalism expected of any other government procurement. The FAR has laid out the both general principles and specific processes that apply not only to traditional procurement methods, but also to use of innovative methods such as online reverse auctions. With proper use of reverse auctions, procurement professionals can maximize competition and savings and increase small business utilization. And just as critically, agency management can use the comprehensive data from those reverse auctions to improve transparency of its procurement processes and actions, better gauge the effectiveness of its procurement strategies and practices, and craft specific means of improving agency performance.

Respectfully submitted,

Luther D. Tupponce
Chief Administrative Officer and General Counsel
FedBid, Inc.
8500 Leesburg Pike, 6th Floor
Vienna, VA 22182
703–738–6886

National Electrical Contractors Association (NECA)

The National Electrical Contractors Association (NECA) appreciates the opportunity to submit a statement for the record ahead of the joint hearing entitled "Contracting Away Accountability – Reverse Auctions in Federal Agency Acquisitions." NECA commends the Committees for holding a joint hearing conducting oversight over this important subject to examine the effects of this procurement tool and the negative effect its utilization will have in the procurement of construction services.

Over a decade ago, advances in high-speed internet computer technology led to the introductory use of a new method of construction contract bidding – the internet reverse auction. Under this technique bidders send relevant project data, specifications, projected construction timetables and price. Owners would ask bidders to

[8] *Id.* at 1.

later gather around computers at a set time and compete for work by further whittling down their bid against the other competitors. The lowest bid is posted for all bidders to see – but the name of the current lowest bidder is withheld. The bidding continues with additional rounds of bidding. After each round of bidding the new low price is posted for all bidders to see. This continues until the lowest price is reached, at which time the bidding is closed and the winner declared.

This scenario paints a clear picture of exactly why NECA and virtually every element of the construction industry has been united in its opposition to misguided attempts by federal agencies to treat construction as a commodity on grounds of efficiency or presumed cost savings—in particular, the use of internet reverse auctions for the procurement of construction services. Construction projects are not commercial commodities, mass-produced in a factory. The differences between even seemingly identical projects can be enormous.

We strongly urge the Department of Veterans Affairs, as well as all of the federal construction agencies, to refrain from using internet reverse auctions or any other procurement tool that would treat construction as a commercial commodity. In fact, we urge Congress and the Administration to revise the Federal Acquisition Regulation (FAR) to expressly prohibit the use of reverse auctions for the procurement of construction-related services. This change in procurement policy would clearly establish that construction is not a commercial item, or commodity, and that Federal agencies shall not have the authority to procure construction-related services by reverse auction.

Reverse Auctions Do Not Serve the Interests of Owners or Construction Contractors Well

Reverse auctions have proven to be an unreliable procurement tool for the selection of construction contractors, specialty contractors, subcontractors, and suppliers. Software vendors promoting reverse auctions have not presented persuasive evidence that reverse auctions generate savings in the procurement of construction or provide benefits of "best value" outweighing currently recognized selection procedures for construction contractors. However, industry experience demonstrates that reverse auctions seldom provide benefits comparable to currently recognized selection procedures for construction contractors.

As we have previously stated, the procurement of construction services cannot be treated like procurement of mass-produced commodities. Unfortunately, that is what reverse auctions accomplish. Every construction project and contract is unique and requires special knowledge, skill and training. Each project design and location is comprised of unique conditions that have to be met in a specific climate and location. Reverse auctions do not allow consideration of those variables.

Electrical contractors spend substantial time, money and effort in preparing their bids. The price they submit is not arbitrary, but based upon the best prices they have been able to obtain from any subcontractors and suppliers they may utilize and their best estimate of the price at which they can bring in a project and still make a reasonable profit. Reverse auctions do not allow for consideration of those very important differences.

For the owner, reverse auctions never guarantee the lowest price. Vendors claim that reverse auctions significantly reduce the cost of construction and save substantial amounts of time. In the context of construction, most of these claims have not been proven and the reverse auction processes do not lower the ultimate cost of construction. In reverse auctions, each bidder recognizes that he or she will have the option to provide successive bids as the auction progresses. As a result, a bidder has little incentive to offer its best and subsequently may never offer its lowest price. Ultimately, best-price sealed bidding is still the most effective way to obtain the highest quality construction at the lowest price. Sealed bidding ensures that competitors have only one opportunity to price the work, encouraging each bidder to present his or her best price.

Where price is not the sole determinant, owners increasingly have utilized processes focused on negotiation to expand communication between the owner and prospective contractors for the purpose of discussing selection criteria such as costs, past performance and unique needs. Unfortunately, reverse auctions do not allow for a contract to be awarded based on "best value," but on driving the price to an absolute minimum and awarding the contract to the lowest bidder. This is a poor use of taxpayers' money. Reverse auctions actually deprive taxpayers the full benefits of fair competition, quality construction and consideration of life-cycle costs. Reducing one's original bid price (as a contractor is forced to do when someone comes in with a lower bid during the reverse auction process) cheats the government by creating cost-value disparity in the finished product. Reducing a bid price requires cutting costs in the areas of materials and/or labor, which is significant in deter-

mining a structure's overall quality and value. Reverse auctions do not promote communication between the parties, they promote a dynamic in which parties repeatedly attempt to best each other's prices. As a result, reverse auctions do not offer owners a good way to evaluate non-price factors.

Reverse Auctions Upend Well Established Bidding Practices

Reverse auctions create an environment in which bid discipline is critical, yet difficult to maintain. The competitors have to deal with multiple rounds of bidding, all in quick succession. The process may move too quickly for competitors to accurately reassess either their costs or the way they would actually do the work. If competitors act rashly and bid imprudently, the results may be detrimental to everyone, including the owner. Imprudent bidding may lead to performance and financial problems for owners and successful bidders, which may have the effect of increasing the ultimate cost of construction as well as the cost of operating and maintaining the structure. Some contractors who have learned to "game" reverse auctions inflate their initial bids to allow room to move their price downward. Should other bidders do the same, owners may actually end up paying more than they would have under a sealed bid system. In fact, responsible estimating practices dissolve during the reverse auction process and drives out the most responsible bidders in favor of those who are willing to cut corners and/or squeeze subcontractors to get at a lower price.

It is clear that the sealed bidding process ensures that the successful bidder is both responsive and responsible. The sealed bid procurement process was established to ensure integrity in the award of construction contracts where price is the sole determinant. In a sealed bid, each bid is evaluated through the use of objective criteria that measure responsiveness of the bid to the owner's articulated requirements and the responsibility of the bidder and ensuring fairness and value for the owner. Reverse auctions ignore and upend this paradigm. The pressure and pace of the auction environment removes any assurance that initial and subsequent bids are responsive and material to the owner's articulated requirements. These auctions expose owners to the real possibility that they may award contracts to what would otherwise be non-responsive bidders. In addition, reverse auctions ignore the protections of the sealed bid procurement's laws, regulations and years of precedent that address these critical factors and ensure the integrity of the process.

Federal Policy Has Not Supported Reverse Auctions for Construction Services

While reverse auctions may demonstrate some value to the government in the purchase of commodities, no public or private studies have presented persuasive evidence that reverse auctions will generate savings in the procurement of construction when compared to currently recognized selection procedures for construction contractors. Upon the advent of the use of reverse auctions, the federal government took careful and decisive action to study this critical issue. First, the Office of Federal Procurement Policy issued a policy memorandum on July 3, 2003 recognizing that construction services cannot be equated to commodities or manufactured goods when it acknowledged, "new construction projects and complex alterations and repairs ... involve a high degree of variability." The policy went on to state unequivocally that "FAR Part 12, which addresses the acquisition of commercial items ... should rarely, if ever, be used for new construction acquisitions or non-routine alteration and repair services." Second, the Department of Defense tasked the U.S. Army Corps of Engineers (USACE) to examine the use of reverse auctions. A subsequent report issued by USACE in 2004 found that there was no proof that reverse auctions provide any significant or marginal edge in savings over the sealed bid process for construction services for the following reasons:

- There was no proof that a consistent, reliable and valid measurement method for projecting savings could be established from reverse auctioning;
- Absent any specific price history for an identical project under identical conditions, there was no practical way to measure or compare any projected savings by reverse auctions over sealed bidding; and,
- There was no proof reverse auctions provided any significant or marginal savings in comparison to the government estimate.

Finally, NECA argues that the use of reverse auctions with respect to construction services may violate procurement laws at the federal and state level. The FAR, as well as other current procurement statutes reflect a clear policy of not disclosing contractor price information. This is especially true once one realizes that price disclosure is a core characteristic of the reverse auction process and violates current federal procurement law.

Concluding Remarks

It is for these reasons we reiterate our recommendation that Congress and the Administration take action and implement what we believe is an appropriate and responsible solution that will meet the acquisition needs of the federal government. The federal agencies need flexibility in the acquisition process and should have all tools available to them to allow for optimized savings. While reverse auctions can be a tool in the acquisition toolbox for mass produced commodities, it is clear that they should not be utilized for the acquisition of construction services. Congress and the Administration should finally codify this policy recommendation and we hope you will support this change. Lastly, we appreciate the time the Committees have taken to examine this complex issue and offer our assistance and expertise to help this process move forward.

COFPAES

Since its inception in 1966, the Council on Federal Procurement of Architectural & Engineering Services (COFPAES) has provided the design community with a common voice on federal procurement law and regulations. COFPAES continues to serve the American public as a well-known and respected forum for the consideration of policy and operational changes in the selection procedures for design professionals. Because of its emphasis on professionalism in the procurement process, COFPAES assists the federal government in assuring that the design of projects to satisfy the building, infrastructure, resource, and program management needs of our Nation are conducted in an efficient and quality manner. Throughout its history, COFPAES has focused on ensuring quality and competence in the procurement of professional architectural and engineering (A/E) services, including surveying and mapping services. COFPAES serves the American public by assisting Congress and federal agencies with policies to ensure that projects to satisfy the building, infrastructure, resource, defense, and security needs of the Nation are conducted in an efficient and quality manner. The member organizations of COFPAES are the American Institute of Architects, American Society of Civil Engineers, MAPPS - the association of private geospatial firms, National Society of Professional Engineers, and National Society of Professional Surveyors.

COFPAES is pleased to submit this statement for the record of the December 11, 2013 hearing of the House Committee on Small Business, Subcommittee on Contracting and Workforce, on "Contracting Away Accountability-Reverse Auctions in Federal Agency Acquisitions".

Over the past decade or more, the federal government's in-house A/E capability has been reduced. Retirements, attrition, recruitment and shifting priorities have all contributed to changes in the federal personnel structure that has resulted in fewer federal employees trained, qualified and actually engaged in evaluating, awarding and managing Federal A/E contracts. Notwithstanding this workforce reduction, the federal government's demand and expenditures for A/E services has remained steady or in some cases increased.

The loss of an A/E acquisition workforce has caused a number of undesirable trends in A/E procurement. Federal contracts for A/E services have become larger in dollar value, longer in duration, bundled with other services, and less competitive. The advantages of QBS are being diminished. Moreover, given that the private A/E market is overwhelmingly comprised of small businesses, the trend has resulted in the creation of a virtual oligopoly. There are now fewer A/E contracts. They are now for longer time periods, with some potentially lasting 15 years when options are exercised. The use of design-build procedures, once reserved for rare and unique projects, has become more common. And the advent of GSA Federal Supply Schedules for services has resulted in rampant abuse of such schedule contracts in violation of the QBS law. And the rise of reverse auctions has threatened the public health, welfare and safety when applied to services that are considered A/E services under the Brooks Act 940 U.S.C. 1101 et. seq. and part 36.6 of the Federal Acquisition Regulation (FAR). None of these trends favor the government, and the taxpayer, and they certainly put small business A/E firms at a disadvantage.

The reason for this trend is simple - - supply and demand - - within the federal government. Fewer government A/E professionals experienced in acquisition are responsible for awarding more work. The decline in the federal A/E acquisition workforce led Congress to enact section 1414 of Public Law 108–136 and a provision in the 2008 National Defense Authorization Act, - 41 USC 1704(h).

For purposes of federal procurement, A/E services are defined in federal law (40 U.S.C. 1101) as:

(A) professional services of an architectural or engineering nature, as defined by State law, if applicable, which are required to be performed or approved by a person licensed, registered, or certified to provide such services as described in this paragraph;

(B) professional services of an architectural or engineering nature performed by contract that are associated with research, planning, development, design, construction, alteration, or repair of real property; and

(C) such other professional services of an architectural or engineering nature, or incidental services, which members of the architectural and engineering professions (and individuals in their employ) may logically or justifiably perform, including studies, investigations, surveying and mapping, tests, evaluations, consultations, comprehensive planning, program management, conceptual designs, plans and specifications, value engineering, construction phase services, soils engineering, drawing reviews, preparation of operating and maintenance manuals, and other related services.

Unlike many products, for which the government awards contracts to the lowest bidder, or other services, which are awarded based on the "best value", A/E services have long been recognized as having a significant impact on public health, welfare and safety. Moreover, A/E services amount to 1/10th of 1 percent of the life cycle cost of a project or program, but the quality of the A/E services determines the price and efficiency of the other 99.9 percent. As a result, Congress has long recognized the efficiency and economy of selecting firms for A/E services "on the basis of demonstrated competence and qualification for the type of professional services required", and negotiating a fee with the most qualified firm only after the firm's credentials have been established. This process, which is commonly known as qualifications based selection, or QBS, is codified in 40 U.S.C. 1101 et.seq. and is implemented in the Federal Acquisition Regulation in 48 CFR 36.6. The definition in the FAR closely follows the statutory definition above and provides further clarification of the application of QBS to surveying and mapping, in subpart 36.601–4:

(a) Contracting officers should consider the following services to be "architect-engineer services" subject to the procedures of this subpart:

(1) Professional services of an architectural or engineering nature, as defined by applicable State law, which the State law requires to be performed or approved by a registered architect or engineer.

(2) Professional services of an architectural or engineering nature associated with design or construction of real property.

(3) Other professional services of an architectural or engineering nature or services incidental thereto (including studies, investigations, surveying and mapping, tests, evaluations, consultations, comprehensive planning, program management, conceptual designs, plans and specifications, value engineering, construction phase services, soils engineering, drawing reviews, preparation of operating and maintenance manuals and other related services) that logically or justifiably require performance by registered architects or engineers or their employees.

(4) Professional surveying and mapping services of an architectural or engineering nature. Surveying is considered to be an architectural and engineering service and shall be procured pursuant to section 36.601 from registered surveyors or architects and engineers. Mapping associated with the research, planning, development, design, construction, or alteration of real property is considered to be an architectural and engineering service and is to be procured pursuant to section 36.601.

COFPAES is deeply concerned that reverse auctions have been attempted by federal agencies. We know of three instances in which such a process, which COFPAES believes to be in violation of the Brooks Act, was attempted.

In once such instance, Solicitation Number 0040073949, issued on April 5, 2013, the U.S. Geological Survey, Department of the Interior, announced its intention "to conduct an online competitive reverse auction to be facilitated by the third-party reverse auction provider, FedBid, Inc." This reverse auction was for an aerial geophysical survey, using the standard NAICS code (541360), which the federal government defines as "Geophysical Surveying and Mapping Services. This industry comprises establishments primarily engaged in gathering, interpreting, and mapping geophysical data. Establishments in this industry often specialize in locating and measuring the extent of subsurface resources, such as oil, gas, and minerals, but they may also conduct surveys for engineering purposes. Establishments in this industry use a variety of surveying techniques depending on the purpose of the sur-

vey, including magnetic surveys, gravity surveys, seismic surveys, or electrical and electromagnetic surveys."

The solicitation was set aside for small business, with a small business size standard of $14 million. These are the NAICS Code and size standard for such surveying and mapping services ordinarily subject to the Brooks Act. The Solicitation was released on April 5 with the reverse auction to be conducted on April 9. For a professional service such as a geophysical survey, this is insufficient time for a firm, particularly a small business, to investigate, analyze and develop a proposal.

The scope of work is consistent to the requirements of the Brooks Act. It required the aerial geophysical survey, including GPS elevations, precise XYZ positions of observed field measurements, and positions computed using the WGS–84 datum and the NAD27 datum. This is clearly a surveying service.

This procurement was executed in such secrecy and haste that COFPAES nor its member organizations were aware of it in time to lodge a protest or attempt to advise the contracting agency of its violation of the law.

Solicitation G13PS00201 was issued by the USGS in August of 2013 for 4-band (true color and near infrared) digital orthoimagery at 0.05 meter ground sample distance, and stereo imagery for select portions of the Edwin B. Forsythe National Wildlife Refuge in coastal New Jersey. This included aerial photography, airborne GPS, rectified image maps, and elevation data. This is clearly a professional surveying and mapping service, yet was proposed to be carried out by FedBid, Inc. as a reverse auction. Fortunately, the public was protected as MAPPS, a COFPAES member organization, contacted the USGS officials responsible for such services and the auction was canceled. The work was assigned as a task order to a firm already under a USGS Geospatial Products and Services (GPSC) contract, a Brooks Act-compliant ID/IIQ contract.

On December 28, 2012, the U.S. Army, Fort Benning, Georgia, issued Solicitation Number: 001025774 for a reverse auction for digital orthophoto mapping, through FedBid, Inc. The response date was January 11, 2013. Officials at Fort Benning were advised by MAPPS that the scope of work was for engineering-related surveying and mapping services as defined by the Brooks Act, the FAR, Corps of Engineers regulations, and applicable Comptroller General decisions. Moreover, such services are the practice of land surveying, as defined by the State of Georgia, § 43–15–2, Code of Georgia, requiring compliance with 40 USC 1101 and FAR 36.6, requiring performance by a Georgia licensed surveyor. Finally, any Georgia licensed surveyor who responds to the solicitation with a price quote would be in violation of state conduct regulation 180–6-.06.1. The Army did not require a surveyor licensed in Georgia.

COFPAES is deeply concerned about this flagrant disregard for the law. The public health, welfare, and safety are jeopardized when reverse auctions are used in lieu of the statutory requirements of the Brooks Act and the FAR, as well as when state licensing law is ignored. Moreover, such processes put law abiding small business architecture, engineering, surveying and mapping firms at a competitive disadvantage.

COFPAES looks forward to working with the Committee on Small Business, other committees of Congress with jurisdiction over this matter, and the relevant federal agencies to assure that reverse auctions are no longer inappropriately applied to A/E services.

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