

Chapter highlights

Purpose: This chapter contains policies and guidelines pertaining to the acquisition of IT goods through the use of public, online and reverse auctions.

Key points:

- The purchase of IT goods and nonprofessional services from a public auction sale shall be permitted by any authority, department, agency or non-exempt institution of higher education if approved in advance by the CIO.
- A reverse auction is a procurement method where suppliers are invited to bid on specified goods or nonprofessional services through real-time electronic bidding, with the award being made to the lowest responsive and responsible supplier.

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19.0 Introduction

The policies and guidelines in this chapter are applicable to procuring IT goods and services utilizing public, online and reverse auctions. Pursuant to Virginia Code §2.2-4303, agencies may purchase IT goods from public auctions and online public auctions upon a determination made in advance by the agency that the purchase of IT goods from a public auction sale is in the best interest of the public.

The purchase of IT goods and nonprofessional services from a public auction or reverse auction sale shall be permitted by any authority, department, agency or non-exempt institution of higher education if approved in advance by the CIO.

19.1 Public and online auctions

When agencies look at the price of IT auction items, the savings may seem substantial; however, often the reasons for the low price(s) at auctions are a result of disadvantages such as:

- Limited warranty or no warranty,
- No return policy,
- Advance payment requirements,
- Items of uncertain history or conditions,
- All auction items are purchased on an "as is/where is" basis.

Usually, a day or two before an auction, the auction house (if a public auction) or an auction website will set aside the day(s) for review and evaluation of the IT goods that will be auctioned. Agencies should take advantage of this pre-auction inspection period to confirm that what appears to be a good value online or in a catalog is really

as represented. This preview period can avoid costly technology mistakes.

Before bidding, agencies should become familiar with the rules and practices of an auction house or online auction site. Buyers should determine what protections the auction site offers auction purchasers. Buyers should make certain that the auction house/auction site offers some protection against purchasing defective or erroneously described merchandise. All agencies should be keenly aware of exactly which technology items they are bidding on during the auction. Look for words like “refurbished,” “close out,” “discontinued” or “off-brand” to get a better idea of the condition of the technology item. Buyers should try to determine the relative value of a technology item before their bids are placed.

Agencies should avoid doing business with sellers that they cannot identify or sellers who try to lure buyers off regulated auction sites with promises of a better deal. Buyers should check on the seller’s return policy. Make sure that it is possible to return an item for a full refund if the agency is not satisfied with it. Determine if the agency will be required to pay shipping costs or a restocking fee.

When purchasing technology through an online auction or auction house, buyers should consider whether the item comes with a warranty and whether follow-up service is available if needed. Buyers should document and understand fully all warranties and other protections offered by the seller or auctioneer. Agencies should decide if they are willing to forfeit support, warranties and maintenance services before placing a bid.

When bidding, buyers should establish a top price for the technology item desired and stick to it. This will enable the agency to get a fair price and protect it from “shill bidding.” (Shill bidding is when fraudulent sellers or their partners, known as “shills,” bid on sellers’ items to drive up the price.) Buyers should not bid on any item that they do not intend to buy. If the agency is the highest bidder, the agency is obligated to follow through with the transaction. Remember to save all transaction information regarding any technology auction purchase.

19.2 Reverse auctions

19.2.1 General Information about reverse auctions

A reverse auction is a procurement method where suppliers are invited to bid on specified goods or nonprofessional services through real-time electronic bidding, with the award being made to the lowest responsive and responsible supplier. Suppliers must be prequalified to participate in a reverse auction. During the bidding process, suppliers’ prices are revealed, and suppliers have the opportunity to modify their bid prices for the duration of the time period established for bid opening. (Refer to Virginia Code § 2.2-4301.)

In a reverse auction, something is purchased from the lowest responsive and responsible supplier (which is the “reverse” of a normal auction, wherein something is sold to the highest bidder). A reverse auction is typically conducted via the Internet (usually through an e-procurement site) where prequalified suppliers anonymously bid against each other for an item or group of items for which an agency has a requirement. Bidding takes place at a specified date and time and continues for a specified amount of time to allow suppliers to reduce their bids during the auction period until no more bids are accepted.

Reverse auctions can allow agencies to minimize the cost of IT goods and services purchased while maximizing the value received. Reverse auctions provide an unbiased method to procure IT as it avoids the appearance of unethical or compromising practices in relationships, actions and communications. Reverse auctions also provide benefits through automating the sourcing process and increasing the agency’s purchasing efficiency.

To begin the reverse auction process, an agency must post a procurement opportunity for suppliers to qualify to participate in the reverse auction event. Suppliers will submit a summary of their products and/or services as well as their qualifications without prices. This prescreening of suppliers is done carefully to ensure that the agency does not contract with irresponsible suppliers offering lower quality products. Suppliers who prequalify are invited to participate in the reverse auction event. Suppliers who were not selected to participate in the reverse auction should be notified by the purchasing agency. The selected suppliers will be contacted and trained on set-up and use of the selected auction tool.

During the course of the auction, suppliers submit progressively lower prices electronically until the lowest bid is

submitted. After the lowest price is obtained, the agency reviews the suppliers' submittals for responsibility, starting with the supplier who submitted the lowest price until the lowest responsible supplier is selected for award.

The table below shows the primary differences between traditional and reverse auctions.

Traditional auction	Reverse auction
Item(s) offered for sale	Items required to be purchased
Multiple buyers compete for the purchase	Multiple suppliers compete for the sale
Price is driven up	Price is driven down

19.2.2 Benefits of reverse auctions

Reverse auctions appeal to buyers for many reasons, including:

- Buyers may realize significant price reductions. Reported price reductions range from five percent to 90 percent.
- Buyers perceive reverse auctions to be a much faster way to get to the final, best price from a qualified group of suppliers.
- The sourcing and supplier selection process becomes more transparent, reducing the influence of personal relationships and sales force efforts.
- Reverse auction software is inexpensive to install and easy to use.
- The Internet provides a low-cost, easily accessible way to connect a buyer with multiple qualified suppliers.
- Spending analysis programs aggregate purchasing volume into quantities that make participation attractive to many suppliers.

Reverse auctions complement strategic procurement strategies and have been shown to effectively leverage volume purchasing and drive real IT savings. Reverse auctions work best when they are used to procure the following IT goods and services:

- Commercial technology commodity buys with well-defined specifications and universally accepted standards.
- Bulk technology or telecommunications purchases.
- Items of definite quantity and definite delivery.
- Technology and services which have a well-qualified and established base of suppliers.
- Technology purchases which have big-dollar volume actions for individual customers.
- Aggregated small buys for multiple users.

19.2.3 Guidelines for using reverse auctions

When considering the use of a reverse auction, agencies should carefully consider the following guidelines:

- Think beyond price. While buyers may feel good about getting the lowest price, ultimately it is the greatest value that matters. Price is only one element of the buyer's value equation. Buyers should also consider quality, reliability and supplier's value-added services. These considerations should be built into the prequalification criteria and specifications.
- Use reverse auctions only when appropriate. Reverse auctions are appropriate for IT transactional situations characterized by one-time purchases, typically for common commodity products available from multiple suppliers. Reverse auctions are generally not appropriate for sourcing of differentiated parts and components where suppliers may need to have specialized capabilities and few suppliers can meet quality and reliability standards.
- Understand the hidden costs of reverse auctions. Savings from the first few reverse auctions an agency conducts can overstate the eventual savings. There is a big difference between the savings measured at the time the auction closes and the savings measured at the end of the transaction. Buyers should account for both direct and indirect losses that may arise during the course of the

procurement cycle. Pilot auction programs may project that the agency will achieve much higher savings because suppliers may engage in “loss-leader pricing” to get the buyer’s business. These prices may not be sustainable because suppliers will look for opportunities to raise prices or add hidden costs once they have won the business.

- Adequate preparation is required. Agencies which do not have sufficient time to detail their specifications and develop their prequalification criteria should think twice before utilizing reverse auctions. The specifications and prequalification of suppliers protects the agency by only allowing suppliers who can provide the exact product needed to participate in the reverse auction.
- There is insufficient competition among suppliers. Reverse auctions only work in highly competitive markets where there are multiple suppliers who can provide the same commodity.
- Agencies should require a clear and concise statement of requirements for all products or services being procured through a reverse auction.
- Agencies may require that all auction sellers submit initial price proposals.
- Suppliers’ identities must be protected.
- Suppliers must give permission before their prices may be disclosed.

19.2.4 “Best value” reverse auctions

“Best value” reverse auctions, when properly utilized, can result in agencies being able to procure a better overall technology value for certain IT commodities. Agencies can realize technology cost savings through “real time” competition during the course of a reverse auction.

Best value technology procurements place importance on factors other than price, such as total cost of ownership (TCO). The agency may establish source selection criteria in advance of the reverse auction with potential suppliers. By doing so, the agency can be assured of being able to efficiently evaluate the bids received to determine which bid represents the “best value” for the Commonwealth. In utilizing “best value” reverse auctions, agencies should follow these guidelines:

- “Best value” source selection and evaluation criteria may be established with input from potential qualified suppliers in advance of the reverse auction.
- Source selection criteria will be made available to all prequalified or potential suppliers prior to the auction.
- Potential qualified suppliers will provide standardized offerings electronically in advance of the reverse auction for all factors other than price.
- Agencies will evaluate factors other than price prior to the reverse auction.
- The agency then performs an integrated evaluation of both price and factors other than price to quantify which supplier is offering the best value.

19.2.5 “Lowest price” reverse auctions

A “lowest price” reverse auction may be utilized to achieve procurement savings for general technology commodities, where there is little product and supplier differentiation and where product price is the only selection criterion. “Lowest price” reverse auctions should be utilized when:

- There is little concern about production specifications or the performance history of the qualified suppliers participating in the auction.
- Comparable bids are expected to be tendered from many suppliers.
- A complete invitation to qualify (IFQ) has been performed which prequalified suppliers based on ability to deliver known technology product.

Potential suppliers are invited to bid on specified technology goods and services through real-time electronic bidding. The IFQ is a solicitation process similar to a request for bid or request for proposal, through which potential suppliers are prequalified to participate in a reverse auction. Only those suppliers that meet the requirements of the IFQ and agree to the terms and conditions contained therein are invited to participate in the reverse auction. Some terms and conditions may be negotiated before the invitations to qualify are issued to potential suppliers.

In a low price reverse auction suppliers may be given 10 calendar days' notice of reverse auctioning opportunities through eVA. Potential suppliers will receive detailed specifications and requirements, along with the terms and conditions relevant to the technology goods or services being purchased. If an IFQ is utilized, the agency should notify responding suppliers as to whether they have met the qualifications and criteria to be prequalified to participate in the reverse auction. Names of those suppliers that have been invited to or prequalified for the reverse auction will not be disclosed until after the reverse auction has occurred.

19.2.6 Reverse auction terms and conditions

Contractual terms and conditions will be defined up front with reverse auctioning opportunities. If there is needed negotiation on a particular term and condition, such negotiation will include all potential suppliers and will be finalized before the reverse auctioning opportunity solicitation is finalized. Suppliers must agree to the reverse auction solicitation's finalized terms and conditions before they will be eligible to participate in the reverse auction. Clarifications, negotiations, and acceptance of all specifications, requirements, terms and conditions, etc., will occur before the agency invites a supplier to participate in a reverse auction event. No changes to the specifications or terms and conditions will be allowed after bidding if the changes in a submitted bid would have rendered the bid unresponsive.

19.2.7 The reverse auction schedule

The reverse auction will run for a set duration. The auction duration may be extended based on a low price entered in the last minute of the auction. A minimum price reduction will be required to extend the auction. Agencies may, utilize a "minimum bid step" wherein each successive bid must differ from the previous bid by an amount known as a minimum bid step. For example, a further reduction of a certain percentage amount or greater in price is required to extend the auction period. The minimum bid step amount will be determined by the agency in advance of the auction and may be different depending on what is being auctioned. In most cases, the minimum bid step will be an amount less than ("bid decrement") the previous bid. The minimum bid step will be included in the posted reverse auction solicitation. However, in some cases, such as when bids are given as a percent off manufacturer's list price, the minimum bid step will be an amount greater than ("bid increment") the previous bid (e.g., 15 percent off is a better price than 10 percent off).

Agencies may also utilize an "extension activation period" (EAP) during its reverse auction procurements. The EAP is defined as the number of minutes before the end of an auction, during which, if a bid is received, the agency may choose to extend the auction by a pre- defined number of additional minutes ("the extension"). For example, if the auction parameters are EAP for three minutes, Extension for five minutes, if a bid is placed within the last three minutes of an auction, the auction would be extended for an additional number of minutes. This process would continue until no more bids were received.

The award will be made to the lowest responsive and responsible supplier immediately after the auction is completed. The award will be posted on eVA for a minimum of ten (10) calendar days. There is no mandatory public opening of the IFQ responses if an IFQ is held prior to the reverse auctioning event. There is also no mandatory public viewing of the reverse auction event. However, IFQ responses and reverse auction logs are considered public record. Upon request, they will be made available to the public after an award has been made.

Clarifications, negotiations, and acceptance of all specifications, requirements, terms and conditions, etc., will occur before the supplier is invited to participate in a reverse auction event. After the auction, the agency will permit such changes only with the limitation that the change(s) do not alter the scope or content of the original reverse auction solicitation to a degree that will affect the justification that was used to eliminate other industry partners from being included in the reverse auction. Changes to the specifications or terms and conditions will not be accepted after bidding if those changes in a submitted bid would have rendered the bid unresponsive.

