January 5, 2001

VIA ELECTRONIC MAIL & HAND DELIVERY

General Services Administration
FAR Secretariat (MVRS)
1800 F Street, N.W.
Room 4035
Washington, D.C. 20405

Attn: Ms. Laurie Duarte

Re: Reverse Auction Notice

Dear Ms. Duarte:

On behalf of the Section of Public Contract Law of the American Bar Association (“the Section”), I am submitting comments in response to the above-referenced matter. The Section consists of attorneys and associated professionals in private practice, industry, and Government service. The Section’s governing Council and substantive committees contain a balance of members representing these three segments to ensure that all points of view are considered. In this manner, the Section seeks to improve the process of public contracting for needed supplies, services, and public works.

The Section is authorized to submit comments on acquisition regulations under special authority granted by the American Bar Association Board of Governors. The views expressed herein have not been approved by the House of Delegates or the Board of Governors and, therefore, should not be construed as representing the policy of the American Bar Association.  

In preparing these comments, the Section has been guided by its long-standing position that procurement practices and procedures should be predictable, that both parties to a procurement contract should be fully informed of the terms and conditions of their relationship, and that fundamental fairness requires a commercially reasonable allocation of risk in the contract formation process.

I. NEED FOR GUIDANCE

The Section believes that there is a need for limited guidance in the area of auctions and reverse auctions. In order to enhance predictability and clarity in contract formation, such guidance should be included in the Federal Acquisition Regulation (“FAR”), and Government procurement officials should receive adequate training on the appropriate use of auction techniques. The Section recommends the following guidance be included in the FAR:

A. An explicit statement that auctions and reverse auctions are permitted provided that they are conducted in accordance with all applicable laws and regulations and do not otherwise compromise the integrity of the procurement process.

Until the FAR Part 15 re-write three years ago, the FAR generally prohibited auctioning. In particular, the use of “auction techniques” such as “[i]ndicating to an offeror a cost or price that it must meet to obtain further consideration; . . . [a]dvising an offeror of its price standing relative to another offeror; . . . [and] [o]therwise furnishing information about another offeror’s price,” was forbidden. See, e.g., FAR 15.610(e)(2) (1996). The revised Part 15 removed this language, suggesting that use of these auction techniques is no longer prohibited.
This conclusion is reinforced by FAR 1.102(d), which provides that “if a specific strategy, practice, policy or procedure is in the best interest of the Government and is not addressed in the FAR, nor prohibited by law (statute or case law), Executive order or other regulation, then the strategy, practice, policy or procedure is a permissible exercise of authority.” On that basis, a reasonable argument may be made that a Government agency may now use auction techniques in connection with its purchase of goods and services, provided that it determines such use to be in the best interests of the Government.

Combined with other changes that were implemented as part of the Part 15 rewrite, including those that expanded the list of permissible communications between the Government and its offerors during the proposal and evaluation process, elimination of the prohibition on auction techniques was particularly appropriate. By eliminating the prohibition, the parties were relieved of a concrete restriction on their communications and discussions. These changes, however, were all implemented prior to the development of electronic reverse auctions.

Because the use of electronic reverse auctions is so new, involving different types of communications among the Government and its offerors, and because the FAR amendment removing the prohibition on use of auction techniques was written before development of this new technique, the Section recommends that the FAR be amended to provide specifically that auctions and reverse auctions are permitted, provided that they are conducted in a manner that complies with all applicable laws and regulations and that does not otherwise compromise the integrity of the procurement process.

B. Without precluding the use of reverse auctions in other situations, a statement that reverse-auction techniques may be used for easily identifiable, commodity-type items or simple services, where there are few if any distinguishing characteristics and where price is the determining factor.

The Section believes that reverse auctions can be used effectively for easily identifiable, commodity-type items or simple services, where the items being procured have few if any distinguishing characteristics and where price is the determining factor. Adding a statement to that effect to the FAR will provide Contracting Officers and contractors with assurance that, in these circumstances, their use of this procurement technique is fully compliant with the law.

Nevertheless, because reverse auctions are new and evolving, there are justifiable concerns about their potential impact on the integrity of the procurement process. Use of reverse-auction techniques in procurements involving goods or services other than simple commodities, where requirements or specifications are unique or more complex, and where Contracting Officers must exercise judgment in the selection process through price/technical tradeoffs or best-value analysis, may require more detailed, specific guidance.

C. A statement that solicitations in which reverse-auction techniques will be utilized must provide adequate notice to potential offerors regarding the procedures to be used for the reverse auction, including a detailed discussion of the logistics, timing, and communication requirements for the event.

Auctions and reverse auctions can be and are conducted using a wide variety of procedures. Contractors participating in a reverse auction with one agency may find the procedures materially different from those used by another agency -- even though both types of procedures qualify as "reverse auctions". Agencies should be required to clearly and prominently spell out, in each solicitation, the precise procedures that will be used in connection with the reverse auction.

II. TOPICS FOR COVERAGE

The Section recommends that the following topics be considered as issues to be addressed through additions, deletions, or clarifications in the FAR.

- **Procurement Integrity Act**

  The Procurement Integrity Act provides that procurement officials, as defined in the Act, “shall not, other than as provided by law, knowingly disclose contractor bid or proposal information or source selection information before award of a contract to which the information relates.” 41 U.S.C. § 423(a)(1) - (2) (2000). See also FAR 3.104-4(a). The Act also includes various “savings provisions,” including a provision permitting disclosure pursuant to applicable agency regulations or procedures and a provision permitting disclosure by the offeror. 41 U.S.C. § 423(h)(1) - (2) (2000). The FAR reflects these “savings provisions” in FAR 15.306(e)(3), which allows a Contracting Officers to disclose an offeror’s price with the offeror’s permission (i.e., where the disclosure is voluntary).
In reverse auctions conducted to date, potential offerors have expressly agreed to disclosure of their pricing in order to participate in the procurement. It appears, however, that they would have been precluded from participating if they had refused, so that the effectiveness and "voluntariness" of their consent may be open to question (i.e., the savings provisions of the Procurement Integrity Act may not provide a statutory safe harbor).[2]

Moreover, there may be legitimate policy concerns in this area. In an analogous situation several years ago, the Department of Defense ("DoD") attempted to require offerors to waive their rights to initiate bid protests in order to participate in certain procurements. The DoD ultimately abandoned that requirement, however, on grounds that it was not in the best interests of either the Government or its contractors.

FAR guidance in this area -- or perhaps even amendments to the Procurement Integrity Act -- would eliminate these ambiguities and provide both contractors and the Government with more predictability as the use of reverse-auction techniques is expanded.

- **Certificate of Independent Price Determination**

  The Certificate of Independent Price Determination at FAR 52.203-2 addresses disclosure of pricing information by an offeror. As that certification is presently written, in a reverse-auction situation in which disclosure is required, the offeror will not be able to sign the certification, but must instead provide an explanation as permitted by subsection (d).

  The Section recommends promulgation of an official "Alternate 1" version of FAR 52.203-2 and the certificate contained therein, to be used in solicitations that contemplate reverse auctions. Such an alternate would be useful and would avoid situations in which contractors inadvertently fail to provide the written explanations.

- **Mistakes**

  The FAR currently provides specific guidance on how contractors can prove mistakes in their bids and offers and what relief may be available. It is not clear, however, that mistakes in reverse auctions fit neatly within this scheme. In particular, proof of an "intended" bid could be problematic.

  Revisions to the FAR may be necessary to either (a) address the peculiar nature of mistakes in the context of reverse auctions, or (b) declare that the Government will not entertain claims of mistakes in these circumstances.

- **Pricing Differentials**

  Certain socio-economic programs require application of a pricing differential to some proposals. Current technology permits these mandatory pricing differentials to be factored into prices in “real time” during a reverse auction through instantaneous application of an algorithm, so that all offerors see the "true" prices in real time. This may or may not be regarded as a distortion of the competitive pricing process, but the manner in which this issue is to be handled should be addressed in the FAR to avoid lack of uniformity among the agencies and possible confusion among offerors.

- **The “Winner’s Curse”**

  The Section is aware of trade literature describing the potential for the so-called "winner's curse" to become an issue in electronic auctions and reverse auctions. See, e.g., Wald, The Auction Model: How the Public Sector Can Leverage the Power of E-Commerce Through Dynamic Pricing, The PricewaterhouseCoopers Endowment for The Business of Government (October 2000), at 15-18. The winner's curse occurs when winning bidders find that, in the heat of a competitive auction being conducted in real time, they have gone too far in attempting to secure or retain the buyer's business. *Id.* at 18.

  The FAR clearly discourages “buying-in” to a contract -- that is, underbidding with the intent of raising the contract price later or securing a follow-on contract at an artificially higher price. See FAR 3.501. Nevertheless, simply underbidding a contract is not prohibited and, in fact, many contractors routinely reduce their margins or bid at a loss for sound business reasons. The Section does not believe that this practice should be limited or discouraged. Contracting Officers are nevertheless required to obtain goods and services at "fair and reasonable prices." FAR 15.402(a). In light of the potential for the "winner's curse" and the unintended difficulties that it may engender for both contractors and the
Government, especially the potential impact on the industrial base, it may be appropriate for the FAR to address the concept of fair and reasonable prices in the context of reverse auctions.

The Section appreciates the opportunity to submit these comments and is available to provide additional information or assistance as you may require.

Sincerely,

Gregory A. Smith
Chair, Section of Public Contract Law

cc: Norman R. Thorpe
Mary Ellen Coster Williams
Herbert J. Bell, Jr.
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David A. Churchill
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Electronic Commerce Committee
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[1] Mary Ellen Coster Williams, an Officer of the Public Contract Law Section, did not participate in the Section’s consideration of these comments, and she abstained from voting to approve and send this letter.

[2] Disclosure of pricing information as a condition of participation may also implicate reverse FOIA issues, where the question of whether information has been "voluntarily" disclosed is critical. See McDonnell Douglas Corp. v. NASA, 180 F.3d 303 (D.C.Cir. 1999).