Reverse Auctions in the Public Sector

Kevin Burke, Director
Trade Interchange
What we will cover

- An introduction to Trade Interchange
- What are reverse auctions (RAs)?
- Emergence of RAs
- Prudent usage
- Its not just about price
- Actual examples
An introduction to Trade Interchange

- A specialist provider of reverse auction services
  - Fixed fee, full practical guidance and support service

- Established in 2000 in the UK
  - Now in Australia

- Experience of 1,000+ auctions
  - Everything from kidney beans to MRI scanners

- Proven, reliable web based software platform
  - Now in it’s 5th major iteration
“For needles and syringes, we have up to 80% swings in prices between hospitals”

Dennis O’Keefe, CEO, Health Purchasing Victoria
What are reverse auctions (RAs)?

Actual bid chart – Toner cartridges

- Each coloured line is a supplier (9 in this auction)
- Extension period. Triggered by new leading bid
- Sealed bid stage (Optional)
- Note duration of 30 minutes (typical)
Emergence of RAs

- GE Manual Reverse Auction
- US Law change. ‘Auctions’ not prohibited in PS
- First PS Reverse Auctions in US
- EU Directive. ‘eAuctions’ sanctioned in PS

1994: Development of first on-line reverse auctions
1997: US Commercial adoption of reverse auctions
2000: US public sector adoption of reverse auctions. European commercial adoption
2004: EU public sector adoption of reverse auctions. Widespread commercial usage US & EU
2005: In UK, 33% of local councils Using RAs
2007:
Emergence of RAs

The auctions you conducted removed any doubt that may have existed that reverse auctions are an essential component of any cost effective Procurement Service.’
Performance feedback: Gabe Furlan, NSW Health Procurement

Total identified savings were $1.6 m (25%) on a baseline spend of $6.5 m. This process allowed HPV to efficiently deal with a larger field of quality suppliers and achieve the best possible price without having to compromise on quality’
HPV reverse auction case study

I’d vouch for their probity and transparency. I’m keen to pursue them and expand the number of items.”
Steve Moro, Director, Strategic Procurement Unit, SA Dept of Health

Our successful pilot proved that there is an immense opportunity at HPV ….This is a technique we will definitely continue to use’
Dennis O’Keefe – CEO Health Procurement Victoria
Prudent Usage

- High Importance / risk
  - Got to do it right
  - Business Critical

- Low Importance / risk
  - Systematise
  - Reverse Auction Territory

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Three Questions

1. Can the supply be unambiguously specified?
2. Is there strong competition amongst suppliers?
3. Is the value of the contract high enough (usually >$200k)?
It’s not just about price

- Negotiate with more suppliers
  - Having just witnessed significant savings in a 7 supplier, 40 minute auction, the excited CEO asked the buyer "How long would that negotiation have taken without an auction?" Buyers reply: "It wouldn't have happened. I would only have had time to deal with the incumbent and maybe 1 or 2 others."

- Increases choice of supplier
  - Narrows the gaps

- Incorporating value
  - Anything that can be numerically codified can be incorporated into the auction.
    - Through absolute weightings, percentage weightings or lot items.
    - eg: Payment terms, lead times, local content, incumbency, switching costs, returns policies, delivery points, recycling, carbon credits.........
It’s not just about price – Probity and Transparency

…”..., agencies should not coerce unsuccessful proponents into lowering prices, nor should they engage in bid-shopping, that is trading off the prices of one proponent against another....“

May 2006 ICAC publication:

‘Guidelines for managing risks in direct negotiations'

South Australian perspective

Panel contracts

Policy prohibits the use of published prices in a panel contract as a negotiating point with other suppliers.

All panellists must be given the opportunity to compete for high value purchases.

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The reverse auction process, which involves bidders progressively offering lower prices, may be mistaken for bid shopping. However, in bid shopping it is typically the buyer who actively seeks a lower price from a supplier by privately revealing the price offered by another supplier, without the knowledge and consent of that supplier. In the reverse auction process, the bidding process is transparent. All participants are provided with, and have access to, the same information at the same time.

This guideline will assist NSW Government agencies use internet-based reverse auctions as a method of procurement. Electronic commerce has the potential to contribute significantly to the procurement process. Agencies are to adopt innovative procurement methods where these may achieve the best value for money.
It’s not just about price – Probity and Transparency

• The buyer as observer
  – The buyer is not a party to the price negotiations - The buyer is protected

• On the record
  – Every bid is recorded and cannot be manipulated - Non repudiable negotiation records produced.

• Transparent, Fair
  – All suppliers have the same information at exactly the same time - No opportunity for favouritism.

• Patronage
  – The skilled relationship salesperson is stripped naked (just during the auction).
  – The power shifts to the market and away from the performance of individuals.

• Collusion
  – Indicators - Over multiple auctions, recorded bidding patterns can be analysed
  – Prevention - Speed, multiple lots, combinatorial auctions reduce the opportunity for collusion - Too many moving parts.

• Public sector
  – Safely negotiate price
  – Significantly improved probity
Usage Examples - The UK local government experience

Usage examples and results

"You have to make sure you pick the right commodities and services before you embark on a reverse auction. If you don't then you often see little effect. But if you do you can make spectacular savings."

Mike Steele, Birmingham’s principal procurement manager

Birmingham CC
Office Supplies

Northampton CC
Telecoms, Voice & Data

Solihull MBC
Telecoms, Voice & Data

East Midlands COE
Wheelie bins

Savings quoted are against confirmed (often tendered) pre-auction prices

Pre-auction tender delivered 5% savings. E-auction reduced this by a further 9% making a total saving of 14%.
Usage examples – UK Government

London Borough of Newham research into usage at all levels of government

Average savings of 18.3% across $870M in purchases (mixed RA providers)
Computers 15%    Paper 18%    Bottled Water 58%    Electricity 9%    Gas 13%
Paper & Paper Board 16%    IT Equipment 32%    Medical Products 10%
Pharmaceutical Products 12%    Stationery 53%    Computers 29%    Court Reporting
& Transcription Services 10%    Electricity 10%    Carrier Bags 31%    Stationery 58%
Pest Control 59%    Agency Staff 39%    Bulk Envelopes 12%    Car & Commercial
Vehicle Hire 8%    Car Hire 26%    Carpet Tiles 29%    Construction Service (x10
Auctions) 16%    Contingent Labour (x6 Auctions) 15%    Architectural design & drawing
services (x3 Auctions) 5%    Electrical cabling & install (x4 Auctions) 13%    Electricity 22%
Envelopes 10%    Mailing & Distribution 12%    Hotel Accommodation (UK) 11%    IT
Recruitment 50%    Logistics 8%    Mobile Telephony 20%    Oils & Lubricants 13%
Statements & Letters 24%    Office Supplies 33%    Temporary Building Hire 23%
Major Electrical Components 15%    Cleaning Services 25%    Fleet – Leased Cars 10%
Hotel Accommodation 28%    Telecommunications – Outbound telephony 35%
Temporary Staff 20%    Mobile Telephony 34%    Inland Revenue Flat Screen Monitors
23%    Environment Agency Stationery 23%    NHS PASA Canned Grapefruit 24%
Inland Revenue Furniture 23%

Trade Interchange: Average savings (against buyers expectations) of 14% over 1,000 auctions.
The UK local government experience

"For example, the first wave of national e-auctions, held in 2005/06, generated efficiency gains of almost £13 million, equivalent to an average saving of 27% on each contract."
Phil Woolas, British Minister for Local Government

"Online reverse auctions are a step up for local government procurement, because they remove the potential for favouritism."
Martin Atherton, Datamonitor analyst

"We are getting the same level of service for a much better price thanks to this new approach. We have been very careful to specify the quality of the service and we know that we are now paying the best price."
Angela Cox, Cheltenham BC procurement officer

"There is nothing particularly difficult about e-auctions. It is simply a change in how the final bids are received for the contracts that you are trying to work up."
Martin Scarfe, Director, Local eGovernment National Projects

"It leaves one question, which should be aimed at all local authorities…. Why aren’t auctions used more often when all the evidence suggests significant cash savings and other process advantages”…?"
Final comment in London Borough of Newham Case study
Usage Examples – Suppliers Perspective

Pre-auction tendered prices.
“Did I guess right?”

Immediate valuable competitive intelligence.
1st, 2nd, 3rd etc. Even if you don’t bid.

Hunting for the market price.
Have as many bites at the cherry as you like.

“See, I told you I’m not a useless salesperson, we’re just not competitive.”

• Fair
• Transparent
• Anonymous
• No favouritism
• Independent

Market price found.
“No wonder we’ve been losing business. We need to get our costs down..”
Usage Examples - SA Dept of Health

Pre 2002
Pre Aggregation
Pre Auction

Pre 2002
Reverse Auction

2002 Contract
Reverse Auction

Mixed supplier reactions

$1.25M PA

$940K PA (-25%)

$756K PA (-20%)

Examination Gloves

2005 Contract
Reverse Auction
Clinical Criteria

Appropriate supplier relationship

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<table>
<thead>
<tr>
<th>Clarity Criteria</th>
<th>Gloves SA Health – Round 2 - 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Ease of Dispensing</strong></td>
<td><strong>Ease of donning</strong></td>
</tr>
<tr>
<td><strong>Skin Irritation</strong> (Note if any irritation is felt while trying on gloves)</td>
<td><strong>Retention of tactile sensitivity / touch</strong> (ET to touch-test a range of materials)</td>
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<tr>
<td><strong>Strength</strong></td>
<td><strong>Odour</strong></td>
</tr>
<tr>
<td><strong>Comfort and Fit</strong> (short-term wear)</td>
<td><strong>Grip</strong> (ET to touch-test a range of materials, both wet &amp; dry)</td>
</tr>
<tr>
<td><strong>Comfort and Fit</strong> (long-term wear - 45 min – time permitting)</td>
<td><strong>Sleeve Rollback</strong> (To be tested while wearing a gown)</td>
</tr>
<tr>
<td><strong>Double-gloving</strong></td>
<td><strong>Suppleness /elasticity /flexibility</strong></td>
</tr>
<tr>
<td><strong>Length of cuff</strong></td>
<td><strong>Ease of removal</strong></td>
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Usage examples

Bulk printing for 600 pubs (UK) – Last month

- Best pre-auction quote
- Aggressive bidding led to 27 minutes of extensions.
- Best bid of £681k 17% below expected (26% below current)
- Customer has choice of 3 suppliers

Current price, using an agency

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“They think there’s something wrong [about reverse auctions] but can’t put their finger on it. Maybe it’s culture or value for money. There seems to be a lot of concern over probity and risk and potential for criticism. I honestly think that is what’s holding people back.”

Steve Moro, Director, Strategic Procurement Unit, SA Dept of Health

'e-Auctions effectively allow for an infinite number of bid re-submissions by suppliers in an open and competitive environment, at a relatively low overhead cost. This turns the concept of a 'true market price' into a reality...'

Source: What are e-Auctions... and how to get started. UK local government guide.
Coming soon: Ascending Dutch and eRFX