Reverse auctions work to produce not just savings for innovative organizations that utilize them—including dozens of federal agencies—but opportunity for suppliers to build their businesses by successfully competing and winning—in the competitive bidding environment.

By David C. Wyld
In today’s business environment, we talk a great deal about innovation. And when we think of innovation, we too often think of new technologies and new techniques for doing things that are complex, sexy, and expensive. We too often get swept up with technologies that begin with prefixes such as “nano,” “bio,” and, of course, “i-anything,” and those that produce the like of “3D” things and “holographic” images. We too often favor exciting innovations that have the potential to transform the way we do things in a big way over innovations that may change things incrementally over time, but result in far more concrete results for a wider audience.

What if there was an innovation available today that has been proven to work every time it is employed? And what if that innovation worked for all parties involved with it and that it had a long track record of doing so? Well, one would safely say that it would be a “no-brainer” to adopt that innovative technology. This innovation I’m speaking of is not new, and in truth, it has been available now for decades. It is reverse auctions.

In this article, we’ll look at some of the federal government’s success stories in leading the way in effectively adopting reverse auction-driven business-to-business, e-commerce technologies as a spend management solution, and the perspectives of the trailblazing leaders behind these success stories. In the telling, we will also dispel some of the myths that persist about reverse auctions. This article will also demonstrate that encouraging reverse auctions is vital to not just making government acquisition better, faster, and cheaper, but also as a mechanism to use public-sector procurement to promote competition and economic opportunities for businesses today. Finally, we will look at the bigger picture of how reverse auctions are a complementary and even essential core component of a larger innovation agenda.

**The Reverse Auction Process Works for Buyers and Sellers Alike**

From my decade of experience working with acquisition leaders across a number of federal agencies, one thing is quite clear: They view the use of reverse auctioning as an important procurement innovation that is a strategic shift in how things get done. They see competitive bidding as a “game-changing” technology in terms of how it works to the benefit of both their agency and their contracting staff, as well as how it can provide opportunity for the suppliers for the agency. They thus see the employment of reverse auctioning as an important contracting innovation that should, must, and will be utilized over the long-term.

Too often, critics of reverse auctions believe that executives turn to reverse auctions as a way to exploit their supplier base and extract short-term savings on the back of their suppliers. They rely on a series of myths
about reverse auctions that have simply proven to be untrue (see “Reverse Auctions: The Myths versus the Realities of Competitive Bidding” on pages 44–45).

Today’s acquisition environment is characterized by the simple, yet complex mantra to “do more without more.” Thus, achieving cost savings is an important way that the acquisition area can contribute to the operability and success of the agency as a whole. Yet, the acquisition leaders with whom I have worked are cognizant of the fact that while the competitive bidding process does work to lower the final price point—often quite significantly—for the awarding of a contract, the process itself is more important than that simple outcome. Indeed, these innovative procurement leaders recognize that the competitive bidding process effectively produces beneficial results for both the buying organization (in this case, the federal agency) and for its suppliers.

Benefits for Agencies

As the adage goes, the proof is in the pudding—from the standpoint that federal agency acquisition executives see reverse auctioning as a long-term success strategy that produces solid savings, along with other tangible benefits for federal agencies. As outlined in my 2011 research report for the IBM Center for the Business of Government, these benefits for the agencies include the fact that the use of competitive bidding in the federal acquisition process can:

- Produce significant levels of savings;
- Be used for a wide variety of goods and services that make up a significant portion of agency spending;
- Make acquisition processes faster and more efficient, enabling agencies to deliver improved service levels and results with the same or fewer staff than before;
- Introduce new levels of competition by providing improved access to government contracting for small businesses; and


A Little Background on Dr. Wyld... and Reverse Auctions

With over a decade’s worth of experience working with reverse auctions in the federal government, and as the founder and director of the Reverse Auction Research Center, Dr. David C. Wyld has had the opportunity to work in a variety of capacities with numerous contracting offices across a swath of federal agencies as they first considered, then implemented, then evaluated the use of reverse auctioning as part of their acquisition strategy.

Wyld’s work has resulted in a number of white papers, academic articles, and research monographs on the use of reverse auctions in the public sector. These can be viewed and downloaded from the Reverse Auction Research Center (www.reverseauctionresearch.org). Most notably, however, his work has produced two research reports authored for the IBM Center for the Business of Government. The first, “The Auction Model: How the Public Sector Can Leverage the Power of e-Commerce through Dynamic Pricing,”** was the first major academic study of reverse auctions in the public sector. Issued in 2000, at the height of the dot-com era, the report looked prospectively at how the federal government could make use of the emerging best practice of reverse auctioning from the commercial sector. Much transpired in the ensuing decade after the bust of the dot-com bubble, but the fundamental concept that competition always works persevered. Thus, while many of the early-era reverse auction–based companies folded or were folded into larger procurement solutions providers, the reverse auction revolution was taking hold in both the private and public sectors.

In the mid-to-late 2000s, reverse auctions rose to become a best practice across leading companies, with the vast majority of Fortune 500 companies employing competitive bidding across their procurement operations. And at the same time, innovative acquisition leaders across the federal government—from Byron Young at the Army Contracting Command to Cathy Read at the U.S. Department of State to John Ely at Customs and Border Protection in the Department of Homeland Security—were change vanguards in leading their procurement operations to employ reverse auctions. Thus, in 2011, Wyld wrote a follow-up report for the IBM Center for the Business of Government, titled “Reverse Auctioning: Saving Money and Increasing Transparency.”** This follow-up was much different than the original, in that this research report chronicled how reverse auctions were being successfully utilized across the federal government. This report examined the experiences of agencies such as the Department of State in using reverse auctioning. It also examined both the realized and potential cost savings and efficiencies in expanding the role of competitive bidding in the federal government, which has become critical in an era where acquisition leaders are challenged to produce tangible results.

Today, Wyld’s work continues to position him as perhaps the leading expert in the field and as an advocate for reverse auctioning across the public sector, both in the United States and abroad. At present, he is conducting research as to how the best practice of using competitive bidding in the federal government can serve as a model for state and local governments to replicate in expanding contracting competition, save taxpayer dollars, and spur small business development at a regional level. Additionally, he is examining the role of reverse auctions in other functions of governmental operations and policy development, such as the proposed Federal Communications Commission use of reverse auctions for the broadcast spectrum. He has been consulted as a subject matter expert on reverse auctions by a variety of governmental bodies and private-sector firms. Additionally, Wyld has delivered a number of keynotes and seminars on reverse auctioning at leading conferences and conventions.

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• Be conducted in a manner that ensures transparency in the acquisition process and ensures competing suppliers and taxpayers a fairer and open competition among a wider field than in alternative procurement methods. 

In an advisory capacity, I have had the opportunity to conduct research over the past few years using reverse auction data from FedBid (www.fedbid.com), based in Vienna, Virginia, which is the reverse auction–driven online marketplace currently used by agencies across the federal government. In doing so, we have reviewed the competitive bidding experience for:

- The Department of the Air Force,
- The Department of the Army,
- The Department of Commerce,
- The Department of Defense,
- The Department of Education,
- The Department of Energy,
- The Department of Health and Human Services,
- The Department of Homeland Security,
- The Department of the Interior,
- The Department of Justice,
- The Department of Labor,
- The Department of the Navy,
- The Department of State,
- The Department of Transportation,
- The Department of the Treasury,
- The Department of Veterans Affairs,
- The Environmental Protection Agency,
- The Federal Communications Commission,
- The Federal Bureau of Investigation,
- The General Services Administration,
- The National Aeronautics and Space Administration,
- The National Transportation Safety Board,
- The Office of Personnel Management,
- The Securities and Exchange Commission,
- The Social Security Administration,
- The U.S. Agency for International Development, and

Collectively, the federal government has saved hundreds of millions of dollars through the use of reverse auctions facilitated through FedBid, and the purchase price savings—approximately 10–12 percent over time, as compared to the independent governmental cost estimates—generated through the competition of the bidding process are consistent across the agencies. In just the past five years, the federal government, as a whole, has achieved aggregate savings of over half a billion dollars, or 11 percent, using reverse auctions through the marketplace.

The studies we have conducted at the Reverse Auction Research Center have drilled down into the experience of several agencies with competitive bidding in their procurement operations. For example, the Reverse Auction Research Center released a research report in mid-2012 examining the levels of cost-savings achieved by the Army Contracting Command. The report, titled “Reverse Auctioning—Producing Solid, Defensible Savings in Military Acquisition: An Analysis of the Experience of the Army Contracting Command (ACC),” concluded that:

In an era with massive budgetary and operational pressures, the ACC stands as an exemplar for how reverse auctioning can
be strategically integrated into acquisition processes to produce significant procurement savings.2

In this study, the results showed that the ACC saved, in aggregate, almost $150 million between fiscal years 2007 and 2011. And, more important, the analysis demonstrated that the savings were defensible even when subjected to the most stringent of screening methods. This led Bryon Young, the executive director of the Aberdeen Proving Ground, a major contracting center for the ACC, to observe:

The precise measurement of cost savings in a process like reverse auctioning is always hard to do. I believe we have achieved verifiable cost savings that have resulted in improved buying power for the army. The reverse auctioning process clearly works to our benefit as a procuring activity.3

Even in situations where savings are not in the 10–12 percent range, the reverse auction process often generates significant savings over what the government agency might have paid had the competitive bidding process not been in place. This applies to increasingly frequent scenarios today where prices for commodity goods—and items with high commodity content—may swing wildly. Thus, the competitive bidding process works to make sure that the government is attaining what is a real-time market price for the item in question.

Next, many items, especially in the area of IT items and services, in long-term contracts may actually serve to cost the government agency as the buyer quite a bit. This is because of the concept of price degradation, where, as we all know from our personal experience, the price you pay today for a piece of computer equipment will always be more than what it will be a year, a month, or even a week later.

Finally, reverse auctions are not meant to be applied across the board to all procurements of goods and services. Indeed, there is a developing knowledge as to when and on what types of acquisitions reverse auctions can and should be applied, and conversely, conditions and categories of goods/services that should not be subject to competitive bidding. So, in the end, in terms of procurement tools, reverse auctions are a scalpel, not a sledgehammer.

The process itself also works to ensure fair competition, which benefits—and changes—the suppliers. Overall, though, the competition that is inherent in reverse auctioning works to capture the market at the moment. This simply means that for any given acquisition, for the quantity, grade, location, terms, etc. of that particular procurement of goods or services, the government, as the buyer, and the seller meet at the price point that is reflective of both parties’ needs. It is pure economics at work. Thus, each supplier has to weigh its own internal cost structure, its
view of the overall marketplace (in which prices for items and services that are commodities can swing greatly), and its desire to gain that particular contract in setting its overall bidding strategy. By doing so, it has full power to decide at what price point bidding on a particular contracting opportunity no longer makes sense for its business.

**Benefits for Suppliers**

While reverse auctions work to benefit the buyer-agency, how do reverse auctions work to benefit the suppliers? One may think that on the surface this is counter-intuitive, and indeed, reverse auction opponents espouse a mistaken belief that reverse auctions have an inherent “win-lose” relationship (i.e., the buyer wins and the supplier loses). Yet, it is quite clear that while incumbent suppliers, whose contracts may not have been competitively challenged for years, may be upset at the prospect of the openly competitive environment that reverse auctioning entails, for other competitors, reverse auction–based acquisitions represent opportunities, not coercion.

The competitive bidding process does offer suppliers the opportunity to “win” contracting opportunities, and so in the process, there will be competitors who will “lose” in the zero-sum game that is an individual reverse auction. However, the level playing field of the competitive bidding process offers the ultimate opportunity for each party’s utility to indeed be maximized through the competition that transpires.

As Steve Kelman, currently the Albert J. Weatherhead III and Richard W. Weatherhead Professor of Public Management at Harvard University’s John F. Kennedy School of Government, and formerly the administrator of the Office of Federal Procurement Policy in the Office of Management and Budget, commented:

> It is of course correct that each party in a business arrangement needs to worry not just about claiming value (dividing up the pie) but also creating value (maximizing the joint pie). Of course, the government needs to worry about good relations with its suppliers. But it would be foolish for the government to think that suppliers only worry about maximizing the joint pie and not at all about getting as large a share of it as possible. In this fiscal environment, for the types of commodities and simple services bought using reverse auctions, it is appropriate for the government to be aggressive in getting a good deal for agencies and taxpayers.

Right now, for instance, there are over 59,000 businesses participating in FedBid’s online marketplace. The experience of these companies shows how competitive bidding “opens-up” the federal procurement process to small firms. Small companies of every category—disadvantaged, minority-owned, women-owned, and veteran-owned—consistently win about 80 percent of all reverse auction–based acquisitions conducted across federal agencies in FedBid’s online marketplace. And small businesses win not just in set-aside competitions, but in competitions open to all. Further, for many of the companies who are part of FedBid’s marketplace community, their owners and managers gain access to buys being made not just by federal agencies, but by state and local governments, as well as private-sector firms in their line of business. They have opportunities to sell their goods and services in fair and open competitions that they likely were not aware of and certainly would not have had access to before joining FedBid. For instance, many small companies in the New Orleans area became part of the FedBid marketplace community after Hurricane Katrina in 2005 to bid on recovery work for federal agencies. They have since built successful businesses based in large measure on their access to federal contracts through the competitive bidding on FedBid. No doubt, this will surely be the case today in the wake of Hurricane Sandy in the New York/New Jersey region as well.

Cost savings are a large part of the reverse auction equation. That is why not just federal agencies, but state and local governments are increasingly turning to competitive bidding. For instance, the Defense Logistics Agency (DLA) mandated in June 2012 that reverse auctions be employed on all contracts in excess of $150,000, working exclusively with a reverse auction tool provided by Procurex (www.procarexinc.com), which is based in Erie, Pennsylvania. Yet, according to DLA, such cost pressures can themselves prove beneficial for suppliers in terms of making sure that their operations are on par with their competitors. To that end, Charles Howerton, a procurement and systems analyst for the DLA Acquisition Programs and Industrial Capabilities Division, recently commented: “Reverse auctions provide incentive for suppliers who are able to restructure their internal operating procedures and costs. It can help them make their operations more efficient and cost effective. It’s a win-win.”

Thus, as all firms have the need to stay competitive and have a cost structure that is in-line with the company’s competitors, reverse auctions do provide a real-time assessment method for managers to know their firm’s standing in the marketplace. This competitive intelligence can prove invaluable as companies make decisions on how to not just be in a position to be competitive today in a single acquisition for a federal agency, but what must be done to be competitive on the broader stage and over the long-term.

**Analysis: The Role of Acquisition Leadership in Innovation**

As my 2011 IBM research report on reverse auctions concluded:

> There is no doubt as to the strong role that acquisition leadership plays in advancing the use of reverse auctions. In every organization studied that has successfully integrated competitive bidding into its acquisition strategies, there have been one or more champions who have emerged to make it their mission to advance the use of reverse auctions in their organization.

What we have seen is that it takes real leadership to change the status quo. That is true in every aspect of life, and it is especially crucial when it comes to making change happen in the acquisition area. We all know that it is far, far easier to keep doing things as they have been done in the past and accept the status quo, letting inertia
## Reverse Auctions: The Myths Versus the Realities of Competitive Bidding

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<tr>
<th>The Myths Surrounding Reverse Auctions</th>
<th>The Reality About Reverse Auctions</th>
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<tbody>
<tr>
<td><strong>Myth</strong> Reverse auctions are only employed in private-sector procurement.</td>
<td><strong>Reality</strong> Today, the public sector, led by federal agencies, has in many cases been a leader in the adoption of reverse auctions for acquisitions.</td>
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<tr>
<td><strong>Myth</strong> Reverse auctions are only used by the largest, Fortune 500 companies.</td>
<td><strong>Reality</strong> Today, reverse auctions have been successfully employed in companies of all sizes.</td>
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<td><strong>Myth</strong> Reverse auctions take a great amount of upfront investment in both money and time.</td>
<td><strong>Reality</strong> Today, with the availability of cloud-based “procurement as a service” reverse auctioning platforms, reverse auctions can be employed quickly, with no upfront cost and minimal employee training.</td>
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<td><strong>Myth</strong> Reverse auctions are limited only to commodities and are not appropriate for services.</td>
<td><strong>Reality</strong> Today, experience has shown that both goods and services that can be clearly specified with exacting requirements, competed on a firm-fixed-price basis, and have multiple able suppliers can be successfully procured using reverse auctions.</td>
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<td><strong>Myth</strong> Reverse auctions are only able to be used on sizeable procurements—with dollar amounts in excess of the hundreds of thousands of dollars range—if not in the seven-figure range.</td>
<td><strong>Reality</strong> Although reverse auctions can be effective on large procurements, today, the minimum dollar amount for a particular acquisition to be suitable for a reverse auction procurement is as little as a couple thousand dollars and most auctions are being used for items under $150,000.</td>
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<td><strong>Myth</strong> Reverse auctions add unnecessary costs to the procurement process.</td>
<td><strong>Reality</strong> Today, reverse auctions are used to drive both direct cost savings as well as operational efficiencies, which also frees up resources to negotiate better value and pricing on complex negotiated procurements. Provider cost structures vary, but there are those that operate at no net cost to buyers through guaranteed cost savings.</td>
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<td><strong>Myth</strong> Reverse auctions hurt suppliers.</td>
<td><strong>Reality</strong> Today, the only suppliers “hurt” by the introduction of competitive bidding into the acquisition process are incumbent companies who have not had their contract openly and actively competed for several years—or more. By opening-up the competition, reverse auctioning creates new opportunities for competitive companies by rewarding more efficient operations and better operational cost structures.</td>
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<td><strong>Myth</strong> Reverse auctions are merely a way of exerting power over suppliers.</td>
<td><strong>Reality</strong> Today, rather than being seen as a coercive measure, reverse auctions are a liberating force for suppliers. Reverse auctions represent a means to open-up the competitive process and create a fair, open, and level playing field for all interested suppliers to compete for a contract on an even basis.</td>
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<td><strong>Myth</strong> Reverse auctions force companies to make awards to the lowest bidder.</td>
<td><strong>Reality</strong> Today, with most reverse auctions, the buyer is not bound to take the lowest bid. Rather, the buyer can take factors other than price into account when making the award decision, including things such as past performance, supplier capabilities, creditworthiness, etc.</td>
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<td><strong>Myth</strong> Reverse auctions benefit the largest competitors who have the scale and size to defeat smaller companies on a cost basis.</td>
<td><strong>Reality</strong> Today, the reality is that reverse auctions are an enabler of small business, as smaller firms are awarded the vast majority of contracts competed through reverse auctioning. Small companies often have both lower overhead and higher desire to win in reverse auctions to gain business to build their businesses.</td>
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<td><strong>Myth</strong> Reverse auctions are a one-time shot to produce savings that cannot be replicated over time.</td>
<td><strong>Reality</strong> Today, both private companies and government agencies have established track records of holding reverse auctions for like goods and/or services over successive months, quarters, and years. These have produced savings time and again to ensure that the buyer is getting the best price possible.</td>
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Reverse auctions can be employed on a global scale, along with the small business opportunities created through the use of competitive bidding. Further, the vast array of goods and services successfully acquired through reverse auctions by CBP in support of its mission shows that there are very few goods or services that cannot be acquired through reverse auctioning. CBP demonstrated that competitive bidding for “unusual” items such as farrier services (horseshoeing), horse saddles, and even canines (live dogs and puppies, along with related supplies) can be successfully contracted for via competitive bidding.6 For the present article, CBP’s Deputy Executive Director for Procurement Diane Sahakian commented:

Reverse Auctioning is a key tool in CBP’s Procurement’s tool kit. Since 2006, we have processed approximately 8,000 reverse auction actions. We use reverse auctioning for commodity and simple service buys where price rules in terms of award decisions. We find that it saves time, adds transparency to the buying process, and allows for increased competition by virtue of having access to the extensive and vetted marketplace which is maintained by the reverse auction provider.

It takes real leadership to take the innovative step to initiate the use of reverse auctioning in acquisition operations. We should praise those courageous acquisition leaders who have initiated the change process to move toward appropriate use of reverse auctioning in their procurement operations and encourage—not discourage in any way—innovation in contracting, especially when the benefits are spread so widely. In fact, one could argue that because the issue of savings is a tricky one (“If I save X dollars, will my budget then be cut by X7), the agency—and the leaders who propel the change—benefit less than the other parties in the bigger picture. Yes, the government saves on its overall acquisition outlay. Yes, businesses benefit from access to government business. And yes, jobs are created and small businesses thrive from the “stimulus” of new contracting opportunities.

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<th>Myth</th>
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<tr>
<td>Reverse auctions don’t always produce savings.</td>
<td>This myth can hold true in that market prices for commodities can vary over a short time frame. It can also be true if reverse auctions are used to purchase inherently noncompetitive items. Thus, a reverse auction might not necessarily produce a lower price than what the company or public agency is paying for the commodity today. However, by having active suppliers engaged in a competitive bidding format, the buying organization will know that it is obtaining the best possible price at the moment through real-time market pricing.</td>
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<tr>
<td>Reverse auctions create animosity between the buying organization and its supply base.</td>
<td>Today, as more and more companies themselves use reverse auctions in their procurement operations, competitive bidding is simply seen as a “best practice” and the way things get done for leading-edge organizations.</td>
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<tr>
<td>Reverse auctions are a short-term tactic for your procurement operations.</td>
<td>Today, reverse auctions are a tool that can—and should—be an important part of your long-term acquisition strategy.</td>
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In working with federal agency acquisition leaders who have taken the reins and steered their procurement staffs to make use of reverse auctions as an innovative tool in their toolkits, we have seen true success stories that serve as models for all government agencies. For instance, in the Department of State (DOS), we have completed two studies to date. DOS has demonstrated that reverse auctions can be employed on a global scale, creating important opportunities for U.S. small businesses to compete and win abroad and to save the taxpayer significantly on procurements.6 Additionally, we found that the use of reverse auctioning meant that for each acquisition routed through the competitive bidding process, acquisition staffers shaved a full day of work out of the acquisition cycle. This translates into significant secondary cost savings, as well as enabling acquisition staffers to deliver better service to internal customers and engage in meaningful supplier outreach and development.7 When contacted for the present article, Cathy Read, who is the director of Acquisitions Management, Office of Logistics Management, for DOS, commented:

Procurement leadership is all about sustainability, and the Department of State established our reverse auction tool in December 2001—11 years ago. Thus, with a decade’s worth of experience in working with our internal customers and our suppliers, State would certainly say that our reverse auction strategy is for the long-term. The tool has both provided significant value to the taxpayer and created opportunities for vendors in doing business with our agency around the world.

Likewise, we have looked extensively at the impact of reverse auctioning on the operations of U.S. Customs and Border Protection (CBP). We found the hard and soft dollar savings for the agency to be impressive, along with the small business opportunities created through the use of competitive bidding. Further, the vast array of goods and services successfully acquired through reverse auctions by CBP in support of its mission shows that there are very few goods or services that cannot be acquired through reverse auctioning. CBP demonstrated that competitive bidding for “unusual” items such as farrier services (horseshoeing), horse saddles, and even canines (live dogs and puppies, along with related supplies) can be successfully contracted for via competitive bidding.8
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Those innovative government acquisition leaders who have implemented reverse auctions in their agencies and those who will do so in the coming years are indeed saving taxpayer dollars and creating economic opportunity through their actions. This is in-line with a November 2012 report from the Brookings Institution on “Building an Innovation-Based Economy.” In this report, the Brookings researchers concluded:

We need policy shifts that encourage the purchase and adoption of technology innovation in the public sector. We should ensure that local, state, and federal government procurement processes are fair, open, and transparent so that public agencies get the best products at the lowest possible prices. Agencies should be empowered to make the best acquisition choices possible, and build on successes across agencies. We should reform government procurement to include reverse auctions for goods and services. Reverse auctions...help small businesses get government contracts and diversify the supply chain.

I would thus call for policy-makers at every level to look at expanding the use of reverse auctions and reinforce the Brookings Institution recommendation to find—and fund—new ways to “reward those who generate innovative ideas.” Sure, reverse auctions may not have a “sexy” prefix or be a cutting-edge technology, but they are an important, proven acquisition innovation that works for the taxpayer that should be fostered and encouraged throughout the public sector.

ENDNOTES
3. Ibid.
5. Wyld, see note 1.
10. Ibid.
11. Ibid.

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