



How Low Can You Go?

**Will Reverse
Auctions
Change the
Way Glazing
Contractors
do Business?**

by Ellen Giard Chilcoat

In your neighborhood there's probably at least one major retail operation (i.e. Target, Wal-Mart, Lowes, Home Depot). Think about what that store looks like.

Now, think about those same stores in different locations you've seen or visited. Chances are they all look the same, or very similar, regardless of the area in which they are located. While glass typically isn't a major construction element, glazing is an integral part of most storefronts and entrances. And for many small- to medium-sized contract-glazing companies winning such a project is an ideal job.

Some people with ties to the construction industry say retail operations that display the same overall look are prime candidates for a new means of awarding subcontract work—electronic reverse auctions. In a construction environment, a reverse auction begins with a project owner in need of a service (such as a glazing subcontractor). The owner establishes the opening bid online, and pre-qualified participants bid down the price. This process, however, has many members of the glass industry in angst.

The Minneapolis-based Target Corp., for example, is one company supporting the reverse auction process (e-bidding, because it takes place online). Glazing subcontractors are pre-qualified and (unlike a traditional auction where bidders bid upward) the reverse auction starts with an opening bid and participants bid lower and lower. While bidders can view the prices of competitors they do not know who the other companies are.

But Target is not the only corporation supporting reverse auctions. Others using the process include General Electric, Best Buy, Home Depot, Intel and Alcoa.

Some say this process not only takes the focus away from important matters, such as safety and quality, but also makes construction subcontract work a commodity—one based on nothing more than price.

How it Works

Before a glazing contractor can venture into a reverse auction it must be pre-qualified by the project owner. Steve Hauser, who teaches construction management at the University of Minnesota and also works for Target Construction Services, said the pre-selection of bidders is a very important part of the process. This, he explained, helps ensure that only qualified subcontractors [glazing contractors] are bidding on the work. (Hauser also led a presentation on e-bidding during the Glass Association of North America's Contract Glazing



Some project owners are using the reverse auction process to award subcontract work, including glazing.

Educational Conference that took place May 13-15 in Minneapolis.)

Bidding begins at a price designated by the e-bid host (usually the owner) and is typically slightly greater than estimated market value. The price drops as participants place bids. Once the designated time period ends so, too, does the bidding.

"If self-discipline is exercised, you will always bid at your pre-determined minimum or higher. Subs sometimes get work at prices higher than they would have under conventional conditions," said Hauser in his presentation.

Bill Sullivan with Heartland Glass Co. of Waite Park, Minn., is a contract glazier who has been involved with a

reverse auction bid for a Target job. He said the experience went well, and explained that his company had worked with the general contractor before and that's how they were selected to bid.

"We sealed the project at a higher price than with a hard bid," he said. "People (bidders) need to know what their bottom number is and treat it like a hard bid."

Sullivan said that one aspect of reverse auctions that can make it a challenging process is the length of time it can often take.

"The reverse auction we participated in had a scheduled bid time that lasted 30 minutes," said Sullivan. "At the end of that 30-minute bidding period if there was a bid submitted in the last three minutes it would automatically extend the bid by three minutes." (In reverse auctions, this extension is called overtime.)

He said bids submitted in overtime automatically extended the bid time three additional minutes.

"In our particular case the overtime lasted approximately 25 minutes for a total of 55 minutes [of bidding]," said Sullivan.

While there are glazing contractors, such as Heartland Glass, that have been successful with reverse auctions, many are opposed to it.

"It makes me a commodity," said one contract glazier who asked to not be identified. "Our organization is selling a service, and [the reverse auction] is not a competition or manner in which we want to compete. We sell based on relationships, not on price."

Anne Bigane Wilson with Chicago-based Bigane Paving, and a past president of the America Subcontractors Association (ASA), has been involved in presentations and panel discussions on the topic.

"It's a form of bid shopping and it's unethical. It's not a negotiation that looks at changes in scope, etc.," Wilson said. "For an industry that relies so much on relationships, [reverse auc-

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tions] are throwing relationships out the window and making [the work] all about price.”

Hauser disagrees that reverse auctions are only focused on price.

“If [e-bidding] were open to the entire world that would be a valid statement,” Hauser said, noting that by pre-selecting subcontractors [owners] are ensuring that only those known to be focused on quality work and safety, for

example, are considered.

So where does someone such as Sullivan stand on this matter? He doesn’t disagree that reverse auctions can fail to take into consideration safety and quality, but says they are not that different compared to conventional situations when owners are after the lowest price.

“Typically, in a hard bid, the contract glazier is bidding to several general contractors for the same project.

The low bidder is going to get the job, regardless of the contract glazier’s qualifications,” Sullivan said. “It is no different in the reverse auction process, except you get the opportunity to see everybody’s bid during the process, and the contract glazier has to make a business decision on how low he can afford to go.”

While Sullivan said he agreed that in most situations reverse auctions pro-

A Matter of Ethics

According to the FMI Survey of Construction Industry Ethical Practices that was conducted this year, 84 percent of respondents, which included owners, architects, construction managers, contractors and subcontractors, said they had experienced or observed unethical practices in the construction industry in the past year. Of those same respondents, 34 percent said they had experience with unethical acts “many times.” (Note: 270 people answered the survey).

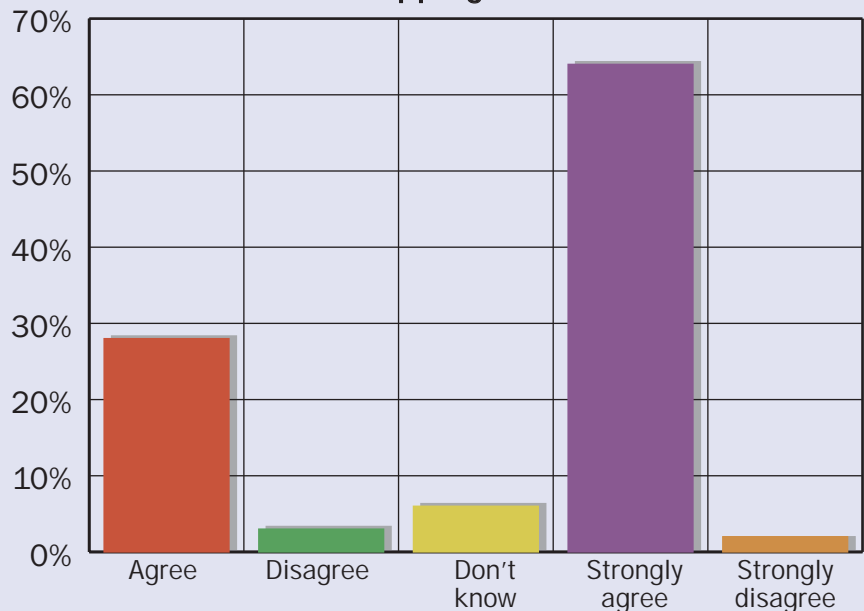
The survey covered numerous topics related to the construction industry. One topic, bid shopping, was viewed as unethical by a large percentage. According to results, bid shopping, was extremely important for specialty and trade contractors—94 percent said it was unethical.

When it came to reverse auctions (considered by many in the construction industry to be a form of bid shopping) survey results said respondents’ feelings about the topic were in queue with how they felt about bid shopping, except 20 percent said they did not know if reverse auctions were unethical.

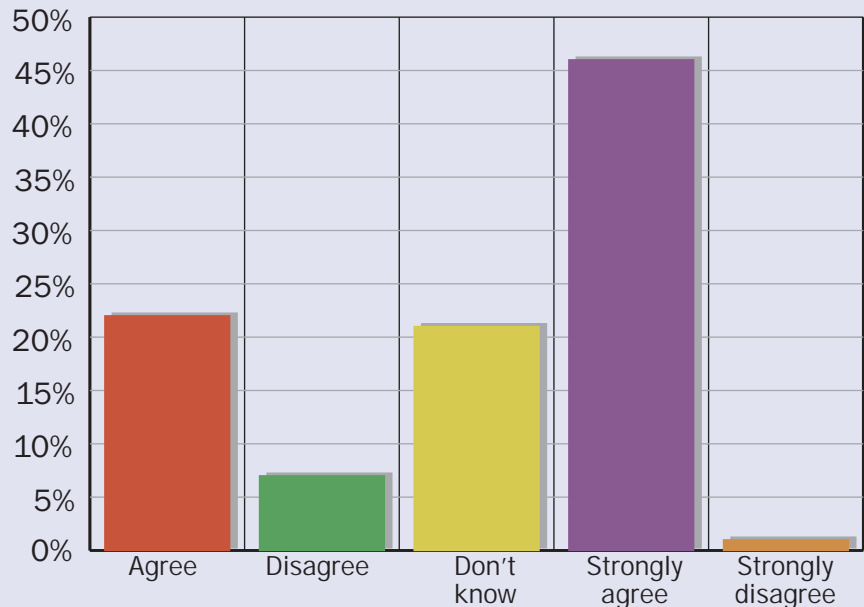
“While very few disagreed that reverse auctions were unethical, more discussion among interested parties could help decide the question of ethics here,” said the results.

The American Subcontractors Association (ASA) is one group further examining the question. A research project, which is also being funded by the American General Contractors and Construction Management Association of America, is reviewing, developing and conducting research on the use of reverse auctions. Completion of the project is expected this fall.

Bid Shopping is Unethical



Reverse Auctions are Unethical



FMI Survey of Construction Industry Ethical Practices

vide the owner with a price lower than in a hard bid situation, in their case it was higher.

"I know this is unusual, but it can, and did, happen for us."

Plans of Action

Still, much of the construction industry is in strong disagreement about reverse auctions, including organizations such as ASA, the Construction Management Association of America (CMAA) and the American General Contractors (AGC).

"The use of reverse auctions essentially removes qualification-based selection from the procurement process," said a statement from CMAA. "Basing construction services on only the lowest bid could threaten the quality of a project, safety and even may lead to an increase in overall project costs due to the necessity of change orders that were not anticipated during the reverse auction process."

"We [at ASA] view reverse auctions as a form of bid-shopping," said Luke McFadden, ASA director of government relations. Looking at the government as the largest construction owner in the world, ASA is supporting legislation (H.R. 1348) that would prohibit all forms of bid shopping, including reverse auctions, on federal construction. "Our goal is to let the government set the example," said McFadden.

The bill ASA supports forbids any party, including the government, prime contractors and subcontractors, from participating in bid shopping. The legislation defines bid shopping as "the practice of divulging a contractor's or subcontractor's bid or proposal or requiring a contractor or subcontractor to divulge its bid or proposal to another prospective contractor or subcontractor before the award of a contract in order to secure a lower bid or proposal."

Reaping the Benefits?

Those in opposition to reverse auctions, and even those who have participated, say one of its biggest selling points is the expected cost savings. The



Some retailers hire glazing contractors via reverse auction.

website of one government agency, the U.S. General Services Administration for example, lists what it sees as reverse auction benefits. Topping the list? "Dynamic real-time competition translates into savings that reflect true market pricing." And just a few bullet points down, "Ordering agencies (i.e. owners) may use Best Value award criteria."

"People are promoting it, saying it will cost less, but I don't think there's been enough research done (as the process has only been around for a few years) to document that," said Wilson.

To learn more about both "real" and "perceived" benefits of reverse auctions the Foundation of ASA, AGC and CMAA have each contributed funds to a research project that will be conducted by Louisiana State University. The project will compile and review existing, scholarly materials, research and studies (such as online documents) on electronic reverse auction bids (ERABs) for the following areas:

- To procure commodities only;
- To procure services only; and
- To procure a combination of commodities and services.

McFadden said the project will review, develop and conduct research on the use of ERABs and will look to answer questions concerning the rules, guides and formats utilized to conduct ERABs to procure construction; the real and perceived detriments, as well as perceived benefits, of the use of ERABs for all members of the construction team; the real and perceived

impact of ERAB on the owner; the impact on construction projects relative to time, price and quality; the impact on the quality of relationships among the members of the construction team; the ethical and legal issues raised by ERABs; and public sector versus private sector experience with ERABs.

Completion of the research project is expected this fall.

And these construction organizations are not alone. The U.S. Army Corps of Engineers conducted a pilot program on reverse auctions and concluded that, as stated on AGC's website, "reverse auctions should not be used to procure construction services and ... fail to realize any additional savings over the sealed bid process." (*The report in its entirety can be found on the AGC's website, www.agc.org.*)

In addition, the AGC has also released a white paper stating "AGC believes that reverse auctions will seldom provide benefits comparable to currently recognized selection procedures for construction contractors." The paper, also available on the AGC's website, offers five points for consideration:

- Reverse auctions do not guarantee the lowest price;
- Reverse auctions may encourage imprudent bidding;
- Negotiated procurements allow thorough evaluation of value;
- Sealed bidding assures that the successful bidder is responsive and responsible; and
- Reverse auctions may contravene federal procurement laws and certain state laws.

What's your opinion on reverse auctions? If you've taken part in one we'd like to hear about your experience. E-mail echilcoat@glass.com and tell us your thoughts on reverse auctions. ■

the author



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