

Competition in Federal Procurement

Presentation to Acquisition Advisory Panel

October 27, 2005

Robert C. Marshall

Professor and Head of Department of Economics, The Pennsylvania State University

Co-Director of Center for the Study of Auctions, Procurements, and Competition Policy, The Pennsylvania State University

Partner, Bates White, LLC

Personal background of relevance

- Research
 - Auction
 - Procurements
 - Bid protests (1988–1994)
 - Understand agency procurement
 - Collusion and cartels
 - Consulting
 - Price fixing conspiracies
 - Understand procurement procedures of private firms

Competition is good

- Why is this true?
- Then why are there detractors?

- Story

- Question
 - How is authorizing a restriction in competition different from authorizing collusion by vendors?

Benefits of competition

- Increases the overall size of the payoff for all of society
 - Without competition, higher prices and lower quality result
 - Reduction in quantity purchased
 - Agency may be willing to buy more at lower prices, and supplier may be willing to supply more at lower prices, but these incremental transactions never occur
 - Future planned purchases may be delayed or canceled because of the higher prices and lower quality
 - Increase public expenditures from higher prices and lower quality imply increased taxes or borrowing
- Revelation of important information
 - Vendors have specific knowledge that is only learned through competition
 - Why reveal a clever cost-reducing solution ex ante if there is no competition?
- Innovative solutions
 - Which question do you want a vendor addressing?
 - What is the minimum required to prevent the procurement official from opening the process to true competitive bidding? OR
 - What innovative solution do we need to put forward, and how cost-effective can we be in implementing this solution, in order to beat our competitors in this contest?

Arguments of the detractors

- Competitive purchasing is expensive
 - Understanding the needs and desires of the agency, writing a “good” bid solicitation, evaluating bids, “fairly” communicating information to bidders so that bids can be revised
- Competitive purchasing requires too much ex ante specificity about the commodity being purchased
 - The agency often does not even know what it wants to buy, so how can it write a bid solicitation?
- Competitive purchasing requires an unrealistic commitment, ex ante, to a scoring function
 - Often the agency does not want to ex ante commit to bid evaluation criteria when the bids may reveal information and aspects of the procurement that are not currently known to the procuring agency
- Competitive bidding is expensive for vendors
 - Also true for bidding in the private sector
- Competitive bidding discourages investment in the vendor-agency relationship
 - Opposite is true. Competitive bidding encourages investment in the vendor-agency relationship (assuming the scoring function is appropriately weighted), while absence of competitive bidding encourages investment in rent-seeking activities.
- Competitive bidding discourages innovation by reducing profits of the awardee
 - Innovation can be part of the scoring function

**Which of these arguments is not true for the private sector?
Why do private sector firms use competitive procurements?**

Competition is not the problem. But something is causing opposition. What is it?

- Competition does not enhance the profits of vendors
 - Successfully advocating for and attaining an ex ante reduction in competition is like successfully colluding, but much better
 - Do we want vendors investing in better products and/or solutions or, alternatively, do we want them investing in influencing decisions regarding awards and award extensions?
- Procurement officials have limited incentives to obtain surplus for taxpayers
 - Takes work to evaluate net gain
 - Little, if any, of their compensation is tied to the net gain produced from a procurement
- Procurement official incentives are largely negative
 - What did it cost to run the procurement? Why so much?
 - Did you learn something from the competitive bidding process that you should have known ahead of time? Why didn't you anticipate that?
 - Did you learn something that has caused you to realize that your bid evaluation criteria are inadequate? Why were they inadequate?
 - Did you select a vendor whose ex post performance is sub-standard? Why didn't you see that ahead of time?

“Nominal competition” (or, how not to have competitive procurements while nominally satisfying a mandate for competition)

- Employ a “consultant” who will knowingly write an excessively restrictive bid solicitation, probably favoring their own firm or a firm with whom they work closely
- Write an excessively restrictive bid solicitation on your own
 - Benign ignorance, or,
 - Motivated by implied incentives, or,
 - Perhaps bad discretion
- Unjustly favor one firm in evaluation of bids
- Have inappropriate discussions with a favored bidder in the process of evaluating bids

Interagency contract vehicles

- How much time and effort should I spend in the procurement of writable CD's for PC's?
 - My one machine at home?
 - All machines at my office?
 - All machines in the entirety of a large university?
 - All machines in the entirety of the Federal government?
- What are the incremental benefits to the effort spent in conducting an ever more rigorous competitive procurement and what are the incremental costs?
 - Each of the four procurements above implies different thresholds
- But, why repeatedly incur procurement costs to buy the same commodity?
 - Good observation. But, delegate to a procurement authority that accounts for the potential magnitude of the purchase and the implications of unduly restricting competition.

Recommendations

- Competition is good. Do not waiver from this principle.
- Propose expansion of budgets for conducting procurements
- Propose expansion of professional training for people responsible for procurements
- Propose clarity in evaluation criteria of people responsible for procurements
 - Propose greater specificity on how ex post evaluations will be done of procurements
- Sharing of information regarding procurement experiences across agencies should be a mandate, not a random occurrence through casual interaction
- Propose modification to interagency contract vehicles—a single agency procuring for many must account for the benefits that the many will attain from open competition
- Bid protests are a good concept (private attorneys general), but need to be revisited
 - Envision a panel of procurement experts
 - Very tight time frame
 - Defer to agency discretion
 - Completely eliminate inter-bidder settlements
 - Remedy—expand inclusion set, and, directed awards (use sparingly)

Competition in Federal Procurement

Presentation to Acquisition Advisory Panel

October 27, 2005

Robert C. Marshall

Professor and Head of Department of Economics, The Pennsylvania State University

Co-Director of Center for the Study of Auctions, Procurements, and Competition Policy, The Pennsylvania State University

Partner, Bates White, LLC