

Statement of

Nigel Cary, Cox Construction Co.

on behalf of

The Associated General Contractors of America

to the

U.S. House of Representatives

**Committee on Veterans Affairs'
Subcommittee on Oversight and Investigations &**

**Committee on Small Business' Subcommittee on Contracting and
Workforce**

For a joint hearing on

**“Contracting Away Accountability—Reverse Auctions in Federal
Agency Acquisitions”**

December 11, 2013

AGC of America
THE ASSOCIATED GENERAL CONTRACTORS OF AMERICA

Quality People. Quality Projects.



The Associated General Contractors of America (AGC) is the largest and oldest national construction trade association in the United States. AGC represents more than 25,000 firms, including America's leading general contractors and specialty-contracting firms. Many of the nation's service providers and suppliers are associated with AGC through a nationwide network of chapters. AGC contractors are engaged in the construction of the nation's commercial buildings, shopping centers, factories, warehouses, highways, bridges, tunnels, airports, waterworks facilities, waste treatment facilities, dams, water conservation projects, defense facilities, multi-family housing projects, site preparation/utilities installation for housing development, and more.

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Cox Construction Co.; San Diego, California
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Chairmen Coffman and Hanna, Ranking Members Kirkpatrick and Meng, and members of the Subcommittees, thank you for inviting the Associated General Contractors of America (AGC) to testify on federal agency use of reverse auctions to procure construction services. AGC represents over 25,000 construction contractors, suppliers and service providers across the nation.

My name is Nigel Cary. I have been a member of AGC for over 30 years and currently serve as vice-chair of the Federal & Heavy Construction Division. I have worked at Cox Construction Co., since 1981 and was president of the firm from 1991 to 2011. We are a federal small business construction contracting firm based in San Diego County, California that specializes in work for government agencies. Since the Cox Construction’s founding in 1979, we have constructed over 150 public projects, ranging in size from \$25 thousand to \$30 million. Cox Construction has bid or proposed on hundreds of projects for federal agencies and completed projects for the U.S. Army Corps of Engineers (USACE), Naval Facilities Engineering Command (NAVFAC), the Air Force Civil Engineer Center (AFCEC), and United States Postal Service (USPS), among others. For our work, we have won Contractor of the Year accolades from USACE four times—in 1991, 1998, 2007 and 2008.

Today, I will discuss:

- I. Why my company and many other construction companies—both small and non-small businesses—**do not participate in reverse auction procurements;**
- II. Why the U.S. Army Corps of Engineers—the largest and most experienced federal construction agency—**no longer procures construction services through reverse auctions;**
- III. How the Department of Veterans Affairs and General Services Administration, among other agencies, continue to use and to push reverse auctions for construction services; and
- IV. Why Congress should enact measures prohibiting reverse auctions for federal construction services contracts, like H.R. 2751, the Commonsense Contracting Act of 2013.

I. The Problems with Reverse Auctions for Construction Services Contracts and How Reverse Auctions Limit Competition

AGC strongly supports full and open competition for contracts necessary to construct improvements to real property. This includes competition among general contractors, specialty contractors, suppliers and service providers. Over the years, it has been established that such competition energizes and improves the construction industry to the benefit of the industry and the nation as a whole, especially taxpayers. As Congress considers the changing the federal procurement landscape, we offer the following points for consideration during your evaluation of reverse auctions.

a. Reverse Auctions Do Not Provide Benefits Comparable to Currently Recognized Selection Procedures for Construction Contractors

Vendors promoting online reverse auctions are selling technology for which there may be legitimate economic justifications for some types of procurements. However, those vendors have yet to present persuasive evidence that reverse auctions will generate real savings in the procurement of construction or will provide benefits of “best value” comparable to currently recognized selection procedures for construction contractors, which have been carefully and specifically tailored for all types of construction. Manufactured goods are commodities subject to little or no variability or change in manufacture or application. In comparison, construction services are project-specific and inherently variable. Each construction services contract is subject to the unique demands of the project, including: the geography—including but not limited to site conditions, the seasonality of certain construction activities, project proximity to major suppliers, and site ingress and egress in conjunction with other landowners—the needs, requirements, personnel and budgetary criteria of the owner, specific and unique design features, construction requirements and parameters, and the composition of the project team.

Federal procurement laws recognize that construction stands apart from commodities or manufactured goods. AGC contends that vendors that promote reverse auctions for construction services misuse a procurement process originally designed for commodities. It ignores the unique nature of construction. Construction contractors, specialty contractors, subcontractors and suppliers offer and provide a mix of services, materials and systems. They do not “manufacture” buildings, highways, or other facilities. In fact, the construction process is fundamentally different from the manufacturing process.

b. Reverse Auctions Do Not Guarantee Lowest Price

In the context of construction, AGC believes that most of the claims of savings are unproven and that reverse auction processes may not lower the ultimate cost of construction. For example, “winning” bids may simply be an established increment below the second lowest bid not the lowest responsible and responsive price. Moreover, in reverse auctions, each bidder recognizes that he or she will have the option to provide successively lower bids as the auction progresses. As a result, a bidder has no incentive to offer its best price and subsequently may never offer its lowest price—as opposed to during low price technically acceptable procurements and other contracting approaches. In addition, savings from reverse auctions can be one time occurrences.

c. Reverse Auctions May Encourage Imprudent Bidding

Reverse auctions create an environment in which bid discipline is critical yet difficult to maintain. The competitors have to deal with multiple rounds of bidding, all in quick succession. The process may move too quickly for competitors to accurately reassess either their costs or the way they would actually do the work. If competitors act rashly and bid imprudently, the results may be detrimental to everyone, including the owner. There are even reported cases in which owners actually step in to keep an overzealous supplier from obtaining an order that would potentially jeopardized the business viability of the supplier. Absent such steps, imprudent bidding may lead to performance and financial problems for owners and successful bidders, which may have the effect of increasing the ultimate cost of construction as well as the cost of operating and maintaining the facility.

During reverse auctions, small construction businesses are most likely to fall victim to such imprudent bidding and experience the greatest harm. Small construction businesses have less cash flow and reduced ability to handle risk than non-small construction businesses. Federal construction spending is down over 20 percent since August 2011 according to the U.S. Census Bureau. And, the outlook for public construction remains grim as agencies at all levels of government continue to cut construction spending. Given this reality, small business contractors may simply bid a job below cost to maintain some form of cash flow to remain in businesses. Additionally, some may fall victim to the auction's time restraints and consequent knowledge gap. Under pressure to win the job, a small business may unwittingly underbid, thinking that the subcontractors it has lined up would perform at that low of a price. Unable to have subcontractors perform the work, the prime small business may not have the capability to actually perform all of the work on its own and default. And, to add insult to injury, the federal government can even file a claim against the contractor when it underbids a contract under the False Claims Act.¹

d. Reverse Auctions Do Not Allow Thorough Evaluation of Value, Unlike Negotiated Procurements

Where price is not the sole determinant, federal owners increasingly have utilized processes focused on negotiation to expand communication between the owner and prospective contractors for the purpose of discussing selection criteria such as costs, past performance and unique project needs. These processes recognize the value and quality of project relationships that share expertise to promote greater collaboration among the owner and project team members. These processes also consider quality, safety, system performance, time to complete and overall value that can, in fact, outweigh the lowest price to arrive at the best value for the owner. Such an

¹ In the case of *Hooper v. Lockheed Martin Corp.*, the U.S. Court of Appeals for the Ninth Circuit ruled for the first time that underbidding or making false estimates in bids or proposals submitted in response to federal government solicitations may constitute violations of the False Claims Act. In a situation where a bidder needs a contract to maintain cash flow, the reverse auction can serve as an easy way for some contractors to do that. However, as this case reflects, there can now be legal liability for doing so that could further endanger the company. For more information see http://www.mckennalong.com/media/site_files/1979_FCA%20Article.pdf

approach also offers both the owner and contractor the opportunity to discuss and to clarify performance requirements of the project.

On the other hand, reverse auctions do not promote communication between the owner and bidders. Rather, they promote a dynamic in which bidders repeatedly attempt to best each other's prices. In fact, reverse auctions between buyers and suppliers often have a deleterious effect on the relationship between buyer and seller. Non-price factors of consequence to the owner, such as quality of relationship, past performance, scheduling, long-term maintenance and unique needs, are deemphasized in the auction. As a result, reverse auctions do not offer owners an opportunity to evaluate non-price factors.

e. Sealed Bidding Assures that the Successful Bidder is Responsive and Responsible

Where price is the sole determinant, the sealed bid procurement process is well-established to ensure integrity in the award of construction contracts. Under sealed bid procurement each proposer offers its best price and bids are evaluated through the use of objective criteria that measure responsiveness of the bid to the owner's articulated requirements and the responsibility of the bidder. In this manner, sealed bidding ensures fairness and value for the federal owner. On the other hand, reverse auctions ignore this tradition. The pressure and pace of the auction environment removes any assurance that initial and subsequent bids are responsive and material to the federal owner's articulated requirements. These auctions expose federal owners to the real possibility that they may award contracts to what would otherwise be non-responsive bidders. In addition, reverse auctions ignore the protections of the sealed bid procurement's laws, regulations and years of precedent that address critical factors and ensure the integrity of the process.

f. Reverse Auctions Limit Competition

My company—as well as many AGC members of all sizes—choose not to participate in reverse auctions for all of their risks and faults articulated above. Again, AGC strongly supports full and open competition for contracts necessary to construct improvements to real property. We contend that reverse auctions create an environment where competition is unnecessarily limited to the detriment of the federal government and taxpayers. In fact, we contend that no objective public or private study, including a U.S. Army Corps of Engineers (USACE) study on the issue, has provided persuasive evidence that reverse auctions generate the best cost, or best value for the procurement of construction services.

II. Federal Agency—USACE—Report, Experience and Policy on Reverse Auctions

We have reviewed the findings of a federal agency—USACE—study, published in 2004 entitled “Final Report Regarding the U.S. Army Corps of Engineers Pilot Program on Reverse Auctioning” (see enclosure). The report determined that although reverse auctioning had potential in the purchase of “simple commodities” where variability is exceedingly small or nil (identical products under identical conditions), its use for the purchase of construction services where the dynamics and variables are just too diverse “should be the very rare exception and not the rule – if used at all.” The USACE report further states that on the rare occasion reverse

auctioning may be considered as an acquisition method, such consideration should only be made after sealed bidding has failed.

On March 6, 2008, Major General Ronald L. Johnson, former Deputy Commanding General of USACE, testified before the House Committee on Small Business on this very issue. MG Johnson testified that “[t]he Corps, through our pilot study, found no basis to claim that reverse auctioning provided any significant or marginal savings over a traditional contracting process for construction or construction services.” MG Johnson also testified that “[w]hile this tool may be appropriate and beneficial in more repetitive types of acquisition, we did not find it to be a useful tool for our construction program and do not currently utilize it today to any great extent.”

Most recently, on May 23, 2013, USACE Engineering and Construction Chief James C. Dalton, P.E., also testified before the House Committee on Small Business on a similar topic. Mr. Dalton noted that reverse auction procurement “provides a benefit when commodities or manufactured goods procured are of a controlled and consistent nature with little or no variability. Construction is not a commodity.” He went on to state that “procuring construction by reverse auction neither ensures a fair and reasonable price nor a selection of the most qualified contractors.” As a result of its experiences, USACE does not procure construction services using reverse auction procurement.

Furthermore, the federal government has elsewhere acknowledged that construction services stand apart from commodities or manufactured goods. In a July 3, 2003 memorandum from Office of Federal Procurement Policy Administrator Angela Styles, the government states that “[n]ew construction projects and complex alteration and repair, in particular, involve a high degree of variability, including innumerable combinations of site requirements, weather and physical conditions, labor availability, and schedules.” This memorandum was sent to all federal procurement executives to encourage them not to treat construction as a commodity for government procurement purposes.

III. Reverse Auctions in the Department of Veterans Affairs and the General Services Administration

Over the years since USACE’s first-hand insight on reverse auction procurement of construction services, AGC has found that some agencies—including the Department of Veterans Affairs (VA) and the General Services Administration (GSA)—continue to use or push this acquisition tool for construction. By no means are these two agencies alone. AGC has also brought the inappropriate use of reverse auctions to the attention of the National Parks Service and other agencies within the Department of Interior. For the purposes of today’s hearing, we will address our concerns with the VA and GSA.

a. Department of Veterans Affairs

The VA construction program separates into two appropriation accounts: (1) minor construction, for projects of \$10 million or less; and (2) major construction, for projects over \$10 million. Similarly, the VA structures its construction program into two organizations, one where the 22 regional Veterans Integrated Services Network (VISNs) offices procure minor construction

contracts and the other in the Office of Construction and Facilities Management (CFM) that handles major construction contracts.

In AGC's experience, the inappropriate use of reverse auction rests with the VISNs and not with CFM. AGC has tried to reach out to VISNs that utilize this acquisition tool to inform them of prior federal agency experience and the inherent risks they bring. However, they have not been responsive. As such, AGC recently reached out to CFM about minor construction project awards procured through the reverse auction process since 2011. Those awards included the following 14 examples:

- 1.** VA261-13-B-0854, Renovation Support – Facility Space Realignment, San Francisco VA Medical Center, California; Award: \$888,508.80
- 2.** VA247-13-R-1355, Floor Maintenance and Repair, Central Alabama Veterans Health Care System (CAVHCS), Montgomery and Tuskegee, Alabama; Award: \$727,924.10
- 3.** VA247-13-Q-1567, Place Ductwork and Equipment, Atlanta VA Medical Center, Decatur, Georgia; Award: \$283,250.00
- 4.** VA247-13-B-1655, Auditorium Upgrades, Ralph H. Johnson VA Medical Center, Charleston, South Carolina; Award: \$224,540.00
- 5.** VA2417-13-R-0228, Stairwell Repairs, Carl Vinson VA Medical Center, Dublin, Georgia; Award: \$208,352.52
- 6.** VA247-13-R-1560, Fall Protection Installation, Atlanta VA Medical Center, Decatur, Georgia; Award: \$101,053.30
- 7.** VA262-12-Q-0950, Construct Concrete Slab Parking Pad with Security Fence, VA Medical Center, North Las Vegas, Nevada; Award: \$86,700.66
- 8.** VA262-13-Q-0514, Install/Replace Flooring, VA Medical Center, North Las Vegas, Nevada; Award: \$82,297
- 9.** VA247-12-R-1390, Floor Restoration Building 802, Charlie Norwood VA Medical Center in Augusta, Georgia; Award: \$81,267.00
- 10.** 542-11-4-5306-0076, Retaining Wall Repair, VA Medical Center, Coatesville, Pennsylvania; Award: \$75,639.08
- 11.** VA247-12-R-1396, Floor Restoration, Charlie Norwood VA Medical Center in Augusta, Georgia; Award: \$52,009.85
- 12.** VA247-13-Q-1348, Medical Air Compressor Installation, VA Medical Center, Fort McPherson, Georgia; Award: \$51,685.40
- 13.** 561-13-4-503-0021, Remodel of Homeless Services Domiciliary, Lyons, New Jersey; Award: \$47,728.71
- 14.** VA247-13-Q-0604-01, Roof Repairs, Carl Vinson VA Medical Center, Dublin, Georgia; Award: \$25,000

All of the solicitations previously mentioned were small business set-aside projects, many of which were for Service-Disabled, Veteran-Owned small businesses. AGC holds that the VA should not jeopardize the financial stability of these veteran small businesses, whose development and well-being is within the VA's mission, for a short-sighted and unproven construction services procurement method already abandoned by the largest federal construction agency.

Additionally, these VA contract awards were for the procurement of professional construction services and not for the purchase of a simple commodity, commercial item or mere maintenance. AGC holds that the VA misclassified these contracts, often as some form of simple maintenance rather than as professional construction services. For example, the VA Northern California Health Care System awarded a nearly \$900,000 contract (VA261-13-B-0854) for “numerous interior renovations throughout multiple buildings at the San Francisco VA Medical Center. . . [for which] [t]he contractor shall provide all labor, materials, and equipment.”

Here, the VA sought to solicit construction services under the guise of simple maintenance of structures and facilities. However, under no circumstance were the tasks equivalent to cleaning bathrooms. In fact, the solicitation called for over 20 rooms to be renovated in some fashion, including but not limited to work on flooring, plumbing, mechanical and electrical installation. The solicitation also included construction services calling for the use of fire-stopping construction practices and construction operations occurring during business hours in a hospital facility. Additionally construction services contractors were responsible for worksite safety for the contractor workforce and the VA facilities employees and patients.

For another example, the Carl Vinson VA Medical Center in Dublin, Georgia, awarded a \$25,000 “roof repair” contract (VA247-13-Q-0604-01) as a simple “repair or alteration of structures and facilities.” However, this project was not merely a roof repair; it appears to be a complete roof replacement. Roof replacement is a complex construction service. It should not be procured through a game-like, online reverse auction process in which price is the only factor.

Whatever the cost of the total project, construction requires professional expertise. It is subject to, among other things, weather conditions, rapidly changing diesel fuel and material prices, as well as conditions that introduce an extreme degree of variability to construction, like changing labor supply, workforce safety, and equipment costs and time. Additionally, construction projects can include unforeseen site issues, such as the existence and necessary safe removal of hazardous materials that were not disclosed to the contractor or known to the owner.

The complexities of these processes simply do not compare to the purchase of an off-the-shelf commercial item or mere maintenance. The reverse auction process ignores the expertise of the contractor or the unique nature of construction. Construction contractors, specialty contractors, subcontractors and suppliers offer and provide a mix of services, materials and systems. Again, they do not “manufacture” buildings, highways, or other facilities.

b. General Services Administration

Earlier this year, GSA launched an online reverse auction platform (<http://reverseauctions.gsa.gov/>) that enables any federal agency to procure construction services through a reverse auction. AGC notified GSA that it should remove from its Reverse Auction Platform the construction services options outlined in Schedule 56—noted below.

Specifically, the Reverse Auction Platform enables federal agencies to procure “Buildings and Building Materials, Industrial Services & Supplies” through Schedule 56. Schedule 56 includes “Ancillary Repair and Alteration requiring minor construction (includes Davis Bacon and

construction clauses); and Installation and Site Preparation requiring Construction, which is necessary for Roof Repair or Replacement, to install a Pre-Engineered or Prefabricated Building or Structure, to install an Above Ground Storage Tank or to Install Alternative Energy and Power Distribution Solutions (includes Davis Bacon and construction clauses) ” and construction of foundations.²

While GSA may intend for the procurement of what is misclassified as “simple,” “ancillary” or “preparatory” construction services through a reverse auction, in practice, such undefined terms could allow for federal agency misuse of the Reverse Auction Platform, costing the federal government—and tax-payers—more in the long run. Determining which contractor is the most qualified at the lowest price to clear and improve land for construction, construct a building foundation, install prefabricated buildings, and repair roofs, among other things in Schedule 56, demands that a procurement agency evaluates a host of source selection factors together, which reverse auctions do not consider. For example, installation of prefabricated buildings can require a degree of design-build project delivery expertise that varies among contractors. However, a reverse auction only evaluates price, whereas established federal procurement practices allow for the consideration of this expertise.

To GSA’s credit, it met with AGC in September on this issue. At the meeting, GSA showed its willingness to consider AGC’s input as to why specific construction services items in Schedule 56 should not be procured through reverse auctions. In addition the agency was open to feedback on how to prevent contract misclassification.

IV. Congress Should Prohibit the Use of Reverse Auctions for Construction Services Contracts and Support Measures Like H.R. 2751.

As our testimony and the record evidence, the experiences of one federal agency do not necessarily mean another federal agency will learn from them. Rather, we find that each federal agency learns the mistake of construction services reverse auction procurement on its own. This will neither benefit competition and the construction industry—especially small businesses—nor the American taxpayer.³

As such, AGC holds that the only solution is for Congress to enact a law that prohibits reverse auction procurement of construction services. To the credit of Chairmen Graves, Hanna and Ranking Member Meng, they recently introduced H.R. 2751, the Commonsense Contracting Act

² General Services Administration, “Buildings and Building Materials, Industrial Services and Supplies Schedule 56: Frequently Asked Questions (FAQs),” available at: <http://www.gsa.gov/graphics/fas/FAQs-Buildings-Schedule56.pdf>

³ As noted previously noted, the federal construction marketplace has retracted by over 20 percent since August 2011. This has come as a direct result of budget cuts—including sequestration—and the prevalence of continuing resolutions that prohibit necessary new project starts, which push back projects to outlying years. Some contractors have, in part, shifted resources towards competing on more private contracts, as that market has slowly improved, than they did previously. As such, competition for federal construction projects may decrease, impacting the price to the government. And, in relation to reverse auctions, those contractors that depend on federal work may become more desperate to win awards and imprudently bid on reverse auctions. Again, as previously noted, this can lead to possible contract defaults that cost federal agencies and taxpayers precious time and resources. In addition, such imprudent bidding can cause desperate prime contractors to put undue pressure on subcontractors, jeopardizing their businesses.

of 2013. This bill would prohibit federal agencies from bidding construction contracts suitable for award to a small business through reverse auctions.

AGC previously testified in support of such a measure earlier this year and echoes its full support for H.R. 2751 today. However, this bill will not completely prevent federal agencies from using reverse auctions to procure all construction services contracts. Consequently, AGC would support additional legislative efforts to prohibit reverse auctions for all construction services federal contracts.

Thank you for this opportunity to provide the views of the construction contractor industry in this important matter.