

NASCA 2006  
Outstanding Program Awards  
Application

Program Title: Minnesota's Online Auction Initiatives

Check one:  Individual State Award  Partnership or State/Private Entity

NASCA Member State: Minnesota

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**Deadline: March 1, 2006**

The application package must be received no later than March 1, 2006 for consideration.

Submit nominations electronically to NASCA Staff at [nasca@csg.org](mailto:nasca@csg.org). Or mail a CD or disk to:  
NASCA,  
c/o Council of State Governments, 2760 Research Park Dr., PO Box 11910, Lexington, KY  
40578-1910.

All submissions must be submitted electronically including copies of the justification and executive summary.

## Executive Summary

The State of Minnesota introduced its online auction program in June 2001 for the procurement of commodities. Since January of 2004, Minnesota has broadened its use of online software to include forward auctions for the sale of surplus items.

A reverse auction is a structured bid process that links Web-based technology with traditional bidding methods to obtain better pricing for the customer. The process is sometimes referred to as “eBay in reverse.” It is called a reverse auction because it is a buyer’s auction in which pre-qualified vendors compete in a real-time, online auction to determine the lowest responsible bidder for award, order or contract.

Since rolling out the program, the Department of Administration’s Materials Management Division has purchased over \$57 million in goods and services by reverse auction for State agencies and local units of government. Recent purchases have ranged from radar detectors and snowmobiles to rainwear and computer software development.

Three years ago, at the urging of Governor Tim Pawlenty, the department greatly accelerated the use of reverse auctions. Through the end of December 2005, the State has conducted 212 reverse auctions, with awards to 183 vendors. Minnesota’s creative method for soliciting reverse auction bids has resulted in documented real savings of over \$5 million.

The screenshot shows a web browser window titled 'Archimedian Software - Microsoft Internet Explorer' displaying an online auction interface. At the top, a blue banner indicates 'Time Remaining: 0 days 0 hrs 2 mins 17 secs'. Below this, the lot name is 'Total Paper Lot' and the discount percent is set to 2.00. Summary statistics show a total value of 693,900.00, a discounted total of 680,022.00, and a lot adjustment total of 671,048.64. A 'Submit' button is visible. The main table lists five line items for different types of copy paper, each with a quantity and a price per case. To the right of the table, there are two 'Results' sections showing the top three ranked bidders for each line item, including their rank and bid amount. A 'Send Message' button is located at the bottom right of the interface.

LI #	Part Number	Quantity	\$ per case	Tot / Adj Tot	Dec	Lead	Submit
1	Copy Paper- 20 pound	1000 Cases	93.90	93,900.00 / 91,749.69			
2	Copy Paper- 24 pound	1000 Cases	125.00	125,000.00 / 124,000.00			
3	Copy Paper- 45 pound	1000 Cases	125.00	125,000.00 / 122,137.50			
4	Legal Sized Copy Paper	1000 Cases	125.00	125,000.00 / 124,000.00			
5	Legal Sized Paper- 45 pound	200 Cases	125.00	25,000.00 / 24,427.50			

  

Rank	Bid
1	671,048.64
2	740,767.67

  

Rank	Bid
1	91,749.69
2	92,601.91
3	96,844.23

  

Rank	Bid
1	124,000.00
2	147,956.80

  

Rank	Bid
1	114,416.41
2	122,137.50
3	137,771.10

  

Rank	Bid
1	124,000.00
2	147,936.96

  

Rank	Bid
1	24,244.20
2	24,427.50
3	27,857.12

*An online reverse auction in progress.*

Reverse auctioning is a growing procurement strategy that has been demonstrated to work effectively and save State resources when purchasing commodities and services, while also benefiting small businesses in Minnesota. Seventy-five percent of the 183 contracts awarded by the department’s program were to vendors with Minnesota addresses. Use of reverse auctions for professional/technical service contracts has resulted in awards to 14 computer consulting firms – all from Minnesota. These auctions saved State agencies 3.7 percent on contracts valued at \$4 million.

Although other governmental organizations have instituted reverse auctions programs, Minnesota’s approach is innovative and unique with respect to risk mitigation, tracking savings

and use with intellectual services. The state's program is fully transferable to other states and to local units of government, and offers the potential for significant cost reductions.

Since 2004, Minnesota has utilized components of its reverse auction software to conduct online forward auctions of surplus property. To date, over 1,000 lots have been sold through 129 auctions. Items have ranged from an airplane and houses to collectible dinnerware from the Governor's Residence. These auctions have generated over \$1.5 million in revenue, over 90 percent of which has been returned the State agencies and local governments that were the owners of the property.

Online surplus auctions have also allowed the State to dispose of items that might otherwise have ended up in landfills. Instead of having to pay for the demolition of structures or for the removal of equipment, online sales have reached markets that have allowed Minnesota to avoid the cost of disposing of these items while generating additional income for the State.

## Reverse Auctions

From the first government office's use of reverse auction, state procurement professionals have been bombarded by promises of millions of dollars in savings. The State of Minnesota, while often an early adopter of new technologies, looked critically at this opportunity. During a time when most states were feeling the pinch of a contracting economy, the idea of saving hundreds of millions of dollars a year on procurements appeared very attractive. Instead of immediately signing on, however, Minnesota decided to approach this new procurement tool cautiously.

Among our questions:

- Do reverse auctions really save money? And if so, how much?
- What is the impact of reverse auctions on small businesses?
- In short, are reverse auctions really, as some software vendors told us, the best thing ever to happen to procurement?

It all just seemed too good to be true. The Department of Administration's Materials Management Division (MMD) was charged with researching the promises and pitfalls of reverse auctions.

Between June 2001 and September 2003, MMD used four different full-service reverse auction providers to issue eight pilot solicitations. Some of the items purchased in this manner included aluminum (for making license plates), copy paper, brochure printing and all-terrain vehicles (ATVs).



*Minnesota's very first reverse auction was for aluminum for license plate manufacturing.*

Next was the task of determining the success of these procurements. The department considered, and rejected, two options for measuring savings:

1. New contract price vs. previous contract price.
2. Reverse auction purchase price vs. recent purchase price.

The first was rejected because it did not consider numerous market factors. When the aluminum reverse auction contract price was compared to the previous contract (from five years earlier), savings were calculated at \$35,000 per year, or 6.6 percent. However, this number failed to include changes in market conditions: a 10 percent increase in the price of aluminum and a doubling in the price of fuel.

The second method was rejected because of the difficulty of accurately comparing purchases. Variables such as required features and delivery locations, for example, made comparing new ATV purchases with vehicles purchased even a week earlier an impossible task. In addition, a printing job for a brochure purchased via reverse auction was a unique purchase. Items that are rarely or infrequently purchased would reintroduce the market issues that were raised in the first method.

Only an “apples to apples” approach could accurately track the savings that were directly attributable to the reverse auction process. The department decided that prospective bidders would be required to submit a standard, paper-based solicitation response, including pricing. The solicitation included the following instructions to prospective vendors:

- Your paper response should be your best offer, consistent with your normal bidding practices, ignoring the reverse auction component.
- You will enter the starting price for the reverse auction during the pre-bid.
- Your reverse auction starting prices can be different from the price submitted in your paper response.

Since reverse auctions are typically scheduled within a few days after the deadline for vendor response submittals, the two separate prices could be compared, with the difference showing the true value of the reverse auction without market effect.

In August 2003, MMD announced a solicitation for software that would allow it to conduct reverse auctions in-house. Eight responses were evaluated and, in September, a contract was awarded to eNegotiation, Inc., dba Archimedian Software, for a one-year license to conduct an unlimited number of reverse auctions.

The unlimited license has given MMD the freedom to experiment with purchases for dollar amounts far below those recommended by most full-service reverse auction providers, with some surprising results. For example, a reverse auction for the purchase of three snowmobiles yielded savings of \$5,360, or 25.3 percent. The software contract was renewed in September 2005 for an additional year. All members of the Minnesota Cooperative Purchasing Venture (CPV) – which includes local governments, school districts and higher education institutions – can order off Minnesota’s contract at annual rates ranging from \$22,500 for fewer than 20 reverse auctions, up to \$70,000 for an unlimited number of reverse auctions.

As of December 2005, Minnesota has awarded 183 contracts by using reverse auctions. Projected savings over the life of the contracts are almost \$5.1 million. Of the 183 contracts, 75 percent were awarded to vendors with a Minnesota address; 37 percent to businesses in non-metropolitan areas of Minnesota; 31 percent to small Minnesota businesses that are formally certified as Targeted Group or Economically Disadvantaged; and 12 percent to other small Minnesota businesses. These numbers are significant because, typically, Minnesota small businesses (all categories combined) bid on only 47 percent of these contracts. None of the contracts awarded by reverse auction went to businesses that are on the StarTribune (startribune.com) list of the “top 100” companies in Minnesota.

Despite some resistance from both agencies and service providers, MMD in early 2005 tested reverse auctions for obtaining professional/technical services. As a result, the department made 14 awards to computer-consulting firms. All are located Minnesota. Seven of the 14 contracts (50 percent) went to small businesses. These auctions will potentially save State agencies \$147,349 on contracts valued at slightly more than \$4 million.

Additionally, MMD has initiated a new master contract program for computer vendors willing to participate in reverse auctions. Despite concerns that businesses would balk at the reverse auction requirement, 218 vendors responded that they would participate in reverse auctions and

were awarded master contracts. Of these master contracts, 178 (82 percent) were awarded to businesses with Minnesota addresses.

Instead of hurting small businesses, the use of reverse auctions may actually be to their benefit, according to the data. Among the findings of an MMD survey of 101 vendors that had received invitations to participate in a Minnesota reverse auction:

- All of those who participated in at least one reverse auction liked at least one aspect of the process.
- Most of those who participated in more than one reverse auction liked the process.
- Those who never participated thought the whole idea was terrible.

Conclusion: People don't like change. However, once they understand how they can be successful using the new process, they become more accepting – and even appreciative – of the change.

Market prices have fluctuated for as long as there have been buyers and sellers. The difference is, instead of taking months or even years to discover the market equilibrium for a given product or service, reverse auctions can give a true market price today. This is important because market prices can change for a great variety of reasons. Fluctuations in the prices of raw materials, increased/decreased competition, shipping costs and new technology are just some of the factors that can affect today's price for any given product. Reverse auctions help ensure that buyers get the best price today.

Reverse auctioning is a tool – one of the many that buyers should employ. Before advertising a solicitation for any purchase, there are several considerations that will help ensure a successful procurement:

- Estimate the size of the potential bidding supplier pool. An effective auction requires at least two bidders.
- Assess the types of vendors that are available. Is it only a manufacturer, or are there dealers? Evaluate the relationship between manufacturers and dealers. Sometimes they compete with each other; sometimes they will not.
- Determine if the market is currently competing on price for business. If not, establish the criteria upon which to base an award decision. This should help in deciding if a reverse auction is appropriate for a purchase.
- Consider the product or service that is being purchased: Is the item highly specialized, or is it widely available? Are there approved equals? Items that are only available from one source are not good reverse auction candidates.
- Market the solicitation.
- Consolidate purchases. Internal advertising of an upcoming purchase can remind others of purchases that they need to make, thereby increasing the opportunity for larger, aggregated purchases. Typically, the larger the purchase, the lower the per-unit cost.

Reverse auctions are a cutting-edge procurement strategy. Minnesota's experience demonstrates that reverse auctions can work effectively and save State resources on purchases while also benefiting local small businesses. Reverse auctions reward those firms that can most efficiently deliver quality products and services.

Minnesota's reverse auctions have also garnered some positive media attention:

- Minneapolis StarTribune story picked up by the Associated Press (2/17/04): "State saves money through Internet reverse auctions"
- Government Performance Project – Grading the States 2005: "Minnesota is a pioneer in the use of reverse auctions"
- The National Association of State Chief Administrators' NASCA News (11/9/05): "Reverse auctions trim \$5 million from Minnesota State government purchases"

## Surplus Auctions

The Surplus Services section of MMD is also a national leader in the online disposal of surplus goods. The public has the opportunity to bid on a wide range of surplus state goods through our department portal, [www.mmd.admin.state.mn.us/mn03008.htm](http://www.mmd.admin.state.mn.us/mn03008.htm). As of the date of this application, Surplus is offering retired fleet vehicles, premium low-mileage pickup trucks, a nearly new embroidery machine, vehicles forfeited to law enforcement agencies and a complete house that must be moved from land controlled by the Minnesota Pollution Control Agency.

Although "live" surplus auctions have been a Minnesota staple for years, the Department of Administration entered the rapidly growing virtual auction arena in January 2004 with the successful sale of a used Cessna airplane.

Initially thought of as a tool for selling "specialty" items, experience with auctions of more mundane property stimulated interest in further online sales. Over the past two years, the department has sold everything from pool tables and scrap steel to power wheelchairs and furniture from the Governor's Residence. The State recently sold two houses (land not included) through the online auction process. But the airplane sale, perhaps because it was the first, remains a defining moment for the program.

Skeptics initially chortled over the \$85,000 minimum price that the State set for the surplus aircraft. MMD was inundated with phone calls from people saying it wouldn't ever sell for that much, and asking what would be done when it didn't sell. When the auction closed, the top bid was \$90,250 from a private party in Ohio. The online aspect of the auction helped MMD reach someone who would not have traveled to Minnesota for a live auction, just for the chance of winning the airplane. Minnesota taxpayers got a better deal, too. Other successes were ahead.



*A State Capitol "Witch's Hat"*

When four vent covers on the State Capitol building were replaced, the State could have sold the century-old originals for scrap (one was claimed by the Minnesota Historical Society), for about \$10. The three surplus vent covers, known as "witches' hats," were instead sold online for a total of \$1,387.

Again, the State questioned whether it was receiving the best possible prices by selling this way. Surplus conducted an apples-to-apples comparison.

Surplus Services in late 2005 received 20 Ford E350 and E450 Super Duty buses from the Minnesota Metropolitan Council's ADA Paratransit Service. On Nov. 2, Surplus sold 10 of the buses online. Three days later, the remaining 10 buses were offered at a live auction. The online sales averaged over \$1,600 above live auction winning bids. Online purchasers also were from as far away as Mississippi and Canada, while the live-auction purchasers were generally from the Twin Cities metropolitan area.

In addition to offering State agencies and local governments an outlet for selling surplus and seized property to the public, online auctions are an effective way of avoiding costs.

When the Faribault correctional facility needed to remove some equipment from their auto-body repair shop, they received a quote of \$45,000 for its disassembly and disposal. Faribault officials contacted Surplus Services about the possibility of selling the equipment, with the understanding that the purchaser had to remove it. MMD decided to sell it through an online auction. The winning bid came in at \$14,802. In addition to realizing over \$13,000 in net proceeds, the agency avoided \$45,000 in removal and disposal costs.

The results were similar from the online sale of several semi-truckloads of surplus office furniture that had accumulated through the merger of the departments of Economic Development and Economic Security. The entire lot sold for only \$10, but it would have cost a small fortune to haul it away and dump it in a landfill.



*The state acquired this house near Long Prairie because it was located within an expanded landfill buffer zone and had to be moved or razed. It sold in an online auction for \$16,000.*

Surplus Services has researched outsourcing online sales to one of the many surplus auction sites that are available today. However, the hefty fees and sometimes-unreasonable requirements placed on bidders can reduce returns and limit the pool of customers. Since starting online sales, Surplus has sold 1,013 lots to the public for a total of \$1,545,028. Of that amount, \$1,395,126 was returned to agency budgets. In several instances, agencies expressed amazement at the sale prices realized through online auctions.

## Conclusion

Minnesota's approach to procurement through reverse auctions is innovative and unique for the following reasons:

- A reasonably priced, unlimited-use contract has allowed Minnesota to experiment broadly at no risk to find out what does and does not work.
- Minnesota's creative method for soliciting both traditional bids and reverse auction bids (and awarding based on whichever method is most advantageous to the State) has resulted in documented real savings of over \$5 million.
- Minnesota is on the leading edge with its use of reverse auctions for intellectual services and has developed master contracts with 218 vendors willing to compete for the State's computer consulting business through the use of reverse auctions.

Minnesota's creative approach to risk mitigation, tracking savings, and use with intellectual services are fully transferable to other states and offer them the potential for significant cost reduction.

The utilization of online surplus auctions has allowed the State of Minnesota to reach across the country and beyond to find bidders who can use the goods that the State no longer needs. This has resulted in positive environmental and economic impacts for the citizens of this State. Online surplus auctions provide a high value service for Department of Administration customers at very little cost.