

CASES OF SBIR WASTE, FRAUD AND ABUSE
COMPILED BY SENATE COMMERCE COMMITTEE STAFF

BACKGROUND

In February 2009, it was publicly disclosed that federal authorities were investigating a Florida technology engineering business called New Era Technology (NETECH) for Small Business Innovation Research (SBIR) Program fraud. In a filing in a Florida federal district court, investigators alleged that NETECH's owners repeatedly submitted fraudulent SBIR proposals and invoices to the National Aeronautics and Space Administration (NASA) and used the award money to enrich their children and to purchase personal property for themselves, including a BMW automobile and a condominium in Ft. Lauderdale, Florida.¹

To learn more about the NETECH case, on March 6, 2009, Chairman Rockefeller wrote a letter to NASA requesting all documents related to contracts awarded to the company.² After discovering that NETECH had won contracts from two other agencies, Chairman Rockefeller made similar requests to DOD and DOE on May 6, 2009.³

According to the documents produced through these requests, since 1999, NETECH has received seven Phase I and five Phase II SBIR or Small Business Technology Transfer (STTR) Program contracts worth \$3,379,566 from NASA, the Air Force, and the Navy. Federal investigators allege that NETECH defrauded the government in the course of performing most of these contracts. NASA Inspector General (IG) officials recently informed Committee staff that their criminal investigation of NETECH is ongoing.

In the course of investigating the NETECH case and the SBIR program, Commerce Committee staff learned of other instances in which SBIR awardees defrauded the government. Using online searches and case files produced by the Inspectors General of NASA and NSF, Committee staff has collected 29 cases of SBIR fraud between 1990 and the present. These cases involved more than 300 SBIR or STTR contracts valued at more than \$100 million dollars. Information about these cases is presented in a table in the following pages.

Some of the cases ended in criminal convictions or civil penalties imposed under the federal False Claims Act, while others were resolved administratively within the respective IG offices and never made public. Based on the facts of each case, the table also estimates the number and dollar value of SBIR contracts that were at risk for waste, fraud, and abuse.⁴

Company Name	Description	Awards at Risk	Dollars at Risk	Year Investigation Closed
New Era Technologies (NeTech)	Company has been accused of improperly funneling NASA SBIR grant funds to personal bank accounts, and submitting fraudulent grant proposals and invoices. Search warrants were executed on February 25, 2009, and an investigation is ongoing. Company also received awards from DOD and DOE.	11	\$3,309,730	Ongoing
Materials and Electrochemical Research Corp.	Whistleblower suit, which the U.S. Department of Justice joined in May 2008, alleges that company forged signatures on financing statements for a number of successful Phase II proposals submitted to NASA, DOE, and the Army.	13	\$9,000,000	Ongoing
<i>Not Public</i>	Company owner made false statements to NSF to transfer a Phase II proposal to a different company than the company that performed the Phase I proposal.	2	\$599,941	2008
<i>Not Public</i>	Submitted two Phase I proposals to NSF that contained plagiarized text and figures.	4	\$1,477,475	2006
<i>Not Public</i>	Submitted proposals to NSF containing falsified information that led to the issue of the award for Phase I and II awards.	21	\$4,315,092	2006
<i>Not Public</i>	Originating from the OIG Hotline, the NASA OIG found in a joint investigation with the DOD OIG, that the company had submitted multiple duplicate proposals and reports to DOD, NSF and NASA .	2	\$159,981	2005

Lithium Power Technologies, Inc.	Through a whistleblower lawsuit, Lithium was found to have submitted false statements and duplicative proposals to various DOD components and NASA.	22	\$5,558,969	2005
M.L. Energia	Whistleblower claims led to a mail fraud conviction for false certifications, duplicative rewards, and plagiarized research. Awards came from NASA, NSF, DOD, DOE, USDA, and US Air Force.	17	\$2,314,000	2005
<i>Not Public</i>	After allegations that the awardee was misusing funds, an NSF OIG audit identified \$34,000 which was unaccounted for.	2	\$599,701	2004
Nanomaterials Research Corporation	A whistleblower alerted DOD that the owner was using awards for personal benefit (including a vacation home), submitting falsified time sheets, falsifying data, and submitting duplicative proposals. The company had received 50 SBIR grants from various agencies including NASA, NSF and DOD between 1994 and 1999.	50	\$19,000,000	2004
Arnav Systems, Inc.	NASA Office of Procurement informed NASA OIG that company was inflating its labor rates for a Phase II project.	2	\$669,946	2004
<i>Not Public</i>	Company was accused of mischarging labor costs on multiple DOD and NASA SBIR contracts.	17	\$5,769,618	2003
<i>Not Public</i>	Owner submitted false statements on proposals, including names and resumes of researchers not employed by the company. Owner overpaid himself \$20,000. Included 3 DOE and 1 NSF awards.	4	\$400,000	2003
LaserGenics Corporation	Submitted duplicative proposals to NASA and NSF, and made 12 false statements in DOD, NASA, DOE, and NSF proposals.	49	\$4,734,995	2002

<i>Not Public</i>	Based on an anonymous complaint, the NASA OIG discovered that the company had charged NASA \$100,000 for unallowable costs.	36	\$12,477,805	2002
<i>Not Public</i>	NASA OIG received information that company made false statements in proposals related to the principal investigator, and also forged signatures on grant applications.	2	\$139,982	2002
<i>Not Public</i>	Company received funding from NSF and the Office of Naval Research for same proposal.	2	\$170,000	2002
<i>Not Public</i>	NSF OIG was alerted by the FBI that the owner of the company had been accused of embezzling \$1.25 million from a foreign company. The NSF OIG determined company had obtained duplicate funding from NASA and the NSF for Phase I proposals, and had forged signatures of the CFO on falsified proposals.	2	\$50,000	1999
<i>Not Public</i>	Received duplicative awards from NSF and the Air Force for identical Phase I and Phase II Projects.	12	\$3,864,700	1999
<i>Not Public</i>	Company failed to disclose simultaneous pending Phase I proposals to the DOD and DOE.	2	\$150,000	1998
GMS Systems	Company submitted duplicate proposals to the Department of Education and National Institutes of Health.	3	\$110,000	1998
<i>Not Public</i>	Submitted duplicate proposals and fraudulently reported research results to NSF, NASA and DOD from 1991-1998. NSF SBIR reviewer purchased stock in company.	4	\$547,000	1998
<i>Not Public</i>	Submitted duplicate proposals to NSF and NASA, mischarged NASA for work, used subcontractors for more than 2/3 of the work.	27	\$6,895,528	1997

Electro-Optek	Received duplicative awards from NSF, NASA and DOD. Charged federal agencies for work that was not performed, plagiarized research, and misrepresented qualifications of researchers.	44	\$6,902,814	1996
AKM Associates	Submitted identical proposals and received duplicative awards from NSF, NASA, the Army and the Air Force.	17	\$2,204,452	1995
Excel Technology, Inc.	Submitted at least 36 false statements about duplicate proposals and rewards, key personnel and billing to NSF, NASA and DOD.	NA	\$2,001,573	1995
<i>Not Public</i>	Submitted false claims about principal investigator's employment eligibility and plagiarized data in final report.	4	\$391,118	1993
High Energy Laser Associates	Received Phase II NSF funds, but did not use them to perform work.	1	\$250,00	1990
<i>Not Public</i>	Anonymous letter alerted NSF OIG to plagiarized report data and duplicative proposals. Company had received grants from 7 federal agencies and submitted identical data tables in 20 different reports to these agencies.	49	\$11,519,521	NA
	TOTAL	300	\$105,583,941	

COMMITTEE STAFF ANALYSIS

The information presented in the table above represents a group of individual cases in which federal investigators and prosecutors collected evidence, developed facts, and in some cases, brought a civil suit or filed criminal charges. Viewed collectively, these cases provide important information about the features of the SBIR program that are most vulnerable to waste, fraud, and abuse.

Duplicative Proposal Fraud A review of the cases described in the table shows that the most common type of SBIR fraud appears to be the submission of so-called “duplicative” proposals to SBIR-awarding agencies. While SBIR regulations allow companies to submit the same research project to multiple agencies, they prohibit companies from accepting payment from more than one agency for the same work.⁵ In spite of this prohibition, there are a number of cases showing that some SBIR awardees have managed to receive multiple payments from different SBIR-awarding agencies for the same research project.

The fact that the SBIR program is vulnerable to duplicative proposal fraud has been a matter of public record since the mid-1990s. In December 1995, in what the New York Times called, “the largest case of fraud involving the main Federal program that steers research money to small businesses,” the government settled cases against two companies for misusing \$1.7 million in SBIR awards. Excel Technology of Hauppauge, NY, agreed to reimburse the government \$1.7 million and to pay \$1.6 million in penalties, while ESDI of Bohemia, NY, agreed to reimburse the government \$600,000 and pay penalties of \$150,000. The companies were accused of illegally accepting money from DOD, NASA and NSF for identical research proposals and for submitting research work that had already been completed at state universities.⁶

At about the same time, Congress heard testimony about the program’s vulnerability to duplicative proposal fraud. In March 1995, the then-Government Accounting Office (GAO) released a study warning, “the SBIR program is at a growing risk of willful or accidental financial abuse.”⁷ The report noted that in some cases, “a few companies received funding for the same proposals twice, three times and even five times before agencies became aware of the duplication.”⁸ According to GAO, unless informed by a whistleblower of the duplicative proposals, agencies had a very limited ability to identify duplicative proposals.⁹

The Senate Commerce Committee heard similar testimony about the vulnerability of the SBIR program to duplicative proposal fraud during a 1997 hearing examining major management issues at agencies under the Committee’s jurisdiction. When he was asked about SBIR fraud, NSF Deputy Inspector General, Philip Sunshine, told the Committee that, “compared to other programs at the agency, there is more fraud in the SBIR program than any other program...it is an ongoing problem and an issue we’re focusing on, I think I can report with confidence that the agency agrees with us that it is an issue.”¹⁰

Both GAO and the NSF Inspector General told Congress that the program was vulnerable to duplication fraud because there was no program-wide information system that allowed an agency to check if a company had submitted duplicative proposals to or recently won duplicative awards from other agencies. As the 1995 GAO report explained this problem, “...individual agencies maintain records of recent awards, but this information is generally not available to

other agencies. If an official in one agency wants to obtain information from another agency about a specific proposal or company, such information is available only through personal contacts and conversations.”¹¹

In the 1997 hearing mentioned above, the Senate Commerce Committee heard similar testimony expressing concern that the lack of information sharing between SBIR-awarding agencies made the program vulnerable to duplicative proposal fraud. NSF Deputy Director, Joe Bordogna, testified that, “a major problem here is one in which the agencies don’t have a system yet that’s quick to use, a computerized system to check all the input coming in. We just did a check with some arduous hand labor on the 208 or so proposals we presently have in hand. We found 12 overlaps.”¹²

When it re-authorized the SBIR program in 2000, Congress ordered the Small Business Administration (SBA) to create and maintain a public database containing information about SBIR awards, and a government-access database containing information about proposals submitted to SBIR-awarding agencies.¹³ In conversations with Commerce Committee staff over the past few months, officials responsible for administering and overseeing SBIR programs have repeatedly stated that a government-wide database of SBIR proposals would be a valuable tool for reducing duplicative proposal fraud. While SBA’s public “Tech Net” website now contains comprehensive SBIR award information, it still does not provide the SBIR proposal database mandated in the 2000 statute.

False Billing and False Representations The table above also shows that some companies have won SBIR awards based on proposals containing false information. Companies have misrepresented the qualifications of their researchers, presented plagiarized data as their own, and forged signatures on proposals in order to win grants or contracts. As a general matter, the awarding agencies rely on companies’ self-certification that the information in their proposals is accurate and truthful. A federal appeals court recently noted that “the DOD generally does not verify all of the information submitted in a proposal, and it depends heavily on the integrity of SBIR applicants.”¹⁴

In addition, after the SBIR grant or contract has been awarded, awardees have sometimes been able to exploit weaknesses in the program’s financial controls to bill the government for work it has not performed. While SBIR grants and contracts are based on a company’s agreement to perform a specified project for a fixed price, the SBIR statute requires agencies to make their payments “on the basis of progress toward or completion of the funding agreement requirements.”¹⁵ In other words, payments to companies are based on their “level of effort” – the actual hours and resources they put into the project.

Evidence collected by Committee staff during this investigation indicates that SBIR award recipients can actually work fewer hours than they propose in their budgets and still receive full award payments. Companies can submit invoices to agencies for the “budgeted” hours worked and then pocket the difference, because the agencies do not generally require the awardees to prove they actually worked the number of hours they proposed in the budget. Without a “budget-to-actual” reconciliation process, there is no way to determine if agencies are overpaying for services performed.¹⁶

For example, when the Department of Energy Inspector General (DOE IG) audited its agency's SBIR program in 2001, it identified significant weaknesses related to the agency's handling of invoiced costs submitted by program awardees. The IG noted that DOE, "generally limited its cost reviews to pre-award evaluations of the costs proposed in the application submitted by grantees; it did not, as we would have expected, place sufficient emphasis on post-award reviews of actual costs."¹⁷

According to this report, once an SBIR award was made, there was no established procedure within the agency to verify that the amount submitted on an invoice actually matched up to the work performed by an awardee. In its 2001 audit, the DOE IG did its own cost review by asking grantees for documentation to support invoiced costs and it found that DOE reimbursed grantees for questionable costs. In one example, three awardees did not provide any documented support for \$2.4 million in claimed costs. These awardees simply sent invoices to DOE and were paid without having properly documented the work. The IG concluded that although it supported the objectives of the SBIR program, it was concerned, "...that the shortcomings identified in this audit undermine the viability of the program."¹⁸

The DOE IG performed a follow-up audit of the DOE SBIR program in 2008 in order to determine if the previously observed weaknesses in the agency's program had been corrected. The audit found that the agency, "had not corrected all previously reported weaknesses in monitoring and administering the SBIR phase II grants program."¹⁹ Specifically, the report cited that, "action had not been completed to resolve about \$1.2 million of the approximately \$2.4 million of questionable costs identified in our previous audit,"²⁰ and that the agency was continuing the practice of, "not reviewing grant costs or closing out completed awards in a timely manner."²¹

ENDNOTES

¹ Verified Complaint for Forfeiture in Rem, *U.S. v. Real Property Located at 501 South Moody Ave., Unit 117, Tampa, FL* (Feb. 19, 2009) N.D. Fla. (No. 1:09 cv 41-MP/AK).

² Letter from Chairman John D. Rockefeller IV to Acting Administrator, NASA, Mr. Christopher J. Scolese (Mar. 6, 2009).

³ Letter from Chairman John D. Rockefeller IV to Secretary of Defense Robert Gates (May 5, 2009); Letter from Chairman John D. Rockefeller IV to Secretary of Energy Steven Chu (May 5, 2009).

⁴ For example, based on the allegation of the contractor's conduct in the NETECH case discussed above, Committee staff determined that 11 contracts worth \$3.3 million are potentially at risk for waste, fraud and abuse.

⁵ Small Business Administration, *SBIR Program Policy Directive 7(a)(1)(iii)* (online at: <http://www.sba.gov/SBIR/SBIR-PolicyDirective.pdf>) (accessed August 4, 2009).

⁶ *2 Companies To Repay U.S. in Fraud Case*, New York Times (December 10, 1995) (online at <http://www.nytimes.com/1995/12/10/us/2-companies-to-repay-us-in-fraud-case.html>)

⁷ General Accounting Office, *Interim Report on the Small Business Innovation Research Program* (March 1995) (GAO RCED-95-59).

⁸ *Id.*

⁹ *Id.*

¹⁰ Senate Committee on Commerce, Science and Transportation, *NASA and NSF Program Efficiency*, 105th Congress, (July 24, 1997) (S. Hrg. 105-722).

¹¹ General Accounting Office, *Interim Report on the Small Business Innovation Research Program* (March 1995) (GAO RCED-95-59).

¹² Senate Committee on Commerce, Science and Transportation, *NASA and NSF Program Efficiency*, 105th Congress (July 24, 1997) (S. Hrg. 105-722).

¹³ P.L. 106-554, codified at 15 USC § 638(k)(2).

¹⁴ *U.S., ex rel. Alfred J. Longhi v. Lithium Power Technologies* (5th Cir., July 9, 2009) (WL 1959259).

¹⁵ 15 USC § 638(g)(7).

¹⁶ As discussed above, one of the government's principal allegations in the NETECH case is that "...on multiple occasions, NETECH submitted fraudulent invoices to NASA on these contracts which represented labor hours for alleged employees that NETECH claimed to have paid or for whom NETECH incurred labor costs." Verified Complaint for Forfeiture in Rem, *U.S. v. Real Property Located at 501 South Moody Ave., Unit 117, Tampa, FL* (Feb. 19, 2009) N.D. Fla. (No. 1:09 cv 41-MP/AK).

¹⁷ Department of Energy Office of Inspector General, *Administration of Small Business Innovation Research Phase II Grants* (Aug. 2001) (DOE/IG-0521).

¹⁸ *Id.*

¹⁹ Department of Energy Office of Inspector General, *Management Controls over Monitoring and Closeout of Small Business Innovation Research Phase II Grants* (July 2008) (OAS-M-08-09).

²⁰ *Id.*

²¹ *Id.*