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DEFENSE LEGAL SERVICES AGENCY
DEFENSE OFFICE OF HEARINGS AND APPEALS
APPEAL BOARD
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Date: December 18, 2024

In the matter of:

Applicant for Security Clearance

ISCR Case No. 23-01614

APPEAL BOARD DECISION

APPEARANCES

FOR GOVERNMENT

Lauren A. Shure, Esq., Department Counsel
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FOR APPLICANT

Todd A. Hull, Esq.

The Department of Defense (DoD) declined to grant Applicant a security clearance. On November 9, 2023, DoD issued a Statement of Reasons (SOR) advising Applicant of the basis of that decision – security concerns raised under Guideline F (Financial Considerations) and Guideline E (Personal Conduct) of the National Security Adjudicative Guidelines (AG) in Appendix A of Security Executive Agent Directive 4 (effective June 8, 2017) and DoD Directive 5220.6 (Jan. 2, 1992, as amended) (Directive). On September 24, 2024, Defense Office of Hearings and Appeals Administrative Judge Pamela C. Benson granted Applicant security clearance eligibility. The Government appealed pursuant to Directive ¶¶ E3.1.28 and E3.1.30.

Under Guideline F, the SOR alleged ten delinquent state and federal income tax debts that begin with tax year 2010. At hearing, the Judge granted the Government's motion to amend the SOR by deleting the word "delinquent" in each of those allegations. The SOR also alleged two failures to timely file tax returns, which, on a motion by the Government, were amended to only allege unpaid taxes similar to the other Guideline F allegations. Finally, the Judge granted the Government's motion to delete the Guideline E allegations.

On appeal, the Government asserts that the Judge's conclusion to grant Applicant eligibility for access to classified information is arbitrary, capricious, contrary to law, and unsupported by the record evidence. For the reasons discussed below, we remand.

Background

Applicant is in his mid-60s, married, and has three adult children. He was honorably discharged from the United States military in May 1990 and has been working in a U.S. Embassy as a contractor employee in the Middle East since 2009. In late October 2023, he was evacuated from his overseas place of employment and returned to the U.S. due to security threats posed by nearby regional conflicts. He remained in the U.S. until returning to his workplace in late April 2024. Tr. at 145.

In response to the SOR and in his hearing testimony, Applicant acknowledged his tax debt but maintained that all of the allegations were covered under a section of the tax code that provides military members serving in designated combat zones and civilians supporting those troops the option to defer filing income tax returns and payment of related taxes. 26 U.S.C. § 7508 (*Time for performing certain acts postponed by reason of service in combat zone or contingency operation*).[1] This deferral is permitted for up to 180 days after leaving the combat zone at which point the tax obligations become due. 26 U.S.C. § 7508(a)(1)(B).[2] Applicant's home state of Missouri also permits deferral of state tax payments. Applicant apparently plans to continue to work in the designated combat zone for another 10 to 12 years and to defer tax payments under Section 7508 until such time as he retires and returns to the United States. Tr. at 147.

For the years alleged in the SOR, Applicant and his wife have filed returns but not paid any federal income taxes beyond those minimal amounts that Applicant elected to withhold. Applicant's withholdings did not cover his total annual tax liability and, as of July 2024, his deferred federal tax debt was in excess of $150,000 and will become due and payable after he is no longer working in a designated combat zone.[3] Applicant Exhibit (AE) E; Tr. at 91. Applicant used the majority of the money that he retained by deferring payment of income taxes to pay for his children's educations and their post-college living expenses. Beyond that, Applicant appears to have lived a modest, debt-free lifestyle during the 14 years that he has claimed this deferral.

Applicant did not invest or escrow money to address the future tax payment and he acknowledged that he would not have sufficient savings to make a lump sum payment of the taxes when due. Instead, he anticipates that his mother or in-laws will die before the taxes are due, allowing him to use inheritance funds to cover the debt. Tr. at 96-97, 158-159. To the extent that

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[1] The parties and the Decision refer to this section of the tax code as the "Combat Zone Tax Exemption – CZTE." However, the CZTE is the Combat Zone Tax Exclusion, which provides that military members may exclude from their taxable income certain earnings received while in the combat zone. 26 C.F.R. § 1.112-1 (C*ombat zone compensation of members of the Armed Forces*). The CZTE has no bearing on this case. Additionally, concurrent citations to Section 7508 and subsection 7508(a) in the briefs and Decision are redundant inasmuch as they are not separate statutes.

[2] The deferral may be extended for an additional period of time depending on when the individual entered the combat zone. *See* IRS Publication 3, Armed Forces' Tax Guide, dated February 27, 2024, at 29.

[3] Applicant also owes approximately $8,000 for his 2018 state tax balance. Government Exhibit (GE) 3 at 15.

the unknown amount of potential inheritance may not cover the tax debt, Applicant plans to establish a payment plan with the IRS when the taxes come due, although he provided no details as to what this might entail, including his ability to make payments or the likelihood that the IRS would agree to a payment plan on his terms. Tr. at 129-130, 132. There was no inquiry at hearing nor is there any evidence shedding light on how Applicant would pay his tax debt in any of the quite foreseeable scenarios that would cause the debt to become due earlier than when he plans to depart the combat zone in about 2035 (*e.g*., loss of employment, his own illness or injury, his wife's illness or injury, another regional conflict that triggers a long-term evacuation, or simply removing the designation of his workplace as a combat zone).

At various times, Applicant consulted with a tax attorney and accountants and presented evidence from professionals who opined that he was eligible to avail himself of the benefits of Section 7508. However, Applicant's tax transcripts reflect that the IRS did not always apply this provision to his tax returns, and, in some instances, he was charged interest and penalties for failing to timely pay taxes. While this was reversed for some years after an accountant contacted the IRS on Applicant's behalf (*e.g.* GE 2 at 7-11; AE D), there remain years for which no deferment was allowed and penalties and interest were assessed. GE 2 at 29-41; AE E (tax years 2017-2020, 2022-2023). Applicant and his wife referred to this as a "coding" problem as opposed to an eligibility issue and said that they have made some efforts to contact the IRS. Tr. 104-106, 108, 188. Still, as of July 2024, there is no evidence that the IRS has applied the Section 7508 deferral to those tax years.[4] Even if Section 7508 is applicable, Applicant owes in excess of $150,000 in federal and state taxes at this time because of the continuing deferral.

Discussion

On appeal, the Government argues that the Judge's decision is arbitrary and capricious. Specifically, the Government asserts that the Judge failed to properly consider the following aspects of the case: whether Applicant previously had the ability to pay his tax debt; whether he has the current ability to satisfy his tax debt or is unduly relying on being allowed to set up a payment plan; Applicant's failure to set up a payment plan when he was out of the combat zone for over 180 days; the unreasonableness of Applicant's support of his adult children well beyond their college education; Applicant's failure to make voluntary payments to reduce his tax debts; Applicant's failure to change his withholdings to reduce his continued tax indebtedness; and Applicant's inability to pay the entirety of the tax debt before his death. Appeal Brief at 11.

In deciding whether the Judge's rulings or conclusions are arbitrary and capricious, we will review the decision to determine whether: it does not examine relevant evidence; it fails to articulate a satisfactory explanation for its conclusions, including a rational connection between the facts found and the choice made; it does not consider relevant factors; it reflects a clear error of judgment; it fails to consider an important aspect of the case; it offers an explanation for the decision that runs contrary to the record evidence; or it is so implausible that it cannot be ascribed

[4] Although the Government appears to have accepted that Applicant has met the IRS criteria for postponing tax payment deadlines (*see* Tr. at 11; Appeal Brief at 20, 22), the record is ambiguous about his eligibility for the extension under Section 7508.

to a mere difference of opinion. *See* ISCR Case No. 97-0435 at 3 (App. Bd. Jul. 14, 1998) (citing *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co*., 463 U.S. 29, 43 (1983).

The Judge found that Applicant was compliant with federal tax laws and that, once he is out of a combat zone for 180 days, he will be required to initiate a payment plan. Limiting her review to AG ¶¶ 19(a), (b), (c), and (f),[5] she concluded that the Government had failed to meet its evidentiary burden "as there is no evidence of any wrongdoing by Applicant." Decision at 6. However, the issue in this case is not exclusively "wrongdoing" but, even assuming Applicant is eligible for the benefits of Section 7508, whether or not he acted responsibly when availing himself of those benefits.

The Government's brief sets out a litany of alleged errors that collectively argue that the Judge failed to adequately evaluate whether or not Applicant's deferral of tax payments and his plan for paying the accumulated balance was reasonable and responsible within the meaning of the broad Guideline F concern.[6] We do not need to address all of the Government's assertions, as we concur that the Judge failed to adequately assess the reasonableness of Applicant's accrual of significant debt in the context of the viability and reasonableness of his proposed plan for repayment.

The operative issue in terms of a potential security concern is whether it was reasonable and responsible for Applicant to have availed himself of Section 7508's benefits year after year when viewed in the context of whether or not he has a viable plan to pay the taxes when due. Simply acting in accord with the deferral aspect of Section 7508 does not *de facto* provide immunity from scrutiny in the context of a security clearance assessment under the Guidelines. While it may be permissible to defer tax payments, mere reliance upon a legally available program does not necessarily erase the security concerns arising from the overall situation. *C.f.* ISCR Case No. 14-06440 at 4 (App. Bd. Jan. 8, 2016). The analysis must include an assessment of how Applicant intends to address the tax debt when it comes due and the viability of that intention because paying the deferred taxes is not a hypothetical event; it is an inevitable reality, whether it occurs in 2035 when he intends to retire or earlier due to some unforeseen event.

It is the Judge's responsibility to assess the reasonableness of deferring tax debt in the context of Applicant's ability to repay it. The Judge concluded that "[she] cannot speculate whether he has the financial means to pay his deferred taxes once he is required by law to do so, but their intentions are to pay the taxes when due." Decision at 6. As such the Judge focused on Applicant's intentions without considering whether those intentions are realistic or assessing the judgment reflected in Applicant's taking advantage of the benefits of Section 7508 relative to his ability to meet the long-term financial obligations when those taxes come due. However, it is the Judge's responsibility to consider the viability of Applicant's conduct relative to his hypothetical payment

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[5] AG ¶¶ 19: (a) an inability to satisfy debts; (b) unwillingness to satisfy debts regardless of the ability to do so; (c) a history of not meeting financial obligations; and (f) failure to file or fraudulently filing annual Federal, state, or local income tax returns or failure to pay annual Federal, state, or local income tax as required.

[6] *See* AG ¶ 18: "The Concern. Failure to live within one's means, satisfy debts, and meet financial obligations may indicate poor self-control, lack of judgment, or unwillingness to abide by rules and regulations, all of which can raise questions about an individual's reliability, trustworthiness, and ability to protect classified or sensitive information."

plan. "[A]n administrative judge is required to make predictive judgments about the likelihood of . . . current and future risks based on present circumstances." ISCR Case No. 02-26978 at 3 (App. Bd. Sep. 21, 2005). Although the grant or denial of a security clearance is an inexact science, a judge must assess an applicant's future actions in the context of the unforeseen impact of outside and unknown influences. *Dep't of the Navy v. Egan*, 484 U.S. 518, 528-29 (1988); *C.f.* ISCR Case No. 18-02641 at 3 (App. Bd. Jul. 10, 2019). In this case, that uncertainty includes Applicant's reliance upon a potential inheritance and the possibility that the taxes may come due sooner than he anticipates. The Judge also must conduct an in-depth assessment of the practicality of Applicant's plans to take certain actions in the future. *See* ISCR Case No. 98-0188 at 2 (App. Bd. Apr. 29, 1999). Promises to take actions in the future, however sincere, are not a substitute for a documented track record or viable plan for debt payment. Review of this aspect of the Judge's decision is not simply a matter of deferring to her weighing of Applicant's credibility as argued by Applicant. The Judge can find Applicant credible in terms of his professed intention to repay the debts, but that does not eliminate the need to evaluate whether or not Applicant's deferral of tax payments was reasonable and responsible and his plan for paying them is feasible and reliable.

Additionally, the federal income tax system is a "pay-as-you-go" tax system, which means that taxpayers must pay income tax as they earn or receive income during the year. This can be accomplished either through withholding or by making estimated tax payments. Taxpayers must generally pay at least 90% of their taxes due during the previous year to avoid an underpayment penalty. *E.g., IRS Tax Tip 2021-81*, June 8, 2021, https://www.irs.gov/newsroom/heres-how-taxpayers-can-pay-the-right-amount-of-tax-throughout-the-year; *Penalty for underpayment of estimated tax*, https://www.irs.gov/taxtopics/tc306. Section 7508 does not provide an exemption from complying with standard withholding and estimated tax payment requirements. Applicant's withholdings averaged approximately 50% of his obligation from taxable wage income. When he received a $130,000 settlement of a lawsuit, Applicant did not pay the related taxes. Had he been in compliance with those payment and withholding requirements, the amount due at the point when Applicant ultimately exits the combat zone would be significantly smaller. As such, not only was it error for the Judge to conclude that Applicant's conduct was not wrongful, there is substantial evidence that Applicant is unwilling to pay taxes when owed under the federal pay-as-you-go system. As such, the Judge erred in finding that AG ¶ 19(b) and AG ¶ 19(c) were inapplicable.

Having minimized his withholding and estimated tax payments, the manner in which Applicant used the funds is a significant facet of assessing the reasonableness of his tax payment deferral. Therefore, the extent of Applicant's support of his adult children is relevant in terms of assessing the long-term plan for repayment inasmuch as it impacted Applicant's ability to address the tax debt in the future. The windfall of funds from the deferral and under-withholding amounted to an interest-free loan. But, as with any loan, it must be entered into with prudence and a realistic plan to repay that loan. Without a lender acting as a gatekeeper to evaluate the ability to repay the loan, individuals invoking Section 7508 must weigh their ability to pay the tax debt when taking advantage of deferral. To do otherwise reflects a lack of judgment under Guideline F.

The reasonableness of Applicant's conduct and the likelihood of actually paying the deferred tax debt raise disqualifying conduct under AG ¶¶ 19(a) and (e),[7] and it was error for the Judge to have concluded that the Government had not met its burden of proof under those paragraphs. AG ¶ 19(a) is not limited to debts currently due. It equally applies in a situation such as this, in which existing debt will become due in the future. Similarly, AG ¶ 19(e) is established when there is consistent spending beyond one's means or frivolous or irresponsible spending. Applicant has deferred taxes over a long period of time to the extent that they exceed $150,000. He spent the proceeds gleaned from deferring tax payments without setting aside funds to pay the taxes, he intends to continue to grow his tax debt, and he presented a tenuous repayment plan. It was error for the Judge not to have found AG ¶ 19(e) applicable in light of substantial evidence that Applicant will be unable to meet his tax obligations regardless of his assertions that he intends to do so.

Finally, the Government's claim that Applicant failed to establish a payment plan when he was out of the designated combat zone for over 180 days raises unanswered factual questions that are critical to the assessment of this case – was Applicant already responsible for payment of the taxes at the time of the hearing and, if so, was he able to meet that obligation? There is substantial evidence that Applicant returned to the United States on October 21 or 22, 2023, and that he returned to his workplace in a designated combat zone on April 26 or 27, 2024. Tr. at 144-145. On its face, this reflects that he was out of the designated combat zone for more than 180 days and, as such, may have triggered immediate payment of deferred taxes. *See* ISCR Case No. 19-02207 at 2 (App. Bd. May 20, 2020). The Judge recognized this issue during Applicant's testimony and questioned him concerning it. In response, Applicant testified that he did not believe that this situation changed his tax deferment status because it was the result of an involuntary evacuation. Tr. at 156. However, there is no evidence that he consulted with a tax professional before reaching this conclusion, nor is there corroboration for why this assumption was a reasonable one given the plain language of the statute. Tr. at 156. The Judge's decision did not address this important aspect of the case and, although she is presumed to have considered all evidence, it was error not to have explicitly done so given this record.[8]

Conclusion

When the Board finds that a judge's decision is unsustainable, we must determine if the appropriate remedy is remand or reversal. The former is appropriate when the legal errors can be corrected through remand and there is a significant chance of reaching a different result upon correction, such as when a judge fails to consider relevant and material evidence. If the identified errors cannot be remedied on remand, the decision must be reversed. ISCR Case No. 22-01002 at 4 (App. Bd. Sep. 26, 2024). In this instance, the Judge's conclusion that the Government failed to

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[7] AG ¶ 19(e): consistent spending beyond one's means or frivolous or irresponsible spending, which may be indicated excessive indebtedness, significant negative cash flow, a history of late payments or of non-payment or other negative financial indicators.

[8] It may be necessary to reopen the record to further explore both the fundamental question of Applicant's eligibility for Section 7508 and the specific question of whether Applicant's return to the U.S. triggered repayment of the deferred taxes. As to the latter, Applicant's appellate argument that he "remained employed **by a site** in a combat zone" (emphasis added) is not tenable in the face of the statute which specifies that that the "individual" be serving in a designated combat zone. Reply Brief at 4, 12, 15; 26 U.S.C. § 7508(a).

present a *prima facie* case under Guideline F, as well as the failure to address the significance of Applicant's return to the United States were clearly erroneous and are best remedied through remand.

Therefore, pursuant to Directive ¶ E3.1.33.2, the Board remands the case to the Judge with instruction to issue a new decision, consistent with the requirements of Directive ¶ E3.1.35, after correction of the identified errors and reconsideration of the record as a whole. The Board retains no jurisdiction over a remanded decision; however, a judge's decision issued after remand may be appealed. Directive ¶¶ E3.1.28 and E3.130.

ORDER

The decision in ISCR Case No. 23-01614 is **REMANDED**.

Signed: Moira Modzelewski
Moira Modzelewski
Administrative Judge
Chair, Appeal Board

Signed: Allison Marie
Allison Marie
Administrative Judge
Member, Appeal Board

Signed: James B. Norman
James B. Norman
Administrative Judge
Member, Appeal Board