KEYWORD: Guideline F

DIGEST: The ability of Judges to meaningfully and accurately apply a state's statutes will very from case to case, depending on the quality of the record. In this case, the Judge was provided with enough specifics to enable her to apply a state anti-deficiency statute. There were sufficient facts in mitigation to support the Judge's ultimate conclusions. Favorable decision affirmed.

CASENO: 12-04806.a1

DATE: 07/03/2014

DATE: July 3, 2014

In Re:	)	
	)	
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	)	
	)	
Applicant for Security Clearance	)	

APPEAL BOARD DECISION

APPEARANCES

FOR GOVERNMENT
James B. Norman, Esq., Chief Department Counsel

FOR APPLICANT
Joseph Testan, Esq.

The Department of Defense (DoD) declined to grant Applicant a security clearance. On November 26, 2013, DoD issued a statement of reasons (SOR) advising Applicant of the basis for that decision—security concerns raised under Guideline F (Financial Considerations) of Department of Defense Directive 5220.6 (Jan. 2, 1992, as amended) (Directive). Applicant requested a hearing.

On April 4, 2014, after the hearing, Defense Office of Hearings and Appeals (DOHA) Administrative Judge Darlene D. Lokey Anderson granted Applicant's request for a security clearance. Department Counsel appealed, pursuant to the Directive ¶¶ E3.1.28 and E3.1.30.

Department Counsel raises the following issues on appeal: (1) whether the Judge's decision is arbitrary and capricious because the Judge erroneously speculated as to the applicability of a state anti-deficiency statute; and (2) whether the Judge's application of Guideline F mitigating conditions was arbitrary, capricious, or contrary to law. For the following reasons, the Board affirms the Judge's favorable security clearance decision.

The Judge made the following findings: Applicant is 59 years old and married. Since the mid-1990s Applicant and his wife have been involved in the real estate business. At that time, they purchased their first rental property. Applicant's wife took real estate courses at the local community college to learn more about the business. The couple then purchased four more properties before 2010, rented them out, and made a profit when they were sold. In 2005, Applicant and his wife purchased a house (L-4) for their personal residence. To purchase the property, they obtained a first and second mortgage from Bank A. Applicant and his wife lived in the house from 2005 to 2008. During that time they spent about $23,000 in remodeling. In 2008, they purchased another property that became their primary residence, and they retained L-4 as investment property.

In 2009, with the collapse of the real estate market, Applicant's rental properties lost significant value and were upside down. Applicant was forced to reduce the amounts of the rents on his properties, which became significantly less than the mortgage payments. He was also confronted with costly repair issues. Between 2009 and 2010, he lost about $50,000 and depleted his reserves. It took six months to evict a tenant who was not paying rent. Confronted with this financial crisis, Applicant chose the one property with the largest discrepancy between rental income and mortgage payment, which was L-4. He tried to obtain a loan modification and was told there were no loan modification programs available for rental properties. At some point, Applicant could no longer afford to make the payments on L-4. To prevent the property from being foreclosed upon, Applicant tried to raise money by selling another property, but was unsuccessful. He also tried to borrow from his 401(k) but was unable to do so. L-4 was foreclosed upon in late 2011.

Applicant reports that the first mortgage loan on the property was settled by the foreclosure, as the property was collateral for the loan. Applicant's credit report confirms this understanding. Applicant contends that the second loan on the property was also charged off. Applicant received two 1099-As from the lender on both the first and second mortgage. Applicant recently contacted the bank to determine whether he could settle a debt that had been charged off (the second loan on L-4). He was advised to send the bank a letter explaining what happened, and that his intentions are to settle the debt. He submitted for the record a copy of the letter he sent to the lender. Applicant testified that if he owes anything to the bank for the second loan, he will honor the agreement and settle the loan, as he has the financial means to do so.

Since L-4 was foreclosed upon, Applicant and his wife have enrolled in and completed an intensive eight week financial counseling course focusing on debt reduction. Applicant is currently practicing the financial principles he learned at the seminar, as evidenced by his purchasing a house for cash, thus eliminating the need for a mortgage. He is currently attempting to sell two of his land

parcels. In addition to the parcels, he presently owns five houses, including his personal residence. Applicant and his wife's current net worth is about $900,000.

The Judge reached the following conclusions: The Government met its initial burden of proving that the Applicant has been financially irresponsible. The evidence shows that Applicant became delinquently indebted beginning in 2009 when the real estate market crashed and property values plummeted to unprecedented lows. Without sufficient financial resources to meet unexpected expenses, one of Applicant's investment properties was foreclosed upon. The question is whether Applicant acted reasonably and responsibly under the circumstances. He has. He made every attempt to avoid foreclosure. He continued to show good judgment. He was able to meet all of his financial responsibilities related to his other investments. He has not incurred any new debt that he cannot afford to pay and in fact has reduced some of his expenses. There is clear evidence of financial rehabilitation. Applicant has inquired about the status on the second loan and has offered to settle the loan if it is determined that he owes anything.

A legal question raised in this case is whether Applicant is liable for a deficiency judgment for the first mortgage on the L-4 property that was foreclosed upon and returned to the bank. L-4 falls within the protection of the state anti-deficiency act, and therefore Applicant owes nothing more to the bank. L-4 was Applicant's residence at the time the loan was taken out, and the statute prohibits a lender from seeking a deficiency judgment against a borrower if he incurred the loan for the sole purpose of purchasing the home. This is considered a non-recourse, purchase money loan, which means that the lender's only recourse is to sell the home to pay the money owed. The state statute also states that if a lender sells a home under a power of sale contained in the mortgage or deed of trust (trustee's sale), as in this case, then he cannot sue the homeowner in a court of law for the deficiency. Since the debt is a non-recourse debt, its cancellation through foreclosure does not result in cancellation of debt income, for which Applicant owes any income tax.

Applicant has overcome the Government's case opposing his request for a security clearance.

Department Counsel argues that the Judge erroneously speculated as to the applicability of of the state anti-deficiency statute. He states that it was error for the Judge to have found the statute applicable, absent direct evidence that the debt in question, in this case the first mortgage on property L-4, has been forgiven by the lenders. Emphasizing that the state anti-deficiency laws are numerous and complex, Department Counsel asserts that DOHA administrative judges are not in a position to resolve the complicated factual and legal issues surrounding the applicability of state anti-deficiency laws as they relate to an applicant's particular situation, nor are DOHA security clearance hearings well suited to this. On the other hand, Applicant asserts that, given the facts of this case and the completeness and the details of the state anti-deficiency statute of which the Judge took administrative notice, the Judge's application of the provisions of the statute were not speculative or improper. On this record, the Board concludes that Applicant has proffered the better argument.

The Board rejects the assertion by Department Counsel that it was error for the Judge to have attempted to interpret the applicability of the state anti-deficiency statute absent direct evidence of debt forgiveness by the lenders. Of course, specific evidence from the lender of debt forgiveness would normally be conclusive on the issue of whether Applicant still owes the debt, but under the substantial evidence standard, that level of proof is not required when there is other evidence that

allows the Judge to determine the status of the debt. There is such evidence in the case before us. The specific language of the state anti-deficiency statute is part of the record, as is case law interpreting that statute. The evidence of the circumstances surrounding Applicant's ownership of the property, the foreclosure process, and Applicant's other financial circumstances was detailed enough to allow the Judge to apply the statute to Applicant's situation.[1] With the aid of case law admitted into the record, interpretation of the anti-deficiency statute was permissible.

The ability of Judges to apply meaningfully and accurately a state's statutes will vary from case to case depending on the quality of the record, but in this case the Judge was provided with enough specifics to enable her to accomplish the task. Department Counsel argues that DOHA judges are not in a position to resolve the complicated factual and legal issues surrounding anti-deficiency statutes and that DOHA security clearance hearings are not well suited to the inquiry. Department Counsel's arguments are not frivolous. In most cases where the issue has arisen, the evidence simply did not support a determination that the loan was forgiven. Just as importantly, in many cases the issue has served to distract from other issues that were ultimately more important, such as: how the Applicant became insolvent; how did they deal with the issue; and how have they documented claims that the circumstances leading to financial delinquencies are unlikely to occur. In most other cases where the issue of the applicability of an anti-deficiency statute has arisen, the purportedly forgiven debts were part of a mosaic of delinquent debts. The record in this case stands out because the forgiven debts were on the property that was the basis for the only delinquencies in the case to begin with. In a case where it is necessary and appropriate to address the issue and the evidentiary foundation has been laid, then it would be inappropriate to accept Department Counsel's proposition.

Cases cited by Department Counsel in support of his arguments are distinguishable from the instant case. These cases contain sparse evidentiary records and were combined with Judge's narratives that lacked specificity and were largely speculative.[2] By contrast, the Judge's analysis

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[1]As a practical matter, had there been direct evidence from lender stating forgiveness of the debt, that evidence would obviate the need to interpret the statute.

[2]*See* ISCR Case No. 10-07393 (App. Bd. Jun. 12, 2012)(Judge's reliance on an unspecified anti-deficiency statute of which he took administrative notice not sufficient to demonstrate that two mortgage debts had been discharged by operation of law. The Judge's finding that Applicant "most probably" does not owe the deficiency is not supported by substantial record evidence); ISCR Case No. 08-11940 (App. Bd. Dec. 2, 2010)(Judge makes no mention of state anti-deficiency statute or how it applied to the facts of the case. Evidence in support of Judge's conclusion that Applicant no longer owed three of four mortgage debts is not specifically described and is not discussed. Therefore, the Judge's conclusion is speculative and is also contradicted by conflicting evidence, i.e. credit reports showing the debt amounts as outstanding); ISCR Case No. 09-02160 (App. Bd. Jun. 21, 2010)(Applicant presented no documentary evidence showing that the lender's rights to collect the deficiencies were limited by the terms of his mortgages, that they were willing to forego efforts to collect the deficiencies, or that a deficiency was precluded by local law. Applicant's assertion that he owed nothing on the mortgages was based on the testimony of his employer, who was experienced in the mortgage business. The employer was not established as an "expert witness" through the commonly accepted qualification process. The weight that could be given to his testimony was diminished commensurately); ISCR Case No. 08-09480 (App. Bd. Mar. 17, 2010)(the Judge applied a state criminal statute to the facts of the case without identifying it with sufficient specificity so that its content could be determined).

ISCR Case No. 10-01978 (App. Bd. Aug. 24, 2011) is the case most similar to the instant case in that the Judge specifically cited the state anti-deficiency statute and included pertinent provisions of same in his decision. However, he does not discuss the applicability of the statute with the same detail as the Judge in the instant case. Moreover, the

in the instant case is thorough and makes use of a more developed evidentiary record. She explains in detail and at some length how the statutory language applies to the case. The Board also rejects Department Counsel's assertion that, while it was not inappropriate for the Judge to take notice of the state anti-deficiency statute, it was inappropriate for the Judge to have interpreted that statute as it might apply to the facts of the case. In other words, it was inappropriate for the Judge to *use* the statute in her analysis of the case. If the Judge cannot use the statute in question, the formality of taking administrative notice of it would appear to be a meaningless exercise.

Department Counsel argues that the Judge's conclusions when applying the Guideline F mitigating conditions and whole person-analysis are unsupported by the record evidence. He also argues that an applicant must do more than merely show that he or she relied on a legally available option such as bankruptcy or some other means of resolving the debt because doing so does not necessarily demonstrate prudence, honesty, and reliability. The Board interprets these arguments as a statement that there is no factual basis for the Judge's conclusion that Applicant mitigated the Government's case, even assuming that the state anti-deficiency statute applies. After a review of the record and the Judge's decision, the Board concludes that the Judge's conclusions regarding mitigation are sustainable.

The gravamen of the Judge's decision was a conclusion that there is substantial record evidence that Applicant did everything he could to avoid foreclosure on property L-4, and since the foreclosure he has taken numerous steps to prevent a recurrence of his financial difficulties. Applicant has expressed a willingness to settle the outstanding second mortgage indebtedness, has the means to do so, and has contacted the lender, both orally and in writing, and indicated his willingness to settle the debt, despite its being in "charged off" status. Furthermore, Applicant corroborated those efforts with documentation (*see* Applicant's Exhibit H). The facts in this record contrast with the records in other cases wherein a debtor has relied on a legally available option to the exclusion of any effort to alleviate the loss to the creditor. Beyond the issue of the state anti-deficiency statute and the loan to which it applies, Applicant has had formal financial counseling and has taken steps to head off other financial problems. The sum of his efforts concerning his finances indicate he has done more than merely used an available legal option to resolve indebtedness. The Board finds no reason to believe that the Judge did not properly weigh the evidence or that she failed to consider all the evidence of record. *See, e.g.*, ISCR Case No. 11-06622 at 4 (App. Bd. Jul. 2, 2012). We have considered the totality of Department Counsel's arguments on appeal and find no error in the Judge's ultimate conclusions regarding mitigation. As the trier of fact, the Judge has to weigh the evidence as a whole and decide whether the favorable evidence outweighs the unfavorable evidence, or *vice versa*. *See, e.g.*, ISCR Case No. 06-10320 at 2 (App. Bd. Nov. 7, 2007). A party's disagreement with the Judge's weighing of the evidence, or an ability

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Board ultimately concluded that the applicability or non-applicability of the statute was not critical to its analysis in reversing the Judge. The Board stated that, even assuming the debts had been extinguished, that fact would not provide an adequate basis for the Judge's favorable decision, given the circumstances under which Applicant acquired the debts. In the instant appeal, Department Counsel states that the Board "cited with approval" his argument in ISCR Case No. 10-01978 that the Judge could not speculate as to the applicability of the anti-deficiency statute in the absence of evidence that the indebtedness was actually forgiven based on the statute. However, the Board did not rule on the issue and, as indicated above, the case was decided on other grounds. The Board's language in ISCR Case No. 10-01978 did not preclude a Judge from addressing the issue where the evidentiary basis has been laid, and the context is otherwise appropriate, as is discussed elsewhere in this decision.

to argue for a different interpretation of the evidence, is not sufficient to demonstrate the Judge weighed the evidence or reached conclusions in a manner that is arbitrary, capricious, or contrary to law. *See, e.g.*, ISCR Case No. 06-17409 at 3 (App. Bd. Oct. 12, 2007).

The Board does not review a case *de novo*. After reviewing the record, the Board concludes that the Judge examined the relevant data and articulated a satisfactory explanation for the decision, "including a 'rational connection between the facts found and the choice made.'" *Motor Vehicle Mfrs. Ass'n of the United States v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (quoting *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168 (1962)). "The general standard is that a clearance may be granted only when 'clearly consistent with the interests of the national security.'" *Department of the Navy v. Egan*, 484 U.S. 518, 528 (1988). Therefore, the Judge's ultimate favorable security clearance decision is sustainable.

Order

The decision of the Judge is AFFIRMED.

Signed: Michael Ra'anan
Michael Ra'anan
Administrative Judge
Chairperson, Appeal Board

Signed: Jeffrey D. Billett
Jeffrey D. Billett
Administrative Judge
Member, Appeal Board

Signed: James E. Moody
James E. Moody
Administrative Judge
Member, Appeal Board