

KEYWORD: Financial

DIGEST: Applicant is a 68-year-old president, and at one time sole stockholder, of a defense contractor. Applicant's company had a business downturn in the 1990s, and did not make a number of quarterly payments to the Internal Revenue Service. Applicant filed Chapter 7 bankruptcy, and his company entered Chapter 11 bankruptcy. The company owes the IRS more than \$2,400,000 in taxes, interest, and penalties. Applicant's personal liability for the tax debt is currently at more than \$1,100,000. Clearance is denied.

CASENO: 05-14853.h1

DATE: 03/30/2007

DATE: March 30, 2007

In re:)	
)	
)	
-----)	ISCR Case No. 05-14853
SSN: -----)	
)	
Applicant for Security Clearance)	
)	

**DECISION OF ADMINISTRATIVE JUDGE
EDWARD W. LOUGHRAN**

APPEARANCES

FOR GOVERNMENT

Francisco Mendez, Esq., Department Counsel

FOR APPLICANT

Eric A. Eisen, Esq.

SYNOPSIS

Applicant is a 68-year-old president, and at one time sole stockholder, of a defense contractor. Applicant's company had a business downturn in the 1990s, and did not make a number of quarterly payments to the Internal Revenue Service. Applicant filed Chapter 7 bankruptcy, and his company entered Chapter 11 bankruptcy. The company owes the IRS more than \$2,400,000 in taxes, interest, and penalties. Applicant's personal liability for the tax debt is currently at more than \$1,100,000. Clearance is denied.

STATEMENT OF THE CASE

The Defense Office of Hearings and Appeals (DOHA) declined to grant or continue a security clearance for Applicant. On June 14, 2006, DOHA issued a Statement of Reasons¹ (SOR) detailing the basis for its decision—security concerns raised under Guideline F (Financial Considerations) of the Directive. Applicant answered the SOR in writing on September 26, 2006, and elected to have a hearing before an administrative judge. The case was assigned to me on December 18, 2006. A notice of hearing was issued on January 24, 2007, scheduling the hearing for February 20, 2007. The hearing was conducted as scheduled to consider whether it is clearly consistent with the national interest to grant or continue a security clearance for Applicant.

Applicant's counsel submitted a Hearing Memorandum which was marked Hearing Exhibit (HE) I. Department Counsel's letter forwarding the Memorandum is HE II. The Government offered eleven exhibits that were marked as Government Exhibits (GE) 1 through 11, and admitted without objection. Applicant testified and offered eight exhibits that were marked Applicant Exhibits (AE) A through H, and admitted without objection. During his testimony, Applicant adopted the facts contained in HE I.² The record was left open to allow Applicant an opportunity to submit additional material. He did so in a timely manner. The documents included income tax forms and returns (AE I), IRS statement (AE J), IRS negotiation documents (AE K), house documents (AE L), and letter from trustee (AE M). The letter from Applicant's counsel was marked HE III. Department Counsel's letter forwarding the documents is HE IV. Department Counsel objected to one of the documents contained in AE L, on the basis of relevancy and lack of foundation. That objection is overruled. AE I through M are admitted. DOHA received the hearing transcript (Tr.) on March 9, 2007.

FINDINGS OF FACT

Applicant's admissions to the allegations in the SOR, are incorporated herein. In addition, after a thorough and careful review of the pleadings, exhibits, and testimony, I make the following findings of fact:

Applicant is a 68-year-old president, and at one time sole stockholder, of a defense contractor. He is married, but separated. He has four adult children from his first marriage, and three minor children from his current marriage. Applicant's wife and children live in a foreign country, where she works for a non-governmental organization (NGO). Applicant has spent time in college, but does not have a degree. Applicant served in the United States Air Force from 1956 to 1959, and was honorably discharged.³

Within two years of his discharge from the Air Force, Applicant started on the ground floor in a company within a high visibility industry. Applicant's background and circumstances were such

¹Pursuant to Exec. Or. 10865, *Safeguarding Classified Information within Industry* (Feb. 20, 1960), as amended and modified, and Department of Defense Directive 5220.6, *Defense Industrial Personnel Security Clearance Review Program* (Jan. 2, 1992), as amended and modified (Directive).

²Tr. at 15.

³Tr. at 66; HE I; GE 3; AE F.

that his hiring by the company was groundbreaking. Applicant was a pioneer in his industry and achieved tremendous success.⁴

Applicant invested in a business in the early 1980s. The business failed, and Applicant filed a Chapter 7 bankruptcy in 1982. He was released from his dischargeable debts in 1982.⁵

In 1987, Applicant invested in a company involved in defense contracts. He purchased 51% of the stock in the company and was installed as the company president. Prior to the purchase, the company entered into a lease of additional facilities at a high price, in anticipation of receiving a new defense contract. In 1988, the contract was awarded to another company. Applicant suspects favoritism was involved in the contract decision, as the new president of that company was a former high-ranking government official. The company that was awarded the contract hired many of Applicant's employees to fulfill their contract. Applicant moved the company several times to smaller spaces as his workforce shrank. His company filed a Chapter 11 bankruptcy petition.⁶ Federal bankruptcy laws govern how companies go out of business or recover from crippling debt. A bankrupt company might use Chapter 11 of the Bankruptcy Code to "reorganize" its business and try to become profitable again. Management continues to run the day-to-day business operations but all significant business decisions must be approved by a bankruptcy court.⁷

The company's business improved. Bankruptcy records show that Applicant received \$245,000 income from the company in 1994, and \$257,000 in 1995.⁸

In the 1990s, Applicant's company won a bid to manufacture items as part of a defense contract. The contract did not provide for prepayment, resulting in a cash flow problem. The company used factors, a form of financing which accrued interest at 18% to 24%, to finance the contract. The factoring costs grew rapidly. Applicant refinanced personal real estate property, and invested an additional \$130,000 in the business. The company could not maintain the contract and had to subcontract it to another company. Applicant's company lost all its profits on the contract, his personal real estate properties were foreclosed, and the Chapter 11 filing was reopened.⁹

As Applicant's business went bad, the company stopped paying their federal taxes. Applicant admitted to owing all the taxes as alleged in the SOR. The company was obligated to withhold tax from their employees' pay, which would be turned over to the Internal Revenue Service (IRS) on a quarterly basis. The company failed to pay the IRS the withholding for their employees during a number of quarters in 1995 and 1996. Applicant's company owed the IRS more than \$2,480,000 in quarterly taxes, interest, and penalties, as reflected in SOR ¶¶ 1.c and 1.d, and 1.f through 1.j. As

⁴Tr. at; HE I at 2-3.

⁵Applicant's response to SOR; HE I at 5.

⁶Tr. at 17-18, 46-50; HE I at 3.

⁷U.S. Securities and Exchange Commission web site, www.sec.gov/investor/pubs/bankrupt.htm.

⁸GE 6 at 18.

⁹Tr. at 51-54, 77; HE I at 3-4.

president and stockholder of the company, Applicant was held personally liable by the IRS for about \$800,000, for the failure to pay the IRS the withholding taxes. As of September 11, 2006, that debt had grown to more than \$1,105,000.¹⁰

Applicant filed a Chapter 11 bankruptcy in 1996. In 1997, the bankruptcy was converted to a Chapter 7 bankruptcy. Applicant was released from his dischargeable debts in 1997.¹¹

Applicant's company remains in Chapter 11. An Examiner was appointed in 1996. By that time, Applicant was the sole stockholder of the company. A reorganization plan was confirmed in 1997. The Examiner now serves as Disbursing Agent and Plan Administrator. The plan provided that the company's stock was extinguished and then the same type of stock reissued and held in trust. The stock continues to be held in trust. Applicant manages and runs the company on a day to day basis, essentially without interference from the Plan Administrator. Upon satisfaction of all debt claims, 50% of the stock in trust will pass to Applicant, and the balance placed in the corporate treasury for issuance to future investors, or for other business purposes.¹²

The Plan Administrator has provided oversight of Applicant and his company for more than ten years. He always found Applicant to be honest, hard-working, and cooperative. He never observed Applicant engage in any illegal or unethical activities, and believes Applicant has always attempted to be "a good American and a good corporate citizen."¹³

There is no evidence that Applicant committed any illegal activity or wrongdoing during the Chapter 11 bankruptcy. It appears he had the best interests of his company and employees in mind. In the early stages of the bankruptcy, Applicant refused to accept a salary, and turned over many of his uncashed salary checks to the Plan Administrator. Those checks are in storage, but the Plan Administrator estimates their value to be in the tens of thousands of dollars.¹⁴

The company has repaid approximately \$100,000 in state tax debt, and \$400,000 in salaries through the Chapter 11. The company has resolved all debts except that owed to the IRS.¹⁵

Applicant has been attempting to negotiate and settle with the IRS for a number of years, issuing several Offers in Compromise (OIC) since 1998. The IRS has not accepted any of his OICs. There are two OICs pending, one on behalf of the company, and one for Applicant's personal liability. Applicant believes the OIC for the company is to pay about \$85,000, and the OIC for his personal liability is about \$15,000. The OIC on behalf of Applicant's company proposed to pay \$1,483 per month. The payments must be made while the IRS is considering the OIC. The company

¹⁰Tr. at 66-75; Applicant's response to SOR; GE 4; GE 5 at 2; AE J.

¹¹Applicant's response to SOR; GE 6.

¹²Tr. at : AE F, G.

¹³AE F.

¹⁴AE M.

¹⁵Tr. at 56-57.

made their payments for November and December 2006. The January, February, and March 2007 payments were made on February 21, 2007. Applicant testified that the IRS levied his company about \$130,000 last year. He stated he has been paying \$250 per month since last fall in connection with the OIC for his personal tax liability. He submitted documentation of three payments of \$250 to the IRS. Documentation appears to show that the IRS levied Applicant's Social Security payment for \$259 per month, starting in February 2006. Applicant testified that to his knowledge, the levy on his Social Security check never started.¹⁶

Applicant now lives a much simpler, less extravagant life. He shares a rented apartment for which he pays \$500 per month. His estranged wife received their house, which is now worth more than \$1,000,000, along with any mortgage payments. His children receive Social Security benefits based upon his earnings, and he has no independent child support obligations. He essentially lives on his annual salary from his company of about \$10,000, his pension, and his Social Security.¹⁷

Applicant presented outstanding character evidence. An internationally prominent and well-respected member of Applicant's prior industry has known Applicant for more than 40 years. He states Applicant is a patriot, with "platinum character, underpinned by sobering honesty, trustworthiness and unflagging dependability."¹⁸ Other letters praise him as a man of high integrity and honor, trustworthy, gifted, talented, kind, and considerate, whose "loyalty to America, its citizens, family and friends is above reproach."¹⁹

POLICIES

"[N]o one has a 'right' to a security clearance."²⁰ As Commander in Chief, the President has "the authority to . . . control access to information bearing on national security and to determine whether an individual is sufficiently trustworthy to occupy a position . . . that will give that person access to such information."²¹ The President authorized the Secretary of Defense or his designee to grant applicants eligibility for access to classified information "only upon a finding that it is clearly consistent with the national interest to do so."²² An applicant has the ultimate burden of demonstrating that it is clearly consistent with the national interest to grant or continue his or her security clearance. The clearly consistent standard indicates that security clearance determinations

¹⁶Tr. at 80-84, 88-90; HE II at 6; GE 4; AE B, C, K.

¹⁷Tr. at 80-83, 91; AE L.

¹⁸AE H.

¹⁹AE D, E.

²⁰*Department of the Navy v. Egan*, 484 U.S. 518, 528 (1988).

²¹*Id.* at 527.

²²Exec. Or. 10865, *Safeguarding Classified Information within Industry* § 2 (Feb. 20, 1960).

should err, if they must, on the side of denials.²³ Any reasonable doubt about whether an applicant should be allowed access to sensitive information must be resolved in favor of protecting such sensitive information.²⁴ The decision to deny an individual a security clearance is not necessarily a determination as to the loyalty of an applicant. It is merely an indication that the applicant has not met the strict guidelines the President and the Secretary of Defense have established for issuing a clearance.²⁵

The Directive sets forth potentially disqualifying conditions (DC) and mitigating conditions (MC) under each guideline. Additionally, each security clearance decision must be a fair and impartial commonsense decision based on the relevant and material facts and circumstances, the whole-person concept, along with the adjudicative process factors listed in ¶ 6.3 and ¶ E2.2.1 of the Directive.

Conditions that could raise a security concern and may be disqualifying, as well as those which would mitigate security concerns, pertaining to the adjudicative guidelines are set forth and discussed in the conclusions section below.

CONCLUSIONS

I have carefully considered all the facts in evidence and the legal standards discussed above. I reach the following conclusions regarding the allegations in the SOR.

Guideline F, Financial Considerations

An individual who is financially overextended is at risk of having to engage in illegal or unethical acts to generate funds to meet financial obligations.

Based on all the evidence, Financial Considerations Disqualifying Condition (FC DC) E2.A6.1.2.1 (*A history of not meeting financial obligations*), and FC DC E2.A6.1.2.3 (*Inability or unwillingness to satisfy debts*), apply in this case. Applicant declared bankruptcy in 1982 and 1996, and has a large unpaid debt to the IRS.

I have considered all the Financial Considerations Mitigating Conditions (FC MC), and especially considered FC MC E2.A6.1.3.1 (*The behavior was not recent*), FC MC E2.A6.1.3.2 (*It was an isolated incident*), FC MC E2.A6.1.3.3 (*The conditions that resulted in the behavior were largely beyond the person's control (e.g., loss of employment, a business downturn, unexpected medical emergency, or a death, divorce or separation)*), FC MC E2.A6.1.3.4 (*The person has received or is receiving counseling for the problem and there are clear indications that the problem is being resolved or is under control*), and FC MC E2.A6.1.3.6 (*The individual initiated a good-faith effort to repay overdue creditors or otherwise resolve debts*).

²³ISCR Case No. 01-20700 at 3 (App. Bd. Dec. 19, 2002).

²⁴*Id.*; Directive, ¶ E2.2.2.

²⁵Exec. Or. 10865 § 7.

Applicant has an extensive debt to the IRS that remains unpaid. He declared bankruptcy in 1982 and 1996. FC MC E2.A6.1.3.1 and FC MC E2.A6.1.3.2 do not apply.

The most important factor related to Applicant's financial difficulties was his business downturn. That condition was largely beyond Applicant's control. I cannot hold that Applicant's failure to pay the IRS during the downturn was largely beyond his control. Applicant's company was obligated to withhold funds from the employees' wages for their federal income tax. The company did not fulfill the further obligation to pay that money to the IRS. The company chose to utilize money owed to the U.S. Government in an attempt to save a floundering company. That is not a valid business decision. FC MC E2.A6.1.3. is partially applicable.

The payments to the IRS by Applicant's company, and by him personally, have been minimal compared with the amount of the debts. Applicant only recently started making payments on his personal debt. At most he has voluntarily paid about \$2,000 toward a \$1,100,000 debt. It is unclear if the IRS is levying Applicant's Social Security check. If the Social Security checks have been levied, approximately \$3,000 additional has been repaid to the IRS. That does not constitute a good-faith effort to repay overdue creditors or otherwise resolve debts. The IRS has not agreed to accept the OICs. Applicant did not submit sufficient evidence for a finding that his financial problem is being resolved or is under control. FC MC E2.A6.1.3.4 and FC MC E2.A6.1.3.6 are not applicable.

Whole Person Analysis

The adjudicative process is an examination of a sufficient period of a person's life to make an affirmative determination that the person is an acceptable security risk. Available, reliable information about the person, past and present, favorable and unfavorable, should be considered in reaching a determination. In evaluating Applicant's case, I have considered the adjudicative process factors listed in the Directive. I have also considered every finding of fact and conclusion discussed above.

Applicable has impeccable character evidence. He served our country in the Air Force and received an Honorable Discharge. In the 1960s, Applicant was a pioneer in his field, accomplishing things never done before. At the pinnacle of his career, he became an entrepreneur, earning about \$250,000, in both 1994 and 1995. Unfortunate business events led to losses and unpaid taxes. Applicant's personal liability to the IRS is at least \$1,100,000. He has been attempting to negotiate with the IRS for a number of years, issuing several OICs. Applicant has addressed his corporate debt for state taxes and other debtors. The corporation's debt and Applicant's personal debt to the IRS remain almost totally unpaid. Applicant's current standard of living is more akin to when he first started out in the 1960s. As long as the debt to the IRS hangs over Applicant's head, he cannot return to his previous standard of living. Applicant's tax debt raises his potential for pressure, coercion, exploitation, or duress.

After weighing the disqualifying and mitigating conditions and evaluating all the evidence in the context of the whole person, I conclude Applicant has not mitigated the security concerns raised by his financial issues.

FORMAL FINDINGS

The following are my conclusions as to each allegation in the SOR:

Paragraph 1. Guideline F: AGAINST APPLICANT

Subparagraphs 1.a-1.j: Against Applicant

DECISION

In light of all of the circumstances presented by the record in this case, it is not clearly consistent with the national interest to grant or continue a security clearance for Applicant. Clearance is denied.

Edward W. Loughran
Administrative Judge