

DATE: December 21, 2007

In re:

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SSN: -----

Applicant for Security Clearance

ISCR Case No. 07-04742

**DECISION OF ADMINISTRATIVE JUDGE  
ELIZABETH M. MATCHINSKI**

**APPEARANCES**

**FOR GOVERNMENT**

Fahryn Hoffman, Esq., Department Counsel

**FOR APPLICANT**

*Pro se*

**SYNOPSIS**

Applicant owes the Internal Revenue Service \$170,945.45 for failure to pay employee withholding taxes in 2002/03 when a business he co-owned was in serious financial difficulties. Other debt was discharged in a November 2004 Chapter 7 bankruptcy, and he is current in his other financial obligations. Financial considerations persist because he lives from paycheck to paycheck despite an annual salary of \$98,700 and he is not in a position to begin repaying the tax debt. 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. As required by ¶ E3.1.2 of Department of Defense Directive 5220.6 (Jan. 2, 1992), as amended, DOHA issued a Statement of Reasons (SOR) on July 10, 2007, detailing the basis for its decision—security concerns raised under Guideline F (financial considerations) of the revised Adjudicative Guidelines (AG) issued on December 29, 2005, and implemented by the Department of Defense effective September 1, 2006. The guidelines were provided to Applicant when the SOR was issued. Applicant answered the SOR on August 7, 2007, and elected to have a hearing before an administrative judge. On September 12, 2007, the government moved to amend the SOR to allege: (1) the filing of a bankruptcy (originally SOR ¶ 1.a) and its discharge (originally SOR ¶ 1.b) as one allegation (SOR ¶ 1.a as amended) and to include in that allegation the amount of debt discharged; and (2) to allege as SOR ¶ 1.b rather than ¶ 1.c and include the amount of a federal tax lien filed against him in August 2003 for failure to pay withholding taxes.

The case was assigned to me on September 19, 2007. On October 4, 2007, I granted the motion and scheduled a hearing for November 8, 2007, to consider whether it is clearly consistent with the national interest to grant or continue a security clearance for Applicant. Five government exhibits (Ex. 1- 5) were admitted, Ex. 3 over Applicant's objection. Applicant testified and submitted six exhibits (Ex. A-F), which were admitted without any objections. DOHA received the hearing transcript (Tr.) on November 21, 2007.

### **FINDINGS OF FACT**

In the SOR as amended, DOHA alleges that Applicant filed a Chapter 7 bankruptcy petition in November 2004 and was granted a discharge of about \$1,627,682.18 in debt in March 2005 (SOR ¶ 1.a), and that the Internal Revenue Service (IRS) filed a federal tax lien against Applicant in August 2003 in the approximate amount of \$327,890.39 for failure to pay withholding taxes and the debt had not been paid as of May 2007 (SOR ¶ 1.b). At his hearing, Applicant admitted the bankruptcy and tax lien, but contested the amounts of debt discharged and taxes owed.

After a thorough review and consideration of the pleadings, exhibits, and hearing transcript, I make the following findings of fact.

Applicant is a 50-year-old senior product designer, who has been employed by a defense contractor since January 2005. Applicant developed a portable satellite signal receiver capable of supporting top secret information and he seeks a secret-level clearance so that he can gather information in the field to further this and other products designed for the U.S. military.

Applicant served in the Army National Guard from July 1978 to July 1988, as a military forward observer in special operations and in winter survival. He held clearances up to the top secret level for his duties in the Guard.

In September 1994, Applicant co-founded a product design and development company that had gross sales of 2.6 million and 20 employees at its peak. Applicant was chief architect of the company's products, which in the commercial sector included wireless devices, specialized electronic enclosures, invasive medical devices (catheter-type drug delivery system), touch screen kiosks, superconductor process machinery, computer peripherals, reconfigurable modular furniture

and ergonomic seating, and yacht building. The company was awarded small business innovative research grants by NASA in 1999/00 for the creation and design of a hygiene system for astronauts, and by the U.S. Navy to design and develop a modular composite cabin for fast attack craft.

After the terrorism acts of September 11, 2001, existing contracts and to his belief guaranteed future business totaling almost \$3 million were cancelled due to government reallocation of funds and non passage of funding legislation. The company had a million-dollar payroll at the time and a cash crunch. In 2002, the company suffered a loss of about \$722,000 from a contract to build a movement tracking device for a sports technology company. Due to enormous design requirements, the product could not be completed within budget, and the company “borrowed” man-hours from other jobs for the project. The customer refused to pay for the overcharges and instead required Applicant’s company to borrow \$500,000 from the customer to complete the project. Applicant’s company was to repay the debt with the first gross receipts from the finished project. Lacking the revenue to cover employee salaries, vendors, and its federal tax obligations, Applicant decided to pay his employees’ salaries first and then a small business administration loan (SBA), and to not pay state and federal employee withholding taxes starting with the second quarter of 2002:

So we were able to eventually complete the project at a loss, we did end up recouping the \$500,000 at that point, and you can see by the nature of the difference in the dates that we were delinquent on our payments, so we made payments as much and as quickly as we could. There were specific months where we absolutely could not make payments to the IRS, and those decisions were made because we were guaranteed money going forward and on the advice of what used to be a friend, my accountant, he suggested that we forego paying some of these and that within a matter of six months we would be able to recoup them, and that was true in certain cases and in other cases that was not true.

It was a very poor decision on my part to do that. I did that with my business partner, I did it with the folks I hired in-house to assist me and my accountant, and we made those in order to not lose my staff. (Tr. 68)

In an effort to keep the business going, the employees took a 20 per cent cut in pay, and Applicant took no pay for a few months. He had earned \$156,915.52 in 2002, but significantly less in 2003 (\$45,570). Employees left on their own accord as they could see the business was failing.

In September 2002, Applicant married his current spouse. He had two children from his previous marriage and she had three children. Needing more room, they put an addition on the home that belonged to his spouse before their marriage. In June 2003, Applicant and his spouse took out a conventional 30-year mortgage loan of \$447,800 on the home. Repayment terms were set at \$3,443 per month.

In August 2003, the IRS filed a tax lien against Applicant and his business partner in the amount of about \$327,890. Applicant’s income tax refunds for 2003 and 2004, totaling about \$15,000 were intercepted and applied toward the debt. Following an offer in compromise by his

business partner, as of October 2007, Applicant is being held personally liable for past due federal taxes of \$154,544.49 for 2002 and \$16,400.96 for 2003.<sup>1</sup>

After speaking with their creditors, include the state tax authority, the IRS, and the bank lender of the SBA loan, Applicant and his business partner determined they should complete whatever contracts they could on their own, and then close down the company and sell assets to repay its obligations. The company ceased operations as a viable entity in September 2003, and was formally closed in August 2004. The vendors were paid and state taxes satisfied with the proceeds from the sale of company assets.

Applicant was self-employed from April 2004 to January 2005. He billed out at \$225 per hour for his consulting services. Applicant had household earned income of at least \$41,188 and unemployment compensation of \$11,166 in 2004.<sup>2</sup>

In November 2004, Applicant filed for Chapter 7 bankruptcy seeking discharge of consumer/non-business debts. He listed liabilities totaling \$1,846,066.34, but that included \$218,384.16 in unsecured priority claims owed the IRS for failure to pay employee withholding taxes in 2002 and 2003. Among the unsecured nonpriority claims were the \$500,000 loan from the sports technology company and a \$411,384.16 claim by his business partner, both disputed as valid debts by Applicant,<sup>3</sup> and also his and his spouse's mortgage obligation of \$441,046.75 that they continued to pay on after the bankruptcy. Consumer credit card obligations totaling \$56,501.27 and loan debt of \$193,000 (including the \$123,000 still owed on the SBA loan) were reportedly used for the business. Applicant was granted a Chapter 7 bankruptcy discharge in March 2005. The tax debt was not subject to the discharge.

With a sizeable mortgage and two children and three stepchildren at home, Applicant was not in a position to repay the tax debt in full. He did not want to negotiate a repayment schedule with the IRS, as the IRS would consider his income and determine a repayment amount from allocation tables that would not take into account his particular expenses. An IRS case officer recommended to Applicant that he get a job, pay down the debts that he could, and then negotiate an offer in compromise with the IRS. Applicant started his present job in January 2005. In his initial interview

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<sup>1</sup>The government alleged a federal tax lien against Applicant in the amount of \$327,890.39 (SOR ¶ 1.a). Applicant listed on his bankruptcy petition a federal tax debt of \$218,384.16 (Ex. 3, Schedule E). On his SF 86, he listed an estimated tax lien of \$125,000 (Ex. 1). Available IRS documentation shows he owes \$170,945.45 (Ex. D). Applicant testified his business partner entered into an offer in compromise, and paid around \$70,000 to settle his debt. (Tr. 102) The \$170,945.45 is solely Applicant's responsibility ("One [option] was to do as much as possible to pay back the IRS debt first, that's why the number went from \$327,000 down to approximately \$200,000, at which time I worked out with my former business partner, who is single with no kids or married with no children, he decided the best thing he was going to do was to do an offer in compromise, succeeded in doing so and cutting that debt in half, so the debt you see here is actually mine, it's not split across two people." Tr. 71).

<sup>2</sup>Applicant indicated on his SF 86 that he was employed as a freelance product designer from April 2004 to January 2005. (Ex. 1) He listed on his bankruptcy petition (Ex. 3) \$41,188 in earnings for 2004, which he now claims was his and his spouse's joint income (Tr. 116). The bankruptcy was not filed jointly.

<sup>3</sup>Applicant testified he was told to list his former business partner as a creditor so that he could not file suit against him in the future. (Tr. 80-81)

with the company, Applicant disclosed that he had operated a company that suffered financial hardship.

Needing a secret clearance for his duties, Applicant executed a questionnaire for sensitive positions (SF 86) on January 31, 2006. He disclosed pleasure travel to the United Kingdom in 1999, to the Carribean in December 2001, April 2002, and April 2004, and to Bermuda in September 2002 and August 2003; an April [sic] 2004 bankruptcy filing to resolve business-related debt of \$150,000; and a federal tax lien of \$125,000 on his personal assets filed in March [sic] 2003. He added that he was currently working out an offer in compromise.

Credit checks of February 28, 2006, and April 24, 2007, reflect the bankruptcy. As of February 2006, Applicant was current in his mortgage, but the account had been 30 days past due. Open revolving charge accounts that he held with his spouse were in good standing. As of April 2007, he had only one outstanding credit card balance, which was in the amount of \$600 and rated as current. His mortgage balance was \$424,000.

In response to DOHA interrogatories concerning the IRS debt, Applicant indicated on May 29, 2007, that he was deferring action on the debt and planned to enter into an offer in compromise at a later date. He indicated that on the advice of a case officer, he was not in contact with the IRS. Applicant estimated it would be about four years before he was in a financial position to negotiate an offer in compromise. Recognizing that the tax lien could jeopardize approval of his clearance, Applicant indicated all he could do was to assure that he presents no security risk.

With the exception of their honeymoon trip in 2002, which was a gift from his parents, Applicant and his spouse's pleasure trips were paid for by his spouse who withdrew funds from her 401(k) and/or cashed out some stocks. She also borrowed against her retirement to pay for their wedding. Applicant continues to pay his mortgage on time, as reflected in a credit report of November 7, 2007. He was continuing to rely on consumer credit, owing respective balances of \$1,366 and \$1,369 on revolving charge accounts opened in December 2002 and March 2003. Both accounts are rated as current. His children and stepchildren, who range in age from 13 to 19, still live at home.

As of November 2007, Applicant and his spouse were spending what they take in ("financially, what goes in goes out" Tr. 84). Every three months, he was withdrawing his 401(k) monies to meet his expenses. Despite an annual salary of \$98,700, Applicant had not saved any funds toward entering into an offer in compromise. He has substantial orthodontia expenses, with one child about to come off braces, two that just started with braces and another about to start. He hopes to qualify for a home equity or line of credit that would give him the funds to pay off the IRS. Applicant has not contacted the IRS as it would open his case and he fears the IRS would then garnish his wages based on an allocation table.

Applicant has been dedicated and reliable in his work performance. Company vice presidents who have had the opportunity to work with Applicant appreciate his openness, his strong work ethic, and his commitment to the company. The chief financial officer has discussed financial matters, working relationships with suppliers, and best practices. He trusts Applicant "implicitly." The executive vice president has found Applicant to be "conscientious, reliable, and accountable" in budget matters. The facility security officer is aware that Applicant had business-related financial

problems in the past. He has not witnessed any conduct on Applicant's part that which cause concerns for Applicant's ability to access classified information.

## **POLICIES**

"[N]o one has a 'right' to a security clearance." *Department of the Navy v. Egan*, 484 U.S. 518, 528 (1988). 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." *Id.* at 527. 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." Exec. Or. 10865, *Safeguarding Classified Information within Industry* § 2 (Feb. 20, 1960). An applicant "has the ultimate burden of demonstrating that it is clearly consistent with the national interest to grant or continue his security clearance." ISCR Case No. 01-20700 at 3 (App. Bd. Dec. 19, 2002).

The revised Adjudicative Guidelines set forth potentially disqualifying conditions (DC) and mitigating conditions (MC) under each guideline. In evaluating the security worthiness of an applicant, the administrative judge must also assess the adjudicative process factors listed in ¶ 6.3 of the Directive. The decision to deny an individual a security clearance is not necessarily a determination as to the loyalty of the applicant. *See* Exec. Or. 10865 § 7. It is merely an indication the applicant has not met the strict guidelines the President and the Secretary of Defense have established for issuing a clearance.

## **CONCLUSIONS**

### **Guideline F—Financial Considerations**

Failure or inability 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 information. An individual who is financially overextended is at risk of having to engage in illegal acts to generate funds. (AG ¶ 18). Applicant was granted a Chapter 7 bankruptcy discharge in March 2005 of debts largely due to a failure of his business in 2002/03. He currently owes the IRS more than \$170,000 in delinquent employee withholding taxes that he had a fiduciary responsibility to pay quarterly between June 2002 and March 2003. Guideline F disqualifying conditions ¶ 19(a) (*inability or unwillingness to satisfy debts*) and ¶ 19(c) (*a history of not meeting financial obligations*) apply.

Applicant had no control over the government's failure to appropriate funds for contracts that Applicant had or anticipated from NASA or the U.S. Navy following the terrorist acts of September 11, 2001. However, mitigating condition ¶ 20(b) (*the conditions that resulted in the financial problem were largely beyond the person's control (e.g., loss of employment, a business downturn, unexpected medical emergency, or a death, divorce or separation), and the individual acted responsibly under the circumstances*), applies only in mitigation of the bankruptcy. Applicant had

control over the decision that was made to utilize money owed to the federal government in an attempt to save his failing company. The government must be assured that those persons granted access can be counted on to fulfill their legal obligations, even if compliance results in personal hardship to self or others.

The debts discharged in bankruptcy and the IRS debts that were not discharged were incurred more than four years ago under circumstances that are not likely to recur (*see* MC 20(a) (*the behavior happened so long ago, was so infrequent, or occurred under such circumstances that it is unlikely to recur and does not cast doubt on the individual's current reliability, trustworthiness, or good judgment*)). Yet, I am unable to apply MC 20 (a) because his decision to withhold payment of payroll taxes casts significant doubt about his judgment.

Applicant remains under significant financial pressure that raises the potential for pressure, coercion, exploitation, or duress, and he is not likely to resolve the situation in the near future. As of November 2007, Applicant had not contacted the IRS about the debt because he did not want the IRS to open a new case and assess a repayment amount based on allocation tables that would not account for his high expenses. While he has a good credit rating, he is taking early withdrawals from his 401(k) every few months so that he can meet his expenses. In the past three years, he has not saved any of the funds he needs to approach the IRS with a reasonable offer in compromise. MC 20(d) (*the individual initiated a good-faith effort to repay overdue creditors or otherwise resolve debts*) is not satisfied by waiting for the IRS to intercept his tax refunds.

### **Whole-Person Analysis**

Under the “whole-person” evaluation required by AG ¶ 2(a) (*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*), Applicant has shown himself to be a valuable contributor to his employer and to the national defense. He held a security clearance for about ten years as a member of the Army National Guard. While the business downturn was central to his decision to not pay the required employee withholding taxes to the IRS, his exercise of poor judgment was not limited to the business, but extended to his personal finances as well. He and his spouse borrowed from her retirement to take vacations to the Caribbean even in 2004, after the IRS had filed the tax lien against him. He continues to put his personal interests ahead of his obligation to repay the tax debt. When he completed his SF 86 in January 2006, he indicated he was “currently working out an offer in compromise,” but in May 2007 told DOHA that it would be about four years before he would even be in a position to make an offer. Under the totality of the circumstances, I cannot conclude that it is clearly consistent with the national interest to grant Applicant access to classified information.

## FORMAL FINDINGS

Paragraph 1. Guideline F:

AGAINST APPLICANT

Subparagraph 1.a (as amended): For Applicant

Subparagraph 1.b (as amended):           Against Applicant

## DECISION

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

Elizabeth M. Matchinski  
Administrative Judge