Employee and Applicant Background Checks and the Fair Credit Reporting Act

Frequently, employers inquire as to the application of the federal Fair Credit Reporting Act (the FCRA or the Act) when conducting applicant and employee background checks. This document outlines the fundamentals of the FCRA so that employers can become more informed of the issues under the Act and make an educated decision regarding the scope of the background check they wish to undertake in a given set of circumstances.

The FCRA generally requires that an employer provide certain notices to an applicant or employee advising that the employer seeks to obtain and utilize a credit report from a credit reporting agency. Under the FCRA, an employer may take "adverse action" based upon a credit report against an applicant or an existing employee with regard to initial employment, promotions, reassignment and retention as an employee, provided that the proper procedures required by the Act are followed. Further, though there is nothing in the Act that requires an employer to consider a candidate who refuses to authorize access to his or her credit report, the Federal Trade Commission (FTC), which, along with the Consumer Financial Protection Bureau (CFPB), is responsible for enforcing the Act, is equivocal on an employer's right in this regard. The FTC, in an Advisory Opinion, stated that even though the FCRA does not prohibit an employer from taking an adverse action against an applicant who refuses to authorize a release of his or her credit report, the Act does not expressly permit the employer to refuse to consider an applicant who does not authorize the release of a credit report. Thus, while the Act does not expressly prohibit an employer from taking an adverse action against a candidate who refuses to authorize an employer to obtain a credit report, an employer may be within its rights to refuse to consider the candidate. The FTC has neither endorsed nor rejected this interpretation.

There are a number of detailed steps an employer must take before obtaining a credit report and before taking an adverse action based on the information contained in the report. At the outset, please note that the guidelines speak only to compliance with the Act and should be considered a supplement to an employer's existing employment procedures.

Further, note that there has been criticism of some of the procedures that must be followed because they appear to be impractical to implement and, at times, redundant. However, the FTC has warned that compliance with all of the notice requirements is mandatory, even if the information is duplicative. The FTC's reasoning is two-fold: first, the statute requires the notices, so they must be given; and second, the rights afforded to the consumers are so important that the redundancy is warranted. Finally, employers must become educated about the differences between a consumer credit report and the more invasive investigative reports and reports containing medical information. Investigative reports and medical reports require the employer to provide additional disclosures and receive additional authorizations from employees and applicants.

The following briefly sets forth the necessary steps to be taken by an employer in obtaining a credit report and highlights some of the nuances of the Act. First, before an employer can obtain a credit report, the employer must disclose to the individual that a credit report may be sought and receive the individual's written authorization. Second, when requesting the report from the credit reporting agency, the employer must make certain certifications to the credit reporting agency. Third, if the credit report contains disqualifying information, the employer must notify the individual of the disqualifying information before an adverse action is actually taken. This is done using a "pre-adverse action notice." Note that a copy of the report and a summary of the consumer's rights must be attached to the pre-adverse action notice.

The Act does not state how much time an employer must wait after giving the pre-adverse action notice before actually taking an adverse action. The FTC has suggested that five business days is reasonable, but has cautioned that the circumstances of a particular situation may call for a different time frame. Further, if the individual contacts the employer with regard to the disqualifying information during this time period, the employer should carefully consider the information. The reason for this is that an employer needs to be conscious of avoiding discrimination claims by protected

classes. The Equal Employment Opportunity Commission has cited U.S. Census figures that demonstrate that a disproportionate number of African Americans would tend to have poor credit histories. Similar data could be developed on women who have frequently been denied credit because of their husband's credit history. While an employer should remain conscious of possible claims for discrimination and should consider the candidate's explanation carefully, it is still safe for an employer to use information contained in credit reports in its employment decisions where the employee will be handling large sums of money or exercising financial discretion.

Fourth, and finally, if an employer ultimately decides to take an adverse action, the employer must then provide the individual with an "adverse action notice." It is important to note that an employer must give an adverse action notice any time the credit report plays a role in the adverse decision, no matter how minor a role. Although the adverse action notice is highly duplicative of the pre-adverse action notice, it still must be given.

The importance of following a uniform set of guidelines cannot be understated because the Act provides some protection to employers that maintain reasonable procedures to assure compliance. More specifically, the Act states that an employer will not be held liable for failing to follow the proper procedure for taking an adverse action if the employer shows by a preponderance of the evidence that, at the time of the alleged violation, the employer maintained reasonable procedures to assure compliance with the Act.

While many employers believe that the FCRA applies only to credit reports, it may, depending upon the circumstances, apply to the obtaining of criminal records and other types of employment-related information. Additionally, various states and cities have enacted laws that place further restrictions on an employer's ability to use information obtained as part of an applicant or employee background check. Therefore, prudent employers should look to state law in addition to federal law when conducting these types of background checks.

One final note with regard to bankruptcy. If the credit check indicates that the individual has declared bankruptcy, the employer must comply with both the FCRA and the Bankruptcy Act. Under the federal Bankruptcy Act, it is unlawful to terminate an employee or to discriminate in the hiring of an employee solely because that person: (1) has sought protection under the Bankruptcy Act; (2) has been insolvent before seeking protection under the Bankruptcy Act; or (3) has not paid a debt that is dischargeable under the Bankruptcy Act. Having said that, under the Bankruptcy Act, employers may, on a case-by-case basis, screen out a bankrupt applicant where the history underlying the debts indicates financial irresponsibility and the position requires financial honesty and aptitude.

This overview of the FCRA's application to employee and applicant background checks does not address all of the statutory and regulatory requirements. Employers should consult legal counsel regarding the specifics of applicable statutory and regulatory requirements. If you need more information about the FCRA's application to employee and applicant background checks, or if you would like to receive sample notices and other forms, please contact a member of Fox Rothschild's Labor & Employment Department.

Fox Rothschild LLP
ATTORNEYS AT LAW

For more information contact:

Ian D. Meklinsky, Esq.
609.895.6756
imeklinsky@foxrothschild.com

Princeton Pike Corporate Center | 997 Lenox Drive, Bldg. 3
Lawrenceville, New Jersey 08648-2311
609.896.3600

Scott Cooper, Esq.
973.994.7513
scooper@foxrothschild.com

75 Eisenhower Parkway | Suite 200
Roseland, NJ 07068-1600
973.992.4800