

# Questions—And Answers

## ***An Employer's Guide to the Fair Credit Reporting Act***

*Kevin J. Smith and Lindsay Colvin*

The Fair Credit Reporting Act (FCRA), along with its state analogues, imposes stringent requirements for employers and will likely present new challenges in the future.<sup>1</sup> The act affects almost every person or company who seeks an individual's credit report from a consumer reporting agency, including employers, mortgage lenders, credit card issuers, and landlords.<sup>2</sup> Most significantly, for employers, the FCRA and similar state laws affect an employer's ability to conduct credit checks on potential or current employees using consumer reporting agencies.<sup>3</sup> This issue of Questions—and Answers provides an overview of the FCRA and its state analogues, describes the act's importance, highlights possible changes to FCRA currently under review by Congress, and recommends best practices for employers who do choose to implement credit checks during the hiring process.

### **WHAT IS THE FCRA AND WHY SHOULD EMPLOYERS PAY ATTENTION TO IT?**

The Fair Credit Reporting Act, which was originally passed in 1970 and amended in 1996, "promote[s] the accuracy, fairness, and privacy of consumer information contained in the files of consumer reporting agencies."<sup>4</sup> The act has a wide reach, regulating many entities that seek and/or use an individual's credit history or information, as well as credit bureaus and specialty agencies.<sup>5</sup> Most notably, the FCRA and subsequent amendments, as well as state fair credit reporting laws that have been passed over time, regulate the means by which employers may conduct credit checks through consumer reporting agencies during the hiring process.<sup>6</sup>

An individual's credit history may be of interest to employers making personnel decisions of all types, including hiring, promotion, retention, or reassignment. However, any time an employer uses a consumer reporting agency to review an applicant's or employee's background information to make an employment decision, it must comply with the FCRA's requirements.<sup>7</sup> It is important to note that the FCRA and state analogues apply only where an employer receives a credit report from a company in the business of compiling background information (such as Experian, Equifax, or others); compliance with the FCRA is not required if an employer runs an independent, or "in-house," credit investigation.<sup>8</sup> Many employers who conduct credit checks choose, however, to rely on consumer reporting companies for efficiency purposes, and are thus bound to follow the FCRA and applicable local laws. An employer's failure to comply with the FCRA when obtaining a credit check from a consumer reporting agency can result in civil penalties of up to \$1,000 per violation, punitive damages, and costs.<sup>9</sup>

### **WHAT ARE THE PROS AND CONS OF APPLICANT/EMPLOYEE CREDIT CHECKS?**

Each employer, whether it already uses credit checks or is considering doing so, must balance the relevant advantages and disadvantages of this type of investigation. The results of an applicant's or employee's credit check can be valuable to an employer. For instance, banking, accounting, or money-management employers often review credit histories to determine whether a particular individual might be financially troubled and thus susceptible to fraud or embezzlement.<sup>10</sup> An applicant's or employee's credit history might also be useful to employers who use credit history as a tool to evaluate the individual's judgment or level of responsibility.<sup>11</sup> Some employers use credit checks to predict future work performance, operating under the assumption that an employee burdened by debt or hounded by creditors might be more likely to focus on personal financial issues than work.<sup>12</sup> Additionally, evaluating credit checks allows employers to confirm or contradict items on an applicant's resume or to distinguish between two otherwise comparable applicants when making a hiring decision.<sup>13</sup>

However, the results of a credit check are not always indicative of an applicant's or employee's skill set or personal credibility, and credit checks may in fact be an inadequate basis for employment decisions.<sup>14</sup> For instance, a poor credit report may not be indicative of employment performance but instead the result of uncontrollable personal circumstance like death, divorce, the recent financial crisis, or a medical emergency.<sup>15</sup> Further, because creditreporting companies are not infallible, individual credit reports may contain undetected errors.<sup>16</sup> Critics of the use of credit checks

in hiring have also disparaged the practice for reducing job prospects and economic opportunity for minorities<sup>17</sup>. As a result of the above factors, use of or reliance on credit history information could result in employers missing out on qualified candidates.

### **WHICH STATES AND CITIES HAVE LAWS ANALOGOUS TO THE FCRA?**

The following states have analogous laws to the FCRA limiting the use of credit checks by employers: California, Colorado, Connecticut, Delaware, Hawaii, Illinois, Maryland, Nevada, Oregon, Vermont, and Washington.<sup>18</sup> Additionally, some cities, including New York City and Chicago, maintain local laws to the same effect.<sup>19</sup> Some of these “mini-FCRA” laws are relatively similar to the FCRA itself, and many include sweeping exemptions to credit-check requirements and restrictions for employees handling cash and goods, employees in management positions, employees with access to financial information, and employees in law enforcement positions.<sup>20</sup> However, some “mini-FCRAs,” such as New York City’s Stop Credit Discrimination in Employment Act (SCDEA), impose much stricter limitations on employers who use credit checks in employment decisions.<sup>21</sup> The SCDEA prohibits almost all New York City employers from running or relying on credit checks to make employment decisions, with limited exceptions for jobs of “public trust” (including police officers and high-level city employees), and for employers who are required by federal or state law to conduct credit checks (such as mortgage bankers and securities broker-dealers).<sup>22</sup> Penalties for an employer’s failure to follow the SCDEA are significant and can be as high as \$250,000 per violation.<sup>23</sup>

### **ARE THERE ANY UPCOMING CHANGES TO THE FCRA THAT EMPLOYERS SHOULD KNOW ABOUT?**

The FCRA recently became a subject of interest for Congress, making it even more critical for employers to track and understand the law’s requirements. On May 19, 2016, Congresswoman Maxine Waters introduced a bill titled the “Comprehensive Consumer Credit Reporting Reform Act of 2016” (CCRRA), aimed at an overhaul of the FCRA’s current requirements.<sup>24</sup> The CCRRA, in contrast to the FCRA, would largely ban employers’ use of credit checks to make employment decisions, with the exception of a few specific industries.<sup>25</sup> Although the bill was only recently introduced and no action has yet been taken on it, the CCRRA’s introduction indicates that Congress may impose in the future even tighter restrictions on the use of credit checks. Employers who use or plan to use credit checks to make employment decisions should examine their need to rely on this type of

information and prepare other forms of evaluation in case credit checks are no longer legally available.

## **HOW SHOULD EMPLOYERS CONDUCT PROPER CREDIT CHECKS UNDER CURRENT LAW?**

Employers who do conduct credit checks through consumer reporting companies should be sure to observe proper procedures set forth by the FCRA (and, where applicable, consult state and local laws, "mini-FCRAs," to ensure compliance). In order to comply with the law and recommended best practices, employers should take the following steps:

Notify the applicant or employee that the employer might use credit-history information to make hiring or employment decisions. The notice must be in writing and must stand alone (i.e., not part of an employment application or employee information packet). The most effective notices are clear and concise, without a large volume of information that might confuse the person receiving the notice or detract from the notice's overall message.<sup>26</sup>

Obtain the employee's written permission to conduct the credit check. The easiest way to keep a record of the employee's assent to a credit check is to include the authorization on the notice form. If the employer plans to conduct credit checks throughout the course of employment, this must be stated clearly and conspicuously so that the applicant or employee knows that he or she is providing consent for this type of monitoring.<sup>27</sup> Employers should be sure to keep a copy of the notice form and authorization for their records.

If adverse employment action is taken based on the results of a credit check, (e.g., not hiring an applicant or terminating an employee), follow proper procedures.

Before the adverse action is taken, give the applicant or employee (1) a notice that includes the copy of the consumer report that the employer relied on to make the decision, and (2) a copy of a "Summary of Your Rights Under the Fair Credit Reporting Act," which should be provided by the company who performed the credit report.<sup>28</sup>

After the adverse action is taken, inform the applicant or employee (1) that the adverse action was taken because of information in the report; (2) the name, address, and phone number of the company that sold the report to the employer; (3) that the company selling the report did not make the decision to take the adverse action and cannot give a specific reason for it; and (4) that he or she has the right to dispute the accuracy or completeness of the report, and to obtain an additional free report from the reporting company within 60 days. This information can be provided orally, in writing, or electronically.<sup>29</sup>

Properly dispose of background reports once all applicable requirements are satisfied. Disposal must be secure, and acceptable methods include burning, pulverizing, or shredding paper documents, as well as disposing of electronic information so that it cannot be read or reconstructed.<sup>30</sup>

Reviewing the credit history of applicants or employees can provide valuable information to an interested employer. However, credit checks may not provide a comprehensive or accurate picture of a particular applicant or employee, and complying with the FCRA and state and local analogues can be complicated. Employers who use or plan to use credit-history information in employment decisions should ensure that their processes for doing so strictly comply with relevant law and should also take note that using credit checks in employment decisions may not always be an option.

## NOTES

1. US House Committee on Financial Services. (2016, May 19). Waters introduces comprehensive bill to fix credit reporting in U.S. Retrieved from <http://democrats.financialservices.house.gov/news/documentsingle.aspx?DocumentID=399837>
2. The Fair Credit Reporting Act, 15 U.S.C. § 1681 (2016).
3. Consumer Information. Employment background checks. Federal Trade Commission (last visited January 4, 2017). Retrieved from <https://www.consumer.ftc.gov/articles/0157-employment-background-checks>
4. A summary of your rights under the Fair Credit Reporting Act. Federal Trade Commission (last visited January 4, 2017). Retrieved from <https://www.consumer.ftc.gov/articles/pdf-0096-fair-credit-reporting-act.pdf>
5. Id.
6. Consumer Information. Employment background checks.
7. EEOC. Background checks: what employers need to know (last visited January 4, 2017). Retrieved from [www.eeoc.gov/eeoc/publications/background\\_checks\\_employers.cfm](http://www.eeoc.gov/eeoc/publications/background_checks_employers.cfm)
8. Id.
9. The Fair Credit Reporting Act, 15 U.S.C. § 1681 (2016).
10. Farrell, R. (2010, July 12). Why do employers care about your credit? CNN. Retrieved from [www.cnn.com/2010/LIVING/07/12/cb/employers.your.credit/index.html](http://www.cnn.com/2010/LIVING/07/12/cb/employers.your.credit/index.html)
11. Id.
12. Levin, A. (2013, September 22). 7 steps to deal with employers looking at your credit report. ABC News. Retrieved from <http://abcnews.go.com/Business/top-steps-deal-employers-credit-report/story?id=20309128>.
13. Gurchiek, K. (2010, November 2). SHRM: Credit checks are legitimate screening tool. Society of Human Resources Managers. Available at <https://www.shrm.org/about-shrm/news-about-shrm/pages/legitimatescreeningtool.aspx>
14. Jackson, N. M. (2011, January 12). Using credit checks to help in hiring. *Entrepreneur*. Retrieved from <https://www.entrepreneur.com/article/217848>
15. Id.

16. Consumer Information. Employment background checks. Federal Trade Commission (last visited January 4, 2017). Retrieved from <https://www.consumer.ftc.gov/articles/0157-employment-background-checks#negative>
17. Id.
18. Id.
19. Id.
20. Id.
21. Mayor De Blasio and Human Rights Commissioner Malalis announce new laws taking effect today to protect New Yorkers against employment discrimination based on credit history. (2015, September 3). City Hall Press Office, New York City. Retrieved from <http://www1.nyc.gov/office-of-the-mayor/news/591-15/mayor-de-blasio-human-rights-commissioner-malalis-new-law-taking-effect-today-to>
22. Id.
23. Credit check law: for employers. New York City Commission on Human Rights (last visited January 4, 2017). Retrieved from <http://www1.nyc.gov/site/cchr/media/credit-check-law-for-employers.page>
24. US House Committee on Financial Services. (2016, May 19). Waters introduces comprehensive bill to fix credit reporting in U.S. Retrieved from <http://democrats.financialservices.house.gov/news/documentsingle.aspx?DocumentID=399837>
25. H.R. Res. 5282, 114th Cong. (2016).
26. 15 U.S.C. § 1681(b); Consumer Information, Background checks.
27. Id.
28. Id.
29. Id.
30. 15 U.S.C. § 1681; Fed. Trade Commission. Disposing of consumer report information? Rule tells how (last visited January 4, 2017). Retrieved from <https://www.ftc.gov/tips-advice/business-center/guidance/disposing-consumer-report-information-rule-tells-how>

**Kevin J. Smith** is special counsel at Sheppard, Mullin, Richter & Hampton LLP in the firm's Labor and Employment group. He has extensive experience in employment litigation, including trials and appeals in federal and state courts, and conducting arbitrations and administrative hearings. His employment law practice also includes counseling Fortune 500 companies in all types of employment and labor-law matters. He may be contacted at [kjsmith@sheppardmullin.com](mailto:kjsmith@sheppardmullin.com). **Lindsay Colvin** is a labor and employment associate at Sheppard, Mullin, Richter & Hampton LLP and may be contacted at [lcolvin@sheppardmullin.com](mailto:lcolvin@sheppardmullin.com).