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CLIENT BULLETIN

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Use of credit reports comes under increased scrutiny
NO CREDIT? NO PROBLEM! (The Sequel)

By William J. McMahon, IV, Winston-Salem Office
and
Kelli P. Hill, Macon Office

In today's economic climate, employers often want to analyze applicants' credit reports. A poor credit history may indicate problems that an employer would prefer to avoid. But using credit reports legally requires a thorough understanding of the various federal and state laws that can come into play in this area.

Fair Credit Reporting Act

A credit report is considered a "consumer report" compiled by a "consumer reporting agency" under the federal Fair Credit Reporting Act. Accordingly, special procedures apply when employers obtain and use such reports to evaluate applicants for hire as well candidates for promotion, reassignment, or retention.

The employer must notify the applicant/employee in a written stand-alone document (in other words, not within the employment application itself) that a consumer report may be used in the evaluation process. In addition to this notice, the employer is required to get the applicant/employee's written authorization for obtaining the consumer report. The authorization may be provided on the initial "notice" document.

Before the employer can take adverse action against an applicant/employee based in whole or in part on the consumer report, it is required to go through a two-step process. The first step is to provide the individual a copy of the consumer report and a copy of the Federal Trade Commission's "A Summary of Your Rights Under the Fair Credit Reporting Act," which will be sent to the employer by the consumer reporting agency providing the credit report. The purpose of this first "pre-adverse action" disclosure is to give the applicant/employee the opportunity to dispute the contents of the report before any adverse employment action is taken. After waiting a reasonable time (at least five business days), the employer takes the second step: providing the applicant/employee with a copy of the adverse action notice. This notice must include the following: (1) the name, address, and telephone number of the consumer reporting agency that supplied the report; (2) a statement that the consumer reporting agency that supplied the report did not make the decision to take the adverse action and cannot give specific reasons for it; and (3) a notice of the individual's right to dispute the accuracy or completeness of any information the agency furnished, and his or her right to an additional free consumer report from the agency upon request within 60 days.

Although the FCRA currently remains the applicable federal law that employers must follow, Rep. Steve Cohen (D-Tenn) has introduced into Congress the Equal Employment for All Act (H.R. 3149), which proposes to amend the FCRA to ban employers from using credit reports in making hiring or promotion decisions, with exceptions for certain financial and governmental positions. The bill, which has 55 Democrat co-sponsors, was referred to the House Committee on Financial Services on July 9, 2009, but to date no further action has been taken on it.

EEOC Takes Renewed Interest

The FCRA is not the end of the story for employers: the Equal Employment Opportunity Commission has taken renewed interest in the use of credit reports in making employment decisions. Credit reports are addressed in the EEOC's **E-RACE initiative ("Eradicating Racism and Colorism from Employment")** (scroll to item 3, first bullet point), and the agency has sued employers who use credit reports when that use results in disparate impact.

In March 2010, the EEOC issued an **informal discussion letter** on credit checks, stating that they have "not been shown to be a valid measure of job performance." The EEOC concedes, however, that courts have found that credit checks are appropriate for certain positions, "such as where an employee handles large amounts of cash," and that in those instances screening out employees based on credit history would be appropriate, even if the practice did have a disparate impact on minority groups.

"Disparate impact" liability occurs where an employer has a practice that is neutral on its face – for example, a requirement that any applicants with credit scores below a certain level will not be considered for hire – but, as applied, tends to disproportionately exclude members of a given protected group. Therefore, if members of certain races tend to have lower credit scores than members of other races, the use of credit reports as a screening criterion could be discriminatory unless the employer can show that use of the credit reports is job-related and consistent with business necessity.

States Take Action

As if complying with the federal laws were not enough, employers must also be cognizant of the ever-increasing number of states that have passed legislation regarding use of individuals' credit reports in the employment setting. Presently, four states have passed legislation restricting employers' use of credit reports: **Illinois**, Oregon, Hawaii, and Washington. Several more states, however, are seeking to pass similar legislation in an effort to help workers in the current economic climate. Employers with multi-state operations must be especially careful, as many of these state laws are more restrictive than the FCRA.

If you need assistance in navigating the various federal and state laws in connection with using credit reports for your applicants or current employees, please contact any member of Constangy's **Litigation Practice Group**, or the Constangy attorney of your choice.

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