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Spotlight On: Consumer Financial Services

Employee Background Checks—A Double-Edged Sword

Businesses regularly conduct background checks on existing or prospective employees. While this practice is legal, employers must remember to comply with some fairly technical rules. The alternative could be costly.

The Fair Credit Reporting Act (FCRA) is a federal statute that governs the use of consumer information. Although few are surprised by the FCRA's role in governing our nation's "big three" credit bureaus—Equifax, Experian, and TransUnion—many may not appreciate that the FCRA also applies to much of the data commonly accessed and used by businesses to make informed hiring and retention decisions. When a job involves access to money or sensitive information, for example, employers often want to screen applicants extra carefully.

Of course, employers typically review the candidate's resume, conduct interviews, and check references. Increasingly, however, businesses are taking an important additional step to protect themselves from untrustworthy applicants: a background and credit check. In this information age, employers are privy to far more than a credit score. Consumer reports available in today's market provide remarkably detailed information about applicants' finances—including assets, liabilities, and bankruptcies—as well as public record information, such as criminal histories.

Unquestionably, a candidate's background is relevant to an informed employment decision. There is the possibility, however, that an existing or prospective employee may be maligned unfairly by a consumer report if that report contains outdated or inaccurate information. For this reason, Congress requires employers to adhere to strict guidelines when they access and use consumer reports to make employment decisions. Those guidelines are found in the FCRA.

One notable requirement of the FCRA applies when an employer anticipates taking "adverse action" against an existing or prospective employee because of information obtained from a consumer report. Before doing so, the employer must give the employee a copy of the consumer report, as well as provide a summary of consumers' rights under the FCRA. This requirement is intended to provide an opportunity to correct any inaccuracies in the report on which the employer might otherwise rely. Additional disclosures are required if the employer ultimately elects to take adverse action because of the report, regardless of whether its content is disputed.

Although the FCRA is not especially complicated, it is detailed and compliance may be burdensome. Employers that hire fewer people and only occasionally use consumer reports are particularly vulnerable to running afoul of the FCRA. In contrast, many of the nation's largest employers which regularly utilize consumer reports have found it economical to avail themselves of the compliance services now offered by consumer reporting agencies. These agencies promise to take the actions necessary to satisfy their clients' FCRA obligations.

Despite this promise, well-meaning consumer groups and plaintiffs' lawyers routinely file class action lawsuits against consumer reporting agencies, alleging that the agencies have violated the FCRA in the course of providing consumer reports to their employer-clients. Consumer class actions against individual employers also are on the rise. For example, two FCRA class actions—one against an employer and one against a consumer reporting agency—recently settled in the Eastern District of Virginia, one for $3 million and the other for $22 million. (Both settlements await the court's approval.)

In the first case, an employer summoned several of its employees to a conference room. There, it provided those employees with copies of their consumer reports and summaries of their rights, informing them that they were being terminated because of their criminal records,

as reflected in their consumer reports; however, the court rejected the employer's position that it could provide the reports immediately before discharging the employees. Instead, the court held that an employer must provide a "sufficient amount of time before it takes adverse action so that the consumer may rectify any inaccuracies in the report. . . ."

The second case involved claims that applicants were denied jobs because a consumer reporting agency provided inaccurate information. According to the applicants, the consumer reporting agencies allegedly reported that several of the job applicants were convicted of felonies when, in fact, they were only convicted of misdemeanors. The job applicants also claimed that, with respect to other applicants, the consumer reporting agencies allegedly provided the prospective employer with someone else's criminal history, perhaps involving "mixed-file" situations (where one consumer's report is mixed with another's due to similar identifying information, such as similarities in their names, dates of birth, and social security numbers).

Not only is defending an FCRA class action costly, recent trends show that employers are finding it increasingly difficult to dispense with these cases at their earliest stages, through dismissal or summary judgment. To avoid summary judgment, for instance, one federal court most recently held that plaintiffs—employees or job applicants—need only "minimally present some evidence from which a [jury] can infer that the credit reporting agency failed to follow reasonable procedures in preparing a consumer report." Thus, plaintiffs need not provide direct evidence of unreasonableness, because "inaccurate credit reports alone can fairly be read as evidencing unreasonable procedures. . . ."

Informed and energized by these cases, consumer groups and the plaintiffs' bar seem likely to continue to pursue claims against employers at all levels. Many of these lawsuits will allege that employers have violated the FCRA, not only due to their own conduct but also due to the alleged failures of third-party compliance services. In addition, consumer groups almost certainly will advance similar claims against smaller, more vulnerable employers. Accordingly, businesses of all sizes should view consumer reports as a double-edged sword. Although such reports are useful for vetting employees, the FCRA can become a costly trap for unsuspecting employers if not strictly followed.

The information in this spotlight should not be considered legal advice. Consult your attorney before acting on anything contained herein.

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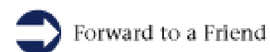

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