# Background Checks: When and How to Use Them

Improperly requiring background checks or misusing the information may subject an employer to significant liability.

*By Ethan L. Don*

Many employers today may feel they have the right, if not the obligation, to look into the backgrounds of all of their existing and potential employees. There are, indeed, several benefits to running background checks; among them are screening potential employees whose actions could result in vicarious liability, avoiding negligent hiring claims, protecting the safety of other employees, and protecting proprietary interests.

Although these benefits are compelling, many employers may be unaware that federal and state laws, along with guidance from agencies, such as the Equal Employment Opportunity Commission (EEOC), significantly restrict when and how background checks can be run and also how such checks can be used in making employment decisions. There is no doubt that employers, particularly ones that deal with financial information or whose employees have frequent direct customer or client contact, certainly have legitimate reasons to run background checks and to make decisions based on the information they provide. Nevertheless, as improperly requiring background checks or misusing information learned from those checks may subject an employer to significant liability, employers need to understand how to properly use background checks. In order to do that, employers must recognize what background checks may reveal, the relevance of that information to their business or the employment position, and what steps and analysis need to be performed as part of obtaining and using a background check.

## What is a background check?

The two primary types of background checks are generally referred to as credit checks and criminal history checks. The term "credit check" is a bit misleading because most credit checks sought by employers actually involve significantly more information than just someone's credit history. The Fair Credit Reporting Act (FCRA), which covers the use of credit checks, refers to "consumer reports" that may include information on an individual's creditworthiness, credit standing, credit capacity, character, general reputation, personal characteristics, and mode of living. Consumer reports may also include criminal background checks, revealing arrest and conviction records, incarceration records, and sex offender lists or registrations, among other things. Other information that might appear on one or more types of background checks include driving records, educational records, workers' compensation records, bankruptcies, state licensing records, military records, and past employers.

## Use of consumer reports including credit checks

The FCRA and state law control an employer's use of consumer reports, including but not limited to credit checks. The FCRA applies only to information furnished by a "consumer reporting agency." Information gathered by an employer through public resources, such as public court websites, state or national sex offender registries, or public tax and real estate data is not covered. It is generally advisable, however, for employers to act in compliance with the FCRA when using any information of this sort, especially if the employer is using a third-party consumer reporting agency to also provide other information.

## FCRA compliance

There are three stages to FCRA compliance:

1. providing separate written notification to the employee or applicant that a consumer report may be obtained;
2. providing an employee or applicant a pre-adverse action notice; and
3. providing an employee or applicant an adverse action notice.

First, an employer must notify an employee or applicant in writing, separate from an employment application or other document, that the employer may obtain a consumer report. It is advisable that the notice provide some specificity about the type of reports that may be run (*i.e.,* credit, criminal, or educational). The employer must also

receive from the employee or applicant a written authorization to obtain the consumer report. The authorization can be part of the notice form, but it must be clear and conspicuous authorization.

Second, if an employer decides that it may take an adverse action against an employee or applicant and information obtained from a consumer report is a factor in that decision, the employer must provide the employee or applicant a pre-adverse action notice. "Adverse action" is defined in the FCRA as "a denial of employment or any other decision for employment purposes that adversely affects any current or prospective employee." Some common adverse actions include rejecting an applicant, not promoting an employee, denying an employee a pay raise, reassigning or demoting an employee, or terminating his or her employment.

The pre-adverse action disclosure must include copies of any reports the employer used and a copy of the Consumer Financial Protection Board's (CFPB) "Summary of Your Rights under the Fair Credit Reporting Act." The notice must also include the name, address, and phone number of the consumer reporting agency issuing the report, along with a statement that the individual must contact the consumer reporting agency directly to dispute the contents of the report. The purpose of this pre-adverse action disclosure is to allow an employee or applicant to explain, challenge, or correct information contained in the consumer report.

Employers are not required to provide the pre-adverse action disclosure if information from the consumer report did not play any role in the employment or business decision at issue. However, information in the consumer report need not be negative to trigger the pre-adverse action disclosure. For instance, an employer looking to hire a CFO may obtain a consumer report that shows that the applicant has a very limited credit and employment history. There is nothing inherently negative about that information, but if the employer wants a CFO with more experience and is relying on the consumer report to reject the applicant, the FCRA requires the provision of the pre-adverse action disclosure.

Once the decision is made to take an adverse action against the employee or applicant, the employer must then provide an adverse action notice. This notice is very similar to the pre-adverse action notice and may be oral, written, or electronic. For preservation and liability purposes, an employer should provide written or electronic notice. The notice must include the name, address, and phone number of the company supplying the report (*i.e.,* the consumer reporting agency, such as one of the three major credit bureaus), a statement that the company did not make the decision and can't give reason for it, and a notice of the employee or applicant's right to dispute the accuracy of the information and get an additional free report if requested within 60 days.

Because the FCRA does not provide a time frame, a question that often arises is how long an employer must wait after the pre-adverse action notice to provide the adverse action notice. A minimum waiting period can be derived from opinion letters issued by the Federal Trade Commission (FTC) and Congress's legislative history. In keeping with the FCRA's purpose to allow an employee or applicant to review and explain or correct any potential errors, omissions, or confusion in the reports, employers should generally allow at least five (5) business days between the pre-adverse action notice and the adverse action notice. This is not a hard and fast rule; some circumstances may call for a longer period of time. Depending on the job position at issue, the applicant or employee's other qualifications, and how much of a factor the consumer report was in the decision to take an adverse action, an employer may want to meet with the employee or applicant to provide a set period of time to correct or explain any issues before an adverse action becomes final.

> Failure to comply with the FCRA can result in significant consequences to the employer

Failure to comply with the FCRA can result in significant consequences to the employer. These include civil liability for willful noncompliance or negligent noncompliance, criminal fines or imprisonment for willfully obtaining a consumer report under false pretenses, and other administrative penalties. In addition, while the employer may be subject to some of these penalties, an individual who obtains a consumer report under false pretenses (*e.g.,* a firm principal in charge of hiring or an HR manager) may be personally liable for actual damages suffered by the applicant or employee. The employer or individual may also be required to pay any costs or attorney's fees incurred by an applicant or employee who successfully brings suit for violation of the FCRA. In the case of an applicant who is rejected for a job, significant damages can occur, such as lost wages.

### State laws

The FCRA is the overarching statutory scheme that employers need to comply with. At least 23 states, however, also have laws that control the use of background checks, including credit or consumer reports. Employers must also make sure that they are complying with these state laws, as they may differ from the FCRA.

The state of Maryland, for example, specifically restricts employers from using an applicant or employee's credit report or history in denying employment, discharging an employee, or determining compensation, terms, conditions, or privileges of employment. The only exceptions to these restrictions are if the applicant has received an offer of employment and the report will not be used to determine the terms, conditions, or privileges of employment, or the employer has a *bona fide* purpose for requesting the report that is substantially job related and disclosed in writing to the applicant/employee. Maryland further defines "substantially job related" to include positions that involve managerial or decision-making powers, access to personal information, fiduciary responsibilities, access to expense accounts or corporate credit cards, or access to privileged or confidential business information.

Along similar lines, in 2011 and 2012, bills were proposed in the District of Columbia that would prohibit: (1) the use of consumer credit checks against prospective and current employees for the purpose of making adverse employment decisions; and (2) employers from considering an applicant or employee's arrest or conviction record unless it was directly relevant to the job sought. The proposed bill on the use of arrest or conviction records failed, but the bill on the use of consumer credit checks remains pending. Other states have other, more burdensome restrictions. For example, Hawaii mandates a conditional offer of employment to be made before an applicant's credit history can be considered, and Illinois requires an employer to meet one of seven factors before a satisfactory credit history can be used as a job requirement.

In summary, employers should comply with the FCRA and make sure that they do not have additional requirements under state law.

### Use of criminal background checks

Criminal background checks are often subject to the same statutes and regulations just discussed. If an employer obtains the criminal background check or history through a consumer reporting agency, then the FCRA will apply. This is because criminal history and other background information (*e.g.,* education and employment verification) touch upon an individual's "character, general reputation, personal characteristics, or mode of living."

It is also important to note that employers who improperly or impermissibly use criminal histories to make employment decisions may find themselves facing lawsuits alleging discrimination in violation of Title VII of the Civil Rights Act of 1964. The EEOC has for the last 40 years issued decisions and guidance related to the use of criminal background checks and histories for employment purposes.

The EEOC is particularly concerned that the use of criminal background checks will have a disparate effect on certain protected classes. In its most recent guidance, issued in April 2012, the EEOC specifically pointed out that arrest and incarceration rates are particularly high for African American and Hispanic men. This means that if employers adopt a blanket policy of using criminal background checks, these groups are more likely to be screened out of employment than others.

The EEOC strongly advises that employers not use blanket policies against convictions for criminal offenses. It further distinguishes between arrest records and conviction records, and states that arrest records alone may not be used to deny employment. Under the EEOC guidance, employers can still make employment decisions based on the conduct underlying the arrest. Several states, however, ban inquiry into arrest records for purposes of employment.

To comply with the EEOC's guidance and help reduce the risk of suit or liability, employers should apply a three-factor test plus an individualized assessment of the applicant or employee's situation. The three factors, designed to help determine the relevance of a criminal conviction to a particular employment position, are as follows:

1. the nature or gravity of the offense or conduct;
2. the time elapsed since the conviction and/or the completion of the sentence; and
3. the nature of the job sought or held.

So, for example, a 10-year-old conviction for felony DUI is not likely relevant to the position of grocery bagger. Yet, an 18-month-old conviction for embezzlement and tax evasion is most likely relevant to a position, such as accounting manager, payroll supervisor, or even a lower position with access to company financial information or resources.

After considering the three factors and before making any decision based on criminal history, the employer needs to perform an individualized assessment with the applicant or employee. This entails informing the individual that he or she may be excluded because of past criminal conduct and also providing an opportunity for the individual to demonstrate that the exclusion does not properly apply to him or her. The employer should then consider the individual's additional information and determine if the conviction is related to the position sought, actually informs the employment decision, and whether that decision is consistent with business necessity.

As with credit histories, many states have laws that restrict the use of criminal histories in employment decisions. For example, in Maryland, employers cannot require the disclosure of criminal charges that have been expunged. Likewise in Virginia, employers are prohibited from requiring

employees or applicants to disclose criminal charges that did not result in a conviction or arrests that have been expunged.

Even though some states or municipalities have laws that require criminal background checks for certain positions, the EEOC's stance is that compliance with these laws will not automatically protect against liability under Title VII. Conducting criminal background checks to comply with federal law or regulations, however, does not violate Title VII.

## Summary

In the face of all this information and the myriad of regulations—some of which is conflicting and all of which is often very fact-dependent—employers are frequently looking for a one-size-fits-all policy on the use of background checks. Unfortunately, there is no single policy that provides an employer the background information it seeks to make an employment decision and which will not run afoul of federal or state laws or guidance. There is, however, a group of actions that an employer can take to help ensure it is using background checks properly and avoiding liability for using the results of those checks.

Employers should have a written background check policy that is applied consistently to employees and applicants, but which in most circumstances is not applicable to all job categories. For example, in most companies there is no justification for conducting background checks on a receptionist. Background checks, whether credit or criminal, should only be run once an applicant field is narrowed down to the best potential applicants, or when a particular set of employees is being considered for a promotion or job reassignment. For both credit and criminal background checks, there should be no blanket exclusions.

Before making any employment decision, employers should provide employees/applicants the opportunity to discuss or refute the information, whether related to credit or criminal history, or any other relevant information contained in a consumer report. For criminal histories in particular, employers need to consider the three factors discussed above. They should also always be aware of applicable local laws and ensure that their employment policies keep up with changes in the law. Finally, if questions or concerns arise, it is always advisable to seek the advice of legal counsel before making an employment decision.

---

**About the author:** Ethan L. Don is an associate in the Employment Law and Litigation practice groups of Paley, Rothman, Goldstein, Rosenberg, Eig & Cooper, Chartered, in Bethesda, Maryland. His practice includes advising clients ranging from sole-proprietorships to FORTUNE 500 companies on a range of labor and employment issues, including discrimination and harassment, employment agreements, wage and hour compliance, reductions in force, and ADA compliance. Ethan also helps clients develop and implement employment policies and practices, such as employee handbooks, to help in the prevention of disputes and liability. He represents companies before federal and state courts as well as governmental agencies. Ethan is also actively engaged in the firm's Litigation practice, representing clients on a wide range of business-related matters. He can be reached at *EDon@paleyrothman.com* or by telephone at (301) 968-1648. The website for Paley, Rothman, Goldstein, Rosenberg, Eig & Cooper, Chartered is *www.PaleyRothman.com*. ✦