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ON BEHALF OF THE

SOCIETY FOR HUMAN RESOURCE MANAGEMENT

PRESENTED TO THE

U.S. HOUSE FINANCIAL SERVICES SUBCOMMITTEE ON

FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

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## **Introduction**

Chairman Gutierrez, Ranking Member Hensarling, and distinguished members of the Subcommittee, my name is Colleen Denston. I am Director of Human Resources at Worcester Preparatory School in Berlin, Maryland, and a member of the Society for Human Resource Management (SHRM). I thank you for the opportunity to appear before the Subcommittee today to discuss the use of credit background checks in employment and H.R. 3149, the "Equal Employment for All Act."

The Society for Human Resource Management is the world's largest association devoted to human resource management. Representing more than 250,000 members in over 140 countries, the Society serves the needs of HR professionals and advances the interests of the HR profession. Founded in 1948, SHRM has more than 575 affiliated chapters within the United States and subsidiary offices in China and India.

SHRM has been monitoring the intensifying debate on both the national and state levels regarding legislation that would restrict an employer's ability to access and consider the credit history of applicants and current employees in the employment process.

To be clear, we believe that employment decisions should be made on the basis of an individual's qualifications – such as education, training, professional experience, demonstrated competence, reliability, integrity – and not on factors that have no bearing on one's ability to perform job-related duties. Furthermore, SHRM and its members fully appreciate that our nation's high unemployment rate, foreclosure rate and the overall health of the economy have had a severe impact on countless individuals' credit history. Therefore, this issue has heightened relevance right now.

However, SHRM believes there is a compelling public interest in enabling our nation's employers to assess the skills, abilities, work habits, and integrity of potential hires. Further, SHRM believes the ability to obtain reliable and accurate job performance information about prospective employees has a direct impact on critical business concerns such as quality, workplace safety and customer satisfaction. SHRM also believes that a job applicant has a right to know that he/she has been denied credit or a job as a result of a third-party report, as per current law under the Fair Credit Reporting Act of 1970 (FCRA).

In my statement today, I will explain what background information employers currently seek, present the problem of occupational theft and fraud and its relevance to today's hearing, review results of SHRM research on employment background screening; and outline our concerns regarding legislation, H.R. 3149, pending before the Subcommittee.

## **The Use of Background Information in Employment**

At private and public organizations, large and small, HR professionals are charged with ensuring that each individual hired possesses the knowledge, skills and abilities needed for the organization's success. The consequences of making a poor hiring choice can be great, possibly leading to financial losses or an unsafe work environment. Also, if the employee engages in severe misconduct, customers, shareholders or other employees may incur legal liability in the form of negligent hiring, negligent retention, vicarious liability lawsuits or

other legal claims. As a result, HR professionals strive to make the most informed choices possible when selecting candidates for their organizations.

Once a group of candidates or a finalist is selected for a position, the HR department may conduct a background check on the candidates or candidate. In addition, some states statutorily require employers to conduct specific background checks for certain positions such as licensed health care professionals, day care providers, teachers and athletic coaches, and police officers and firefighters.

While the background check process is often a standard practice for most employers, the process varies, depending on the employer and the position in question. The process may include checking previous work history, personal references, education, professional credentials, motor vehicle history, criminal history and credit history. In addition, employers may place a different emphasis on each element of the process. For example, some employers put a great deal of importance on a steady work history, personal references, and credit history. Others value education and work history above all else.

Furthermore, many employers are compliant with Payment Card Industry Data Security Standards (PCI DSS), otherwise known as PCI Compliance. PCI Compliance is a complex set of network security and business practice guidelines adopted by Visa, MasterCard, American Express, Discover Card, and JCB to establish a “minimum security standard” to protect customers’ credit card information. In short, all businesses that accept, handle, store, or process consumer credit card data must be PCI Compliant. The PCI DSS requires employers complete a background check on certain employees who handle credit card information or have access to software code that process credit card information. PCI Compliance is not strictly based on federal law, but is an industry standard designed to facilitate the broad adoption of consistent data measures on a global basis.

A major problem of the current process is that employers are reluctant to provide an accurate assessment of a former employee’s work history, strengths, and weaknesses. They fear that an unabridged assessment of a candidate’s work background—whether good or bad—could expose them to liability in claims made by the candidate (in the form of a defamation or retaliation lawsuit) or the potential employer (negligent referral) . As a result, most employers provide only the minimum in a reference check – “name, rank, and serial number.” They confirm that the candidate had worked for them, his or her title, and dates of employment.

This lack of direct, complete reference information forces many employers to seek additional information about the candidate that can be legally obtained through the use of third-party background check companies. Employers may employ the services of such companies to obtain the most accurate picture of a potential employee’s work history, personal references, education and professional credentials, criminal history and credit history. Under the FCRA, an employer that uses a third-party provider or Consumer Reporting Agency (CRA) in the background process must notify the potential employee in advance, and it must obtain the applicant’s approval to have his or her background checked by the provider.

*Before* taking any adverse action based on a background report, such as deciding to not hire an individual, an employer is first required to give the applicant a pre-adverse action notice. That notice must include:

- (1) a copy of the background report; and
- (2) a copy of “A Summary of Your Rights Under the Fair Credit Reporting Act” — a document prescribed by the Federal Trade Commission (FTC).

The individual must then be given a “reasonable” period of time to contact the employer if any of the information in the report is incorrect. This protects an individual from losing an employment opportunity due to incorrect information, such as a transposed Social Security number, or an incorrectly reported date of birth, resulting in “bad” credit information being reported about the wrong individual. It is only after that “reasonable” period that the employer may decide to not hire the individual. In that instance, the employer must provide the candidate with an Adverse Action notice that includes:

- (1) the name, address, and phone number of the CRA that supplied the report;
- (2) a declaration that the CRA 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 report from the agency upon request within 60 days.

As explained earlier, credit histories are but just piece of the puzzle used by HR professionals in evaluating job candidates. Credit history information can not only be useful in determining whether a candidate has the skills and responsibility necessary for a particular job, but also whether the individual is qualified to handle money. A stellar credit history may provide evidence of and responsibility, while a poor credit history may reflect irresponsibility or carelessness.

### **The Problem of Occupational Theft and Fraud in the Workplace**

While employee advocates make strong arguments in the credit-check debate, we believe arguments by employers are also compelling. At a time when financial pressures on households are increasing, employee theft is on the rise. The result is a major financial problem for companies. The National Retail Security Survey estimates that the U.S. retail industry lost about \$14.4 billion in 2009 due to employee theft.<sup>1</sup> These data show why employers are using every type of screening method they can to avoid making poor hiring decisions.

According to the Association of Certified Fraud Examiners’ 2010 Report to the Nation on Occupational Fraud and Abuse, financial pressures are one of the “key motivating factors” behind check tampering, theft, and fraudulent reimbursement schemes by employees, who are usually first-time offenders. The study found that “living beyond financial means” (43

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<sup>1</sup> National Retail Security Survey (2010). National Retail Federation and the University of Florida.

percent of cases) and “experiencing financial difficulties” (36 percent) were the two most common warning signs displayed by perpetrators of workplace fraud.<sup>2</sup> A previous report by the association, in 2008, concluded, “Given that financial difficulties are often associated with fraudulent behavior, it would seem advisable for organizations to devote more efforts to conducting credit background checks on new applicants.”

### **SHRM Research on the Use of Credit Checks in Hiring**

Recent media reports have implied that *nearly all* employers run credit checks on *nearly all* job applicants, and then use the results to deny employment regardless of the position sought. Many of these publications have even used SHRM data to support this interpretation. In the current economic climate, such stories are particularly compelling. But they also give the public a misleading description of the use of credit reports during the hiring process.

In order to provide a more complete picture of the background check process, SHRM in January 2010, and followed up in a subsequent report in August 2010, released one of the most complete set of data employer background screening practices ever conducted. The resulting report included data from large employers (500 or more workers), medium-sized employers (100-499 employees), and small employers (1-99 employees) from both the public and private sectors.

Here were the survey’s key findings:

- **Credit checks on all job candidates is the exception—not the rule.** Only 13 percent of organizations conduct credit checks on all job candidates. While another 47 percent of employers consider credit history, they do so only for candidates for select jobs. Those findings are little changed from SHRM’s last survey in 2004, when 19 percent of respondents said they “always” check the credit history of job candidates and a combined 42 percent do so “sometimes” or “rarely.”
- **Many organizations do not conduct credit checks at all.** Four out of 10 organizations revealed that they do not conduct credit checks at all.
- **Employers generally conduct credit checks only for certain positions.** Those positions include ones with financial or fiduciary responsibilities, senior executive positions, and ones with access to highly confidential employee information. In other words, HR professionals use credit checks when this information is most job-relevant.
- **Credit history is not among the most important factors in making a hiring decision.** Credit checks ranked the *lowest* among a list of criteria employers typically use in making hiring decisions. In fact, only 9 percent of organizations reported that favorable credit checks were among the most influential factors in their hiring decisions.
- **Employers overwhelmingly use credit checks at the end of the hiring process, not to screen out applicants.** At least 87 percent of organizations initiate credit checks only after a contingent offer (57 percent) or after the job interview (30

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<sup>2</sup> Report to the Nations on Occupational Fraud and Abuse (2010). Association of Certified Fraud Examiners.

percent). This finding substantiates other data showing that organizations place relatively more importance on other job-relevant factors in making hiring decisions.

- **Employers regularly go beyond current law requirements and allow candidates to explain their credit history.** The survey showed that 87 percent of organizations allow job candidates, in certain circumstances, the opportunity to explain results of their credit report.<sup>3</sup> Employers are not required by the FCRA to provide individuals such an opportunity.

### **Concerns with Federal Legislation**

Today's hearing is focused on legislation introduced in the U.S. House of Representatives to amend the FCRA. Entitled the "Equal Employment for All Act (H.R. 3149)," the bill would prohibit the use of credit checks on prospective and current employees for employment purposes. H.R. 3149 would not apply to job applicants subject to a national security clearance, people applying for public-sector positions that require a credit check, or candidates for supervisory or managerial positions at financial institutions.

These exceptions appear to concede that credit history is indeed relevant for positions in which a professional is required to manage sensitive information, including financial and security information. But there are many more positions in myriad industries where ensuring employee integrity is in the public interest. Such positions include those with responsibility for managing money, property, personal identity or financial information, and other critical resources. For example:

- Managerial positions at institutions of higher education that manage significant endowments, including taxpayer-funded federal and state grants and appropriations
- Real estate professionals that process financial transactions
- Nearly all positions in airline companies, from customer service representatives to maintenance workers, that provide access to financial or security-related information
- Private security professionals that have access to sensitive physical security information for public facilities
- Human resource positions that have access to Social Security numbers, bank account numbers, and other personal information
- Positions at all organizations that process or store consumer credit card data and must be PCI Compliant

Under current federal law, employees already enjoy significant protections from unauthorized uses of credit checks. First, as noted above, the FCRA requires that an employer give a job applicant advance notice and secure the applicant's signed consent before a credit check can be performed. If an applicant is not hired in part because of a credit report, the employer must also inform the applicant of the decision, plus provide a copy of the report and a statement of the individual's rights under the FCRA.

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<sup>3</sup> Conducting Credit Background Checks (2010). Society for Human Resource Management.

A second statute, Title VII of the Civil Rights Act of 1964, prohibits employment discrimination based on race, color, religion, sex, or national origin. It bars employment decisions based on policies, tests, or standards, such as credit checks, that have a “disparate impact” on protected groups, unless those policies, tests or standards are job-related and consistent with business necessity. Disparate impact refers to any test or system that appears to be neutral, but results in a disproportionate impact on specific groups of people protected by the equal employment opportunity laws.

In cases of disparate treatment, employees or applicants must show that intentional discriminatory practices took place. In response, an employer must show a legitimate reason for the practice.

Thus, employers are already barred from using credit background checks to screen out applicants from protected classes. Subsequently, H.R. 3149 would be redundant federal policy.

### **Conclusion**

For all these reasons, SHRM continues to have significant concerns with H.R. 3149, the “Equal Employment for All Act.” Given current economic pressures, SHRM and its members understand the heightened relevance of the issue of credit history and employment. SHRM believes there is a compelling public interest in ensuring that employers can assess the skills, abilities, work habits, and integrity of potential hires. HR professionals, whether working in the public or private sector, need a consistent set of rules to follow in obtaining background information about applicants during the hiring process.

Those professionals commend the Subcommittee’s efforts to balance the needs of both the management and employees of a company. SHRM believes that employees already enjoy significant federal protections from misuse of credit background reviews. The Fair Credit Reporting Act of 1970 requires employers to secure written permission from applicants and employees before conducting a credit check, and to inform applicants if an adverse employment decision was based on a credit-related issue. In addition, employers are barred by the Civil Rights Act of 1964 from using background checks to screen out protected job applicants.

SHRM’s research reveals that only a small minority of organizations conduct credit checks on all job candidates, and organizations generally conduct credit checks only for certain positions with responsibilities that affect other employees and consumers. Credit check results are rarely a very influential hiring criterion, but rather one small component of the overall consideration of a job candidate. Overwhelmingly, employers review credit history of applicants only after an interview, not to screen out applicants early in the hiring process. What’s more, even in the downtrodden economy of recent years, the use of credit background checks in employment decisions has not increased.

Thank you for your invitation to participate in today’s hearing.