

Employee Solvency

Credit-based employment decisions: the next wave in the subprime tsunami

The current subprime crisis was caused by fundamental human and institutional deficits: greed, irresponsibility, non-existent internal controls, selective and non-existent enforcement of existing laws, exotic and lucrative secondary markets and relentless market optimism in the face of cyclical history. While the causes are all too familiar, at least one unintended consequence is the heightened scrutiny of personal credit history in employment decisions.

As employers assess qualifications and competence of not just applicants, but existing employees, credit histories increasingly are perceived as an “objective” measure of personal responsibility and performance. But is there a valid correlation between credit history and job performance? And, even if there is, what are the risks within the workplace of pulling credit history to assess job performance?

More than 25% of U.S. companies use credit checks when considering job candidates — a 55%-increase over the past five years. This practice was initially common primarily within the financial sector, but these days, all industries are performing the checks. Over the coming months, less-than-perfect credit history will progressively cut into job offers for prospects, and will limit current employees’ prospects for promotions. Recent surveys show many employers believe a heavy debt burden may be the result of or lead to criminal behavior, including theft, drugs, prostitution or violence. In fact, there is significant evidence that this perception may not be supported by facts. Take, for example, the insurance industry, which has used credit history to underwrite insurance risks for more than a decade. In May 2003, the Center for Economic Justice stated that the perceived relationship between credit scoring and expected insurance losses was “neither credible nor reliable.”



EMPLOYMENT LAW

John T. Palter

Accurate or not, though, credit reports are perceived as “neutral” measures of employee integrity and performance. And, indeed, employers are authorized to use the information under limited circumstances. Under the Federal Fair Credit Reporting Act, employers have the right to review the credit history of job applicants, as long as they obtain a prior signed release.

As employers move to gather employees’ credit data, it’s important to note the difference between a credit report and a credit score. A credit report comprises raw credit data, providing a detailed history of payments, liabilities and total debts and financial obligations. A credit score is a three-digit number that uses historic credit performance to assess future credit risk. In fact, credit scores are not considered suitable for employment screening, which is why reporting bureaus offer reports without credit scores or account identifiers specifically for employers.

When it comes to hiring, companies should approach the use of credit reports with strong caution. First, many applicants perceive credit checks as a violation of privacy, legal or not. Unnecessary credit reports discourage otherwise qualified applicants from applying, and create a subtle sense of paranoia with existing employees that may result in a loss of productivity and work force stability.

Second, a negative credit entry could be due to something that is not job-related, such as a contested debt, identity theft, divorce or family medical bills. More important, the use of credit reports may crack open the floodgates of discrimination-based claims if negative employment decisions have a disparate

ON-THE-JOB CREDIT REPORTS: BEST PRACTICE TIPS

FOR EMPLOYERS:

- Secure a signed release before requesting credit history.
- Use credit reports only to make sound business decisions.
- Apply objective criteria when reviewing credit information.
- Implement appropriate company policy based on employee level.
- Maintain the confidentiality of all credit information obtained.

FOR EMPLOYEES:

- Review your credit report regularly — at least once a year.
- Correct all inaccurate or incomplete information.
- Notify all three credit bureaus of the corrections.

impact on members of protected classes. Finally, as credit information becomes relevant in the workplace, litigation against credit bureaus for inaccurate information and against employers for relying on such data almost certainly will increase.

As a result, employers should enact policies and procedures that ensure credit information is used for and limited to relevant business purposes. Is there a sound business reason to obtain a credit report? Does it make sense to run a credit report for an entry-level person with low levels of responsibility or no access to cash?

Companies should consistently apply objective standards across the same employee responsibility levels, and take pains to rely only upon current information and “big ticket” credit factors. Most important, credit data should be kept strictly confidential.

For their side, employees have a vested interest in verifying and protecting their accurate credit history and score. If an error is discovered, it should be corrected, and employees should be sure to notify all three bureaus and request the change.