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## FTC Issues Final Rules Clarifying Fair Credit Reporting Act Requirements (2006)

Richard Stokes

*Municipal Technical Advisory Service*

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# MTAS Municipal Technical Advisory Service

*In cooperation with the  
Tennessee Municipal League*

#122

HOT  
topic

January 18, 2006

## FTC ISSUES FINAL RULES CLARIFYING FAIR CREDIT REPORTING ACT REQUIREMENTS Richard L. Stokes, PHR, IPMA-CP, Human Resources Consultant

Provisions of the Fair Credit Reporting Act (FCRA) (15 U.S.C. § 1681 *et seq.*), which is the federal law governing consumer information, have been amended by the Consumer Reporting Employment Clarification Act (CRECA) of 1998 (Pub. L. No. 105-347) and the Fair and Accurate Credit Transaction Act (FACTA) of 2003 (Pub. L. No. 108-159). Specifically, the FCRA requires employers who use outside agencies to perform credit or other background checks (including criminal, reference, or driving record checks), as defined by CRECA, to comply with comprehensive notice, consent, and disclosure obligations both prior to doing the checks and after the results are reported. The provisions of FCRA, CRECA and FACTA directly affect those cities that use outside agencies to secure information about applicants and employees.

The rules apply to anyone over whom the Federal Trade Commission (FTC) has jurisdiction and who maintains or possesses consumer information for business purposes. It applies to individuals and to both large and small organizations that use consumer reports, including consumer reporting companies, lenders, insurers, employers, landlords, government agencies, mortgage

brokers, car dealers, attorneys, private investigators, debt collectors, individuals who pull consumer reports on prospective at-home employees, and entities that maintain information in consumer reports as part of their role as a service provider to other organizations covered by the rule.

According to the act, the definition of a consumer report includes any written, oral, or other communication of any information by a consumer reporting agency regarding a consumer's reputation, personal characteristics or mode of living that is used as a factor to establish the consumer's eligibility for employment. Consumer information is defined as any record about an individual that is a consumer report or is derived from a consumer report. However, according to the FACTA amendment, a consumer report does not include communications made to an employer while investigating suspected employee misconduct relating to employment or employee compliance with applicable laws or with pre-existing written policies of the employer.

Generally, a city that accesses a consumer report while conducting a background check on an applicant has two main obligations: (1) to comply with disclosure requirements

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and inform the applicant in a separate document that a consumer report may be secured for employment purposes and (2) to obtain authorization in written form from the applicant to request the consumer report. The city must certify to the consumer reporting agency that it has satisfied these disclosure and consent requirements as a condition of receiving the consumer report.

An investigative consumer report, which is viewed as a much more intrusive inquiry and which contains information collected from personal interviews with neighbors, friends, or associates of the consumer, requires additional obligations. If a city wants to use an investigative consumer report, it must disclose to the applicant that the investigative consumer report may be obtained and generally must secure written authorization to acquire the report. A city that requests an investigative report must inform the employee or applicant that he or she has a right to request additional disclosures of the nature and scope of the investigation and provide the current or prospective employee with a summary of the consumer's rights.

If the city decides to reject the applicant based in whole or in part on a consumer report or investigative consumer report, the city must provide the applicant with a copy of the report and the summary of rights before taking such action. After taking adverse action, the city must also provide notice to the applicant or employee of the adverse action, provide the name, address

and telephone number of the consumer reporting agency that furnished the consumer report on which the adverse action was based, and notify the applicant or employee of the right to obtain the consumer reporting agency report.

FACTA requires that any person who maintains or possesses "consumer information" must be prepared to dispose of those records in a way that ensures that the information will not be accessed or used improperly. It addresses only the disposal of consumer information, not all employment information. It also does not address retention schedules or how records should be kept or maintained. This requirement is intended to protect consumer privacy and to prevent identity theft.

A consumer report is covered, however, if it is in paper, electronic, or other forms. If a city acquires consumer information, the city must take "reasonable measures" to protect against unauthorized access to or use of the information "when" the city disposes of it. Reasonable measures for disposing of consumer report information could include establishing and complying with policies to

- Burn, pulverize, or shred papers containing consumer report information so that the information cannot be read or reconstructed;
- Destroy or erase electronic files or media containing consumer report information so that the information cannot be read or reconstructed; and

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- Conduct due diligence, and hire a document destruction contractor to dispose of material specifically identified as consumer report information consistent with the rule.

Due diligence includes

- Reviewing an independent audit of a disposal company's operations and/or its compliance with the rule;
- Obtaining information about the disposal company from several references;
- Requiring that the disposal company be certified by a recognized trade association; and
- Reviewing and evaluating the disposal company's security policies or procedures.

The rules further define "dispose," "disposing" and "disposal" to mean the discarding or abandonment of the consumer information or the sale, donation, or transfer of any medium (such as computer equipment) that stores the information.

Employers who fail to comply with the rules are subject to FTC fines and penalties, which can be substantial if a large number of files are involved. In the event of a knowing violation, the individual/company is liable for a civil penalty of not more than \$2,500 per violation. Additionally, if the state has reason to believe that any person has violated the act, it may bring action to enjoin such violation in any appropriate United States district court and fine such person damages of not more than \$1,000 for each willful

or negligent violation. In the case of any successful action, the individual/company will have to pay for the cost of the action and reasonable attorney fees as determined by the court.

New model notices are now available and can be found in the November 30, 2004, "Federal Register." The new notices, effective last January 31, 2005, contain the following modifications:

- The User Notice has a new section titled "Special Procedures for Employee Investigations" that expressly states that covered investigations of "suspected misconduct" by employees or "for compliance" by employees with applicable laws or the written policies of the employer are not treated as consumer reports, so long as certain conditions are met;
- When consumers have placed a fraud (identity theft) alert or military alert with a consumer reporting agency, the User Notice provides that "users" must have reasonable policies in place to confirm the identity of the consumer (as a check against identity theft)
- The Summary of Rights adds a new disclosure regarding consumer rights to access credit scores; and
- The Summary of Rights has expanded information on consumer access to files maintained by the consumer reporting agency and free file disclosure in the event of adverse action or identity theft.

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Sample notice forms are available on the FTC Web site at [www.ftc.gov/credit](http://www.ftc.gov/credit). For more information about the FCRA or the FACTA, contact Richard L. Stokes, municipal human resources consultant, directly at (615) 532-6827 or via e-mail at [richard.stokes@tennessee.edu](mailto:richard.stokes@tennessee.edu). You also may contact your MTAS municipal management consultant in Knoxville, Johnson City, Nashville, or Jackson.

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