The Impact of the FACT Act on Employee Misconduct Investigations and Implications for FCRA and Title VII Compliance

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I. Introduction

On December 4, 2003, President George W. Bush signed the Fair and Accurate Credit Transactions Act of 2003 (FACT).[1] The final bill[2] amends the federal Fair Credit Reporting Act (FCRA)[3] in response to, among other things, the controversial *Vail* opinion letter from the Federal Trade Commission (FTC).[4] The *Vail* letter memorialized the FTC's novel opinion that the FCRA applied to workplace harassment investigations conducted by third parties such as private investigators.[5] Although Title VI of the FACT nullifies the *Vail* letter by excluding certain employee misconduct investigations from the FCRA, employers must adhere to strict procedures to keep the communications at issue within the "safe harbor" protection afforded for misconduct investigations. In addition, in conducting harassment or discrimination investigations, employers must carefully balance the accused's privacy rights under the FCRA with the complainant's right to learn the investigation results under Title VII of the Civil Rights Act of 1964.[6]

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1. Fair and Accurate Credit Transactions Act of 2003, Pub. L. No. 108–159, 117 Stat. 1952 (codified in scattered subsections of 15 U.S.C. § 1681).

2. H.R. 2622, 108th Cong. (2003).

3. 15 U.S.C.S. §§ 1681–81x (2004).

4. Letter from Christopher W. Keller, Attorney, Federal Trade Commission, to Judi Vail (Apr. 5, 1999), *at* http:www.ftc.gov/os/statutes/fcra/vail.htm (last visited Jan. 21, 2004) [hereinafter the *Vail* letter].

5. *Id.* For a further discussion of FCRA procedures in the employment context and court decisions regarding the *Vail* letter, *see* Teresa Butler Stivarius, *An Update on the FTC's* Vail *Letter and Application of the FCRA to Investigations of Employee Wrongdoing,* 19 LAB. LAW. 83 (2003).

6. 42 U.S.C. §§ 2000e to e-17 (2000 & Supp. I 2001) (Title VII).

II. Brief History of the FACT

In 1999, Rep. Peter Sessions (R-Tex.) first sponsored a bill exempting certain employee misconduct investigations from the purview of the FCRA.[7] That bill was known as the Fair Credit Reporting Amendments Act of 1999.[8] Later, on May 3, 2000, Rep. Janice D. Schakowsky (D-Ill.) introduced a bill to create a narrower "safe harbor" protection for disclosure of investigative reports involving employee misconduct.[9]

In April 2001, Reps. Sessions and Sheila Jackson Lee (D-Tex.) introduced the Civil Rights and Employee Investigation Clarification Act.[10] In July 2003, the House Financial Services Committee approved H.R. 2622, which incorporated H.R. 1543, by a 61–3 vote.[11] Numerous amendments were voted down or withdrawn, including one allowing the accused to demand a reinvestigation.[12] The Senate passed its own version of the legislation,[13] but committee members reconciled the two bills.[14] The House approved the conference report on November 21 by a 379–49 vote,[15] the Senate gave unanimous approval the next day.[16] The final version of the legislation was signed by President Bush on December 4, 2003.[17]

III. Effective Date of Title VI of the FACT

Congress has charged the FTC and the Board of Governors of the Federal Reserve System with implementing regulations setting effective dates for those sections of the FACT that do not specify an effective date, including Title VI.[18] Pursuant to joint final rulemaking by the agencies, March 12, 2004, was set as the effective date for Title VI of the FACT.[19]

IV. What Title VI of the FACT Means for Employers

A. *The FACT Nullifies the* Vail *Letter*

The FCRA generally prohibits "consumer-reporting agencies" from furnishing "consumer reports" to employers for "employment purposes," unless the advance consent and disclosure requirements of the

7. H.R. 3408, 106th Cong. (1999).
8. *See id.*
9. H.R. 4373, 106th Cong. (2000).
10. H.R. 1543, 107th Cong. (2001).
11. 149 CONG. REC. H8122 (daily ed. Sept. 10, 2003).
12. *Id.*
13. S. 1753, 108th Cong. (2003).
14. *See* 149 CONG. REC. S15,570 (daily ed. Nov. 22, 2003).
15. 149 CONG. REC. H12,247 (daily ed. Nov. 21, 2003).
16. 149 CONG. REC. S15,570 (daily ed. Nov. 22, 2003).
17. Pub. L. No. 108–159, 117 Stat. 1952.
18. P.L. 108–159, 117 Stat. 1953.
19. Effective Dates for the Fair and Accurate Credit Transactions Act of 2003, 69 Fed. Reg. 6526 (Feb. 11, 2004), codified at 12 C.F.R. pt. 222 and 16 C.F.R. pt. 602.

Act are met.[20] The FCRA defines "employment purposes" to include "evaluating a consumer for employment, promotion, reassignment or retention as an employee."[21] Generally, the "consumer" (*i.e.*, the employee) must be notified of and consent to disclosure of the report and be furnished with a copy of the report if it results in an "adverse" personnel action (*e.g.*, discipline, demotion, termination, etc.).[22] Consumer-reporting agencies include background check vendors and credit-reporting agencies, and in some circumstances, private investigators and even law firms.[23] Consumer reports are broadly defined to include "any written, oral, or other communication of any information by a consumer-reporting agency bearing on a consumer's . . . character, general reputation, personal characteristics, or mode of living . . ."[24] "Investigative consumer reports" are a subset of consumer reports that trigger additional notices to the consumer.[25] Investigative consumer reports are reports in which protected information is obtained "through personal interviews with neighbors, friends, or associates . . . or others with whom [the consumer] is acquainted . . ."[26]

The *Vail* letter, written by FTC staff attorney Christopher Keller, expressed the novel view that third-party investigators hired by employers to conduct investigations into complaints of unlawful harassment are "consumer-reporting agencies" and that reports prepared by such investigators are "most likely 'investigative consumer reports.'"[27] By issuing the *Vail* letter, the FTC took the position that whenever an investigation into unlawful harassment in the workplace was conducted by a third party, the employer was required to comply with the advance notice and consent requirements imposed by the FCRA.[28]

Title VI of the FACT obviates the *Vail* letter by excluding from the definition of "consumer reports" certain communications relating to

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20. 15 U.S.C. §§ 1681b(b) and 1681a(d)(1)(B) (2000).
21. *See id.* § 1681a(h).
22. *See id.* §§ 1681b(b) and 1681a(d)(1)(B).
23. *See, e.g.*, Phillips v. Grendahl, 312 F.3d 357, 370 (8th Cir. 2002) (private investigator); Duncan v. Handmaker, 149 F.3d 424, 429 (6th Cir. 1998) (law firm liable for violating FCRA); Auriemma v. Montgomery, 860 F.2d 273, 280 (7th Cir. 1988) (law firm potentially liable for FCRA violation).
24. 15 U.S.C. § 1681a(d) (2000).
25. *See id.* § 1681a(e).
26. *See id.*
27. *Vail* letter, *supra* note 4.
28. *Id. See also* Letter from David Medine, Associate Director, Division of Financial Practices, Federal Trade Commission, to Susan R. Meisinger (Aug. 31, 1999), *available at* http:www.ftc.gov/os/statutes/fcra/meisinger.htm (last visited Jan. 26, 2004) (expressing FTC's opinion that FCRA applies to *all* workplace misconduct investigations by third parties, not just those relating to complaints of harassment), and Letter from Robert Pitofsky, Chairman, Federal Trade Commission, to the Hon. Pete Sessions (Mar. 31, 2000), *available at* http:www.ftc.gov/os/2000/03/sessionletterrehr3408.htm (last visited Jan. 26, 2004) (requesting that Congress not amend FCRA to exempt workplace investigations from all requirements of the Act).

investigations of employee misconduct and investigations into "compliance with Federal, State, or local laws and regulations, the rules of a self-regulatory organization, or any preexisting written policies of the employer."[29] Consequently, employers who engage third parties to investigate employee misconduct arguably no longer have to (1) notify the accused of the investigation in advance of the investigation; (2) seek consent from the accused; (3) provide the accused with a copy of the investigation report; or (4) wait a "reasonable" amount of time between giving the accused a copy of the report and taking adverse action (provided that the investigation otherwise meets the requirements of the FACT). Eliminating the requirements that employers notify and seek advance consent from the accused helps minimize the risk the accused will alter or destroy evidence, intimidate or influence witnesses, or otherwise impair the reliability of the investigation. Moreover, eliminating the requirement that employers provide a complete report to the accused helps minimize the risk that witnesses will refuse to participate in the investigation for fear of retribution, particularly where the accused is a supervisory employee.

Under the FACT, if adverse action is taken against the accused based at least in part upon a report that would otherwise be a consumer or investigative consumer report, the accused is entitled to a "summary" of the "nature and substance" of the report.[30] Title VI does not prescribe the amount of information that must be disclosed, but permits exclusion of "the sources of the information acquired solely for use in preparing [the report] . . .", *e.g.*, the names of any witnesses.[31] Title VI leaves open whether the summary must be in writing (presumably it does), and exactly how long after the adverse action is taken the summary must be provided to the subject of the report (presumably a reasonable amount of time).

B. *Circulation of the Investigation Report Restricted*

Title VI of the FACT restricts circulation of the report to "the employer or an agent of the employer," to government agencies, and "as otherwise required by law."[32] The safe harbor protection afforded by Title VI for employee misconduct investigations may be forfeited by making overbroad or unnecessary disclosures.

Because an employee who makes the initial allegation or complaint is not the "employer" or its "agent," an important question is what information the complainant is entitled to know. The EEOC has taken the position that in harassment or discrimination investigations, the complainant is entitled to learn at least the results of the investiga-

29. 15 U.S.C.S. § 1681a(x)(1)(B)(ii) (2004).
30. *See id.* § 1681a(x)(2).
31. *See id.*
32. *See id.* § 1681(a)(x)(1)(D)(i), (ii), and (iv).

tion.[33] Likewise unclear is whether disclosures may be made to the board of directors, shareholders, or "joint employers" (for example, a temporary agency that employs the accused) without jeopardizing the safe harbor protection.

One solution may be that Title VI does not, on its face, restrict the disclosure of a *summary* of the report. Thus, narrow and business-related disclosures of summaries may be permissible and in accordance with procedures mandated by the antidiscrimination laws, such as Title VII.

C. *Foundational Requirements for Initiating Investigations under Title VI*

Under Title VI, no foundational requirements are imposed on employers for initiating investigations under FACT. For example, there is no express requirement that the employer have a "reasonable suspicion" of misconduct or that the destruction of evidence is likely to occur. Although the FTC recommended such a requirement to Congress in connection with the amendments proposed in 1999,[34] this recommendation was not incorporated into the bill.[35] Moreover, Title VI does not limit the types of "misconduct" investigations that are exempted (*e.g.*, threats of serious harm or violence, abuse of controlled substances, the loss of more than $1,000 in cash or property, etc.). Indeed, provided the investigation is being conducted pursuant to the "preexisting written policies of the employer," there is no requirement that "misconduct" be involved.[36] Likewise falling under the Title VI's safe harbor provision are investigations into "compliance with Federal, State, or local laws and regulations."[37] Title VI thus would appear to protect financial audits, information technology audits, loss prevention audits, etc. On the other hand, the FACT's text suggests at least some substantive limitations. For example, the suspected misconduct must relate to employment and the policies must predate the investigation and be in writing.[38] In addition, the scope of Title VI arguably derives from the specific objectives furthered by the legislation: eliminating the *Vail* letter as an obstacle to the use of neutral investigative resources.

Another important question regarding the scope of Title VI is whether it is limited to investigations of current employees. The legislative purpose of Title VI seems to presuppose an existing employment relationship. However, the FACT refers to "consumers," not to

33. This issue is discussed in greater detail *infra* Part V.B.

34. *See* Letter from Robert Pitofsky, *supra* note 28.

35. Although there is no express foundational requirement in the statute, misconduct investigations should never be conducted as a pretense for an improper purpose (*i.e.*, as a pretense to check an employee's credit history).

36. 16 U.S.C.S. § 1681a(x)(1)(B)(ii) (2004).

37. *See id.*

38. *See id.* § 1681(x)(1)(B)(i)–(iii).

"employees" (*e.g.*, the consumer is entitled to a summary of the investigation report).[39] Therefore, it remains to be seen whether Title VI permits investigations of former employees. Such investigations are not uncommon, especially during or in connection with litigation. For example, Able Company is sued for fraud. The board of directors hires a third party to investigate the current and former officers. On the one hand, the investigation "relates to" the current and former officers' employment. On the other hand, by speaking to "adverse action," the FACT appears to contemplate an ongoing relationship. Thus, both interpretations find support in the text and structure of the legislation.

A related question raised by Title VI is whether the safe harbor protection for misconduct investigations applies with respect to investigations of nonemployees such as independent contractors, vendors, or even customers where such investigations could impact the employment of the nonemployees. Such investigations are often required by law when an employee complains of misconduct, such as unlawful harassment, by a nonemployee.[40] If the employer conducts an investigation of a nonemployee, the safe harbor protection of Title VI may still apply if the employer has a written policy regarding harassment by nonemployees and the investigation otherwise comports with the requirements of Title VI of the FACT. In addition, if the investigation is necessary for the employer to comply with federal, state, or local law, then the investigation into nonemployee misconduct should fall within the Title VI safe harbor provision.

V. The EEOC's Position with Respect to the FCRA and Investigations of Harassment and/or Discrimination

A. *EEOC's Concern Regarding Impact of FCRA on Effective Workplace Investigations*

The EEOC has consistently taken issue with the extent to which the FCRA obstructs effective employer-initiated investigations into complaints of unlawful harassment or discrimination. On May 4, 2000, a hearing took place before the Financial Institutions and Consumer Credit Subcommittee of the House Banking and Financial Services Committee in order to address the FCRA's effect on employer investigations into employee misconduct.[41] At that meeting, then EEOC

39. *See id.* § 1681a(x).

40. For example, the California Fair Employment and Housing Act states that employers can be liable for harassment by nonemployees. CAL. GOV'T CODE § 12940(j)(1) (West Supp. 2004).

41. *H.R. 3408—The Fair Credit Reporting Amendments Act of 1999: Hearing Before the Subcomm. on Financial Inst. and Consumer Credit of the House Comm. on Banking and Financial Servs.,* 106th Cong. (2000) (statement of Ida L. Castro, Chairwoman, EEOC), *available at* http: www.securitymanagement.com/library/Castro_ftc0800.html; (last visited Jan. 27, 2004) [hereinafter Castro Testimony].

Chairwoman Ida L. Castro testified regarding the EEOC's position with respect to the issue before the Subcommittee.[42] Specifically, Chairwoman Castro observed that requiring employers to obtain prior consent from accused harassers can "give the employee accused of harassment or other discriminatory activities the ability to control whether the investigation will occur" promptly or at all, and that the accused harasser had the opportunity "to tailor his or her responses to avoid responsibility, influence the testimony of potential witnesses, or even destroy evidence."[43] She further cautioned that giving the complete investigation report prior to disciplining the alleged harasser would "deter both victims of discrimination and witnesses from making complaints and participating in investigations."[44]

B. *EEOC's View with Respect to Providing a Copy of the Investigation Report to the Victim of Harassment*

While Title VI of the FACT may help alleviate some of the concerns identified by Chairwoman Castro, the fact that Title VI apparently prevents the company from disclosing the report to the victim of harassment may run afoul of EEOC guidance on the subject. EEOC guidelines clearly state that the victim *should* be informed of the results of the employer-initiated investigation.[45] The EEOC has not yet expressed an unambiguous opinion as to whether a copy of the investigation *report,* as opposed to the results of the investigation, should be provided to the complainant. However, under the EEOC guidelines,[46] if the employee does not have confidence that his or her investigation was appropriate, and this lack of confidence is reasonable, the employer will not be able to show that the employee unreasonably failed to participate in the investigation process, a necessary prong of the *Faragher/Ellerth* defense.[47] This raises the following question: How can a victim of harassment have reasonable confidence that the investigation was appropriate if the victim does not know the details of the investigation, such as who was interviewed and what was said? Perhaps this is a reason that many human resource professionals believe that a copy of the investigation report should be provided to the complainant, where possible.

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42. *Id.* at 7–23.
43. *Id.* at 63–64.
44. *Id.* at 64.
45. U.S. EEOC, Enforcement Guidance: Vicarious Employer Liability for Unlawful Harassment by Supervisors, V.C.1.e.iii (June 18, 1999), *available at* http://www.eeoc.gov/policy/docs/harassment.html (last visited Jan. 27, 2004).
46. *Id.* at V.D.1.c.
47. *See* Burlington Indus. Inc. v. Ellerth, 524 U.S. 742 (1998), and Faragher v. City of Boca Raton, 524 U.S. 775 (1998) (holding that employers are automatically liable for unlawful harassment by supervisors unless the employer can show that the employer had a reasonable complaint procedure in place for addressing harassment and that the employee unreasonably failed to utilize the complaint procedure).

What is clear is that an employer who wishes to satisfy its obligation to conduct a complete and thorough investigation, at least under EEOC guidance, must clearly disclose at least some information about the investigation and/or investigation results to the individual complaining of harassment. What is not clear, however, is how much information can be disclosed to the victim before the employer loses the Title VI safe harbor protection. Until regulators and/or the courts provide further guidance in this regard, employers are advised to consult experienced employment counsel to determine the permissible scope of any disclosures.

C. *EEOC's Position with Respect to the Use of Outside Investigators to Conduct Workplace Investigations*

In her testimony before the Subcommittee, Chairwoman Castro discussed the EEOC's position with respect to the importance of using outside investigators to conduct investigations into suspected discrimination or harassment.[48] Specifically, Chairwoman Castro noted that the use of outside investigators to conduct investigations of harassment or discrimination is important (1) where the employer lacks the resources to conduct investigations "in house"; (2) where the employer wishes to have an objective and unbiased party investigate the conduct at issue; and (3) where the conduct complained of was perpetrated by very high-level employees within the company.[49] Chairwoman Castro further observed that in settling cases with employers accused of harassment, the EEOC "frequently seek[s] commitments from employers to use outside entities to monitor and investigate claims of harassment and other forms of discrimination."[50] Although the EEOC does not generally require employers to use outside parties to conduct investigations into harassment claims, the EEOC has expressed the view that using outside investigators is important in certain circumstances, and may even be necessary where the accused harasser is a senior company official or where there is otherwise a conflict of interest.[51] Thus, employers wishing to avoid the requirements of the FCRA altogether by conducting harassment investigations in house not only lose what advantages exist for having neutral third parties conduct such investigations, they risk running afoul of EEOC guidance on the subject.[52]

48. *See* Castro Testimony, *supra* note 41 at 59–60.
49. *Id.*
50. *Id* at 60.
51. *Id.* at 59–60.
52. It also should be noted that some states regulate investigations conducted in-house, where such investigations would otherwise be subject to FCRA-like notice and consent requirements. For example, in California, entities that choose *not* to use a third-party "investigative consumer-reporting agency" to conduct misconduct investigations must nevertheless comply with certain notice requirements. CAL. CIV. CODE § 1786.53 (West Supp. 2004).

VI. The Regulation of Medical Information

In a separate section of the FACT, Title IV prohibits consumer-reporting agencies from furnishing employment-related consumer reports containing medical information unless the information is "relevant to process or effect the employment transaction" and the consumer provides "specific written consent."[53] Title IV likely does not encompass the results of drug tests or preemployment examinations, because such results usually come within the FCRA's exception for "direct transactions" between the consumer and the reporting agency.[54] On the other hand, Title IV may encompass some third party reports of workers' compensation cases and claims for disability or medical benefits.[55]

VII. Best Practices Under the FACT

Until regulators and the courts provide further guidance on the FACT, certain practical considerations can assist employers in their efforts to comply with the new law. For example, as discussed, employers can keep employee misconduct investigations outside the purview of the FCRA by conducting the investigation into employee misconduct in house. Again, the EEOC may frown upon the practice if it finds that, under the circumstances, a neutral third party would have conducted a more neutral investigation.[56]

If third party investigators are used to conduct misconduct investigations, employers should adopt strict policies and procedures to enable the investigation to remain within Title VI's safe harbor provision. Such policies and procedures should, at a minimum, restrict the disclosure of the investigation report and its contents to only those interested persons identified in section 1681a(x)(1)(D) of the amended FCRA.[57] In addition, although there is no express requirement that the summary of the investigation report described in section 1681a(x)(2) be in writing, employers should consider preparing the summary in writing with the sources of information used in preparing the report omitted from the summary. Employers also may consider adopting a policy of providing the summary of the investigation report (but not the report itself) to the victim in order to satisfy the EEOC, should it become necessary, that a complete and effective investigation into the suspected misconduct took place.

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53. 15 U.S.C.S. § 1681b(g)(1)(B)(i)-(ii) (2004).

54. *See id.* 15 U.S.C.S. § 1681a(d)(2)(A)(i) (2000); *see also* Hodge v. Texaco, Inc., 975 F.2d 1093 (5th Cir. 1992) (communication of drug-testing results directly from the collection or testing agency to the current or prospective employer exempted from FCRA); Salazar v. Golden State Warriors 124 F. Supp. 2d 1155 (N.D. Cal. 2000).

55. The effective date of Title IV of the FACT is June 1, 2004. 15 U.S.C.S. § 1681a (2004).

56. As discussed *supra* note 52, some states, such as California, regulate misconduct investigations conducted in house. *See, e.g.*, CAL. CIV. CODE § 1786.53.

57. 15 U.S.C.S. § 1681a(x)(1)(D) (2004).

Employers interested in adopting any of the foregoing policies or procedures should consult experienced employment counsel and consider state and local laws before implementing any such policies or procedures.

VIII. Conclusion

Thorough and impartial workplace investigations are becoming increasingly important, even indispensable, in today's legal and business climate. Title VI of the FACT gives employers more latitude regarding such investigations and is a timely and welcome development. Employers, however, must be mindful of Title VI's scope limitations and the interplay between the FCRA and Title VI, as well as new obligations regarding medical information.