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Disparate Impact Theory Post-Freeman: Down, But Not Out

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The Fourth Circuit slapped down the U.S. Equal Employment Opportunity Commission's claim of disparate impact discrimination in EEOC v. Freeman involving an employer's use of criminal background and credit checks. In a strongly worded opinion, the court affirmed a trial court's decision granting summary judgment to the employer because of the EEOC's failure to produce reliable statistical evidence showing a prima facie case of discrimination against job applicants. While some press reports have misapprehended the scope of the court's opinion, Freeman is a serious setback for the EEOC's approach to litigating many background check cases. The decision may also help employers defeat other employment law class actions based on disparate impact theory.

The District Court's Opinion

The defendant in Freeman is a privately held corporate events services provider with 3,500 full-time and 25,000 part-time employees located in offices around the country. The EEOC brought a pattern and practice lawsuit against the company in 2009, alleging its criminal background check and credit check policies violated Title VII because those practices had a discriminatory disparate impact on certain applicants. After some of the claims were dismissed through pretrial motions, the EEOC focused on its remaining allegations that the company's credit check practices had a disparate impact on black and male job applicants, and that its criminal background check practices had a disparate impact on black applicants.

The district court granted the employer's motion for summary judgment in an opinion in which the court excluded the statistical evidence offered by an expert retained by EEOC. The district judge followed the U.S. Supreme Court's landmark decision in Daubert v. Merrell Dow Pharmaceuticals Inc. in applying Federal Rule of Evidence 702. The court concluded that the EEOC's expert report should be excluded because of a "plethora of errors and analytical fallacies" that rendered the expert's conclusions "completely unreliable, and insufficient to support a finding of disparate impact." 961 F.Supp. 2d at 793. After providing a catalog of the defects in the expert's report, the court concluded:

[A]ny rational employer in the United States should pause to consider the implications of actions of this nature brought based upon such inadequate data. By bringing actions of this nature, the EEOC has placed many employers in the "Hobson's choice" of ignoring criminal history and credit background, thus exposing themselves to potential liability for criminal and fraudulent acts committed by employees, on the one hand, or incurring the wrath of the EEOC for having utilized information deemed fundamental by most employers. Something more, far more, than what is relied upon by the EEOC in this case must be utilized to justify a disparate impact claim based upon criminal history and credit checks. To require less, would be to condemn the use of common sense, and this is simply not what the discrimination laws of this country require.

961 F.Supp. 2d at 803.

The Appellate Court's Decision

A three-judge panel of the Fourth Circuit affirmed on Feb. 20, 2015. The appellate court held that the district court did not abuse its discretion in excluding the EEOC's expert report. Judge Roger L. Gregory's majority opinion recited several examples of sloppiness in the report, observing that the district court "identified an alarming number of errors and analytical fallacies" in the expert's work. Mistakes included double counting certain applicants, inaccurate coding of race and gender and the expert's inexplicable failure (at least in the reported opinions) to analyze hundreds of applicants who applied for work with the defendant during the relevant time period. The majority cited Daubert and its progeny for the notion that a district court exercises a "special gatekeeping obligation" in deciding whether expert testimony "rests on a reliable foundation and is relevant." The court concluded that "the sheer number of mistakes and omissions" in the EEOC's expert's analysis rendered his report unreliable within the meaning of Rule 702.

Judge G. Steven Agee wrote a concurring opinion that includes an unusually pointed critique of EEOC's litigation tactics. Concluding that the decision to exclude the EEOC's expert report was "not a close question," Judge Agee chastised the agency for continuing to rely on an expert whose work has been rejected by several other courts going back over a decade. Judge Agee observed that, in light of its significant power and considerable resources as a government agency, the EEOC "must be constantly vigilant that it does not abuse the power conferred upon it by Congress." He concluded that the agency's conduct "in this case suggests that its exercise of vigilance has been lacking. It would serve the agency well in the future to reconsider how it might better discharge the responsibilities delegated to it or face the consequences for failing to do so."

Takeaways for Employers

Suggestions that Freeman effectively marks the end of litigation over the use of criminal background checks are wide off the mark. Employers using background checks need to remain mindful of the complex requirements of federal and state law addressing this topic, including the federal Fair Credit Reporting Act.

The district court described the EEOC's litigation strategy as a "theory in search of facts to support it." 961 F.Supp. 2d at 803. Yet the theory has not gone away. From all reports, EEOC remains committed to an aggressive litigation position regarding claims that background checks result in a disparate impact on groups protected by Title VII. Class actions alleging violations of federal and state background check laws

continue to be filed on a regular basis.

Freeman is nonetheless an important decision for employers litigating background check cases. The Fourth Circuit endorsed the district court's careful application of Daubert principles in rejecting an expert report that appears to represent statistical "junk science" at its worst. And, while the Fourth Circuit was careful to say that it did not reach the merits (or any issue other than the proprietary of the district court's decision to exclude the expert report), the court blessed the district judge's complete demolition of the EEOC's expert. The district court's opinion contains a thorough review of the legal requirements of a prima facie case based on disparate impact theory. The court's rigorous approach to the plaintiff's obligation to prove, through reliable statistical evidence, that a specific employment practice results in a disparate impact, is particularly helpful for employers litigating these issues.

The district court's concern about the "Hobson's choice" facing employers makes an important point. Sophisticated employers that conduct background checks do so as a prudent exercise of risk avoidance. Sloppy statistical analysis should not be sufficient to subject such employers to the substantial exposure presented by class actions based on disparate impact theory.

Employers that utilize background checks should continue to take appropriate steps to ensure that their practices are defensible. For many employers, this will require careful review of how information of prior criminal activity in individual cases should be assessed as part of the application process. As with any requirement that can disqualify job applicants, employers should be mindful of the consequences of utilizing a standard on a categorical "pass/fail" basis, as disparate impact claims are relatively easier to pursue in those circumstances.

Finally, Freeman is not likely to be the last word on the use of disparate impact theory. This issue will remain visible because of the Supreme Court's pending resolution of Texas Department of Housing and Community Affairs v. The Inclusive Communities Project Inc. In that case, the Supreme Court is being asked to consider whether disparate impact theory is appropriate under the federal Fair Housing Act. Like that statute, nothing in Title VII specifically endorses the use of disparate impact theory to find liability against employers administering facially neutral policies and practices. Some commentators suggest that disparate impact theory should be restricted, notwithstanding its well-established role in Title VII litigation following the Supreme Court's landmark 1971 decision in Griggs v. Duke Power. The Supreme Court's resolution of the Texas fair housing cases may provide additional guidance to companies facing employment litigation based on disparate impact theory.

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