

CLIENT ALERT

Supreme Court Decision Unlikely to Provide Regulatory Relief in *Perez v. MBA*

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On Dec. 1, the U.S. Supreme Court heard oral arguments in *Perez v. Mortgage Bankers Association*, addressing the question whether an agency can revise a definitive interpretation of its own regulation without subjecting the revised interpretation to the Administrative Procedure Act's notice-and-comment rule-making procedures. At issue—and of great interest to the broader regulated community and followers of the Supreme Court's administrative law jurisprudence—is an almost-20-year-old D.C. Circuit precedent that discourages agency flip-flopping by requiring changes to interpretations of rules that are integral to the public's understanding of those rules to go through notice-and-comment rulemaking.

Factual and Procedural Background

Perez v. MBA arises from the Fair Labor Standards Act's requirement that employers pay overtime wages to employees unless the employees fit within certain exemptions, which include employees with administrative responsibilities and certain salespersons. The U.S. Department of Labor has promulgated regulations giving effect to this overtime-pay law, and, for decades, it has interpreted the exemptions (as stated in its regulations) as not including mortgage loan officers (thus requiring mortgage banks to pay overtime to such officers). In 2006, the DOL reinterpreted its regulations to place mortgage loan officers within the exemption (thus eliminating their employers' duty to pay overtime wages). Then, in 2010, the DOL flip-flopped once more, placing mortgage loan officers outside the exemption to the overtime-pay rule, and yet again requiring mortgage banks to pay them overtime.

The trade group Mortgage Bankers Association, whose members employ loan officers, challenged the DOL's 2010 interpretation in D.C. federal court. A few individual loan officers were granted leave to intervene as defendants to support the DOL's interpretation. The MBA challenged the interpretation substantively and also argued that the interpretation was procedurally improper under D.C. Circuit case law, primarily the 1997 case *Paralyzed Veterans of America v. D.C. Arena LP* and the 1999 case *Alaska Professional Hunters Ass'n v. FAA*.

In *Alaska Hunters*, the D.C. Circuit articulated the so-called Paralyzed Veterans doctrine as follows: "When an agency has given its regulation a definitive interpretation, and later significantly revises that interpretation, the agency has in effect amended its rule, something it may not accomplish without notice and comment." The district court here entered summary judgment for the DOL because MBA did not show reliance on the 2006 interpretation. MBA appealed and the D.C. Circuit reversed, clarifying that *Paralyzed Veterans* did not require a petitioner to show reliance on the earlier interpretation. The government petitioned for, and was granted, Supreme Court review on the question whether "a federal agency must engage in notice-and-comment rulemaking before it can significantly alter an interpretive rule that articulates an interpretation of an agency regulation."

The Parties' Arguments

The government and the intervenors filed separate briefs urging the Supreme Court to reverse the D.C. Circuit and overrule the Paralyzed Veterans line of cases. The government's argument relies primarily on the text and structure of the APA. The intervenors too argue that the APA cannot be reconciled with Paralyzed Veterans and add that, in any event, the Paralyzed Veterans doctrine is not needed because the APA and the court's administrative law doctrines already sufficiently guard the regulated community from agency flip-flopping. MBA counters that an interpretation that affects substantive rights effectively modifies a legislative rule and so requires an agency to follow the APA's notice-and-comment procedures applicable to such modifications.

The government points out that the APA defines a rule to include "an agency statement ... designed to implement, interpret, or prescribe law or policy" and argues that, by the APA's own terms, a rule may either prescribe (a legislative rule) or interpret (an interpretive rule). Yet the APA mandates public notice-and-comment procedures only for legislative rules and expressly exempts interpretive rules. Based on these APA definitions and requirements, the government contends that the courts may not (as it says the D.C. Circuit has done) require an agency to employ notice-and-comment procedures when repealing or amending interpretive rules without running afoul of the Supreme Court's 1978 decision in *Vermont Yankee Nuclear Power Corp. v. Natural Resources Defense Council Inc.*, which forbids courts from imposing on agencies duties not already found in the APA.

The intervenors echo the government's core argument, that the Paralyzed Veterans doctrine conflicts with the APA, and also contend that the doctrine is needless because of five existing checks on agencies' abuse of their interpretive-rulemaking power. First, under the APA's judicial review provisions, an agency action, including changing an interpretation, may be vacated if the agency does not explain it. Second, judicial deference doctrines, which ordinarily lend considerable weight to an agency's interpretation of its own regulation, apply with less force when an agency's position has changed over time. Third, an agency may not issue an interpretation at odds with the rule being interpreted. Fourth, many statutes, including the FLSA provision at issue here, contain a safe harbor provision limiting a regulated entity's liability when it relies in good faith on an interpretation that has since been modified or rescinded. And fifth, the Due Process Clause of the Fifth Amendment prevents an agency from imposing liability on a regulated entity without giving it fair notice that certain conduct is forbidden or required. The intervenors thus conclude that the Paralyzed Veterans doctrine needlessly prevents agencies from issuing well-reasoned interpretations without employing cumbersome notice-and-comment procedures.

The MBA responds by explaining the wisdom of and need for the Paralyzed Veterans doctrine to prevent agencies' abuse of their interpretive rule-making power. In particular, because an agency interpretation of a legislative rule effectively modifies the rule itself, an agency may not issue such an interpretation without employing the notice-and-comment procedures applicable to legislative rules. In other words, the courts should apply the APA functionally to make sure agencies are not hiding substantive changes behind what they characterize as mere interpretations.

To the Vermont Yankee critique, the MBA responds that Paralyzed Veterans does not impose procedures outside the APA; on the contrary, it relies on the familiar notice-and-comment requirement that applies to any formulation, repeal or amendment of a substantive rule, regardless of whether the agency labels its action "interpretive." Indeed, the DOL itself characterized its 2010 interpretation as definitive and controlling.

Analysis

The government has had the Paralyzed Veterans doctrine in its crosshairs for years and, with *Perez v. MBA*, finally has it squarely before the court. The regulated community, for its part, has cherished Paralyzed Veterans as one of the few doctrines to check agencies' misuse of their prerogative to interpret their own rules. But the doctrine also stands on shaky ground: Despite the seemingly fundamental fairness of its premise, the Supreme Court is likely to invalidate it as an unlawful judicial encroachment on agency discretion.

While the court may, in the abstract, sympathize with the regulated community, the MBA's position is vulnerable on three fronts. First, the MBA frames the question presented as whether an interpretation that so affects a regulation's substance that it is legislative in its own right must go through notice-and-comment procedures. But this framing distorts the question on which the court actually granted certiorari — whether an agency must employ notice-and-comment rulemaking before it may significantly alter an interpretive rule. After all, Paralyzed Veterans and its progeny do not rest on the proposition that rules that are in substance "legislative" but labeled by the agency as "interpretive" will be treated as legislative rules and so require notice and comment. That substance-over-form principle of law has certainly been embraced by some courts in other cases, but it is not the foundation for Paralyzed Veterans, which is concerned only with interpretive rules.

Second, even taken on its own terms, the MBA's position creates a difficult line-drawing problem by asking the courts (and the agencies) to figure out when an interpretation affects a regulation's substance enough to make it legislative in its own right. Taking the MBA up on its argument would probably only encourage more litigation over the character of interpretive rules. Although the court's canon is replete with multifactor tests of one sort or another (a habit it has been chided by judicial pundits and its own members alike for), the current court prefers bright-line tests and is sensitive to how its decisions affect lower courts' case dockets.

Third, the MBA contends that enhanced rule-making procedures are necessary to counter judicial deference doctrines. The Supreme Court announced in the 1945 case *Bowles v. Seminole Rock & Sand Co.* (and reaffirmed in the 1997 case *Auer v. Robbins*) that an agency's interpretation of its own regulation is entitled to deference where the regulation is ambiguous and the interpretation is not inconsistent with the regulation. *Seminole Rock* and *Auer* make it hard for a regulated entity to obtain meaningful judicial review of a rule, regardless of the label the agency gives it. But at least with a legislative rule, the policy reasons for granting deference (i.e., the presumption that, through the rule-making process, the agency engaged in reasoned and fully informed decision-making) have some plausibility. Less so with interpretive rules. Paralyzed Veterans thus gives regulated parties some relief by requiring the agency to subject changes to a definitive interpretation of a legislative rule to the same procedures as a change to the rule itself. Be that as it may, upholding that argument would seem to undermine Vermont Yankee, something the court is highly unlikely to do.

Agency overreach is a real concern. But for better or worse, the Supreme Court has generally declined the invitation to fill what the regulated community views as procedural gaps in the APA. Nevertheless, there may yet be solace on the horizon.

First, while the courts are not in a position to alter the APA, Congress certainly is. The results of the recent election, on top of recent bipartisan efforts to reform the APA (including the proposed Regulatory Accountability Act of 2013), could augur well for the possibility of real reform in the near future. A significant overhaul of the APA may be a long shot, but so may be the Supreme Court's siding with the MBA in *Perez v. MBA*.

Second, whatever the Supreme Court undoes in *Perez v. MBA* could be more than alleviated if, as several justices have openly expressed a willingness to do, the Supreme Court were to reconsider and turn back its *Seminole Rock* and *Auer* precedents, thereby removing an incentive for agencies to promulgate vague regulations on the theory that they can fill the interstices through interpretive rules to which the courts will defer. Indeed, justices have in concurring opinions over the past couple years all but solicited petitions that would ask the court to do just that, and it would not surprise us to see one or more concurring opinions in *Perez v. MBA* tee the issue up anew.

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For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

Thomas (Tim) C. Means

Retired Partner – Washington, D.C.

Email: tmeans@crowellretiredpartners.com

Daniel W. Wolff

Partner – Washington, D.C.

Phone: +1 202.624.2621

Email: dwolff@crowell.com