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Volume 38 | Issue 40 | March 18, 2015

Supreme Court Says Federal Agencies Can Change Regulatory Interpretations Without Formal Rulemaking

In 2006, the DOL issued an opinion letter concluding that mortgage loan officers qualified for the administrative exemption to FLSA overtime pay requirements. Four years later, the DOL reversed itself and reclassified mortgage loan officers as nonexempt. On March 9, the Supreme Court rejected challenges to this about-face, ruling that changes to interpretive rules do not require "notice-and-comment" rulemaking. Because this decision should make it easier for regulatory agencies to shift course, developing effective compliance strategies may prove more complicated than ever.

Background

The Administrative Procedure Act (APA) establishes procedures federal agencies use to formulate, amend, or repeal a rule. An agency must provide notice and allow comments from stakeholders during the rulemaking process when it formulates a "legislative" rule — a rule that has the force of law and is binding on employers. In contrast, the APA exempts from the notice-and-comment requirement "interpretive" rules — an agency's explanation of the regulations or laws it administers. Interpretive rules, which do not have the force and effect of law, come in many forms, including guidance documents, FAQs, opinion letters, interpretive bulletins, and agency manuals. Over the past few decades, regulators have increasingly relied on interpretive rules to establish or reinterpret compliance standards without formal rulemaking or advance notice to employers.

The FLSA's Administrative Exemption

The federal Fair Labor Standards Act (FLSA) generally requires that covered employers pay overtime wages to employees who work more than 40 hours per week, unless the employees qualify for an exemption. The FLSA provides such an exemption for employees working in a *bona fide* executive, administrative, or professional capacity, or in the capacity of outside salesman. (See our April 3, 2014 *FYI In-Depth*.)

Controversy Over the Classification of Mortgage Loan Officers

For over a decade, the DOL's Wage and Hour Division (WHD) has taken conflicting positions on whether mortgage loan officers are overtime-eligible under the FLSA. In 1999 and again in 2001, the WHD issued opinion letters concluding that mortgage loan officers are non-exempt. After the current FLSA regulations were issued in 2004, the Mortgage Bankers Association (MBA) asked the DOL whether mortgage loan officers were exempt under the new regulations. In a 2006 opinion letter, the WHD concluded that mortgage loan officers would typically qualify for the administrative exemption.

Four years later, the WHD withdrew the 2006 opinion letter and reversed course. In 2010, it issued an unsolicited Administrator's Interpretation of the FLSA regulations that reclassified mortgage loan officers as nonexempt. The MBA sued, contending that the DOL's about-face without formal rulemaking violated the APA. Notably, the MBA did not dispute that the rule at issue was an interpretive — rather than a legislative — one.

The district court agreed with the DOL. The DC Circuit Court of Appeals reversed, vacating the agency's reclassification of mortgage loan officers. Relying on its 1997 decision in *Paralyzed Veterans of Am. v. D. C. Arena L. P.*, the appeals court concluded that a federal agency must follow the APA's formal rulemaking procedures before reversing or making significant changes to an existing interpretation of a regulation. The DOL appealed.

Outside Sales Exemption

Mortgage loan officers may still qualify for the FLSA's outside sales exemption if they satisfy certain criteria. However, employers are likely to see changes in the so-called "white collar" exemptions when the DOL proposes updates to the FLSA's overtime regulations.

The Supreme Court Decision

When asked "whether a federal agency must engage in notice-and-comment rulemaking pursuant to the Administrative Procedure Act before it can significantly alter an interpretive rule that articulates an interpretation of an agency regulation," the Supreme Court answered with a resounding no.

In *Perez v. Mortgage Bankers Association*, the Court ruled that the APA categorically exempts interpretive rules from notice-and-comment rulemaking requirements — unless required by another federal statute. Rejecting the *Paralyzed Veterans* doctrine as contrary to the APA, the Court concluded that an agency that is not required to use notice-and-comment procedures to issue an interpretive rule in the first place is also not required to use those procedures to amend *or* repeal that rule.

> **Comment.** While the ruling on interpretive rules was unanimous, three concurring opinions highlighted a split among the justices on the extent to which courts should defer to agencies' interpretive opinions. Whether the Court will tackle the issue in a future case remains to be seen.

In Closing

In the wake of this ruling, it should be far easier for the DOL and other federal agencies — such as the IRS and Health and Human Services — to change long-standing policies and enforcement positions for the employers they regulate. Future administrations should find it simpler and quicker to shift course by changing the interpretive rules of previous administrations rather than engaging in formal notice-and-comment rulemaking. As a result, developing effective long-term compliance strategies based on current agency guidance may prove more complicated than ever.

Volume 38 | Issue 40 | March 18, 2015

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