No. 13-1052

In The Supreme Court of the United States

JEROME NICKOLS, RYAN HENRY, and BEVERLY BUCK,

Petitioners,

v.

MORTGAGE BANKERS ASSOCIATION,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

REPLY BRIEF FOR PETITIONERS

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REPLY BRIEF FOR PETITIONERS

The unambiguous text of the Administrative Procedure Act ("APA") exempts interpretive rules from notice-and-comment rulemaking. 5 U.S.C. § 553(b). Under the D.C. Circuit's *Paralyzed Veterans* doctrine, however, "an agency cannot significantly change its position . . . *even between two interpretive rules*, without prior notice and comment." *Transp. Workers Union of Am., AFL-CIO v. TSA*, 492 F.3d 471, 475 (D.C. Cir. 2007) (emphasis added). This is so, according to the D.C. Circuit, because when an agency "significantly revises [its initial] interpretation, the agency has in effect amended its rule." *Alaska Prof'l Hunters Ass'n v. FAA*, 177 F.3d 1030, 1034 (D.C. Cir. 1999).

Respondent Mortgage Bankers Association refuses to defend the *Paralyzed Veterans* doctrine on its own terms. Instead, Respondent attacks the doctrine's premise that the agency's revised interpretation qualifies as an "interpretive rule" in the first place. In so doing, Respondent asks this Court to depart significantly from its settled understanding of interpretive rules and consider arguments that were neither raised nor passed on below.

This Court should decline Respondent's invitation. The Department of Labor ("DOL") in 2010 validly – and correctly – interpreted the agency's own regulations to give mortgage loan officers the protections afforded by the Fair Labor Standards Act ("FLSA"). Because the APA does not require notice-and-comment rulemaking before issuing such an interpretive rule,

the D.C. Circuit's decision in this case must be reversed.

I. MORTGAGE BANKERS' ARGUMENTS ARE NOT SUPPORTED BY THE RECORD.

Before responding to Mortgage Bankers' arguments, it is necessary to clarify a few points about the record in this case.

Mortgage Bankers predicates its argument on a hypothetical set of facts that goes something like this: a federal agency, seeking to maximize its own power, issues a hopelessly vague regulation. Regulated parties, unsure how the regulation applies to their circumstances, seek to learn how the agency will apply the regulation in practice. The agency issues an interpretation addressing the regulated parties' question, and private parties rely heavily on that interpretive answer. Later, the agency, in a fit of caprice and without explanation, changes its interpretation.

This case tells a very different story. The DOL first issued FLSA regulations over seventy-five years ago. 3 Fed. Reg. 2518 (Oct. 20, 1938). Those regulations have served admirably as a clear and durable guide to employers and employees, and the substance of the relevant regulations has remained unchanged since 1949. 14 Fed. Reg. 7705 (Dec. 24, 1949). Through the years, the agency has consistently treated loan officers as sales employees – eligible for the outside

sales exemption but ineligible for the administrative exemption.[1]

Respondent Mortgage Bankers did not approach the DOL in 2005 in order to clarify some regulatory ambiguity. Mortgage Bankers sought to *change* the agency's established interpretation to benefit its members in ongoing litigation. The incentive to do so was obvious. Mortgage Bankers' members could (and did) hold up the 2006 interpretation in court, demand deference under *Auer v. Robbins*, and claim immunity

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[1] Wage & Hour Div., U.S. Dep't of Labor, Opinion Letter, WH-115, 1971 WL 33052 (Jan. 15, 1971), App. 72a; Wage & Hour Div., U.S. Dep't of Labor, Opinion Letter, 1999 WL 1002401 (May 17, 1999), App. 75a. The agency last revised its regulations in 2004, but did not change the substance of the administrative exemption, and thus did not undermine the vitality of the agency's pre-existing interpretations. *See* Br. for Respondent Mortg. Bankers Ass'n at 3. The agency did add a new provision addressing the application of the administrative exemption to employees in the financial services industry. *See* 29 C.F.R. § 541.203(b). That section explained that while employees could qualify for the exemption if they "analyz[ed]" investments, "advis[ed] the customer" regarding financial options, and engaged in "marketing, servicing or promot[ion]" work, "an employee whose primary duty is selling financial products does not qualify for the administrative exemption." *Id.* The agency cited numerous examples of both exempt and nonexempt employees, but specifically identified *loan officers* as the prime example of employees whose primary duty is selling financial products. *See* Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees, 69 Fed. Reg. at 22,145 (citing *Casas v. Conseco Fin. Corp.*, No. Civ.00-1512, 2002 WL 507059, at *9 (D. Minn. Mar. 31, 2002)).

from liability under the Portal-to-Portal Act's good faith defense.

When the DOL acted in 2010 to restore its original interpretation, the agency was not, as Respondent suggests, engaged in policymaking under the guise of interpretation. The agency was correcting a mistake – revoking a short-lived and legally erroneous interpretation widely understood to be the unfortunate (but fortunately, rare) product of regulatory capture. *See* R. Intervenors' Mem. Opp'n Summ. J., Ex. 10 at 7, 17, ECF No. 30-10 (Murphy, J.) (calling the 2006 interpretation "a novel approach toward settled law" and "the only exception to the entire statutory regulatory case law scheme that we've seen interpreting 29 U.S.C. 213(a)(1) through regulation and case law in the entire time that the statute has been in place.").

Mortgage Bankers ignores this history. It ignores the fact that the agency acted reasonably to fix a legal error. It ignores the extent to which existing protections – most prominently arbitrary and capricious review – already prevent agencies from engaging in the sort of heavy-handed conduct Mortgage Bankers hypothesizes. Most fundamentally, Mortgage Bankers ignores its own conduct in this case. Respondent insists that *Paralyzed Veterans* is necessary to "prevent[ ] agencies from unseemly flip-flopping," Br. for Respondent Mort. Bankers Ass'n at 13, but fails to explain why the DOL's first flip flop – caused by Respondent – should be treated any differently. It should not. When an agency issues an interpretive rule, notice-and-comment rulemaking is not required.

II. THE COURT SHOULD LIMIT ITS REVIEW TO THE ISSUES ADDRESSED BELOW.

Respondent's arguments to this Court share a crucial premise: that the DOL's 2010 interpretation was a legislative – not an interpretive – rule. But this argument suffers from a serious problem. The *Paralyzed Veterans* doctrine, as articulated by the D.C. Circuit, is based on the opposite premise: that "an agency cannot significantly change its position . . . *even between two interpretive rules*, without prior notice and comment." *Transp. Workers Union of Am.*, 492 F.3d at 475 (emphasis added).[2]

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[2] The D.C. Circuit has always treated as conceptually distinct the questions of (1) whether an agency pronouncement is legislative, and, if not, (2) whether that pronouncement is nevertheless invalid under the *Paralyzed Veterans* doctrine. One recent case, *Scenic America, Inc. v. United States Department of Transportation*, helpfully illustrates the circuit's settled approach. ___ F. Supp. 2d ___, 2014 WL 2803084 (D.D.C. June 20, 2014). In that case, an environmental group sought to invalidate an agency document permitting states to allow the construction of digital billboards along interstate highways. *Id.* at *1-3. The plaintiff first asserted that the agency document amounted to a legislative rule. *Id.* at *3. That assertion required the court to apply the circuit's familiar four factor test, which asks:

> (1) whether in the absence of the rule there would not be an adequate legislative basis for enforcement action or other agency action to confer benefits or ensure the performance of duties, (2) whether the agency has published the rule in the Code of Federal Regulations, (3) whether the agency has explicitly invoked its general legislative authority, or (4) whether the rule effectively amends a prior legislative rule.

(Continued on following page)

Compounding the problem, Mortgage Bankers fully embraced the D.C. Circuit's premise below, stating that "[e]ven if [a] pronouncement can be considered an interpretative rule, it still may be subject to notice-and-comment rulemaking[ ] under *Paralyzed Veterans* and its progeny." R. Plaintiff's Reply Mem. Supp. Summ. J. at 7 n.10, ECF No. 17. Mortgage Bankers never argued below that the agency's 2010 interpretation amounted to a legislative rule. And as a consequence of that choice, the argument was not addressed by Petitioners, the district court, or the court of appeals.

This Court considers grounds in support of a judgment not raised below only in extraordinary cases. *See Heckler v. Campbell*, 461 U.S. 458, 468 n.12 (1983). Because Mortgage Bankers failed to argue below that the DOL's 2010 interpretation amounted to a legislative rule, the argument is waived. *See Genesis Healthcare Corp. v. Symczyk*, 133 S. Ct. 1523, 1529 (2013) (finding waiver where a party failed to challenge circuit precedent holding

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Am. Min. Cong. v. Mine Safety & Health Admin., 995 F.2d 1106, 1112 (D.C. Cir. 1993) *cited in Scenic America*, 2014 WL 2803084, at *5. Applying this test, the *Scenic America* court determined that the agency pronouncement was an interpretive – not legislative – rule. 2014 WL 280308 at *10. But that conclusion meant the court had to confront the challenger's second argument: that an agency's interpretation "may nevertheless be subject to the APA's notice-and-comment requirements under the [*Paralyzed Veterans*] doctrine," because "an agency must still use notice-and-comment procedures to issue an interpretative rule when that rule" significantly revises a prior interpretation. *Id.*

that an unaccepted Rule 68 offer mooted an individual claim).

And even setting aside general waiver principles, there are compelling reasons to proceed cautiously here. The circuit courts apply a variety of tests to determine whether a rule is legislative or interpretive. *See* 32 Charles Alan Wright & Charles H. Koch, Jr., Federal Practice & Procedure § 8155 (1st ed.). While that question may require this Court's attention in a future case, it would be imprudent to pass on the question here without the benefit of full briefing and opinions below.

This Court should instead proceed from the same premise accepted by the parties and courts below – that the DOL's 2010 interpretation is an interpretive rule – and determine whether notice-and-comment rulemaking was still required under the terms of the *Paralyzed Veterans* doctrine.

III. THE *PARALYZED VETERANS* DOCTRINE CONFLICTS WITH THE APA.

Even if this Court considers Respondent's arguments in full, the result would be the same. The DOL's 2010 interpretation fully qualifies as an "interpretive rule" exempt from notice and comment under the APA.

A. Respondent Would Depart Significantly from This Court's Settled Understanding of Interpretive Rules.

Respondent first suggests that this Court abandon its established definition of interpretive rules. Under this Court's precedent, interpretive rules are rules "'issued by an agency to advise the public of the agency's construction of the statutes and rules which it administers.'" *Chrysler Corp. v. Brown*, 441 U.S. 281, 302, n.31 (1979) (quoting U.S. Dep't of Justice, *Attorney General's Manual on the Administrative Procedure Act* 30 n.3 (1947)); *see also Shalala v. Guernsey Mem'l Hosp.*, 514 U.S. 87, 99 (1995).

Mortgage Bankers proposes a wholesale change to the APA's definition of interpretive rules. Under Mortgage Bankers' proposal, interpretive rules would encompass only "(i) non-authoritative interpretations of statutes, or (ii) interpretations of regulations issued *at the same time as the regulations themselves*." *See* Br. for Respondent Mortg. Bankers Ass'n at 42 (emphasis added). But the APA admits no such temporal limitation on interpretive rules. Indeed, such a limitation would effectively prevent agencies from responding to public inquiries over how a regulation might apply to unforeseen circumstances, undermining the agency's ability to "advise the public" – the very rationale for exempting interpretive rules from notice and comment in the first place. In any event, Mortgage Bankers' proposed definition, if accepted, would not vindicate Respondent's position in this case. Neither the 2006 nor the 2010 interpretation

(nor, for that matter, the DOL's prior interpretations) was issued contemporaneously with the relevant FLSA regulations.

B. Respondent's Argument Is Inconsistent with This Court's Understanding of Legislative Rules.

The 2010 interpretation's proper status as an interpretive rule is further demonstrated by the Court's characterization of legislative rules. This Court has cited "the proxy rules issued by the Securities and Exchange Commission" as the prime example of legislative rules. *Chrysler Corp.*, 441 U.S. at 302-03. Section 14(b) of the Securities Exchange Act prohibits certain persons from giving or withholding a proxy "in contravention of such rules and regulations as the Commission may prescribe." 15 U.S.C. § 78n(b)(1). The statute itself creates no independently enforceable rights, duties, or obligations. When the agency, through its regulations, declares that the form of proxy "shall indicate in bold-face type whether or not the proxy is solicited on behalf of the registrant's board of directors," 17 C.F.R. § 240.14a-4(a), the agency is exercising legislative power delegated by Congress. The legal norms contained in the proxy regulation are created from whole cloth (but pursuant to congressional authority); they cannot be independently ascertained by interpreting any pre-existing legal source. "[W]hen a statute does not impose a duty on the persons subject to it but instead authorizes . . . an agency to impose a duty, the formulation

of that duty becomes a legislative task entrusted to the agency." *Hoctor v. U.S. Dep't of Agric.*, 82 F.3d 165, 169 (7th Cir. 1996) (Posner, C.J.).

If the Commission later opines that twelve-point, bolded Century Schoolbook font does (or does not) satisfy the proxy regulation's requirements, such a statement would qualify as an interpretive rule, issued to "advise the public of the agency's construction" of the "rules which it administers." *Chrysler Corp.*, 441 U.S. at 302, n.31. Interpretation "is the ascertainment of meaning." *Hoctor*, 82 F.3d at 170. "[I]nterpretive rules merely explain, but do not add to, the substantive law that already exists in the form of a statute or legislative rule[.]" *Miller v. Cal. Speedway Corp.*, 536 F.3d 1020, 1033 (9th Cir. 2008).[3]

The foregoing legal principles dictate a straightforward result in this case: (1) the FLSA is a statute, (2) the regulations contained in the Code of Federal Regulations "defining and delimiting" the scope of the statute's exemptions are legislative rules, and (3) the agency's interpretations explaining how the regulations apply to various workplace scenarios are interpretive rules.

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[3] Of course, an agency remains free to elevate an otherwise valid interpretive rule to the status of legislative rule. To do so, however, the agency must first subject the interpretation to the heightened procedural requirements contained in the APA, including notice-and-comment rulemaking.

C. An Agency Does Not Amend Its Regulations When It Modifies Its Interpretations.

This seemingly straightforward result faces one last hurdle: the D.C. Circuit's insistence that when an agency "significantly revises [its initial] interpretation, the agency has in effect amended its rule." *Alaska Hunters*, 177 F.3d at 1034. But that simply isn't so. An agency's interpretation of its regulation no more changes the meaning of the regulation than a court's interpretation of a statute amends the statute. And just as courts from time to time find it necessary to change or reverse erroneous interpretations, so too agencies must occasionally correct course on their own interpretive rules. A changed interpretation is still an interpretation, not an act of legislation.

Recognizing this shortfall, the panel below offered a doctrinal fix. The court called the *Paralyzed Veterans* doctrine's "operative assumption" "the belief that a definitive interpretation is so closely intertwined with the regulation that a significant change to the former constitutes a repeal or amendment of the latter." *Mortg. Bankers Ass'n v. Harris*, 720 F.3d 966, 969 n.3 (D.C. Cir. 2013), App. 5a.

But the D.C. Circuit's "closely intertwined" assumption suffers from fatal flaws of its own. In order to make the *Paralyzed Veterans* doctrine work in practice, its defenders must establish three things: first, that the agency's initial interpretation qualifies as an interpretive rule; second, that at some point,

and by some mechanism, that initial interpretation calcifies into part of the regulation itself; and third, that a subsequent interpretation, by modifying the original interpretation, amends the (now modified) regulation.

The doctrine's assumption that an *initial* interpretation may be issued as a valid interpretive rule is correct as far as it goes. But the point exposes the doctrine's key flaw: its asymmetrical treatment of agency interpretations. Simply put, if the initial interpretation is to carry the force and effect of law, such that it cannot be changed without notice and comment, then the *initial interpretation itself* must be the product of notice and comment. The converse is equally true: if an agency's initial interpretation qualifies as an interpretive rule lacking the force and effect of law, then a later-in-time interpretation modifying the original interpretation does not change any of the substantive regulations and therefore need not follow notice-and-comment rulemaking. The *Paralyzed Veterans* doctrine thus rests on an illusion, a sort of Venn diagram where the circles fail to intersect. An interpretation cannot be simultaneously interpretive (for purposes of issuance) and also legislative (for purposes of repeal). But *Paralyzed Veterans* compels adherence to this failed logic.

The doctrine's second assumption – that an initial interpretation somehow morphs into part of the regulation itself, is equally flawed. An agency's interpretation of its own regulations achieves the force and effect of law through – and only through –

the process of notice-and-comment rulemaking. *See Chrysler Corp.*, 441 U.S. at 302-03. Mortgage Bankers, for its part, never fully explains how or why (or when) an interpretive rule loses its interpretive status. Mortgage Bankers at times suggests the change is instantaneous. *See* Br. for Respondent Mortg. Bankers Ass'n at 45 ("[T]he prior interpretation essentially 'finishes the job' of creating the regulation itself."). But Mortgage Bankers later concedes that an agency would not be estopped from revoking an errant interpretation after one month. *Id.* at 31-32. Respondent at other times suggests that an interpretive rule can become legislative "over the course of years of consistent application." *Id.* at 18. But this, too, is a non-sequitur. Applying the law one, ten, or a thousand times does not change the law itself. The text of the APA suggests a simple and straightforward standard: an agency can enact, or repeal, a formal regulation only through the process of notice-and-comment rulemaking; an agency can issue, or repeal, an interpretative rule without notice-and-comment rulemaking. Mortgage Bankers' alternative is not so much an unworkable set of standards as the absence of standards altogether. Under Respondent's conception of the *Paralyzed Veterans* doctrine, an agency can sometimes change its interpretations and sometimes not, because some interpretations effectively become part of the regulations while others do not. The APA's drafters knew better than to follow this course.

Mortgage Bankers casts the *Paralyzed Veterans* doctrine as a corollary of *Auer v. Robbins*, 519 U.S.

452 (1997). But this argument, too, misses the mark. An interpretive rule's potential eligibility for deference does not act as a stand-in for having the force and effect of law. There is an enormous theoretical and practical difference between formal regulations, which "bind[ ] members of the public, the agency, and even the courts," Kenneth Davis & Richard Pierce, *Administrative Law Treatise* 233 (3d ed. 1994), and interpretive rules, which may (or may not) command some level of judicial deference. "[A] court is not required to give effect to an interpretative [rule]." *Batterton v. Francis*, 432 U.S. 416, 424-26, n.9 (1977). Instead, "[v]arying degrees of deference are accorded to administrative interpretations, based on such factors as the timing and consistency of the agency's position, and the nature of its expertise." *Id.*

Practical experience demonstrates the real-world significance of the distinction. In one recent study, the authors concluded that lower federal courts upheld agency interpretations in seventy-six percent of cases where *Auer* deference was sought – a number not materially different from the seventy percent of cases where courts affirmed agency action using traditional interpretive tools. Richard J. Pierce, Jr. & Joshua Weiss, *An Empirical Study of Judicial Review of Agency Interpretations of Agency Rules*, 63 Admin. L. Rev. 515, 519 (2011).[4]

[4] The potential for *Auer* deference is a particularly poor justification for the *Paralyzed Veterans* doctrine because *Auer*

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Mortgage Bankers spends considerable energy focusing on the potential practical effects of agency interpretations. But such practical effects do not confer legislative status on otherwise interpretive rules.

There is no question that interpretive rules, although lacking the force and effect of law, have real-world consequences. Interpretations can clarify important duties, create norms of conduct between regulated parties, and engender reliance interests and investment-backed expectations. And Petitioners understand – keenly – the frustration that occurs when an agency changes its interpretation.

But these frustrations do not come with a license to rewrite the plain language of the APA. Instead, such concerns are best addressed on a case-by-case basis using the legal tools designed to prevent arbitrary agency conduct and to protect private parties from unforeseen interpretive shifts. *See* Br. for Petitioners Nickols, et al. at 41-48 (explaining that arbitrary and capricious review, judicial deference doctrines, statutory safe harbors, and due process, among others, adequately protect regulated communities for

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deference is frequently not warranted "when the agency's interpretation conflicts with a prior interpretation." *Christopher v. SmithKline Beecham Corp.*, 132 S. Ct. 2156, 2166 (2012) (citing *Auer*, 519 U.S. at 462). Respondent fails to explain why an initial interpretation – far more likely to be eligible for *Auer* deference – may be issued without notice and comment, but a revised interpretation – much less likely to receive *Auer* deference – must follow notice-and-comment rulemaking procedures.

unfair and unforeseen shifts in agency interpretations).

CONCLUSION

The APA is "a legislative enactment which settled 'long-continued and hard-fought contentions, and enacts a formula upon which opposing social and political forces have come to rest.'" *Vt. Yankee Nuclear Power Corp. v. Natural Res. Def. Council, Inc.*, 435 U.S. 519, 523 (1978) (quoting *Wong Yang Sung v. McGrath*, 339 U.S. 33, 40 (1950)). In many ways, Mortgage Bankers seeks to reopen the ten-year debate that preceded the APA's enactment and impose procedural constraints beyond those Congress saw fit to write into law. But this Court has repeatedly cautioned that it is courts' role to interpret the APA as written – not to take sides in that long-continued debate or second-guess Congress' judgment. *See id.*; *Chrysler Corp.*, 441 U.S. at 313. The *Paralyzed Veterans* doctrine is incompatible with the text of the APA and unfaithful to the careful balance struck by Congress. Petitioners respectfully ask this Court to reverse the court of appeals.

Respectfully submitted.

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