Client Alert

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Supreme Court Allows Agencies to Reinterpret the Law at Their Discretion

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In a decision published on March 9, 2015, the Supreme Court ended the D.C. Circuit Court's Paralyzed Veterans doctrine, which required administrative agencies to utilize the Administrative Procedure Act's (APA) notice-and-comment process in order to substantially alter an interpretation. *See Perez v. Mortgage Bankers Assoc.*, 575 U.S. ___, No. 13-1041, slip op. (March 9, 2015). According to the Court, this doctrine improperly imposed procedural requirements on agencies that are not required by the APA.

Pursuant to the APA, legislative rulemaking requires a period for notice and comment by industry stakeholders because, unlike interpretive rules, a legislative rule has the "force and effect of law." On the other hand, interpretative rulemaking, e.g., when an agency adopts an interpretation of its regulation, is exempted from the notice-and-comment process. Nonetheless, the D.C. Circuit's Paralyzed Veterans doctrine held that an agency must use the APA's notice-and-comment process when it issues a new interpretation that deviates significantly from one the agency has previously adopted. In its opinion, the Court held that the Paralyzed Veterans doctrine is inconsistent with the APA and unnecessary to further its purpose, which, in the Court's view, already adequately provides recourse to regulated entities when an agency issues or amends interpretive rules.

Accordingly, agencies are now free to issue guidance documents, such as interpretive bulletins and memoranda, which alter previous regulatory interpretations without so much as a "heads-up" provided to the industry. Practically speaking, in light of the potential for fluid agency interpretations, which may change every 4-8 years as new presidential administrations come into power and agency leadership turns over, regulated entities will find it even more difficult to maintain compliance with the law. As a case in point, lenders were taken by surprise when the CFPB issued a bulletin regarding fair lending risks for indirect automobile lenders. The bulletin indicated that the CFPB would apply the disparate impact doctrine under the Equal Credit Opportunity Act to indirect automobile lenders that compensate dealers based on discretionary pricing. However, the bulletin was light on details regarding how these automobile lenders could compliantly structure their pricing while maintaining such discretionary pricing, which is the industry standard practice. Citing the Paralyzed Veterans doctrine, some argued that this guidance should have required a notice-and-comment period that would have forced the CFPB to weigh its impact on the industry, as well as allow companies time to bring their practices into compliance. With its holding here, the Supreme Court has made clear that such an argument will not succeed, leaving lenders with no choice but to try to develop revised compliance management systems on the fly. Moreover, lenders cannot be sure that these investments in compliance management, some of which may result in lost market share, will still be relevant and/or effective when a new presidential administration comes into power in January 2017 with its own take on the law.

That said, some see a silver lining in the fact that the opinion did not rule on what happens when agencies issue interpretive rules that are given judicial deference, and thereby assume the authority of a legislative rule. Justices Scalia and Thomas recognized this issue in their own separate opinions, each arguing against judicial deference being used on interpretive rules. Stay tuned for further developments on that front.

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