In the Matter of:

TIMOTHY E. FLAKE, **ARB CASE NO. 03-126**

COMPLAINANT, **ALJ CASE NO. 2003-SOX-18**

v. **DATE: February 25, 2004**

NEW WORLD PASTA COMPANY,

RESPONDENT.

BEFORE: THE ADMINISTRATIVE REVIEW BOARD

Appearances:

For the Complainant:
Kirk L. Wolgemuth, Esq., ***Reading, Pennsylvania***

For the Respondent:
Jay S. Berke Esq., Aney D. Chandy, Esq., ***Skadden, Arps, Slate, Meagher & Flom, New York, New York***

FINAL DECISION AND ORDER

This case arises under the whistleblower protection provision of the Corporate and Criminal Fraud Accountability Act of 2002, title VIII of the Sarbanes-Oxley Act of 2002, codified at 18 U.S.C.A. § 1514A (West Supp. 2003). On January 29, 2003, Timothy E. Flake filed a Complaint with the Occupational Safety and Health Administration (OSHA) alleging that his employer, New World Pasta Company (New World) suspended him from employment in November 2002 in violation of § 1514A(a). A Labor Department Administrative Law Judge (ALJ) issued a Recommended Decision and Order (R. D. & O.) granting summary judgment for New World. *Flake v. New World Pasta Co.,* ALJ No. 2003-SOX-00018 (July 7, 2003). The ALJ concluded that New World is not an employer covered by the corporate whistleblower provision. We concur.

BACKGROUND

Section 1514A protects employees of publicly traded companies who report securities fraud. It applies to two classes of publicly traded companies – companies required to register their securities under § 12, and companies required to register their securities under § 15(d) of the Securities Exchange Act of 1934 (Exchange Act):

> § 1514A. Civil Action to protect against retaliation in fraud cases
>
> (a) Whistleblower protection for employees of publicly traded companies. – **No company with a class of securities** registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. § 78*l*), or **that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. § 78o(d)),** or any officer, employee, contractor, subcontractor, or agent of such company, may discharge, demote, suspend, threaten, harass, or in any other manner discriminate against an employee in the terms and conditions of employment because of any lawful act done by the employee –
>
> (1) to provide information, cause information to be provided, or otherwise assist in an investigation regarding any conduct which the employee reasonably believes constitutes a violation of [certain securities statutes, rules, and regulations] relating to fraud against shareholders. . . . or
>
> (2) to file, cause to be filed, testify, participate in, or otherwise assist in a proceeding filed or about to be filed . . . relating to an alleged violation of [certain securities statutes, rules and regulations] relating to fraud against shareholders.

18 U.S.C.A. § 1514A (emphasis added).

The parties agree that New World is not subject to the whistleblower provision based on § 12 of the Securities Exchange Act. This dispute is whether New World is required to file reports under § 15(d) and is therefore subject to the whistleblower provisions of the Sarbanes-Oxley Act.

Section 15(d) requires companies ("issuers") to file information, documents, and reports with the Securities and Exchange Commission. But these reporting requirements

are "automatically suspended" when a company's securities are held at the beginning of the fiscal year by fewer than 300 persons:

> **15 U.S.C.A. § 78o(d) Filing of supplementary or periodic information**
>
> Each issuer which has filed a registration statement containing an undertaking which is or becomes operative under this subject as in effect prior to August 20, 1964, and **each issuer which shall after such date file a registration statement which has become effective pursuant to the Securities Act of 1933 as amended** . . . shall file with the [Securities & Exchange] Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, such supplementary and periodic information, documents, and reports as may be required pursuant to section 78m of this title in respect of a security registered pursuant to section 78*l* of this title. . . .
> The duty to file under this subsection shall also be automatically suspended as to any fiscal year, other than the fiscal year within which such registration statement became effective, if, at the beginning of such fiscal year, the securities of each class to which the registration statement relates are held of record by less than three hundred persons.

15 U.S.C.A. § 78o(d) (emphasis added). The parties agree that New World's securities have been held of record by less than three hundred persons since 1999.

Even so, Flake argues that SEC Rule 12h-3 is applicable. Rule 12h-3 provides, in relevant part:

> **Rule 12h-3 Suspension of Duty to file reports under section 15(d)**
>
> (a) Subject to paragraphs (c) and (d) of this section, the duty under section 15(d) to file reports required by section 13(a) of the Act with respect to a class of securities specified in paragraph (b) of this section shall be suspended for such class of securities immediately upon filing a certification on Form 15 (17 C.F.R. 249.323) if the issuer of such class has filed all reports required by section 13(a) . . . for the shorter of its most recent three fiscal years and the portion of the current year preceding the date of filing Form 15, or the period since the issuer became subject to such reporting obligation. If the certification on Form 15 is

> subsequently withdrawn or denied, the issuer shall, within 60 days, file with the Commission all reports which would have been required if such certification had not be filed.

17 C.F.R. § 240.12h-3 (2003).

Flake asserts that since New World has not filed Form 15, as the Rule dictates, it does not qualify for the suspension. In other words, New World is required to file the reports under § 15(d) and is therefore covered and liable under the whistleblower protection provisions of Sarbanes-Oxley. New World concedes it has not filed a Form 15 but argues that it is not subject to Rule 12h-3.

The ALJ concluded that New World's reporting requirements were suspended by operation of law in fiscal years 2000, 2001, 2002, and 2003. R. D. & O. at 4. The ALJ agreed with New World that Rule 12h-3 does not apply. *Id.* at 5.

DISCUSSION

We review a recommended decision granting summary decision de novo. That is, the standard the ALJ applies, which is prescribed in 29 C.F.R. § 18.40 (2003), also governs our review. *Somerson v. Mail Contractors of America*, ARB No. 03-042, ALJ No. 03-STAA-11 (ARB Oct. 14, 2003). The standard for granting summary decision under § 18.40 is essentially the same as that found in Fed. R. Civ. P. 56, the rule governing summary judgment in the federal courts. Summary decision is appropriate under § 18.40 if no genuine issue of material fact exists. *Somerson; Anderson v. Liberty Lobby, Inc.* 477 U.S. 242, 248 (1986).

As noted, the whistleblower protection provisions of Sarbanes-Oxley cover only companies with securities registered under § 12 or companies required to file reports under § 15(d) of the Exchange Act. Here the parties agree that New World is not subject to § 12 of the Securities Exchange Act. They also agree that in 1999 New World registered securities pursuant to the Securities Act of 1933 and that at the beginning of each fiscal year thereafter New World's securities were held of record by fewer than 300 persons. Therefore, unless, as Flake contends, an SEC rule such as 12h-3 applies, New World does not have to file reports pursuant to § 15(d) of the Exchange Act and is therefore not covered under the whistleblower protection portion of Sarbanes-Oxley.

New World counters Flake's assertion that Rule 12h-3 applies here. It argues that the rule applies only to companies that become eligible for suspension of reporting **during** a fiscal year based on the amount of their assets and number of shareholders. Companies like New World, which have fewer than 300 shareholders at the beginning of a fiscal year after the year in which the company registered its securities, are subject to a different SEC rule, Rule 15d-6. Rule 15d-6 does not condition eligibility for suspended reporting on filing of Form 15. Rule 15d-6 only requires that a company that suspends

reporting based on number of shareholders file a Form 15 within thirty days after the beginning of the fiscal year. *See* 17 C.F.R. § 240.15d-6.[1]

In support of this argument, New World cites an informal, non-binding interpretive SEC statement concerning the meaning of the term "issuer" in the Sarbanes-Oxley Act of 2002 and § 15(d) of the Exchange Act:

> Question 1: Section 2(a)(7) of the Sarbanes-Oxley Act of 2002 (the "Act") defines an "issuer" as an "issuer (as defined in Section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78(c)), the securities of which are registered under Section 12 of that Act (15 U.S.C. 78l), or that is required to file reports under Section 15(d) . . . ." A company has offered and sold debt securities pursuant to a registration statement filed under the Securities Act of 1933, thus subjecting it to the reporting requirements of Section 15(d). The company did not register the debt securities under Section 12 of the Exchange Act of 1934. Subsequently, the company's reporting obligations have been statutorily suspended under Section 15(d) because it had fewer than 300 security holders of record at the beginning of its fiscal year. The company has not filed a Form 15 and has continued to file reports pursuant to its indenture. Is the company considered an "issuer" under the Act?
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> Answer: **No. Because the issuer had fewer than 300 security holders of record at the beginning of its fiscal year, the suspension is granted by statute and is not contingent on filing a Form 15.** The definition of issuer applies only to issuers required to file reports. However, see Question 9 regarding these kinds of filers under Section 302 of the Act.

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[1] **Suspension of duty to file reports**.

> If the duty of an issuer to file reports pursuant to section 15(d) of the Act as to any fiscal year is suspended as provided in section 15(d) of the Act, such issuer shall, within 30 days after the beginning of the first fiscal year, file a notice on Form 15 informing the Commission of such suspension unless Form 15 has already been filed pursuant to Rule 12h-3.

17 C.F.R. § 240.15d-6 (2003).

http://www.sec.gov/divisions/corpfin/faqs/soxact2002.htm, SEC Division of Corporate Finance, "Sarbanes-Oxley Act of 2002 – Frequently Asked Questions," Nov. 8, 2002. (Emphasis added).

New World also cites an informal, non-binding interpretive statement in SEC's 1997 Telephone Interpretations Manual:

> 38. Rule 15d-6; Rule 12h-3; Form 15
>
> Section 15(d) of the Exchange Act provides an automatic suspension of the periodic reporting obligation as to any fiscal year (except for the fiscal year in which the registration statement became effective) if an issuer has fewer than 300 security holders of record at the beginning of such fiscal year. Under Rule 15d-6, a Form 15 should be filed to notify the Commission of such suspension, **but the suspension is granted by statute and is not contingent on filing the Form 15.** In contrast, Rule 12h-3 permits a company to suspend its reporting obligation under Section 15(d) if the requirements of the rule are met at any time during the fiscal year. Because situations exempted by Rule 12h-3 (e.g. fewer than 300 security holders of record in the middle of a fiscal year) do not meet the literal test of Section 15(d), Rule 12h-3 requires the filing of Form 15 as a condition of the suspension.

http://www.sec.gov/interps/telephone/1997manual.txt. (Emphasis added).

Flake argued that these statements should be disregarded because they are informal and non-binding. However, the SEC explained circumstances under which the automatic suspension goes into effect not only in the informal guidance New World cites, but also in notice and comment rulemakings. The Commission specifically addressed the difference between Rule 12h-3 and Rule 15d-6 when it amended Rules 12 and 15 to their present form. "Suspension of the duty to file reports [pursuant to Rule 12h-3] would be contingent on the filing of the form [15]." 48 Fed. Reg. at 48247 (Oct. 18, 1983) (proposed rule); promulgated as proposed at 49 Fed. Reg. 12688 (Mar. 20, 1984). "This would not be true of a suspension effected solely on the basis of the provision of Section 15(d) of the Exchange Act. In that case, failure to file the Form would be a violation of reporting requirements under the Exchange Act pursuant to Rule 15d-6." *Id*.

An agency's views expressed by notice and comment rulemaking are controlling when, as here, the statute expressly authorizes the agency to issue implementing rules and regulations. *United States v. Mead*, 533 U.S. 218 (2001). Thus, because the SEC has clearly indicated that § 15(d)'s automatic suspension goes into effect by operation of law

and a company's failure to file Form 15 has no effect on the automatic suspension, we conclude that Rule 12h-3 does not apply to New World.[2]

Flake also argues that we should interpret § 1514A to include any publicly traded company, regardless of size or value, because Congress had all publicly traded companies in mind when drafting the whistleblower provision. This argument assumes the untenable proposition that Congress did not know what it was doing when it limited coverage under § 1514A by reference to coverage provisions in the Securities Exchange Act. *See* 15 U.S.C.A. § 78*l* (value of assets and number of security holders); 15 U.S.C.A. § 78o(d) (number of security holders). *Cf.* 48 Fed. Reg. at 48245 ("Congress recognized, with respect to Section 15(d), that the benefits of periodic reporting by an issuer might not always be commensurate with the burdens imposed, particularly where smaller companies were involved"); 61 Fed. Reg. 21354 (May 9, 1996) ("The Commission has long recognized that the cost of compliance with Exchange Act reporting requirements is relatively greater for smaller companies than for larger ones. [footnote omitted] The amendments adopted today [raising § 12(g)'s assets threshold to reduce the number of issuers subject to reporting requirements] are designed to strike the appropriate balance between such costs and investors' needs for the information required in Exchange Act reports").

CONCLUSION

Accordingly, we dismiss the Complaint because no genuine issue of material fact exists as to whether the whistleblower protection provision of the Sarbanes-Oxley Act applies to New World, and New World is entitled to judgment as a matter of law.

SO ORDERED.

OLIVER M. TRANSUE
Administrative Appeals Judge

M. CYNTHIA DOUGLASS
Chief Administrative Appeals Judge

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[2] *See also* PLI "Registration and Reporting under the Securities Exchange Act of 1934" (2003) § 1.3 (Rule 15d-6 provides that "if the duty [under § 15(d)] is automatically suspended, the issuer shall, within 30 days after the beginning of the first fiscal year file a Form 15 informing the SEC of such suspension unless a Form 15 was already filed pursuant to Rule 12h-3").