Federal Court Rejects Mutual Fund Excessive Fee Claims

On February 27, 2007, the federal trial court for the Northern District of Illinois granted summary judgment in favor of a mutual fund adviser, rejecting shareholders' claims of excessive management fees under Section 36(b) of the Investment Company Act. This decision appears to mark the first time a court has granted summary judgment in a Section 36(b) excessive fee case, rejecting the plaintiffs' claims on the merits without a trial following full discovery.

The plaintiffs' main theory of liability in these cases is that fund advisers achieve significant economies of scale as funds grow in size, and that these cost savings are not adequately passed along to shareholders through breakpoints or other fee reductions. As evidence of this, plaintiffs rely heavily on differences between the fees that advisers charge to mutual funds and what they charge to institutional and sub-advisory clients.

In rejecting these claims, the judge made several key rulings that affirm the limited role of the court in reviewing the fees negotiated by independent trustees:

- Mutual fund fees are the result of a give-and-take negotiation. There is no single correct outcome for this process. Instead, "there is a range of acceptable results."
- It is not the court's job to determine whether the trustees negotiated the lowest possible fees. The fees are subject to challenge only if they are not within the range of fees that could be expected to result from arm's-length bargaining. Plaintiffs must therefore show a "fundamental disconnect" between the fees paid and what the services were worth.
- The fact that an adviser charges higher fees to manage a mutual fund than it charges to manage institutional or sub-advisory accounts does not demonstrate that the fund fees are excessive. Evidence that others paid different amounts for similar services does not allow an inference that the fund paid fees outside the range of what could result from arm's-length bargaining.

This suit is one of a large group of virtually identical cases brought by a consortium of plaintiffs' firms against various fund advisers in courts around the country, many of which are still pending. Ropes & Gray litigators John Donovan and Rob Skinner led the team that achieved this victory on behalf of the adviser defendant.

For the full text of the court's decision in *Jones v. Harris Associates L.P.*, please click here.

Contact Information

If you have any questions or would like to learn more about the issues raised in the court's decision, please contact the Ropes & Gray lawyer who normally represents you or one of the following Ropes & Gray litigators involved in the case:

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