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CASE ALERT
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NCLC Urges Supreme Court Not To Permit Litigation Explosion Concerning Mutual Fund Fees

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Today, the National Chamber Litigation Center (NCLC) filed an *amicus* brief in the United States Supreme Court in *Jones v. Harris Associates, L.P.*, urging the court to affirm the Seventh Circuit's decision in favor of a mutual fund adviser and to adopt a standard for lawsuits alleging the receipt of unlawfully "excessive" fees by mutual fund advisers that is supported by the language and purpose of the Investment Company Act and that would prevent a tidal wave of litigation aimed against fund advisers.

The plaintiffs in Jones are shareholders in certain of the Oakmark family of mutual funds, for which Harris Associates served as investment adviser. The complaint alleges that Harris breached its fiduciary duty with respect to the management fees it received from the funds for its services, and thereby violated Section 36(b) of the Investment Company Act. Among other alleged misdeeds, plaintiffs claim that Harris did not provide complete information to the fund boards during the fee negotiation process and charged the funds higher fees than Harris charged to institutional clients.

In 2007, the district court granted summary judgment for Harris, applying the standard laid out by the Second Circuit in its 1982 decision, *Gartenberg v. Merrill Lynch Asset Management, Inc*. Finding that the fees charged to the Oakmark funds were not "so disproportionately large that they could not have been the result of arm's-length bargaining between Harris and the [fund's] board," the court dismissed the case. Plaintiffs appealed.

The Seventh Circuit affirmed the judgment for Harris, holding that an adviser has a fiduciary duty to make full disclosure to a fund's board of directors and "play no tricks," but that the adviser is not subject to a court-imposed cap on its compensation. Instead, it is the role of the fund's directors, who approve the fees, and investors, who are free to move their money elsewhere, to determine the proper value of the advisory services rendered.

Following the Seventh Circuit's decision, plaintiffs moved for a rehearing of their appeal *en banc*. This motion was denied over a strongly-worded dissent from Judge Posner, who wrote that marketplace competition cannot be trusted to police compensation levels. The Supreme Court granted *certiorari* to resolve a perceived split among the circuit courts as to the proper standard

for assessing claims that fund advisers breached their fiduciary duties with respect to the receipt of compensation for their services.

In its *amicus* brief, NCLC argued that plaintiffs' expansive approach, which would hold advisers liable for procedural flaws in the fee negotiation process even where the fee arrived at was competitive, is contrary to the language of the Investment Company Act and related statutes, and would improperly encroach on the SEC's exclusive authority to regulate aspects of mutual fund and investment adviser behavior. NCLC also warned that plaintiffs' approach would open the floodgates of vexatious litigation against funds with modest fees and above-average performance. NCLC urged an approach that would enable defendants and courts to dismiss meritless claims early on. It is particularly important that frivolous suits are disposed of prior to expensive and time-consuming discovery, because it is ultimately mutual funds and their shareholders that will suffer those burdens.

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The National Chamber Litigation Center is the leading voice of business in the courts. For more information about this and other NCLC litigation, please contact Amar Sarwal, (202) 463-5337, asarwal@uschamber.com.