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Supreme Court Adopts Standard for Assessing Mutual Fund Fees

On March 30, 2010, the Supreme Court issued its decision in Jones v. Harris Associates, *which addressed mutual fund fee issues under the Investment Company Act of 1940. Although arising in a non-ERISA context, the Court's holding may have relevance for retirement plan fiduciaries.*

Background

In recent years there has been much litigation involving fees paid by retirement plans to providers of administrative services and investment advice. This litigation has commonly focused on the ERISA fiduciary duties applicable to the selection of service and investment providers, the payment of fees to these providers, and the disclosure of fees to plan participants.

Jones v. Harris Associates

In *Jones v. Harris Associates*, the Supreme Court addressed the standard to be applied under the Investment Company Act of 1940 (ICA) in reviewing whether fees charged by investment advisers to a mutual fund were excessive. Rejecting the conclusion reached by the U.S. Court of Appeals for the Seventh Circuit that the ICA generally requires only fair and open dealings regarding the disclosure of fees, the Supreme Court instead adopted the approach applied by the U.S. Court of Appeals for the Second Circuit in *Gartenberg v. Merrill Lynch Asset Management.* Under the *Gartenberg* standard, the party claiming the fiduciary breach bears the burden of proving the investment advisor charged "a fee that is so disproportionately large that it bears no reasonable relationship to the services rendered and could not have been the product of arm's length bargaining." The Supreme Court notes that a measure of deference to the board's judgment to approve fees is appropriate in some instances. Further, the appropriate measure of deference varies depending on the circumstances – e.g., the rigor of the board's review and the degree to which it considered certain factors. The Court stated that there can be no categorical rule on comparisons of fees charged to different clients, and courts "should be wary of inapt comparisons" as the services provided by investment advisers may be different.

Applicability to ERISA Plans

While the *Jones v. Harris Associates* case did not arise in the context of retirement plan investment-related fees, the *Gartenberg* standard the Court adopted has been applied by a lower court in at least one unreported ERISA excessive fee case. The Supreme Court's decision may influence future litigation regarding the standard to be applied in excessive fee cases involving retirement plans.

What Should Retirement Plan Fiduciaries Be Doing Now?

A retirement plan with a well-designed approach to complying with ERISA's fiduciary duty requirements should have a comprehensive set of processes and procedures to evaluate and retain providers of administrative and investment-related services. In light of the Supreme Court's ruling, it may be useful to review these procedures. To the extent that a plan currently relies on market-based investment fees in negotiating with service providers, it may be prudent to conduct an additional level of analysis to determine whether the actual fees to be charged to the plan bear a reasonable relationship to the services that will be received by the plan.

As part of an overall ERISA fiduciary duty compliance strategy, it may also be useful to review the fee structures in existing relationships with plan service providers and existing plan fee disclosure policies.

Conclusion

Buck's consultants would be pleased to discuss this decision with you and help assure that your plans are in compliance with fiduciary duty requirements.

This FYI is intended to provide general information. It does not offer legal advice or purport to treat all the issues surrounding any one topic.