

1           IN THE SUPREME COURT OF THE UNITED STATES

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3   JERRY N. JONES, ET AL.,                        :

4                            Petitioners                        :

5                    v.                                        :   No. 08-586

6   HARRIS ASSOCIATES L.P.                        :

7   - - - - - x

8    Washington, D.C.

9    Monday, November 2, 2009

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11                           The above-entitled matter came on for oral  
12 argument before the Supreme Court of the United States  
13 at 10:04 a.m.

14 APPEARANCES:

15 DAVID C. FREDERICK, ESQ., Washington, D.C.; on behalf of  
16 the Petitioners.

17 CURTIS E. GANNON, ESQ., Assistant to the Solicitor  
18 General, Department of Justice, Washington,  
19 D.C.; on behalf of the United States, as amicus  
20 curiae, supporting the Petitioners.

21 JOHN D. DONOVAN, JR., ESQ., Boston, Mass.; on behalf of  
22 the Respondent.

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P R O C E E D I N G S

(10:04 a.m.)

CHIEF JUSTICE ROBERTS: We will hear argument first this morning in Case 08-586, Jones v. Harris Associates.

Mr. Frederick.

ORAL ARGUMENT OF DAVID C. FREDERICK

ON BEHALF OF THE PETITIONERS

MR. FREDERICK: Thank you, Mr. Chief Justice, and may it please the Court:

In 1970, Congress amended the Investment Company Act to provide a cause of action when an investment adviser breaches its fiduciary duty with respect to compensation.

The Seventh Circuit upheld summary judgment for Respondent under a legal standard for fiduciary duty that Respondent here no longer defends.

For three reasons, the Seventh Circuit's judgment should be reversed. First, under the Court's longstanding precedent, in this context a fiduciary duty requires a fair fee, achieved through full disclosure and good-faith negotiation.

Second, the best gauge of a fair fee is what the investment adviser charges at arm's-length in other transactions for similar services.

1           And, third, applying that standard here,  
2 Harris charged twice as much in percentage terms for  
3 providing virtually identical advisory services in  
4 arm's-length transactions with institutional investors.

5           With respect to the first point, the  
6 standard for fiduciary duty has been clear from this  
7 Court's cases, at least since *Pepper v. Litton*, in which  
8 the Court said that a fair result in the  
9 circumstances -- a fair fee -- was an important  
10 component of a fiduciary duty.

11           Congress was aware of that standard when it  
12 enacted the 1970 amendments to the Investment Company  
13 Act. The SEC brought the case to the Congress'  
14 attention, and that standard, we submit, is one that  
15 Congress intended to incorporate.

16           Applying that standard, where *Pepper* said  
17 that the best gauge of a fair fee is what the person --  
18 the fiduciary charges in arm's-length transactions,  
19 applied here, the best way to understand how that  
20 fiduciary duty is being breached in this context is what  
21 Harris is charging for same or similar services at  
22 arm's-length to institutional investors.

23           JUSTICE KENNEDY: Is Harris a fiduciary in  
24 the same sense as a corporate officer and a corporate  
25 director? Or does his fiduciary duty differ? Is it

1 higher or lower, same with a guardian, same with a  
2 trustee?

3 I mean, the word "fiduciary" -- does  
4 fiduciary imply different standards, depending on what  
5 kind of fiduciary you are?

6 MR. FREDERICK: The basic concept,  
7 Justice Kennedy, is the same. There are two components,  
8 where there must be full disclosure of information and a  
9 fair result, and that fair result translates in  
10 different contexts in different ways. Here, because of  
11 the statutory references to fiduciary duty with respect  
12 to compensation, one focuses on the fairness of the fee  
13 charged.

14 But, as Professor Dumont points out in her  
15 amicus brief, the idea of a fiduciary duty is one that  
16 is well known in various circumstances of the law, and  
17 as applied here the concept goes to the fairness of the  
18 fee.

19 JUSTICE KENNEDY: Well, would the test for  
20 compensation in this case be the same as any director or  
21 any officer of a corporation?

22 MR. FREDERICK: The difference here, Justice  
23 Kennedy, is that in those circumstances the indicia of  
24 an arm's-length transaction may be achieved. The  
25 directors can fire the head of a company. They can call

1 for changes.

2 Here, the investment adviser has appointed  
3 the members of the board. As this Court said in the  
4 Daily Income Fund case, the earmarks of an -- of an  
5 arm's-length transaction are absent precisely because --

6 JUSTICE KENNEDY: I just want to know, is  
7 the fiduciary duties the same? Is the fiduciary  
8 standard the same, without getting into how its applied?

9 Is the fiduciary standard the same for  
10 Jones, for a guardian, for a trustee, for a corporate  
11 officer or a corporate director, always the same?

12 MR. FREDERICK: Yes. The concept is fair  
13 result through full information and good-faith  
14 negotiations.

15 JUSTICE SCALIA: And for lawyers?

16 MR. FREDERICK: For lawyers --

17 JUSTICE SCALIA: Lawyers have a fiduciary  
18 obligation to their clients; right?

19 MR. FREDERICK: That is true.

20 JUSTICE SCALIA: So courts should review  
21 lawyers' fees for -- on the basis of whether it's a fair  
22 result.

23 MR. FREDERICK: That is how courts do it  
24 every day in this country, Justice Scalia, when they are  
25 asked to make fee applications for reasonableness.

1 CHIEF JUSTICE ROBERTS: Well, but this is  
2 different. I mean, this is part of an expense of a  
3 fund. They don't get fees, but -- but they get -- they  
4 have to pay for the lawyers, just like they have to pay  
5 for management advice.

6 So why wouldn't you review the lawyers' fees  
7 to make sure they are fair?

8 MR. FREDERICK: The lawyers' fees in which  
9 context, Mr. Chief Justice? I'm not sure I understand  
10 the question.

11 CHIEF JUSTICE ROBERTS: Counsel for the  
12 fund.

13 MR. FREDERICK: Counsel for the fund is --  
14 that is actually not at issue here, but the issue of  
15 what constitutes reasonable expenses may arise in  
16 various circumstances.

17 The statute prohibits fees that are  
18 unreasonable in terms of their unfairness to the fund.  
19 The concept here is that the board cannot fire the  
20 investment adviser. So in evaluating the fairness of  
21 the fee the adviser is charging the fund, the normal  
22 indicia of an arm's-length transaction is absent, and  
23 that is the key principle here because this adviser is  
24 using the same manager to provide the same research  
25 analytics from the same research group, from the same

1 meetings, buying the same stocks, and simply allocating  
2 them to different accounts and charging those to whom it  
3 owes a fiduciary duty twice what it is getting at  
4 arm's-length.

5 JUSTICE GINSBURG: But there was in this  
6 record, was there not, a submission by the adviser  
7 comparing what mutual funds this fund was charged, what  
8 institutional funds were charged, but explaining the  
9 differential in terms of the services provided, that  
10 more services were provided to the fund and less  
11 services were provided to the institutional investors.

12 MR. FREDERICK: And, Justice Ginsburg, that  
13 is where there is a disputed issue of fact for which  
14 summary judgment is not appropriate, because the  
15 plaintiffs submitted evidence that in fact the services  
16 provided to the institutional investors were greater,  
17 even though they were being charged a lower amount of  
18 money.

19 JUSTICE GINSBURG: Who would have the  
20 burden? You said that is an issue that has not been  
21 decided, it's a disputed issue of fact, appropriate for  
22 remand. Who -- would you have the burden if they came  
23 forward and said, look, this is what our situation is.  
24 These are the services. Would you have the burden to  
25 show that in fact they were comparable and the



1 differences did not warrant the differences in the fee?

2 MR. FREDERICK: Yes.

3 JUSTICE GINSBURG: You would have the  
4 burden?

5 MR. FREDERICK: We have the burden.

6 JUSTICE SCALIA: That's different from  
7 normal trust law, isn't it?

8 MR. FREDERICK: It is.

9 JUSTICE SCALIA: Normally where you are a  
10 fiduciary, it's up to you to prove that it was  
11 reasonable.

12 MR. FREDERICK: That's true.

13 JUSTICE SCALIA: So Congress evidently did  
14 not mean ordinary trust law to apply in this context.

15 MR. FREDERICK: We disagree with that last  
16 part, Justice Scalia. We agree that Congress did make  
17 modifications to the way a cause of action ordinarily  
18 would have been brought at common law for breach of  
19 fiduciary duty in several respects, including imposing  
20 the burden of proof on the investor. Where we disagree  
21 is that when they used the phrase "fiduciary duty" they  
22 intended to mean something less than what fiduciary duty  
23 had meant at common law.

24 CHIEF JUSTICE ROBERTS: What if -- if you  
25 are having courts decide -- review what is fair, a fair

1 fee, what if the adviser had given such good advice that  
2 the fund beat the industry average for his category of  
3 fund by 5 percent over the last 5 years. Does he get  
4 double the normal compensation of the average fees?  
5 Does he get triple? 50 percent more? How is the court  
6 supposed to decide that?

7 MR. FREDERICK: Well, there is an issue of  
8 fact as to how relevant performance is. They didn't  
9 give the money back when their performance lagged behind  
10 the market, Mr. Chief Justice, in this case. So the  
11 question of whether or not a performance metric is  
12 relevant is certainly a factor that will be entitled to  
13 less --

14 CHIEF JUSTICE ROBERTS: Well, surely you  
15 think it is. When you say they don't give the money  
16 back, you are not suggesting that the amount of the fees  
17 should be the same regardless of whether they outperform  
18 by 10 percent or not?

19 MR. FREDERICK: My point, Mr. Chief Justice,  
20 is that when they charge the same amount, buying the  
21 same stocks, to institutional investors and achieve the  
22 same performance, there is no reason why the mutual fund  
23 should be charged twice as much.

24 CHIEF JUSTICE ROBERTS: Well, but there is  
25 different parameters, right, in the sense that you're

1 trying -- the company is trying to attract investors to  
2 the mutual fund. If you are advising a pension fund, it  
3 is not the case that they are trying to attract  
4 pensioners who have other choices.

5 MR. FREDERICK: But the investor doesn't  
6 gain because of the marketing skill of the adviser.  
7 Simply having a larger asset pool which increases the  
8 fee that the adviser can charge doesn't inure to the  
9 individual benefit of the investor. And the point of  
10 this statute was to provide protection against investors  
11 so that when the adviser charged excessive fees that  
12 excess would be returned to the fund for the pro  
13 rata benefit --

14 JUSTICE KENNEDY: You said that Congress  
15 used "fiduciary" in a special sense. Then -- then, I  
16 have to conclude that your earlier answer is confusing  
17 for me, because I thought you were going to tell us that  
18 this investment adviser has the same fiduciary standard  
19 that officers and directors of corporations have. Then  
20 you say that Congress used it in this special sense. So  
21 that doesn't quite square.

22 MR. FREDERICK: Well, Justice Kennedy, let  
23 me just add the extra words of the statute, because what  
24 Congress said was a fiduciary duty "with respect to  
25 compensation." And so when I say special sense, I mean

1 that Congress used additional words to elaborate on the  
2 circumstance in which the fiduciary duty would be  
3 examined.

4 Here what is happening is that an  
5 arm's-length transaction for the same services -- the  
6 same manager is going out and touting his services to  
7 the institutional investor, but simply charging them  
8 half as much money for providing the same portfolio of  
9 management.

10 CHIEF JUSTICE ROBERTS: Do technological  
11 changes make a difference in terms of disclosures  
12 required? These days all you have to do is push a  
13 button and you find out exactly what the management fees  
14 are. I mean, you just look it up on Morningstar and  
15 it's right there and you can make -- as an investor you  
16 can make whatever determination you'd like, including to  
17 take your money out.

18 MR. FREDERICK: The fact that an investor  
19 may know going in what the fee is does not address the  
20 problem Congress was intending to address, which is that  
21 as larger and larger sums of assets were accreted to the  
22 mutual fund, the investor was not obtaining the benefits  
23 of economies of scale. And that's the central point --

24 CHIEF JUSTICE ROBERTS: So we could look  
25 at -- you know, as the fund grows bigger and he doesn't

1 get those benefits he can go look at another fund. It  
2 takes 30 seconds.

3 MR. FREDERICK: And that again doesn't  
4 address the problem Congress was trying to get at, which  
5 is to protect the company, not the individual investor.  
6 The individual investor might lessen the damages that  
7 that investor suffers, but the fund, the people  
8 remaining, continue to pay excessive fees.

9 JUSTICE SCALIA: No, but he protects the  
10 company ultimately, because when investors leave the  
11 company that is charging excessive fees to go to other  
12 companies, the company that they are leaving sees that  
13 something's wrong and has to lower its compensation to  
14 its adviser. Why doesn't that affect the company at  
15 issue?

16 MR. FREDERICK: A large number of assets  
17 under management in mutual funds, something like 26 to  
18 35 percent according to materials that are in the  
19 record, are from 401(k) plans, where the investor is  
20 essentially locked into the fund that his or her company  
21 chooses to make that investment. And even as to  
22 investors who are not locked in, there are significant  
23 tax consequences where over time an investor might be in  
24 the Oakmark Fund and have to suffer large tax  
25 consequences in order to get the benefit of the

1 statute --

2 CHIEF JUSTICE ROBERTS: Companies --  
3 companies change who they invest with under the 401(k)'s  
4 all the time. The employees are not happy with the  
5 return they are getting because the company has limited  
6 their choices, they change. It happens all the time.

7 MR. FREDERICK: And Mr. Chief Justice, as  
8 the Court recognized in the Daily Income Fund case, this  
9 is a unique cause of action in which Congress was  
10 intending to protect the entire corpus of the investors  
11 in the fund, because --

12 CHIEF JUSTICE ROBERTS: You told me just a  
13 little while ago, or told somebody, Congress wasn't  
14 interested in protecting investors; they were interested  
15 in protecting the companies.

16 MR. FREDERICK: The company is comprised of  
17 the investors, Mr. Chief Justice. What the right of  
18 action does not do is to provide individual damages to  
19 the investor who brings the suit. The recovery inures  
20 to the entire benefit of all the investors.

21 JUSTICE SOTOMAYOR: Counsel, can I unpackage  
22 your argument a little bit. Because using the word  
23 "fair fee" in my mind is meaningless, because it has to  
24 be fair in relationship to something. And so what is  
25 your definition of what that something is that it's fair

1 to, and -- or unfair against? And start from there,  
2 because I understood the Seventh Circuit to be saying:  
3 Look, a fair fee is paying market value. If one takes a  
4 sort of reading -- whatever negotiation goes on between  
5 the two, as long as there has been full disclosure as  
6 required, that's the market. So that's fair. You're  
7 saying it's something else. What's that something else?

8 MR. FREDERICK: Well, what the Court said in  
9 pepper is that fair is what is reflective of what an  
10 arm's-length agreement would produce.

11 JUSTICE SOTOMAYOR: All right. So you start  
12 there.

13 MR. FREDERICK: Yes.

14 JUSTICE SOTOMAYOR: All right. So let's  
15 stop confusing this -- the articulation of the standard,  
16 which is -- that's fair. What would an arm's-length  
17 transaction produce? And let's go to what seems to be  
18 part of your argument and sort of what everyone's  
19 skirting around, which is what's the proof that a  
20 particular transaction is not arm's-length?

21 The Seventh Circuit appeared to be saying,  
22 it's arm's-length when the parties have done all of the  
23 disclosure that is required, because then the buyer can  
24 decide whether they want to pay that fee or not, and  
25 once they choose to it's a fair price. It's an arm's-

1 length transaction. You are saying not, and that's  
2 what -- that's where I am trying to get to the nub of  
3 why not? Why is --

4 MR. FREDERICK: Because the directors can't  
5 fire and walk away from the advisor. In any arm's-  
6 length transaction, if I sell you a car and you don't  
7 like the price can you walk away.

8 JUSTICE SOTOMAYOR: That's -- now, that's  
9 begging the question, because Congress hasn't said a  
10 reasonable fee. It did say fiduciary duty, but it  
11 didn't -- there is a subtle but very important  
12 difference between reasonable and -- a reasonable fee  
13 and a fiduciary duty with respect to fees.

14 MR. FREDERICK: True. There are two  
15 components: Was there full information and good faith  
16 negotiating; and was the result fair. In Pepper, the  
17 Court said if the result is not fair there can be a  
18 breach of fiduciary duty.

19 JUSTICE SOTOMAYOR: I'm still begging the  
20 question, fair against what.

21 MR. FREDERICK: Fair against what the  
22 adviser actually charged for same or similar services to  
23 an outsider who had the right to walk away.

24 JUSTICE SCALIA: Mr. Frederick, I don't  
25 understand your statement that they can't fire the



1 investment adviser. Maybe they can't fire him, but they  
2 can insist that he accept a lower fee, right? Surely  
3 they can do that, can't they?

4 MR. FREDERICK: They --

5 JUSTICE SCALIA: Can they insist that he  
6 accept a lower fee? Can they do that.

7 MR. FREDERICK: In practical terms, no.

8 JUSTICE SCALIA: Why?

9 MR. FREDERICK: Because the adviser picks  
10 the board of directors.

11 JUSTICE SCALIA: Oh, no, that's something  
12 different. Let's assume you have a disinterested board  
13 of directors, which is what the statute requires. You  
14 tell me even though they are disinterested, they can't  
15 fire the adviser. It seems to me, while they can't fire  
16 him, they can say: We are going to cut your fee in  
17 half. Whereupon they don't have to fire him. He will  
18 pack up and leave, and they will get a new adviser.  
19 Doesn't that work?

20 MR. FREDERICK: There is actually no  
21 evidence in any record I am aware of where that has  
22 actually happened. The directors have no leverage. And  
23 that's the problem the Court -- this Court recognized in  
24 the Daily Income Fund case.

25 If I could reserve the balance of my time,

1 please.

2 CHIEF JUSTICE ROBERTS: Thank you, counsel.

3 Mr. Gannon.

4 ORAL ARGUMENT OF CURTIS E. GANNON

5 ON BEHALF OF THE UNITED STATES,

6 AS AMICUS CURIAE,

7 SUPPORTING THE PETITIONERS

8 MR. GANNON: Mr. Chief Justice, and may it

9 please the Court:

10 The fiduciary duty imposed by section 36(b)  
11 prohibits an investment adviser's fee from being outside  
12 the range that arm's-length bargaining would produce.  
13 The courts below erred by failing to consider evidence  
14 about what the investment adviser in this case charges  
15 its unaffiliated clients when it provides services that  
16 Petitioners claim are, in fact, comparable to the  
17 services at issue here.

18 JUSTICE KENNEDY: Do you think Congress used  
19 the term "fiduciary" in a very special sense here? I  
20 will just tell you the problem I'm having with the case.  
21 If I look at a standard that the fees must be reasonable  
22 and I compare that with what a fiduciary would do, I  
23 thought a fiduciary has the highest possible duty. But  
24 apparently the submission is the fiduciary has a lower  
25 duty, a lesser duty than to charge a reasonable fee. I

1 just find that quite a puzzling use of the word  
2 "fiduciary."

3 Now, if Congress uses it as a term of art or  
4 in some special sense, fine.

5 MR. GANNON: Well, we do think that --

6 JUSTICE KENNEDY: But it seems to me an odd  
7 use of the term "fiduciary." I don't know why Congress  
8 didn't use some other word.

9 MR. GANNON: Well, we do think that the term  
10 "fiduciary duty" is here used to counterbalance the lack  
11 of arm's-length bargaining that exists between the board  
12 of directors and the investment adviser, and we do think  
13 that it drew upon the established term of art in  
14 *Pepper v. Litton*, the case that counsel for Petitioners  
15 was already referring to. That's a case that actually  
16 involved corporate directors and there the same test,  
17 the same ultimate standard, was stated, which is whether  
18 the bargain carries the earmarks of an arm's length  
19 bargain and whether it's inherently fair.

20 And so we do think that in the development  
21 of the legislation in 1969, the memorandum that the SEC  
22 submitted to Congress in 1969 explained that the shift  
23 from reasonableness to fiduciary duty largely achieved  
24 some procedural objectives of shifting the focus from  
25 the board of directors to the investment adviser, and

1 the text of the statute specifically makes it a  
2 fiduciary duty with respect to receipt of compensation.

3 We think one salutary affect of that was to  
4 -- to make it clear that the Court's burden here, the  
5 Court's duty here, wasn't just to establish what the  
6 single most reasonable fee would be, but harking back to  
7 the Pepper v. Litton test, whether the bargain fell  
8 within the range of what arm's length bargaining  
9 otherwise would have achieved.

10 CHIEF JUSTICE ROBERTS: Counsel, if we are  
11 going to have regulation of what fees can be charged,  
12 you cite in your brief the various regulations the SEC  
13 has issued. It makes a lot more sense to have the SEC  
14 regulate rates than to have courts do it, doesn't it?

15 MR. GANNON: Well, in the abstract, it might  
16 make more sense, Mr. Chief Justice. I think the choice  
17 that Congress made here was to counterbalance the --

18 CHIEF JUSTICE ROBERTS: You are not  
19 suggesting the SEC wouldn't have authority to do that,  
20 are you?

21 MR. GANNON: Well, even under this statute,  
22 the SEC has the authority to file suits under section  
23 36(b).

24 JUSTICE GINSBURG: Has it filed any?

25 MR. GANNON: It hasn't filed any since --

1 since 1980, Justice Ginsburg. I think that the SEC in  
2 this context -- it has -- it has primarily directed its  
3 resources and energies into encouraging there to be  
4 better disclosure of fees, both the disclosure of  
5 information to the board, disclosure to investors,  
6 better education to shareholders so that they would be  
7 able to go --

8 JUSTICE SCALIA: Well, it must be aware of  
9 the -- of the divergence between the fees that  
10 investment advisers charge to these companies and what  
11 they charge to other clients. Isn't the SEC aware of  
12 that?

13 MR. GANNON: It is aware of that.

14 JUSTICE SCALIA: And yet has brought no  
15 suits against this industry?

16 MR. GANNON: Since 1980 it hasn't used  
17 section 36(b). It has used less formal mechanisms in  
18 the context of examinations and investigators -- -

19 JUSTICE SCALIA: For disclosure, just for  
20 disclosure. But that suggests to me that the SEC may  
21 think that this is indeed a self-contained industry and  
22 that the comparison with investment advice given to  
23 other entities is -- is not a fair one.

24 MR. GANNON: Well, when the SEC helped draft  
25 the statute in the 1960s, it recognized that there was

1 this systematic disparity between the amounts that  
2 mutual funds were being charged by investment advisers  
3 and the amounts that investment advisers were charging  
4 their unaffiliated clients, and in the 1969 memorandum  
5 that I referred to, which is reprinted in an appendix to  
6 the amicus brief by John Bogel in its entirety, the SEC  
7 mentioned that comparison as being something that may  
8 well be relevant in proving in an individual case that  
9 that particular investment adviser's fees are excessive.

10           And we think that the test here of whether  
11 under all the circumstances, which is what section  
12 36(b)(2) points the Court towards, of having to weigh --  
13 having to weigh the board's approval of fees in light of  
14 all the circumstances, that those circumstances include  
15 things like the evidence that petitioners have presented  
16 here.

17           JUSTICE GINSBURG: Mr. Gannon, the -- all  
18 the circumstances, that comes from the Second Circuit's  
19 Gartenberg case?

20           MR. GANNON: Well, it also comes,  
21 Justice Ginsburg, from the text of section 36(b)(2).

22           JUSTICE GINSBURG: But in -- in that case,  
23 at least there was a footnote that seemed to say, you  
24 don't have to engage in a -- in the comparison with what  
25 institutional investors are paid.

1           MR. GANNON: The footnote that you are  
2 talking about did point out that in that case the  
3 comparison that the plaintiffs were attempting to draw  
4 between the money market fund at issue and a pension  
5 fund wasn't a particularly relevant one, because the  
6 services at issue were so different. And here the  
7 parties appear to dispute how different the services  
8 are. And at the summary judgment stage, the Respondent  
9 stated that it disputed how comparable the relevant  
10 services were.

11           The district court and the court of appeals  
12 considered that dispute immaterial because, instead of  
13 comparing, instead of determining whether this  
14 investment adviser is selling the same services at half  
15 the price to its unaffiliated clients who actually can  
16 engage in arm's length bargaining, those courts simply  
17 said that if it -- if it falls within the range that is  
18 charged by other mutual funds, that would be acceptable.  
19 And we --

20           CHIEF JUSTICE ROBERTS: Counsel, the statute  
21 does not say, in considering the rates you look at all  
22 the circumstances. Am I right? It says, in considering  
23 whether to defer to the board, you look at all the  
24 circumstances.

25           MR. GANNON: It does say that you should

1 give the board --

2 CHIEF JUSTICE ROBERTS: The board.

3 MR. GANNON: -- such consideration as is  
4 deemed appropriate under all the circumstances. That's  
5 correct.

6 CHIEF JUSTICE ROBERTS: Right. But isn't  
7 that different than saying, in looking at what the rates  
8 should be or whether they are excessive, you look at all  
9 the circumstances? It may well be that you don't defer  
10 to the board, but that doesn't mean it's a free-for-all  
11 in deciding what you do look at.

12 MR. GANNON: Well, I think that it  
13 demonstrates that the Court is obligated to look to all  
14 the circumstances simply to determine whether the  
15 board's approval -- how much weight it should be given.

16 And as this Court explained in Daily Income  
17 Fund, the entire point of section 36(b) is to provide an  
18 independent check, the -- independent of the fact that  
19 the directors approved the fees. We think that an  
20 appropriately informed board that asks the right  
21 questions, that gets the right information and fully  
22 considers the sort of factors that are discussed --

23 JUSTICE SOTOMAYOR: Even if they agree to  
24 pay double the price?

25 MR. GANNON: We think that -- that the right



1 process followed by the board would be probative, but  
2 something like double the price may -- may demonstrate  
3 that that is an unfair bargain.

4 JUSTICE SOTOMAYOR: That -- that's what --  
5 are you advocating that there is a stand-alone cause of  
6 action or breach of duty when there isn't full  
7 disclosure, even if the fee is within arm's length --  
8 normal -- begging the question of what's normal, but  
9 assuming that it's within an arm's-length transaction  
10 range in the market?

11 MR. GANNON: If there was a lack of full  
12 disclosure, that might in the abstract be a breach of  
13 fiduciary duty even under the Seventh Circuit's test.  
14 We think that if it didn't actually have an effect on  
15 the fees, then it wouldn't be actionable here because  
16 there would be no actual damages flowing from the lack  
17 of disclosure.

18 JUSTICE SCALIA: But even if there is full  
19 disclosure, your position is in every case a court must  
20 decide whether the fee is reasonable or not.

21 MR. GANNON: A court would need to decide  
22 whether the plaintiff has met its burden of proving that  
23 it falls outside the range of fees that arm's-length  
24 bargaining would have arrived at, and that's a cause of  
25 action that would be --

1 JUSTICE SOTOMAYOR: Well, how much deviance,  
2 and what is the scope of the range?

3 MR. GANNON: Well, I think that the term of  
4 art of "fiduciary duty" doesn't necessarily demonstrate  
5 how much deviance away from the range there would be. I  
6 think that depending upon the segment of the market the  
7 range might be more or less narrow.

8 In segments of the market where services are  
9 more commodified and standardized, perhaps with index  
10 funds, there might be a much narrower range of fees that  
11 are arrived at through arm's-length bargaining, and even  
12 -- and smaller disparities might be inappropriate there.

13 JUSTICE KENNEDY: How is the -- how is the  
14 standard you've just described different from a standard  
15 of reasonableness?

16 MR. GANNON: It -- I think that the chief  
17 way it differs from reasonableness, Justice Kennedy, is  
18 in saying that the Court doesn't actually have to decide  
19 what the single most reasonable fee is. But as the SEC  
20 explained in 1969, the shift from reasonableness to --

21 JUSTICE KENNEDY: Well, I would be very  
22 surprised if "reasonableness" always meant one -- one  
23 figure. It could mean a range.

24 MR. GANNON: Well, I think reasonableness  
25 is - is inevitably going to be part of the inherent

1 fairness inquiry that this Court referred to in Pepper  
2 v. Litton as being part of the fiduciary duty status as  
3 to whether the transaction --

4 JUSTICE STEVENS: May I ask you a question  
5 going back to Justice Kennedy's early question? Do you  
6 think the fiduciary status of the defendant in this case  
7 is different from the fiduciary status of a president of  
8 a corporation?

9 MR. GANNON: I -- I -- I think that it is  
10 different from the status of a president of a  
11 corporation; that -- that the term of art, "fiduciary"  
12 which Congress was invoking here can mean different  
13 things in different circumstances.

14 Pepper was a case that involved corporate  
15 directors. The chief difference here and what Congress  
16 was intending to counteract was the inherent structural  
17 impediment to arm's-length bargaining between the  
18 investment adviser and the board of directors. And  
19 that's what makes that high burden that was used in  
20 Pepper v. Litton for controlling shareholders the  
21 relevant analogy, we believe.

22 CHIEF JUSTICE ROBERTS: Thank you, counsel.

23 MR. GANNON: Thank you, Mr. Chief Justice.

24 CHIEF JUSTICE ROBERTS: Mr. Donovan.

25 ORAL ARGUMENT OF JOHN D. DONOVAN, JR.

1 ON BEHALF OF THE RESPONDENT

2 MR. DONOVAN: Mr. Chief Justice, and may it  
3 please the Court:

4 The point that Mr. Gannon just made and that  
5 Mr. Frederick made before, that there was some  
6 structural impediment to negotiations between a mutual  
7 fund board and adviser, is at the heart of this dispute,  
8 because that is a judgment that Congress made. The  
9 Investment Company Act in the first instance delegates  
10 responsibility to the board of directors to approve  
11 fees. A fee may not be approved that does not have the  
12 consent of a majority of the independent trustees in the  
13 first instance.

14 The independent check on fees that is  
15 erected by section 36(b) --

16 JUSTICE SOTOMAYOR: Let's assume -- let's  
17 assume that all of the independent board of director  
18 members vote for a particular fee, but the fee is  
19 negotiated by an insider, and the insider is the one who  
20 does the evaluation, looks at them and says: I think  
21 this is really a great deal, guys. And they just fell  
22 for it. Is that a process that would guarantee an  
23 arm's-length transaction in the sense that Congress  
24 intended in this act?

25 MR. DONOVAN: It may not and it may give

1 rise to a cause of action. But as I started --

2 JUSTICE SOTOMAYOR: Which cause of action --

3 MR. DONOVAN: A cause of action --

4 JUSTICE SOTOMAYOR: -- under what?

5 MR. DONOVAN: It may give a cause of action

6 under section 36(b) if the circumstances you described,

7 Justice Sotomayor are -- have an impact upon the fee.

8 And the reason --

9 JUSTICE SOTOMAYOR: So, then their process  
10 is part of your definition of "fiduciary duty"? A court  
11 has to look at the nature of process?

12 MR. DONOVAN: If there is an impact upon fee  
13 that is outside of the range of what could have been  
14 bargained. The reason for that --

15 JUSTICE SOTOMAYOR: Now -- now you are  
16 adding what has been added, which is outside of the  
17 range, correct?

18 MR. DONOVAN: Yes.

19 JUSTICE SOTOMAYOR: All right.

20 MR. DONOVAN: If I understand your question  
21 correctly, will a process flaw alone justify a  
22 section 36(b) cause of action? My answer is no. Will a  
23 process flaw that affects a fee justify a 36(b) action?  
24 Yes, it will.

25 JUSTICE SOTOMAYOR: All right. But what you

1 are -- but what you are arguing is, if the process is  
2 fair, even if the fee is outside the range of an arm's-  
3 length transaction, there is no cause of action?

4 MR. DONOVAN: No, I -- I -- I doubt that as  
5 well. There are two separate causes of action, I can  
6 imagine, under 36(b): One, a process flaw that has a  
7 fee impact; and second, a fee that is so far outside of  
8 the bounds of what could have been bargained that it  
9 justifies independent review.

10 The question under 36(b) is whether, having  
11 delegated responsibility in the first instance to a  
12 board, there is a reason to second-guess their judgment.  
13 And the independent check that Mr. Gannon referred to at  
14 section 36(b) or (a) should not be a de novo judicial  
15 review of the size of the fee for a couple of reasons,  
16 the first of which is section 36(b)(2). That statute  
17 instructs courts to give such consideration as they  
18 consider due to the deliberations of the board. What  
19 did they see? What did they get? Did they negotiate?

20 JUSTICE SCALIA: That's a wonderfully clear  
21 command, isn't it? Such consideration as is  
22 appropriate? What is the language? Read it. What is  
23 it?

24 MR. DONOVAN: The language is "such  
25 consideration that the court considers due under the

1 circumstances."

2 JUSTICE SCALIA: Wow.

3 (Laughter.)

4 MR. DONOVAN: But there would be no reason  
5 for that instruction at all, Your Honor, if a court were  
6 to make its own judgments about what is fair and  
7 reasonable.

8 JUSTICE SCALIA: No, it's meaningless. It  
9 tells the court to make its own judgment. Such  
10 consideration as the court deems due. Give it  
11 whatever -- whatever consideration you -- you feel like.  
12 It's utterly meaningless to me.

13 MR. DONOVAN: What I think Congress was  
14 doing was considering what the source of the common law  
15 had been before. The corporate context,  
16 Justice Kennedy, I think was what inspired. At  
17 corporate law, a decision would not be second-guessed by  
18 a court unless there was a reason to do so, unless the  
19 judgment of directors and the presumption of regularity  
20 that attached to their decisions could for some reason  
21 be second-guessed. Was there a process flaw? Was it so  
22 far out of bounds?

23 CHIEF JUSTICE ROBERTS: Well, what is "so  
24 far out of bounds"? In other words, you are saying, you  
25 can look at what the directors did if it's, as you said,

1 too far out of bounds, but 10 percent off, 50 percent  
2 off?

3 MR. DONOVAN: Mr. Chief --

4 CHIEF JUSTICE ROBERTS: Double, as they say  
5 is the case here?

6 MR. DONOVAN: I'm sorry?

7 CHIEF JUSTICE ROBERTS: Double, as they say  
8 is the case here?

9 MR. DONOVAN: As the plaintiffs say is the  
10 case here.

11 CHIEF JUSTICE ROBERTS: Yes.

12 MR. DONOVAN: I suggest there is no  
13 numerical basis, because in fact every kind of mutual  
14 fund and ever stripe of mutual fund is different.

15 CHIEF JUSTICE ROBERTS: Well, then you say:  
16 Look to see if it's outside the bounds, and now you tell  
17 me there is no way to look to see if it's outside the  
18 bounds.

19 MR. DONOVAN: Well, I think -- the first  
20 comparative would be other funds of a similar stripe.  
21 So, for example, you could imagine that a mutual fund  
22 with the same investment objective and style that is two  
23 times might be inappropriate. You could also imagine a  
24 different circumstance where, passively managed funds  
25 for example, a multiple of fees would be inappropriate.



1           You could also, though, imagine a case where  
2 there is substantial risk taken, where the types of  
3 securities that are invested in are unusual, where  
4 substantial differences could be justified.

5           JUSTICE SCALIA: Is that the test that the  
6 court of appeals here applied?

7           MR. DONOVAN: Pardon?

8           JUSTICE SCALIA: Is that the test that the  
9 court of appeals here applied, whose judgment you want  
10 us to affirm?

11          MR. DONOVAN: The court of appeals did not  
12 apply the test. Judge Easterbrook --

13          JUSTICE SCALIA: So we should remand it for  
14 application of the test that you propose?

15          MR. DONOVAN: I don't think you have to.  
16 And the reason is because of what the district court  
17 did. And there I get to, Justice Ginsburg, what you  
18 said. The -- the argument is made that services are the  
19 same. In fact, that is not the record. And if you look  
20 at page 161 of the Joint Appendix and following, there  
21 is a list of services that the trust -- the investment  
22 adviser gave to the trustees in this case, about all of  
23 the services that they did for their fee in the case.

24          JUSTICE SCALIA: Surely that's a disputed  
25 fact, isn't it? And you want us to dispose -- or you

1 want this to be disposed of on summary judgment. The  
2 other side says the services aren't that much different.

3 MR. DONOVAN: They are very different. Page  
4 161 and following will tell you how. And the district  
5 court at page 360 -- 16a, excuse me, of the district  
6 court's opinion, notices that the services were  
7 different. So, under --

8 JUSTICE SCALIA: It wasn't talking about  
9 this particular case. It was talking about in general,  
10 wasn't --

11 MR. DONOVAN: No, he was talking about this  
12 case, Justice Scalia.

13 JUSTICE SOTOMAYOR: Except that they claim  
14 that you were receiving additional payment for the  
15 services, or some or at least a substantial number of  
16 the services, that you claim are attributed by the  
17 difference. So they're saying if you compare apples to  
18 apples, you are charging twice the amount. If you  
19 compare apples to oranges, there are differences because  
20 the oranges were different, but you were getting paid  
21 for those oranges separately. I think that was their  
22 argument.

23 MR. DONOVAN: That is their argument and  
24 it's not accurate, Your Honor.

25 JUSTICE SOTOMAYOR: Well, that's the issue

1 of disputed fact. So let's go back. Are you disavowing  
2 the Seventh Circuit's approach? Because I read your  
3 brief and it doesn't appear as if you are defending  
4 their market approach that says so long as the process  
5 was fair, any fee is okay. That's how I thought they  
6 had reached their conclusion.

7 MR. DONOVAN: I think what Judge Easterbrook  
8 said, and we don't agree, is if there is deceit of  
9 directors that would justify a cause of action under  
10 36(b). But in the absence of, in his words, "pulling  
11 the wool over the eyes of the trustees" --

12 JUSTICE SOTOMAYOR: That's what I'm talking  
13 -- I am using his words in terms of case --

14 MR. DONOVAN: I do --

15 JUSTICE SOTOMAYOR: And you're disavowing  
16 that?

17 MR. DONOVAN: I do not defend that, because  
18 I can imagine, as your hypothetical asked earlier,  
19 directors or trustees who -- are not paying attention --

20 JUSTICE SOTOMAYOR: Your position is no  
21 different than the solicitor general's, that there has  
22 to be some measure of fair process and some measure of a  
23 fair fee, at least within -- in terms of it not being  
24 outside the range an arm's length transaction?

25 MR. DONOVAN: The solicitor general gets it

1 right when she describes Gartenberg as the standard. Is  
2 this a result that could have been fairly bargained at  
3 arm's length. Where we part company is with respect to  
4 two things: One is, she says and Mr. Gannon said today,  
5 that the most important consideration is a comparison to  
6 other kinds of fees, and that is required in the  
7 calculus in the district court. In fact, that would  
8 make mandatory what the SEC rules only make  
9 discretionary.

10 Chief Justice, you asked earlier about the  
11 SEC's rules in this area. And in fact, they compel  
12 disclosure of fees charged by advisers to their funds  
13 and their conflicts of similar investment objectives.  
14 They do not require disclosure of accounts within an  
15 advisor's business operations that are institutional  
16 accounts. Now to be sure --

17 JUSTICE SCALIA: That are what?

18 MR. DONOVAN: That are -- advisers --  
19 institutional accounts adviser services. If --

20 JUSTICE GINSBURG: But the -- the fund  
21 adviser here -- I mean, the investment adviser did  
22 disclose -- that's in the record -- did disclose the  
23 difference between what were charged mutual funds, what  
24 were charged institutional investors, and then explained  
25 that the services were different and that justified the

1 difference. But they weren't trying to think, no, we  
2 don't have to come forward with this information.

3 MR. DONOVAN: That's precisely correct, Your  
4 Honor. In this case the trustees did have the  
5 information. The adviser did disclose it, but the SEC  
6 does not require them to ask that question. All it  
7 requires them to do is if they do ask the question, if  
8 they do study the material, they must disclose the  
9 weight they put on to it.

10 JUSTICE BREYER: Suppose you were appointed  
11 to a committee, just set my pay, that might be helpful.  
12 I'd say I'll pay you \$50,000 a year to do it, as long as  
13 I am satisfied with your results.

14 Now, would you, for example, not have in  
15 your mind, I would like to know what he's paid by other  
16 people that don't have someone like me setting his pay?  
17 Wouldn't that be in your mind?

18 MR. DONOVAN: It could be, sure.

19 JUSTICE BREYER: Yeah, so wouldn't that be a  
20 normal question to ask?

21 MR. DONOVAN: And the trustees did ask it  
22 here.

23 JUSTICE BREYER: Well, I don't know if they  
24 asked it -- I mean, I think we are reviewing the  
25 district court opinion, I think we are reversing -- we

1 are reviewing -- sorry. We're reviewing.

2 (Laughter.)

3 JUSTICE BREYER: I have laryngitis; I don't  
4 speak accurately.

5 (Laughter.)

6 JUSTICE BREYER: I think we are reviewing a  
7 -- a decision of a court of appeals setting a standard,  
8 and so wouldn't, when we set the standard, say, we can't  
9 say if in every case you are not going to go out and ask  
10 him what he charges when he mows the neighbor's lawn,  
11 but we would like to know what he charges when he asks  
12 for money from people who do not have this kind of  
13 supervision, and we would like if it's a lot different  
14 to ask him why.

15 MR. DONOVAN: Justice Breyer --

16 JUSTICE BREYER: Okay, so what's the problem  
17 then with saying that in the opinion?

18 MR. DONOVAN: There is no problem with  
19 saying that if it is a relevant consideration.

20 JUSTICE BREYER: Well, it's pretty unusual  
21 that it won't be, and I think certainly you have in the  
22 case in front of us a case where it would be relevant.  
23 You may have an answer to the question. There may be a  
24 perfectly good answer, so let's listen to it.

25 MR. DONOVAN: The difference, Your Honor, is

1 that the Solicitor General and the plaintiffs would make  
2 the question and the answer dispositive in every case.  
3 I would acknowledge as --

4 JUSTICE BREYER: The answer dispositive?  
5 Well, I don't see it should be dispositive, maybe the  
6 answers would be quite different.

7 MR. DONOVAN: Precisely.

8 JUSTICE BREYER: All right. So -- but you  
9 no objection, then I'm not sure there is much of an  
10 issue. There might -- I mean, maybe there is some.  
11 That's the only issue, whether this should be  
12 dispositive always, or whether it should be a factor to  
13 take into account where relevant?

14 MR. DONOVAN: It is a factor that I consider  
15 that is likely to be relevant --

16 JUSTICE BREYER: So you have no objection to  
17 send it back and say look, of course this is relevant,  
18 perhaps quite often relevant; why don't you look at it?

19 MR. DONOVAN: My objection -- my objection  
20 to sending it back is only that that analysis was done.

21 JUSTICE GINSBURG: But did -- but in the  
22 Seventh Circuit, Judge Easterbrook said, mainly you have  
23 to look to see if there was full disclosure, and then  
24 there might be cases where it's so out of line. And he  
25 said the comparison would be to other mutual funds. He

1 excluded the comparison with institutional investors.  
2 So to that extent, was the Second Circuit wrong, saying  
3 this is not a relevant factor; what other mutual funds  
4 pay investment advisors may be a relevant factor?

5 MR. DONOVAN: I think the Seventh Circuit  
6 made that comparison. Judge Easterbrook did say that  
7 the services of institutional accounts ordinarily are  
8 different from mutual fund accounts. I agree that in  
9 the first instance, the first comparator usually should  
10 be mutual funds, and regrettably Judge Easterbrook did  
11 not cite to the record for the reasons to identify those  
12 differences. But it is in fact in the record, and there  
13 is no other record that suggests that they were the  
14 same. All we had below was the assertion that on the  
15 one hand, an advisory contract for an institutional  
16 account said advisory services. And in the other we had  
17 a mutual fund advisory contract that said advisory  
18 services.

19 CHIEF JUSTICE ROBERTS: When you say you  
20 should look at the range and how far it's off, do you  
21 mean that in the Gartenberg sense -- in other words, if  
22 it is way out of line, then you assume or can at least  
23 look further at whether there was a fair process? Or do  
24 you mean it in the normal case, in sort of setting the  
25 rates you just look how far it is off.



1           MR. DONOVAN: I look at it in the Gartenberg  
2 sense, Your Honor. And the reason is because as I --  
3 from what I said the first question is, is when do you  
4 ask courts to substitute their judgment?

5           CHIEF JUSTICE ROBERTS: It's probably --  
6 you're not the person to -- to ask, but do you  
7 understand the Solicitor General's position to be your  
8 understanding of the Gartenberg sense or something else?

9           MR. DONOVAN: I believe they interpret in  
10 the Gartenberg sense. I think that the Solicitor  
11 General's position and the Respondent's, with respect to  
12 the standard that you ought to apply, is Gartenberg.

13           JUSTICE BREYER: What do we do about  
14 Gartenberg? That is to say, the key sentence you can  
15 read either way. The key sentence could mean -- it just  
16 depends on tone of voice. You must charge a fee that is  
17 not so disproportionately large that it bears no  
18 reasonable relationship to the services rendered and  
19 could not -- could not have been the product of  
20 arms-length bargaining. Or you could say, look, it's  
21 unlawful where it's so large -- it doesn't -- where  
22 there is no reasonable relationship. And if there is no  
23 reasonable relationship, how could it have been the  
24 product of arm's-length bargaining?

25           MR. DONOVAN: I agree you can turn the words

1 upside down. I think they turned it upside down --

2 JUSTICE BREYER: You object if we turn them  
3 upside down?

4 MR. DONOVAN: I think they turned them  
5 upside down for a reason, and the reason is 36(b)(1),  
6 which imposes the burden of proof upon --

7 JUSTICE BREYER: Well, I'm saying the tone,  
8 be a little careful here.

9 MR. DONOVAN: Well --

10 JUSTICE BREYER: So we can say the substance  
11 is -- I'm just trying this out -- the substance is to  
12 look and see if it's reasonable, and if it's reasonable  
13 it certainly is the product of arm-length bargaining, if  
14 it's not reasonable, how could it be? Got to get an  
15 answer to that, okay? So, that way you see the tone is  
16 be careful, you are a judge, you are not a rate-setter.  
17 How's that?

18 MR. DONOVAN: I would accept the proposition  
19 that it is reasonable if it is outside of what could  
20 have been bargained at arm's length. I think they  
21 turned it upside down the fact for the reason that the  
22 statute reverses the burden of proof and I think that  
23 they also acknowledge that it is a process-oriented  
24 thing for judges to do, because after all you are asking  
25 here a standard for judges to apply in a contested

1 situation that recognizes the responsibility of the  
2 board in the first instance. That's what 36(b)(2) is  
3 all about.

4 JUSTICE SCALIA: Would -- would you give us  
5 the citations of the parts of the record that you say  
6 render it unnecessary for us to remand for the lower  
7 court to consider a comparison with non- -- with  
8 institutional charges?

9 MR. DONOVAN: Yes, Your Honor. I start at  
10 page 16a and 17a of the district court's opinion where  
11 at page 16a at the bottom the district court said the  
12 services supplied are different. And --

13 JUSTICE SCALIA: At 16a of the Joint  
14 Appendix you are talking about?

15 MR. DONOVAN: I'm sorry, Your Honor, the  
16 petition.

17 JUSTICE SCALIA: Of the petition.

18 MR. DONOVAN: Correct, it's 16a of the  
19 petition, which is Judge Kocoras' opinion. At the  
20 bottom of the page you will see that he said, the  
21 services Harris provided to institutional clients varied  
22 but in all events were more limited than those provided  
23 the funds.

24 If you then go on to page 17, he goes  
25 through with respect to each of these three funds and

1 chronicles the fees they paid and by comparison the fees  
2 charged to institutional accounts with similar  
3 investment objectives. The statement by the plaintiff,  
4 Petitioners here, that the fee charged was a 2X  
5 multiple, does not refer to that array of institutional  
6 accounts. It takes one in order to make the comparison  
7 what it is.

8           And then, Justice Scalia, I would then go to  
9 page 32a of the district court's opinion where he  
10 describes what appear to be disputed issues of fact.  
11 And what he said those dispute issues of fact were about  
12 were what the Petitioners claimed were flaws in the  
13 negotiation process, in substance, what they would have  
14 done had they been negotiating, rather than the  
15 trustees. It is not a dispute about the ultimate test,  
16 was this fee so far out of bounds it could not have been  
17 reasonable.

18           To be sure, throughout a record that is as  
19 large as this one, you could imagine the parties  
20 disputed lots of things. What you could not fairly  
21 dispute is whether these fees, for these funds, using  
22 comparable funds and using institutional accounts, as  
23 Judge Kocoras did, were so far out of bounds, they could  
24 not have been fairly bargained, and if that is the test,  
25 there is no need for remand.

1           If, as I suggest and as the Solicitor  
2 General suggests, Gartenberg is the appropriate  
3 standard, Gartenberg is what the district court applied.

4           This Court has to be sure, on occasion, and  
5 it is rare, both announce the test and apply it in the  
6 same circumstances.

7           In circumstances where courts are looking  
8 for guidance on what the standard is and how to apply  
9 it, I suggest this is a case in which affirming what the  
10 district court did would be appropriate.

11           JUSTICE GINSBURG: What about the  
12 petitioners' allegation that the investment adviser did  
13 not provide full and accurate information? And they  
14 mention particularly concerning economies of scale,  
15 profitability, and several other matters, that what  
16 everybody agrees is necessary, full disclosure, had not  
17 occurred.

18           Is that a disputed issue of fact or of  
19 further inquiry?

20           MR. DONOVAN: I don't think it is, Your  
21 Honor. And, again, I would go back to what Judge  
22 Kocoras said on 32(a).

23           There was absolutely suggestions in the  
24 record by the plaintiff that they would have negotiated  
25 differently, but, for example, with respect to

1 ostensible misrepresentations on -- among other things,  
2 profitability and the rest, this was because the  
3 plaintiffs' expert did an accounting and accounted for  
4 costs differently and said, had you accounted for costs  
5 and allocated them the way I did, you would have reached  
6 a negotiated result that was different.

7 Well, that just isn't what happened. That's  
8 why Judge Kocoras said, this goes to the integrity of  
9 the negotiation. Would the negotiation have been  
10 different?

11 The plaintiffs say, I would have done it  
12 differently, but that's all they said, and it's not a  
13 misrepresentation to say, I would have accounted for  
14 costs differently.

15 Finally, I would -- the other question you  
16 asked is where in the record -- Justice Scalia, I'm  
17 sorry. It's at page 161 and following, where the  
18 background of all the difference in fees and the  
19 difference in services is chronicled.

20 You can tell, from the pull-out charts at  
21 page 171, what fee is charged for each of these mutual  
22 funds and what fee is charged for institutional  
23 accounts.

24 If you take the plaintiffs' point of view  
25 and say that a comparison to institutional accounts is

1 always required and may be dispositive and is always a  
2 fraction of what mutual fund charges and that judges are  
3 the, in the first instance, the ones to decide who is  
4 fair and reasonable or what is fair and reasonable, as  
5 opposed to directors, I suggest you consign 8,000 mutual  
6 funds to a trial.

7 On this record, these were funds that had  
8 best in class performance for fees that were at or below  
9 industry averages.

10 That is not a record upon which a reasonable  
11 person could conclude that the adviser has over-reached.  
12 That is at the heart of fiduciary duty. I see my time  
13 is about to expire.

14 Thank you, Your Honor.

15 CHIEF JUSTICE ROBERTS: Thank you, counsel.

16 Mr. Frederick, you have three minutes  
17 remaining.

18 REBUTTAL ARGUMENT OF DAVID C. FREDERICK

19 ON BEHALF OF THE PETITIONERS

20 MR. FREDERICK: At this recording here did  
21 not make findings -- this was a summary judgment case,  
22 and in fact, the Court didn't find that the disputes  
23 were nonexistent.

24 In fact, on page 30a, the district court  
25 said that the disputes were nonmaterial, and that's a

1 very important distinction because the joint appendix  
2 that you have before you contains a lot of evidence in  
3 which it is disputed whether or not these were similar  
4 services.

5           The Harris manager on page 6 -- JA 650, the  
6 portfolio holdings of the funds, are very similar. On  
7 512, the Harris fund manager testimony that, when he  
8 buys a stock, he buys it for all mutual funds and  
9 independent accounts, with the same investment  
10 objective.

11           On 505 to 506, the Harris research director  
12 testimony that the managers of the mutual funds and  
13 independent accounts share equally all work done by the  
14 research department, and 513 to 514, that the Harris  
15 fund manager says all of our analysts do research for  
16 all of our clients.

17           There is disputed evidence here as to what  
18 constitutes similarity, Justice Sotomayor, these are  
19 comparing apples to apples because the record indicates  
20 that there are separate contracts for the additional  
21 fees that they charge to the mutual funds for the  
22 additional services provided.

23           We're simply talking about comparisons of  
24 money management, but --

25           CHIEF JUSTICE ROBERTS: Was your friend



1 correct, that these funds have better than average  
2 performance and lower than average fees?

3 MR. FREDERICK: In one small aspect of the  
4 damages period, that is correct, and after that was  
5 found, they had lower than average performance and  
6 higher than average fees, Mr. Chief Justice. It's a  
7 damages period that encompasses several years.

8 If I could go back to the point, though,  
9 about the fiduciary duty, what Judge Cardozo, when he  
10 was on the New York Court of Appeals, said, a fiduciary  
11 represents the punctilio of honor, and that is  
12 contrasted with the morals of the marketplace operating  
13 at arm's-length.

14 It surely cannot be the case that, where you  
15 are dealing with a fiduciary duty -- which is a higher  
16 standard recognized in the law -- that you can charge  
17 twice as much as what you are obtaining at arm's-length  
18 for services that you are providing.

19 The Gartenberg court, Justice Breyer, in  
20 fact, had the opposite language that you are averting  
21 to, and that is at page 694 F.2nd 928, where the Court  
22 said, "The test is essentially whether the fee schedule  
23 represents a charge within the range of what would have  
24 been negotiated at arm's-length in the light of all the  
25 surrounding circumstances."

1 JUSTICE BREYER: I thought, by reversing  
2 that, picking out what the essence was, you would get  
3 pretty close to what you are arguing for, without  
4 getting into all this thing of whether it's just like a  
5 trustee or whether a lawyer should be a trustee or --  
6 you know, there are a lot of questions here that could  
7 float around, of any language we use.

8 MR. FREDERICK: That's right. The Second  
9 Circuit that went on to flip it and say, we had to prove  
10 a negative, which is not ordinarily what a plaintiff has  
11 to prove in any law case, by showing it -- it is so  
12 disproportionate it could not have been achieved at  
13 arm's-length, and that is where we think the court --  
14 courts have gotten this wrong.

15 CHIEF JUSTICE ROBERTS: Thank you, counsel.  
16 The case is submitted.

17 (Whereupon, at 10:57 a.m., the case in the  
18 above-entitled matter was submitted.)

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21  
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23  
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25

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