Fee-Case Plaintiffs Still Win Early, but That May Change

By Greg Saitz, BoardIQ, April 25, 2017 [subscription required]
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Plaintiffs may lose excessive fee cases at trial, but they continue to survive early efforts to have the complaints thrown out. Shareholders suing **State Farm Investment Management** and **T. Rowe Price Associates** got past defense motions to dismiss in recent weeks, giving them leverage for potential settlements and the ability to depose independent directors and others as the cases move forward.

At the same time, however, House Republicans unveiled draft legislation last week that includes tweaks to Section 36(b) that would make it easier for judges to throw out such complaints and harder for plaintiffs to prove their cases. Industry attorneys say it would provide a much needed check on litigation that has flooded fund groups in recent years and cost them millions of dollars to fight.

The plaintiff's bar, which has been stymied when it comes to winning excessive fee trials, has logged a considerably better record in recent years overcoming motions to dismiss. Those motions are typically the first major hurdle suing shareholders must clear in Section 36(b) litigation, and judges accept allegations made in a thorough complaint as true in deciding whether to let it continue.

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Almost all of the roughly 20 excessive fee lawsuits filed since 2011 have survived motions to dismiss, and the few that have been thrown out were based on issues unrelated to fees, such as a plaintiff's no longer owning shares of the fund in question, attorneys say.

Niels Holch, founding partner of **Holch & Erickson** and executive director of the Coalition of Mutual Fund Investors, says the losses plaintiffs suffered at trials involving Axa and The Hartford aren't necessarily indicative of what will happen with other pending cases.

"I don't think the defense bar can claim victory yet," he says. "The plaintiff's bar will learn from their mistakes and put on better cases."

But plaintiff's attorneys may have to up their game considerably if draft legislation released by Rep. Jeb Hensarling (R-Texas) becomes law. The main thrust of the Financial Choice Act 2.0 is to roll back provisions of the Dodd-Frank Act. But included on page 452 of the 593-page draft is a section that would amend Section 36(b) by adding two parts.

One would require excessive fee complaints to "state with particularity" the facts on which plaintiffs are basing their allegations. The wording mimics language found in the 1995 Private Securities Litigation Reform Act, which established stricter standards for filing securities fraud class actions.

Adding such a requirement would make it easier for judges to throw out cases at the motion to dismiss stage, Holch and other attorneys say.

The other proposed addition to Section 36(b) would elevate plaintiffs' standard of proof to win a case from what it is now – a "preponderance of evidence," which is the common bar for most civil lawsuits – to "clear and convincing evidence," which is a higher threshold, attorneys say.

The proposed changes come after a slew of more than 20 excessive fee lawsuits filed in the past six years. Fund groups have spent millions of dollars defending themselves against the complaints, and industry attorneys say amending the law would help ease the burden by requiring more fulsome allegations.