

Legislation would make it harder for investors to sue mutual funds over high fees

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By **Mark Schoeff Jr.**

Legislation that would make it more difficult for investors to sue mutual fund companies for excessive fees was poised to advance in the House on Wednesday.

The House Financial Services Committee was set to take up **a bill** that would impose a higher legal burden for plaintiffs when they allege that a fund has violated its fiduciary duty by charging high fees.

Under Section 36(b) of the Investment Company Act of 1940, investors can sue a fund for breaching fiduciary duty regarding compensation for services. The bill's author, Rep. Tom Emmer, R-Minn., asserted that these suits lack merit.

"By cutting down the number of frivolous lawsuits targeted at mutual funds, we can allow Americans to continue to make the investments they need for their future," Mr. Emmer said in a **Jan. 10 statement** after introducing the bill, the Mutual Fund Litigation Reform Act.

The legislation was **one of 17 bills** the House financial panel began debating on Wednesday. The markup was to continue Wednesday evening. Votes could be postponed until Thursday.

Most of the legislation, including Mr. Emmer's bill, is likely to be approved by the Republican-majority committee and head to the House floor.

So far, mutual fund companies **have not lost** an excessive fee case. But **more than a dozen cases** are moving through the court system that are focused on sub-adviser fees.

For instance, plaintiffs allege that when a fund sponsor, such as a financial firm or insurance company, charges 75 basis points in management fees and then outsources management to a sub-adviser who it pays 25 bps, the difference amounts to an excessive fee.

"The sub-adviser arguments are getting the attention of a lot of judges," said Niels Holch, executive director of the Coalition of Mutual Fund Investors. "Now is not the time to change the rules, while we're in the middle of all these lawsuits."

Under Mr. Emmer's bill, a plaintiff would have to state "with particularity" in their initial complaint why fiduciary duty was breached, and then prove the violation with "clear and convincing evidence" rather than a preponderance of the evidence.

The Consumer Federation of America said the bill would force plaintiffs to plead with particularity before they have access to evidence.

The bill "would impose two new requirements that, between them, would make it virtually impossible for mutual fund shareholders to bring claims for excessive fees," Barbara Roper, CFA director of investor protection, and Micah Hauptman, CFA financial services counsel, **wrote in a Jan. 16 letter** to committee lawmakers. "The effect would be to further immunize fund companies from accountability when they charge excessive fees."

The Investment Company Institute, the mutual fund industry trade association, backs Mr. Emmer's bill, which it said would not curtail all Section 36(b) lawsuits, just the "abusive" ones.

"Rather, the legislation would discourage plaintiffs' attorneys from bringing non-meritorious lawsuits by allowing judges to dismiss those suits at an earlier stage," ICI president and chief executive Paul Schott Stevens wrote in a **Jan. 16 letter** to House Financial Services Chairman Jeb Hensarling, R-Texas, and ranking member Maxine Waters, D-Calif.

The language in Mr. Emmer's bill also is a provision of Mr. Hensarling's **Financial Choice Act**, a broad overhaul of the Dodd-Frank financial reform law that the House approved last year.

Mr. Hensarling's bill is unlikely to go anywhere in the Senate, where Democrats have 49 members in their caucus — plenty to support a filibuster.

If approved by the full House, it's unclear whether Mr. Emmer's bill or similar legislation would get traction in the Senate, especially if it depends mostly on Republicans for House passage.