

MEMO# 1201

June 12, 1989

COURT OF APPEALS AFFIRMS DISMISSAL OF EXCESSIVE FEE CLAIM IN KRINSK CASE

June 12, 1989 TO: SEC RULES MEMBERS NO. 29-89 RE: COURT OF APPEALS AFFIRMS DISMISSAL OF EXCESSIVE FEE CLAIM IN KRINSK CASE

Attached is a copy of the opinion of the U.S. Court of Appeals for the Second Circuit in *Krinsk v. Fund Asset Management, Inc.*, in which the court unanimously affirmed the holding of the district court, which dismissed all of the plaintiff's claims. Plaintiff Krinsk, a money market fund shareholder, had alleged breach of fiduciary duty due to excessive fees, an improper distribution plan under rule 12b-1 and misleading disclosure in the fund's proxy statement. With respect to the plaintiff's claim under Section 36(b) of the 1940 Act concerning the level of fees, the court applied the Gartenberg standard, namely "whether the fee schedule represents a charge within the range of what would have been negotiated at arm's length in light of all of the surrounding circumstances". The court stated that six factors were to be considered in applying that standard: (1) the nature and quality of the services provided to shareholders, (2) profitability to the adviser-manager, (3) "fall-out benefits" to the adviser-manager, (4) economies of scale, (5) comparative fee structures, and (6) the independence and conscientiousness of the trustees. The court explicitly rejected the plaintiff's argument that "excessive profitability alone should suffice to support a finding of unreasonableness". The court also laid particular emphasis on the role of the trustees, stating: "The expertise of the trustees, whether they are fully informed, and the extent of care and conscientiousness with which they perform their duties are among the most important factors to be examined in evaluating the reasonableness of compensation under section 36(b)." The court rejected the plaintiff's argument that 12b-1 plan violated section 12(b) became the fee, based on the fund's assets, did not vary with the number of shares sold. The court stated that this claim was indistinguishable from the plaintiff's section 36(b) claim and that he could not circumvent this by bringing the claim under section 12(b). The court also noted that the 12b-1 fee "seems to have benefited the shareholders". - 2 - The court also rejected the plaintiff's argument that a fixed fee for participation in the cash management program, of which the fund was one component, violated section 15(a) since it was not described in the advisory agreement and affirmed the finding of the lower court that the fund's proxy statement was not false and misleading. Craig S. Tyle Assistant General Counsel

Attachment

abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.