Syllabus

NOTE: Where it is feasible, a syllabus (headnote) will be released, as is being done in connection with this case, at the time the opinion is issued. The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States* v. *Detroit Timber & Lumber Co.,* 200 U. S. 321, 337.

SUPREME COURT OF THE UNITED STATES

Syllabus

JONES ET AL. *v.* HARRIS ASSOCIATES L. P.

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

No. 08–586. Argued November 2, 2009—Decided March 30, 2010

Petitioners, shareholders in mutual funds managed by respondent investment adviser, filed this suit alleging that respondent violated §36(b)(1) of the Investment Company Act of 1940, which imposes a "fiduciary duty [on investment advisers] with respect to the receipt of compensation for services," 15 U. S. C. §80a–35(b). Granting respondent summary judgment, the District Court concluded that petitioners had not raised a triable issue of fact under the applicable standard set forth in *Gartenberg* v. *Merrill Lynch Asset Management, Inc.*, 694 F. 2d 923, 928 (CA2): "[T]he test is essentially 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. . . . To be guilty of a violation of §36(b), . . . the adviser must charge a fee that is so disproportionately large it bears no reasonable relationship to the services rendered and could not have been the product of arm's length bargaining." Rejecting the *Gartenberg* standard, the Seventh Circuit panel affirmed based on different reasoning.

Held: Based on §36(b)'s terms and the role that a shareholder action for breach of the investment adviser's fiduciary duty plays in the Act's overall structure, *Gartenberg* applied the correct standard. Pp. 7–17.

(a) A consensus has developed regarding the standard *Gartenberg* set forth over 25 years ago: The standard has been adopted by other federal courts, and the Securities and Exchange Commission's regulations have recognized, and formalized, *Gartenberg*-like factors. Both petitioners and respondents generally endorse the *Gartenberg* approach but disagree in some respects about its meaning. Pp. 7–9.

(b) Section 36(b)'s "fiduciary duty" phrase finds its meaning in *Pepper* v. *Linton*, 308 U. S. 295, 306–307, where the Court discussed the

concept in the analogous bankruptcy context: "The essence of the test is whether or not under all the circumstances the transaction carries the earmarks of an arm's length bargain. If it does not, equity will set it aside." *Gartenberg*'s approach fully incorporates this understanding, insisting that all relevant circumstances be taken into account and using the range of fees that might result from arm's-length bargaining as the benchmark for reviewing challenged fees. Pp. 9–11.

(c) *Gartenberg*'s approach also reflects §36(b)'s place in the statutory scheme and, in particular, its relationship to the other protections the Act affords investors. Under the Act, scrutiny of investment adviser compensation by a fully informed mutual fund board, see *Burks* v. *Lasker*, 441 U. S. 471, 482, and shareholder suits under §36(b) are mutually reinforcing but independent mechanisms for controlling adviser conflicts of interest, see *Daily Income Fund, Inc.* v. *Fox*, 464 U. S. 523, 541. In recognition of the disinterested directors' role, the Act instructs courts to give board approval of an adviser's compensation "such consideration . . . as is deemed appropriate under all the circumstances." §80a–35(b)(1). It may be inferred from this formulation that (1) a measure of deference to a board's judgment may be appropriate in some instances, and (2) the appropriate measure of deference varies depending on the circumstances. *Gartenberg* heeds these precepts. See 694 F. 2d, at 930. Pp. 11–12.

(d) The Court resolves the parties' disagreements on several important questions. First, since the Act requires consideration of all relevant factors, §80a–35(b)(2), courts must give comparisons between the fees an investment adviser charges a captive mutual fund and the fees it charges its independent clients the weight they merit in light of the similarities and differences between the services the clients in question require. In doing so, the Court must be wary of inapt comparisons based on significant differences between those services and must be mindful that the Act does not necessarily ensure fee parity between the two types of clients. However, courts should not rely too heavily on comparisons with fees charged mutual funds by other advisers, which may not result from arm's-length negotiations. Finally, a court's evaluation of an investment adviser's fiduciary duty must take into account both procedure and substance. Where disinterested directors consider all of the relevant factors, their decision to approve a particular fee agreement is entitled to considerable weight, even if the court might weigh the factors differently. Cf. *Lasker,* 441 U. S., at 486. In contrast, where the board's process was deficient or the adviser withheld important information, the court must take a more rigorous look at the outcome. *Id.,* at 484. *Gartenberg*'s "so disproportionately large" standard, 694 F. 2d, at

928, reflects Congress' choice to "rely largely upon [independent] 'watchdogs' to protect shareholders interests," *Lasker, supra*, at 482. Pp. 12–16.

(e) The Seventh Circuit erred in focusing on disclosure by investment advisers rather than the *Gartenberg* standard, which the panel rejected. That standard may lack sharp analytical clarity, but it accurately reflects the compromise embodied in §36(b) as to the appropriate method of testing investment adviser compensation, and it has provided a workable standard for nearly three decades. Pp. 16–17.

527 F. 3d 627, vacated and remanded.

ALITO, J., delivered the opinion for a unanimous Court. THOMAS, J., filed a concurring opinion.