



BITS AND PIECES

TIPS AND IDEAS ABOUT THE FIDUCIARY RULE

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The Backbone of Excessive Fees

Regulations call for reasonableness of fees but while the term may seem vague, there is a very specific standard that has been affirmed by the Supreme Court. Reliance on this standard is the best possible compliance and protection from excessive fee litigation and regulatory action.

In 2010 the US Supreme Court unanimously affirmed that five factors determine if an RIA's fees are excessive. The five determinants of excessive fees are:

- **Services**
The nature, extent, and quality of the services to be provided by the investment adviser;
- **Performance**
the investment performance of the investment and the investment adviser;
- **Costs and Profits**
the costs of the services to be provided and profits to be realized by the investment adviser and its affiliates;
- **Economies of Scale**
the extent to which economies of scale would be realized as the investment grows; and
- **Benefit to Investors**
whether fee levels reflect these economies of scale for the benefit of investors.



In its decision, the Supreme Court pointed out that in order to be excessive:

"...an investment adviser must charge a fee that is so disproportionately large that it bears no reasonable relationship to the services rendered and could not have been the product of arm's length bargaining."

The Court also warned against placing too much emphasis on a comparison of one advisory fee against fees charged to others by other advisers (Statistical benchmarks). The Supreme Court wrote:

"These comparisons are problematic because these fees, like those challenged, may not be the product of negotiations conducted at arm's length."

This guidance (known as the Gartenberg Standard) is the ultimate measure courts now use to determine if fees are excessive. While the 2010 case involved an RIA advising a mutual fund, it is applicable to all compensation for investment advice.



Note: A comprehensive DALBAR paper on *Assessing Compensation Reasonableness* is forthcoming in October, 2016. See the application of the *Gartenberg Standards* [here](#).