# THIRD CIRCUIT AFFIRMS JUDGMENT FOR INVESTMENT ADVISER IN SECTION 36(B) ACTION

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**U.S. Investment Management & Securities and Transactional Litigation Alert**

In a non-precedential opinion, the Third Circuit has affirmed a district court's ruling in favor of AXA Equitable Fund Management Group ("FMG") in a case in which the plaintiffs had claimed that FMG charged excessive fees for its mutual fund investment and administrative services.[1] Plaintiffs were parties to variable annuity contracts who opted to allocate certain annuity contributions to mutual funds for which FMG served as investment manager and administrator.

In August 2016, following a 25-day bench trial, the U.S. District Court for the District of New Jersey issued a 146-page opinion dismissing the plaintiffs' claims.[2] Plaintiffs had alleged that FMG's compensation was excessive and could not have been the product of arms-length bargaining, purportedly in violation of Section 36(b) of the Investment Company Act of 1940 ("Section 36(b)"). Plaintiffs' claims were based, in large part, on FMG's use of a "manager-of-managers" business model, a structure in which FMG provided advisory and management services to the funds and engaged third-party service providers to perform certain tasks. In its opinion, the district court made numerous findings of fact relating to each of six so-called "*Gartenberg* factors," the test adopted by the Supreme Court in 2010 for analyzing liability under Section 36(b).[3] The district court also made specific determinations regarding the credibility of many of the witnesses, including negative assessments of the credibility of three of plaintiffs' four experts.[4] Of particular note, the district court determined that FMG's treatment of subadvisory and subadministrative expenses as FMG expenses for purposes of calculating FMG's profitability was "within ordinary accounting principles."[5] The district court ultimately concluded that plaintiffs had failed to meet their burden on any of the *Gartenberg* factors and entered judgment for FMG.[6] Plaintiffs' appeal followed.

On July 10, 2018, the Third Circuit Court of Appeals affirmed the district court's ruling. In doing so, the Court of Appeals relied extensively on the findings of fact and credibility determinations made by the district court. Thus, at the outset of its opinion, the Court of Appeals observed that it "need only briefly address each of the *Gartenberg* factors at issue on appeal because the Petitioners' arguments boil down to assertions that we should overturn the District Court's factual findings and credibility determinations, which we will not do."[7] Finding that the plaintiffs had "attempt[ed] to relitigate the testimony that was presented at trial,"[8] the Court of Appeals summarily affirmed the district court's judgment, holding that the plaintiffs had failed "to demonstrate that the District Court's findings were clearly erroneous."[9]

Notwithstanding the non-precedential nature of the decision (written, as the Court of Appeals stated, "primarily for the parties") and the Third Circuit's heavy reliance on the district court's findings of fact and credibility determinations, the practical impact of the decision on the course of Section 36(b) litigation is significant. After an enormous investment of time and effort, the plaintiffs' bar once again has come away empty-handed in litigation against a determined adviser. The decision marks yet another in the recent string of victories for advisers in so-called "excessive fee" litigation, and should serve as a further deterrent to future filings.

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**Notes**

[1] *Sivolella, et al. v. AXA Equitable Life Ins. Co., et al.*, No. 16-4241 (3d Cir. *filed* July 10, 2018), *available* at http://www2.ca3.uscourts.gov/opinarch/164241np.pdf (last visited July 11, 2018) (the "opinion").
[2] *Sivolella, et al. v. AXA Equitable Life Ins. Co., et al.*, No. 11-cv-4194, 2016 WL 4487857 (D.N.J. Aug. 25, 2016) (the "district court opinion").
[3] *See id*., *generally*; opinion at 6.
[4] opinion at 4.
[5] District court opinion at *51.
[6] *Id.* at *72.
[7] Opinion at 6.
[8] *Id.* at 8.
[9] *Id.* at 7.

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