GOLDMAN, SACHS & CO.

Investment Advisers Act of 1940 — Rule 204-3

Goldman, Sachs & Co.

June 20, 2013

RESPONSE OF THE OFFICE OF CHIEF COUNSEL
DIVISION OF INVESTMENT MANAGEMENT
IM Ref. No. 2013413717

In your letter of June 17, 2013, you request our assurance that we would not recommend enforcement action to the Securities and Exchange Commission ("Commission") under rule 204-3 under the Investment Advisers Act of 1940 ("Advisers Act") against unaffiliated registered investment advisers (each, a "subadviser") selected by Goldman, Sachs & Co. ("GS&Co.") to manage client assets if the subadviser delivers its Form ADV Part 2 to GS&Co., rather than the client, where GS&Co. acts as investment adviser and agent for the client, including for the management of client assets and the receipt of Form ADV Part 2.

Background

You state the following:

GS&Co. is an investment adviser registered under the Advisers Act. GS&Co. sponsors wrap-fee or managed account programs or arrangements under which clients grant GS&Co. discretionary authority over their accounts, including the discretionary authority to select subadvisers1 to manage client assets (the wrap-fee or managed account programs and arrangements will be referred to herein collectively as the "Discretionary Programs"). GS&Co. currently includes within the Discretionary Programs more than 40 unaffiliated subadvisers. While, depending on the Discretionary Program, GS&Co. may have the discretionary authority to manage client assets directly, GS&Co. generally hires and allocates (and reallocates) client assets across multiple subadvisers on behalf of a client. If a subadviser manages assets of a client and, therefore, may have an investment advisory relationship with the client, the subadviser has responsibilities under the Advisers Act to provide clients with various disclosures, including information required by Form ADV Part 2A and 2B ("Brochure Documents").2 You propose that GS&Co. would permit clients to elect not to receive the Brochure Documents and, instead, to rely on GS&Co., whom they have tasked with selecting and overseeing the subadvisers, to do so on their behalf.

You state that GS&Co. proposes to proceed as follows:

1. The client would appoint GS&Co. as the client's investment adviser and grant GS&Co. discretionary authority to manage client assets or appoint one or more subadvisers to do so;

2. GS&Co. would offer the client the choice of receiving the Brochure Documents of unaffiliated subadvisers directly or having GS&Co., as agent and on behalf of the client, receive Brochure Documents of subadvisers engaged by GS&Co. to manage the client's assets. When offering clients this choice, GS&Co. would provide clients with sufficient information for them to make an informed choice. In this connection, GS&Co. would briefly explain in plain English the information and disclosures in the Brochure Documents;3

3. If the client so wishes, the client would appoint GS&Co. to receive Brochure Documents of subadvisers engaged by GS&Co. to manage the client's assets;4

4. GS&Co. would inform the client of the identity of any subadvisers it engages to manage the client's assets;

5. GS&Co. would retain copies of each subadvisers' Brochure Documents it receives on behalf of a client for at least the period required by Rule 204-2 under the Advisers Act;

6. GS&Co. would, upon the client's request, provide the client with copies of any Brochure Documents of subadvisers managing the client's assets either on paper or electronically in accordance with the Commission's guidance on the use of electronic media;5

7. GS&Co. would maintain policies and procedures, including those pursuant to Advisers Act Rule 206(4)-7, designed to ensure, among other things, that the Brochure Documents are appropriately reviewed by GS&Co., that GS&Co. is appropriately managing any material conflicts related to any business relationship GS&Co. may have with a subadviser, and that GS&Co.'s decisions on the hiring and firing of subadvisers are exercised in accordance with its fiduciary obligations; and

8. Clients would be free to change their minds at any time and request, for no additional cost, that subadvisers' Brochure Documents be delivered to them directly.

Analysis

Rule 204-3 under the Advisers Act generally requires an investment adviser registered with the Commission to deliver to prospective clients initially and existing clients annually a written disclosure statement containing the information required by Form ADV. A purpose of rule 204-3 is to provide new and prospective advisory clients with clearly written, meaningful, current disclosure of the business practices, conflicts of interest and background of the investment adviser and its advisory personnel.6 A client may use this disclosure to select his or her own adviser and evaluate the adviser's business practices and conflicts on an ongoing basis. As a result, the disclosure that clients and prospective clients receive is critical to their ability to make an informed decision about whether to engage an adviser and, having engaged the adviser, to manage that relationship.7

You argue that, in this instance, delivery of the Brochure Documents to a properly authorized agent (i.e., GS&Co.)8 should be deemed to constitute delivery to the agent's principal (i.e., the client), in accordance with well-established common-law agency principles (which you refer to as "constructive delivery" principles). You state that the arrangements between each client and GS&Co. would establish a principal/agent relationship.9 You state that both the Commission and its staff have endorsed constructive delivery principles in a variety of contexts. In particular, you argue that the Commission and its staff have applied constructive delivery principles to permit: (i) investment advisers (like GS&Co.) to receive various types of communications on behalf (and instead) of their clients; and (ii) investment advisers (like the subadvisers) to satisfy their delivery obligations for various communications by delivering the communications to an agent of the client.

First, in a variety of settings, you argue that the Commission and its staff have applied constructive delivery principles to permit investment advisers to receive various types of communications on behalf (and instead) of their clients. You state, for example, that investment advisers may receive prospectuses for offerings on behalf of their clients,10 and argue that the same principle should apply to the Brochure Documents. As another example, you note that the Commission has approved various self-regulatory organization rules allowing broker-dealers to satisfy their obligations to deliver proxies, annual and semiannual reports, and other shareholder communications to customers by sending the materials to the customers' investment advisers in lieu of the customers. Specifically, FINRA Rule 2251 and NYSE Rules 451 and 465 generally require a broker-dealer that carries customer positions in "street name" to forward proxies and shareholder communications, including annual and semiannual reports, to customers. However, a broker-dealer may deliver such materials to a customer's designated investment adviser instead of the customer if the broker-dealer has received a written instruction from the customer to send the communications to the investment adviser designated to receive them.11

Second, you argue that, in various contexts, the Commission and its staff have applied constructive delivery principles to permit investment advisers to satisfy their delivery obligations for various communications by delivering the communications to an agent of the client. For example, Regulation S-P permits investment advisers to satisfy their obligations to deliver initial and opt-out notices to consumers by sending the notices to the consumers' legal representatives. As another example, in connection with the 2003 amendments to the Advisers Act custody rule, the Commission recognized that "some clients may not wish to receive custodial reports" required under rule 206(4)-2 and provided, in

effect, that an investment adviser may satisfy its obligations to send notices of custodial arrangements and any required account statements to a client by sending them to an "independent representative" designated by the client.12

You argue that under your facts, it is appropriate for the client to have the option to rely on GS&Co. to receive Brochure Documents on his or her behalf. As described above, GS&Co. would offer the client the choice of having GS&Co., as agent and on behalf of the client, receive Brochure Documents of subadvisers engaged by GS&Co. to manage the client's assets, and, if the client so wishes, the client would appoint GS&Co. to do so. When offering clients this choice, GS&Co. would apprise clients of the disclosures covered and briefly explain in plain English the information in the Brochure Documents. GS&Co. would inform the client of the identity of any subadvisers it engages to manage the client's assets. You recognize that clients have an important right to receive Brochure Documents from their investment advisers and you note that GS&Co.'s proposal is not intended to waive or diminish these important rights. GS&Co. would preserve the Brochure Documents it receives and make them available to clients on request as described above. Clients would be free to change their minds at any time and request, for no additional cost, that subadvisers' Brochure Documents be delivered to them directly.

You emphasize that the relief would apply only where the client appoints GS&Co., an investment adviser registered with the Commission under the Advisers Act, as the client's investment adviser, and grants GS&Co. discretionary authority to manage client assets or appoint one or more subadvisers to do so. In these arrangements, GS&Co. is responsible for and makes the decision to engage or retain the subadviser, and for overseeing the subadviser.13

The Commission has stated:

> Under the Advisers Act, an adviser is a fiduciary whose duty is to serve the best interests of its clients, which includes an obligation not to subrogate clients' interests to its own. An adviser must deal fairly with clients and prospective clients, seek to avoid conflicts with its clients and, at a minimum, make full disclosure of any material conflict... [footnotes omitted]14

As the client's investment adviser, GS&Co. is required to serve the best interests of the client, seek to avoid conflicts with its clients and, at a minimum, make full disclosure of any material conflict. GS&Co. will deliver its Brochure Documents to clients as required by Rule 204-3. In the event that GS&Co. determines it has a material conflict with a subadviser or for other reasons, GS&Co. might seek to manage the conflict by sending that subadviser's Brochure Document to clients directly so they could evaluate the Brochure Document for themselves or suggest that clients engage another party to evaluate the conflict. Beyond conflicts, there may be other circumstances in which GS&Co. may decide to send disclosures directly to clients when GS&Co. believes this is appropriate given its fiduciary role and responsibilities. You state that such circumstances might include, for example, disclosures relating to extraordinary financial events (e.g., insolvency or bankruptcy) or disciplinary matters that a subadviser would be required to disclose to clients through Form ADV Part 2 or otherwise.

In addition, GS&Co. would maintain policies and procedures, including pursuant to Rule 206(4)-7 under the Advisers Act, designed to ensure, among other things, that the Brochure Documents are appropriately reviewed by GS&Co., that GS&Co. is appropriately managing any conflicts related to any business relationship GS&Co. may have with a subadviser, and that GS&Co.'s decisions on the hiring and firing of subadvisers are exercised in accordance with its fiduciary obligations. These policies, procedures and related controls would include conducting due diligence on subadvisers (e.g., qualifications, performance, fees, and disciplinary history), monitoring the activities of subadvisers, and reviewing their Form ADV and other disclosures.15

Beyond the oversight of subadvisers described above, you recognize that stepping "in the shoes" as agent of the client for purposes of receiving Brochure Documents poses significant added responsibilities on GS&Co. In particular, because the clients would no longer receive the disclosures to evaluate the subadvisers and would not be expected to independently evaluate the subadvisers, having delegated this responsibility to GS&Co., GS&Co. will be solely responsible for acting in the client's best interest with respect to any disclosure by the subadviser. GS&Co. represents that if a particular disclosure of any subadviser poses material conflicts to GS&Co. or the client, it would consider whether to (1) not retain

the subadviser or (2) inform affected clients of the specific conflict and seek client consent, even though the client may have elected not to receive Brochure Documents generally.

Based on your facts and representations, we would not recommend enforcement action to the Commission under rule 204-3 under the Advisers Act against an unaffiliated subadviser if a subadviser selected by GS&Co. to manage GS&Co. client assets delivers its Brochure Document to GS&Co., rather than the client.16 This response expresses our view on enforcement action only and does not express any legal or interpretive position on the issues presented. Because our position is based upon all of your facts and representations, any different facts or representations may require a different conclusion.

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Footnotes

1 Each subadviser is an "investment adviser" as defined in Section 202(a)(11) of the Advisers Act, and currently is registered as an "investment adviser" under this Act.

2 See National Regulatory Services, Inc., SEC Staff No-Action Letter (Dec. 2, 1992). The proposed arrangement would cover disclosures that subadvisers may be required to deliver when establishing an advisory relationship with a client, with some exceptions in the case of an affiliated subadviser like GSAM. Specifically, the disclosures would include Brochure Documents of subadvisers that contain information required by Part 2A and Part 2B of Form ADV.

3 See Instruction 2 of General Instructions for Part 2 of Form ADV.

4 You state that, in some cases, the client's appointment may be implicit in the existing agreements governing the client relationship, in which case GS&Co. expects that it would confirm that the client wishes GS&Co. to receive such Brochures Documents on behalf of the client.

5 See, e.g., Use of Electronic Media for Delivery Purposes, Securities Exchange Act Rel. No. 36345 (Oct. 6, 1995); Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information, Securities Exchange Act Rel. No. 37182 (May 9, 1996); Use of Electronic Media, Securities Exchange Act Rel. No. 42728 (Apr. 28, 2000).

6 See Amendments to Form ADV, Advisers Act Rel. No. IA-3060 (July 28, 2010).

7 Id.

8 You represent that an agent is a person authorized by another to act on his behalf under his control. See Proctor & Gamble v. Haugen, 222 F.3d 1262, 56 U.S.P.Q.2D (BNA) 1098, 104 A.L.R. 5th 737 (10th Cir. 2000). "An agency relationship has three essential characteristics: (1) the power of the agent to alter the legal relationship between the principal and third parties and the principal and himself; (2) the existence of a fiduciary relationship toward the principal with respect to matters within the scope of the agency; and (3) the right of the principal to control the agent's conduct with respect to matters within the scope of the agency." Sabel v. Mead Johnson & Co., 737 F. Supp. 135, 138 (D. Mass. 1990) (citing Restatement (Second) of Agency §§ 12-14 (1958)).

9 See Leib v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 461 F. Supp. 951, 953-54 (E.D. Mich. 1978); and Robinson v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 337 F. Supp. 107, 111 (N.D. Ala. 1971).

10 You note that a leading securities law treatise suggests that prospectus delivery to an investor's agent should satisfy prospectus delivery requirements under Section 5 of the Securities Act of 1933. In particular, you state that Professors Loss and Seligman have stated in various past editions of their treatise, Securities Regulation, that "presumably" delivery of a prospectus to the buyer's broker is

sufficient compliance by the seller and his or her broker, even though the buyer's broker never delivers the prospectus to his principal, provided the buyer's broker is authorized or otherwise empowered under general principles of agency law to receive delivery. You state that, in the current edition of this treatise (last updated Dec. 2012), Loss, Seligman write: "Is delivery of a prospectus to the buyer's broker sufficient compliance with §5(b) by the seller and his or her broker, even though the buyer's broker never delivers the prospectus to the principal? Presumably, it is if the buyer's broker is authorized or otherwise empowered under general principles of agency law to receive delivery."

11 See, e.g., FINRA Conduct Rule 2251(f)(4). Beneficial owners may rescind this designation at any time through a written instruction to the member firm.

12 See Custody of Funds or Securities of Clients by Investment Advisers, Advisers Act Rel. No. 2176 (Sept. 25, 2003), text accompanying n.35; Advisers Act Rule 206(4)-2(a)(7).

13 In contrast, you do not ask, and we express no view, regarding a situation in which the client retains responsibility to engage or retain a subadviser, including where a client decides to retain the services of a so-called "legacy" subadviser with which the client already has a relationship. GS&Co. recognizes that, where a client is responsible for, and makes the decision to, engage a subadviser, the client should have the benefit of the Brochure Documents to inform that decision.

14 Amendments to Form ADV, supra note 5.

15 GS&Co. also maintains information barriers and other controls designed to ensure that its decisions on the hiring, retention and termination of subadvisers are exercised independently and without regard to any material business relationships GS&Co. may have with the subadvisers. These include information barriers designed to "wall off" the business unit involved in making decisions to hire, retain or terminate subadvisers from other GS&Co. business units that might have business relationships with a subadviser that could pose a material conflict (e.g., business units engaged in transaction execution).

16 Such advisers are still required to file Form ADV Part 2A electronically with the Commission through the Investment Adviser Registration Depository. See Amendments to Form ADV, supra note 5.