Financial Services Authority

FINAL NOTICE

To: Goldman Sachs International

Of: Peterborough Court, 133 Fleet Street, London EC4A 2BB

Dated: 9 September 2010

TAKE NOTICE: the Financial Services Authority of 25 the North Colonnade, Canary Wharf, London E14 5HS ("the FSA") gives you final notice about a requirement to pay a financial penalty:

1. ACTION

1.1 The FSA gave Goldman Sachs International ("**GSI**" or the "**Firm**") a Decision Notice on 6 September 2010 which notified the Firm that pursuant to section 206 of the Financial Services and Markets Act 2000 ("**FSMA**" or the "**Act**"), the FSA had decided to impose a financial penalty of £17.5 million on the Firm in respect of breaches of Principles 2, 3 and 11 of the FSA's Principles for Businesses (the "**Principles**") which occurred between July 2009 at the latest and 16 April 2010 (the "**Relevant Period**").

1.2 The Firm confirmed on 3 September 2010 that it will not be referring the matter to the Upper Tribunal (Tax and Chancery Chamber).

1.3 Accordingly, for the reasons set out below, the FSA imposes a financial penalty on GSI in the amount of £17.5 million.

1.4 GSI agreed to settle at an early stage of the FSA's investigation. GSI, therefore, qualified for a Stage 1 discount under the FSA's executive settlement procedures. Were it not for this discount, the FSA would have imposed a financial penalty of £25 million on GSI.

2. REASONS FOR THE ACTION

Summary of conduct in issue

2.1 The FSA imposes the financial penalty on GSI for breaches of Principles 2, 3 and 11 in relation to:

(1) GSI's failure to inform the FSA, until 16 April 2010, that the staff of the United States Securities and Exchange Commission ("**SEC**") had indicated by a Wells Call on 28 September 2009 that it would serve, and then on 29 September 2009 served, a Wells Notice indicating the SEC staff's proposal to recommend an enforcement action for serious violations of US securities law by an approved person employed by GSI, Mr Fabrice Tourre, relating to his prior activities when working in the US for Goldman, Sachs & Co. ("**the Tourre Wells Notice**");

(2) GSI's failure to ensure that it had proper and effective systems and controls in place for the communication to GSI Compliance of information about regulatory investigations relating to other members of The Goldman Sachs Group, Inc. ("**GS Group**") that might affect GSI, as a result of which GSI failed to consider providing the FSA with information concerning the SEC's investigation ("**the SEC Investigation**") into the Abacus 2007-AC1 synthetic collateralised debt obligation ("**Abacus**" or "**the Abacus transaction**"), which Goldman, Sachs & Co. ("**GSC**") structured and which was marketed to sophisticated institutional investors, including by GSI from the UK. This could have been considered from February 2009 when approved persons at GSI were called to give testimony to the SEC regarding Abacus and should have been considered at the latest in July 2009, when GSC received a Wells Notice from the SEC staff indicating the SEC staff's proposal to recommend an enforcement action against GSC for serious violations of US securities law relating to Abacus ("**the GSC Wells Notice**"); and

(3) GSI's failure to conduct its business with due skill, care and diligence with respect to its regulatory reporting obligations.

2.2 During the Relevant Period, GSI breached Principle 11 by failing to disclose the Tourre Wells Notice to the FSA, which was information of which the FSA would reasonably expect notice and which was reasonably material to the assessment of Mr Tourre's fitness and propriety to hold a controlled function. The FSA accepts that this failure was not as a result of GSI deliberately withholding information.

2.3 During the Relevant Period, GSI breached Principle 2 by failing to conduct its business with due skill, care and diligence in relation to its regulatory reporting obligations. Specifically, GSI failed to consider the regulatory implications for GSI of the SEC Investigation, including the GSC Wells Notice and the Tourre Wells Notice.

2.4 During the Relevant Period, GSI breached Principle 3 by failing to take reasonable care to organise and control its affairs responsibly and effectively with adequate policies, procedures, systems and controls in relation to internal communications within the GS Group and GSI to enable GSI to fulfil its external regulatory reporting obligations.

2.5 In particular, GSI failed to:

(1) Comply with its UK regulatory reporting obligations because it did not notify the FSA of the Tourre Wells Notice until 16 April 2010;

(2) Put in place proper and effective systems to ensure that relevant information regarding the SEC Investigation was shared between the UK and US operations of the GS Group;

(3) Focus (or have procedures in place that were effective to ensure that those handling the matter at GSC focused) on the potential impact of the SEC Investigation (and in particular the GSC Wells Notice) upon GSI; and

(4) Ensure that GSI's compliance department was made specifically aware of the SEC Investigation (and in particular the GSC Wells Notice) so that it could consider whether any matters should be disclosed to the FSA in compliance with GSI's regulatory reporting obligations.

2.6 The FSA views these failings as particularly serious because:

(1) GSI is a premier financial institution with significant operations in the United Kingdom and globally;

(2) Given GSI's sophistication and global operations and the operation of Goldman Sachs as an integrated global firm, it should have had in place systems and controls that were effective to ensure relevant information concerning the SEC Investigation (and the Wells Notices issued to GSC and Mr Tourre) potentially affecting GSI was communicated appropriately and, in particular, to its compliance department to enable it to consider whether it needed to make appropriate notifications to the FSA;

(3) In particular, throughout the Relevant Period, there were a number of developments which either individually or cumulatively should have been brought to the attention of GSI's compliance function so that it could properly consider their impact on GSI's regulatory reporting obligations. This, however, did not occur. These developments included the following:

(a) when (from February 2009) the SEC staff indicated its intention to interview and subsequently (in March and May 2009) took testimony from certain GSI employees, who were holders of FSA approved functions, for the purposes of its investigation;

(b) when the SEC staff issued a Wells Notice to GSC in respect of the SEC staff's proposal to recommend an enforcement action for serious violations of US securities law relating to Abacus, which was marketed and sold by GSI from the UK to sophisticated institutional investors (on 28 July 2009); and

(c) when the SEC staff indicated that it would recommend enforcement action against Mr Tourre, a GSI employee and the holder of a controlled function, by a Wells Call on 28 September 2009 and subsequently issued a Wells Notice to Mr Tourre indicating the SEC staff's proposal to recommend an enforcement action for serious violations of US securities law against him personally (on 29 September 2009);

(4) A number of senior managers and other GSI personnel, including approved persons, were aware of certain aspects of the SEC Investigation, including that Mr Tourre had received a Wells Notice containing allegations of serious securities violations, well before 16 April 2010, but took no steps to ensure that GSI Compliance was made aware. Whilst it was not in the circumstances unreasonable for those people to assume that the matter would be properly handled, the FSA is disappointed that none of them raised the matter directly with GSI Compliance; and

(5) As a result of GSI's failure to inform the FSA about the Tourre Wells Notice, the FSA was not made aware by GSI that an approved person (Mr Tourre) holding controlled function 30 (customer function) was the subject of proposed enforcement action by an overseas regulator for serious violations of US securities law, a matter which was reasonably material to the assessment of Mr Tourre's fitness and propriety to hold a controlled function, with the consequence that Mr Tourre remained approved in the UK and able to perform a controlled function without further enquiry or challenge from the FSA for several months until the fact of the SEC Investigation became public knowledge on 16 April 2010.

2.7 In determining the level of financial penalty, the FSA has taken into account the following mitigating factors:

(1) GSI did not deliberately withhold any information from the FSA;

(2) GSI has a strong working relationship with the FSA, it has a good record of providing information to the FSA, and it has always been open and cooperative with the FSA;

(3) A programme of enhancements is being made to global systems and controls, to ensure that similar issues should not arise in the future;

(4) Immediately upon becoming aware that the SEC had filed proceedings, GSI took appropriate steps with respect to FSA notification and with respect to Mr Tourre;

(5) GSI has co-operated with the FSA in its investigation;

(6) The breaches did not cause any harm or risk of loss to any customers, they had no impact on the market, and GSI did not profit from them; and

(7) GSI has not previously been the subject of disciplinary action by the FSA.

3. STATUTORY AND REGULATORY PROVISIONS

3.1 The FSA is authorised, pursuant to section 206 of the Financial Services and Markets Act 2000, if it considers that an authorised person has contravened a requirement imposed on him by or under the Act, to impose on such person a penalty in respect of the contravention of such amount as it considers appropriate in the circumstances.

3.2 Pursuant to section 2(2) and section 3 of the Act, one of the FSA's statutory objectives is maintaining confidence in the financial system.

3.3 Principle 2 of the Principles states that:

"A firm must conduct its business with due skill, care and diligence."

3.4 Principle 3 of the Principles states that:

"A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems."

3.5 Principle 11 of the Principles states that:

"A firm must deal with its regulators in an open and cooperative way, and must disclose to the FSA appropriately anything relating to the firm of which the FSA would reasonably expect notice."

3.6 FIT 2.1.1.G states that:

"*In determining a person's honesty, integrity and reputation, the FSA will have regard to all relevant matters including, but not limited to, those set out in FIT 2.1.3G which may have arisen either in the United Kingdom or elsewhere. The FSA should be informed of these matters (see SUP 10.13.16 R), but will consider the circumstances only where relevant to the requirements and standards of the regulatory system …*"

3.7 FIT 2.1.3G states that:

"The matters referred to in FIT 2.1.1G to which the FSA will have regard include, but are not limited to: […]

(3) whether the person has been the subject of, or interviewed in the course of, any existing or previous investigation or disciplinary proceedings, by the FSA, by other regulatory authorities (including a previous regulator), clearing

houses and exchanges, professional bodies, or government bodies or agencies;

(4) whether the person is or has been the subject of any proceedings of a disciplinary or criminal nature, or has been notified of any potential proceedings or of any investigation which might lead to those proceedings"

3.8 The FSA's approach to exercising its enforcement powers to impose a financial penalty on an authorised person is set out in the Enforcement Guide ("**EG**").

4. FACTS AND MATTERS RELIED ON

Background

GSI, GSC and Fabrice Tourre

4.1 GSI is a London-based, wholly-owned subsidiary of the GS Group, a global financial institution with its head office in the USA. The GS Group's European activities are headquartered at GSI in London.

4.2 GSI is an investment banking, securities and investment management firm and is regulated and authorised by the FSA. GSI is authorised to carry on investment business, including dealing in investments (as agent and principal) and arranging (bringing about) deals in investments.

4.3 As a regulated firm, GSI is required to comply with the rules set out in the FSA's Handbook.

4.4 GSC is a New York-based US entity that is also part of the GS Group. It carries on in the United States business broadly similar to that of GSI in the UK.

4.5 Mr Tourre was a GSC employee at the time of the Abacus transaction, but was transferred to GSI in October 2007, and was approved by the FSA as an approved person with controlled function 30 (customer function) on 24 November 2008. His approval was withdrawn on 19 April 2010, following publication (on 16 April 2010) of the complaint issued by the SEC to him and GSC alleging serious violations of US securities law in relation to the Abacus transaction (the "**Complaint**"). As set out below, Mr Tourre does not accept the allegations made in the Complaint.

The SEC Complaint

4.6 The SEC began seeking information from GSC concerning the Abacus transaction in August 2008, as part of its broader enquiry about subprime matters. Over a period of almost a year from August 2008, documents (including GSI documents) were obtained by the SEC from GSC and evidence was obtained from GSC and GSI personnel in relation to the genesis, structuring and marketing of the Abacus transaction. Subsequently, the SEC

staff issued a Wells Notice to GSC in July 2009 and issued a Wells Notice to Fabrice Tourre in September 2009. A Wells Notice is, in effect, an indication from the SEC staff that they are considering recommending or that they intend to recommend – subject to hearing facts and arguments to the contrary as part of the Wells process – that the SEC file an enforcement action against the person or entity to whom the notice is addressed. If such a recommendation were made, it would then be put before the SEC Commissioners for a decision on whether enforcement action should be initiated.

4.7 Subsequently, the SEC commenced enforcement proceedings against GSC and Mr Tourre by filing the Complaint with the United States District Court for the Southern District of New York on 16 April 2010 (without any warning to GSC). The SEC alleged in the Complaint that GSC and Fabrice Tourre committed serious violations of US securities law by making misleading statements and omissions in connection with the Abacus transaction.

4.8 In particular, the SEC Complaint averred that GSC and Mr Tourre produced and utilised marketing materials in connection with Abacus which included a term sheet, flip book and offering memorandum (the "**Marketing Documents**") which failed to disclose that a hedge fund, Paulson & Co, Inc. ("**Paulson**") (i) had played a significant role in the portfolio selection process by making suggestions to the selection agent in relation to the subprime residential mortgage-backed securities ("**RMBS**") underlying Abacus; and (ii) had, through a transaction with a Goldman entity, arranged to take a short position in respect of Abacus.

4.9 On 15 July 2010, the SEC announced that it had reached a settlement with GSC (subject to the approval of the US courts), under which GSC would pay US$550 million to cover disgorgement and a civil penalty (including payment of compensation in the amount of US$150 million to funds managed by IKB Deutsche Industriebank ("**IKB**"), which invested in Abacus Class A-1 and Class A-2 Notes and US$100 million to Royal Bank of Scotland, owner of ABN Amro Bank N.V., which had entered into a related credit default swap with GSI, as set out below). Under the terms of the settlement GSC neither admitted nor denied the allegations in the Complaint. A final judgment approving the settlement was entered by the Court on 20 July 2010. As part of the settlement GSC accepted that:

"*Goldman acknowledges that the marketing materials for the ABACUS 2007-AC1 transaction contained incomplete information. In particular, it was a mistake for the Goldman marketing materials to state that the reference portfolio was "selected by" ACA Management LLC without disclosing the role of Paulson & Co. Inc. in the portfolio selection process and that Paulson's economic interests were adverse to CDO investors. Goldman regrets that the marketing materials did not contain that disclosure.*"

4.10 The SEC's claim against Mr Tourre continues. Mr Tourre filed his response to the Complaint on 19 July 2010. He denies the allegations against him.

Abacus

4.11 Abacus was a synthetic collateralised debt obligation (a "**synthetic CDO**") linked to the performance of a reference portfolio of RMBS (the "**RMBS Portfolio**"). Abacus was structured by GSC in New York in late 2006 / early 2007 and was subsequently marketed to sophisticated institutional investors, including by GSI in the UK.

4.12 Abacus was the 23rd transaction to be structured under the Abacus platform, which was first developed in 2004 at the request of IKB, with whom GSC worked closely on development of the platform.

4.13 ACA Management LLC ("**ACA**"), a firm which had previously constructed and managed numerous CDOs and had previously written credit protection in connection with synthetic CDOs, was appointed as portfolio selection agent for Abacus, meaning that it would select the RMBS Portfolio. The marketing materials for Abacus identify ACA as having selected the portfolio. A key allegation of the SEC Complaint is that Paulson played an undisclosed role in the portfolio selection process and that ACA mistakenly believed that Paulson was investing in the equity tranche, therefore having a "long" position and economic interests aligned with ACA's, when in fact it was Paulson's intention to take a "short" position on the transaction, with the consequence that its economic interests were opposed to ACA's.

4.14 Mr Tourre was part of the GSC team which structured Abacus, and he was involved in the preparation of marketing materials and communicated directly with investors. It was the SEC's case that Mr Tourre and GSC contributed to ACA's misunderstanding that Paulson had a "long" position, rather than a "short" position, in relation to Abacus.

4.15 The Abacus notes were offered by GSC in the United States under Rule 144A of the Securities Act of 1933 (the "**Securities Act**") and were offered outside the United States by GSI, which was described in the Abacus offering memorandum as GSC's agent, in reliance on Regulation S of the Securities Act.

4.16 Abacus was marketed by GSI in London to potential investors, including IKB. GSI also sought counterparties to intermediate a related credit default swap ("**CDS**")with an ACA affiliate representing the super-senior tranche of Abacus, including ABN Amro Bank N.V., London Branch ("**ABN**"). IKB and ABN ultimately both participated in Abacus-related transactions in the manner set out below. In addition, the Abacus-related CDS transactions with Paulson entities were booked through GSI.

4.17 The entities set out below participated in Abacus-related transactions in the following way:

(1) **ACA** acted as portfolio selection agent for Abacus and, through three separate entities, purchased US$42 million Class A-2 notes;

(2) **IKB** purchased US$50 million Class A-1 notes and US$100 million Class A-2 notes through two separate entities;

(3) **ACA Capital Holdings, Inc.** (**"ACA Capital"**), ACA's parent company, sold protection to ABN for a notional amount of $909 million referencing the super senior tranche (50-100%). In other words ACA Capital assumed the credit risk associated with the super senior tranche of Abacus via a CDS;

(4) **ABN** entered into a CDS with GSI (intermediating the CDS between ACA and GSI) for a notional amount of $909 million referencing the super senior tranche (50-100%) of Abacus, in which ABN sold protection. In addition, ABN entered into a CDS with GSI to buy protection on ACA Financial Guaranty Corporation for $27 million;

(5) **Paulson**, through its entity Paulson Credit Opportunities Master II Limited, entered into CDSs with GSI to buy (a) credit protection for a notional amount of $1 billion referencing the super senior tranche (45-100%) of the Abacus CDO; and (b) $192 million credit protection with respect to the reference portfolio underlying Abacus; and

(6) **Goldman Sachs** entities retained a position in the 45-50% tranche of the CDO, as well as having a number of other roles in connection with the transaction.

Analysis of Breaches

4.18 GSI has breached the following FSA rules and principles:

(1) Principle 2 (skill, care and diligence);

(2) Principle 3 (management and control); and

(3) Principle 11 (relations with regulators).

4.19 During the Relevant Period, there were a number of key events in relation to the SEC Investigation which should have been notified to GSI Compliance to enable it properly to consider GSI's regulatory reporting obligations. Furthermore, the Tourre Wells Notice is a matter that should specifically have been disclosed to the FSA in accordance with GSI's obligations under Principle 11. The key events are set out below.

Key Events

4.20 For several months prior to 16 April 2010, when the SEC issued its Complaint and the SEC Investigation became public knowledge, the SEC Investigation was well known to individuals within relevant control functions in New York (i.e. GSC's legal and compliance functions) and relevant business people in New York. In addition, a number of senior managers at GSI, including approved persons, knew about certain aspects of the SEC Investigation, including the GSC and/or Tourre Wells Notices, but did not inform GSI Compliance.

4.21 As set out below, there were at least three key events which GSI's systems and controls should have ensured were, cumulatively or individually, brought to

the attention of GSI Compliance so that it could consider whether appropriate notifications needed to be made to the FSA in order to fulfil GSI's regulatory reporting obligations:

(1) When the SEC staff indicated its intention to interview (in February 2009) and subsequently took testimony from certain GSI employees, who held controlled functions, in the USA for the purposes of its investigation (in March and May 2009 respectively);

(2) When the SEC staff issued a Wells Notice to GSC indicating the SEC staff's proposal to recommend an enforcement action for serious securities violations relating to Abacus, which was marketed and sold by GSI from the UK to sophisticated institutional investors (on 28 July 2009);

(3) When the SEC staff indicated it proposed to recommend an enforcement action against Mr Tourre, a GSI employee and the holder of a controlled function, by a Wells Call on 28 September 2009, and subsequently issued a Wells Notice to Mr Tourre indicating the SEC staff's proposal to recommend an enforcement action for serious securities violations against him personally (on 29 September 2009); (each a "**Key Event**"; collectively the "**Key Events**").

Knowledge of Senior Managers and Approved Persons at GSI of the Key Events: SEC Investigation into GSC and testimony of GSI approved persons

4.22 Various senior managers and approved persons at GSI were aware, by various channels of communication, of certain aspects of the SEC Investigation and the Key Event(s) during the course of 2009.

4.23 In early February 2009, four senior personnel at GSI were made aware that Mr Tourre or another GSI employee who was an approved person had been asked to give testimony in connection with the SEC Investigation. They were not made aware of the details of the SEC Investigation. They assumed that, as Goldman Sachs operated as a global firm, other staff at GSI would have been briefed, if they needed to know. In fact, GSC had not considered the possible regulatory implications of the SEC Investigation for GSI and had not briefed anyone in GSI Compliance on the details of the matter.

Knowledge of Senior Managers and Approved Persons at GSI of the Key Events: Service by the SEC staff of Wells Notices on GSC and Mr Tourre

4.24 From July 2009 to 29 September 2009 – more than six months before the SEC formally commenced legal proceedings against GSC and Mr Tourre – the SEC Investigation progressed from "evidence gathering" to the point where the SEC staff indicated that they intended to recommend to the SEC Commissioners that a civil enforcement action be filed against both GSC and Mr Tourre.

4.25 On 28 July 2009, the SEC staff held a "Wells Call" with GSC stating that the SEC staff intended to recommend to the SEC Commissioners that a civil

enforcement action be filed against GSC in relation to serious violations of US securities law relating to Abacus. This was followed by a formal Wells Notice issued by the SEC staff.

4.26 On 10 and 25 September 2009, GSC filed its submissions and supplemental submissions to the Wells Notice.

4.27 On 15 September 2009, the SEC staff indicated to GSC's US external counsel that the staff intended to recommend a civil enforcement action be brought against Mr Tourre for securities violations.

4.28 On 28 September 2009 the SEC staff held a "Wells Call" with Mr Tourre informing him that the SEC staff was considering bringing legal proceedings against him for securities violations. This was followed by service of the Tourre Wells Notice on 29 September 2009.

4.29 On 26 October 2009, Mr Tourre filed his submissions in response to the Tourre Wells Notice.

4.30 From July 2009 onwards, a number of senior managers within GSC were aware that a Wells Notice had been issued to GSC. From September 2009, certain senior managers at GSI also became aware of the GSC Wells Notice in the context of being made aware of the Tourre Wells Notice (as set out below). It appears that none of these individuals, nor the personnel in New York who were managing or involved with GSC's engagement with the SEC Investigation, considered the potential impact of the GSC Wells Notice on GSI. Consequently, relevant information relating to the GSC Wells Notice was not communicated to GSI Compliance.

4.31 From September 2009 certain senior managers, including approved persons, within GSI were aware of the Tourre Wells Notice and the seriousness of the allegations that had been made by the SEC staff against Mr Tourre. It was clear by this time that Mr Tourre was under investigation personally for alleged non-disclosure of material facts to investors in connection with Abacus. Although it was understood that such allegations related to Mr Tourre's activities when he had previously worked for GSC (and not from his activities when working at GSI), the regulatory implications for GSI of the Tourre Wells Notice should have been obvious since Mr Tourre was now an employee of GSI and an FSA approved person. However, the individuals concerned did not bring the Tourre Wells Notice to the attention of GSI Compliance so that GSI's regulatory reporting obligations in respect of the Tourre Wells Notice could be considered.

Conclusion

4.32 A number of senior managers, including approved persons, at GSI were aware of certain aspects of the SEC Investigation, including the Tourre Wells Notice and/or the GSC Wells Notice. However, none of these individuals appears to have appreciated the potential regulatory impact of these matters on GSI, not least because those handling the matter at GSC did not focus on Mr Tourre's status as an FSA approved person or the implications of the SEC's allegations

for GSI. Those handling the matter at GSC did not brief the relevant senior managers at GSI on the involvement that GSI had had in the Abacus transaction and the implications of the SEC's allegations for GSI. The relevant senior managers at GSI do not appear to have considered the potential regulatory impact on GSI because they understood that GSC Legal was engaged and handling the matter and that GSI Legal was being made aware of it. They assumed that since legal was engaged, relevant information would be passed to those individuals within the GS Group who needed to know. However, neither legal, nor compliance in New York, passed on relevant information to GSI Compliance. Those handling the matter in New York appear to have focused exclusively on the regulatory implications of the SEC Investigation for GSC and do not appear to have focused on the potential for specific regulatory impact on GSI, even though certain relevant personnel in New York were aware that Abacus had been marketed by GSI to investors in other jurisdictions.

4.33 Whilst it was not unreasonable for the senior managers at GSI to assume that the matter would be properly handled as the legal department (in New York and London) was aware of it, that assumption turned out in this case to be wrong because GSI's procedures, policies, systems or controls were not adequate to ensure that information about the SEC Investigation, including the Wells Notice, was communicated to those within GSI who needed to know. Consequently, GSI Compliance was not provided with the necessary information to enable it to consider whether an appropriate notification needed to be made by GSI to the FSA regarding these matters.

4.34 Furthermore, from September 2009, a number of senior managers at GSI were aware that Mr Tourre had received (or was about to receive) a Wells Notice. This was information of which the FSA would reasonably expect notice and which reasonably was material to an assessment of the fitness and propriety of an FSA approved person. However, the individuals concerned did not consider the regulatory implications of the Tourre Wells Notice for GSI. They did not inform GSI Compliance about the Tourre Wells Notice and GSI did not inform the FSA. As set out below, GSI's failure to inform the FSA about the Tourre Wells Notice constitutes a breach by GSI of Principle 11.

Principles 2 (due skill, care and diligence) and 3 (management and control)

4.35 By reason of the facts and matters set out below, the FSA considers that GSI breached the requirements of Principles 2 and 3 by failing to exercise due skill, care and diligence, and by failing to put in place systems and controls that were effective to ensure that relevant information concerning the SEC Investigation and the Wells Notices was communicated to GSI Compliance so that it could properly consider GSI's regulatory reporting obligations.

4.36 In particular, GSI:

(1) Failed to focus (or ensure that those handling the matter at GSC focused) on the potential impact of the SEC Investigation (and in particular the GSC Wells Notice) upon GSI; and

(2) Failed to ensure that appropriate procedures, policies, systems and controls were in place to ensure that relevant information relating to the SEC Investigation (including the Wells Notices) and the potential implications for GSI was communicated to GSI Compliance, so that it could consider whether appropriate notifications needed to be made to the FSA in compliance with GSI's regulatory reporting obligations.

4.37 The particular respects in which GSI failed to exercise due skill, care and diligence and/or in which its systems and controls were insufficiently effective are as follows.

Failure to appreciate that the SEC Investigation had a potential impact on GSI

4.38 Those who were aware of the SEC Investigation and the Wells Notices, both at GSC and at GSI, did not focus upon their potential impact on GSI as they should have done.

4.39 The FSA understands that GSC did not believe that the SEC Investigation would conclude with an outcome that was material for the firm. After it received the GSC Wells Notice, GSC continued to believe either that it would be able to persuade the SEC staff not to proceed or that the matter could be settled on terms that would not be material, and that any resolution would at most involve only GSC (and not any individuals). In addition, although GSI's role in marketing Abacus was apparent from the Offering Memorandum, those at GSC handling the matter viewed it as a matter that involved a US regulator looking into products originated in the US by a US regulated entity involving the US subprime market, and failed to appreciate the potential regulatory impact on GSI.

4.40 At no point was any kind of detailed briefing given by GSC staff to GSI staff regarding the SEC Investigation and its potential impact on GSI. Although descriptions of the SEC Investigation were provided to some extent at meetings attended by GSI personnel, to the best of the recollection of the GSC staff who presented at such meetings, discussion of the SEC Investigation did not focus on GSI or on any potential impact on GSI.

4.41 Although a number of senior managers and other GSI employees, including approved persons, were at certain times made aware of certain aspects of the SEC Investigation, none of them considered the question of whether the FSA should be informed or even whether GSI Compliance was aware of the matter. The likely reason for this is that such individuals did not have sufficient knowledge or understanding of the SEC Investigation for its potential impact on GSI to be apparent to them. They were aware that GSC Legal was dealing with the SEC Investigation. They assumed that, as Goldman Sachs operated as an integrated global firm, GSC would communicate relevant information regarding the SEC Investigation to those within the GS Group who "needed to know". While this assumption was not unreasonable, it turned out nevertheless to be wrong since GSI's procedures, policies, systems and controls were insufficient to ensure that such relevant information was shared with GSI Compliance.

The absence of effective systems and controls to ensure relevant information was communicated to GSI Compliance

4.42 GSI was necessarily reliant upon GSC to inform it of matters, arising in the context of US SEC investigations, that were relevant to GSI's compliance with its regulatory obligations. However, GSI's procedures, policies, systems and controls were insufficient to ensure that GSC would (i) take due account of the potential regulatory impact on GSI and (ii) communicate relevant information to GSI Compliance so that the impact on GSI's local regulatory reporting obligations could be considered and appropriate notifications made, if necessary.

4.43 The absence of sufficient systems and controls for ensuring the appropriate communication flow of relevant information relating to the SEC Investigation within the GS Group on a "need to know" basis and for considering the regulatory implications for other GS Group entities, in particular GSI, and the fact that those senior managers in GSI who became aware of Mr Tourre's Wells Notice also did not inform GSI Compliance, created an unacceptable risk that GSI's regulatory obligations would not be considered at all. In an organisation of the resources and sophistication of GSI, this is unacceptable.

4.44 Goldman Sachs is a highly sophisticated firm and among the world's premier financial institutions. The firm itself and its legal and compliance functions are integrated on a global basis and the senior management of those functions are (or ought to be) in constant communication with each other regarding legal and regulatory matters across the multiple jurisdictions in which Goldman Sachs operates its global business.

4.45 GSI should have ensured that its procedures, policies, systems and controls would operate so as to ensure that those handling the SEC Investigation would consider, identify and raise specifically with GSI and its compliance function matters which could reasonably be expected to have a significant impact upon GSI. This was necessary to ensure that GSI would be in a position to consider and comply with its own regulatory reporting obligations to the FSA.

Such procedures and controls as existed were ineffective

4.46 Such limited systems and controls as were in place and which may have brought relevant information to the attention of GSI Compliance were ineffective for the reasons described above.

4.47 In addition, the compliance department's global registrations team, based in New York, London and Asia, is responsible for the registration of Goldman Sachs employees with relevant regulators and exchanges, including the FSA. Information concerning staff members, including their registrations, is available to the registrations team globally on a system called "REPS". The registration teams in different jurisdictions liaise where necessary where an individual has dual registrations. It is the registrations team that would take the necessary steps to provide information about an approved person to the FSA.

4.48 Those people who were handling the SEC Investigation at GSC focused on responding to the SEC's investigative requests and, subsequently, the Wells Notices. Neither they nor others at GSC or GSI who were aware of the Tourre Wells Notice focused upon the regulatory implications for Mr Tourre, or GSI, and so the necessary steps were not taken to deal with such matters. This meant that the registrations team was not informed of the Tourre Wells Notice. Consequently, no information concerning it was provided to the relevant regulators: FINRA (the United States' Financial Industry Regulatory Authority) and the FSA.

4.49 Had the registrations team been notified, it is likely that Mr Tourre's FSA approval would have been identified and that GSI Compliance would have been provided with relevant information regarding the SEC Investigation and the Tourre Wells Notice to enable it to give due consideration to whether GSI was required to make an appropriate notification to the FSA.

4.50 GSI had too few controls in this area. There was insufficient means for GSI Compliance to check whether it was being provided with relevant information concerning the SEC Investigation in order satisfactorily to assess what GSI needed to do in order to comply with its regulatory reporting obligations.

Principle 11 (relations with regulators)

4.51 By reason of the facts and matters set out below, the FSA considers that GSI failed, in breach of Principle 11, to disclose to the FSA the Tourre Wells Notice, which constituted information of which the FSA would reasonably expect notice and which reasonably was material to the assessment of the fitness and propriety of an FSA approved person. Specifically, GSI failed to inform the FSA of the Tourre Wells Notice in September 2009 or at any time prior to 16 April 2010.

4.52 The Tourre Wells Notice was a matter of which the FSA would reasonably expect notice in accordance with Principle 11 because:

(1) The allegations set out in the Wells Call placed by the SEC staff to Mr Tourre's counsel were, in summary, that (i) the Marketing Documents and/or other information produced by GSC did not disclose, accurately and completely, all information as to the roles of Paulson and ACA in the selection of the RMBS Portfolio for the Abacus transaction; and (ii) Mr Tourre misled ACA as to Paulson's economic interest in relation to Abacus; and

(2) Such allegations would, if charges were brought and proved, constitute serious violations of US securities law. Consequently, the Tourre Wells Notice was a matter of which the FSA would reasonably expect notice under Principle 11 and constituted information which reasonably was material to the assessment of Mr Tourre's fitness and propriety to hold a controlled function. Nothing in this Notice, however, is intended to indicate any view on the part of the FSA as to Mr Tourre's fitness and propriety or as to the merits of the case brought against him by the SEC.

GSI senior managers knew about the Tourre Wells Notice but did not take steps to ensure that GSI Compliance was aware

4.53 As set out above, certain senior managers at GSI knew about the Tourre Wells Notice, but did not take steps to ensure that GSI Compliance was informed so that it could inform the FSA.

4.54 Those senior managers at GSI who received information about the Tourre Wells Notice, either did not understand the regulatory implications of the notice for GSI or assumed that others would ensure that such implications were considered. Whilst it was not unreasonable for the senior managers at GSI to assume that the matter would be properly handled as the legal department (in New York and London) was aware of it, the FSA is disappointed, given the experience and seniority of the individuals concerned, that none of them raised the matter with GSI Compliance to ensure that GSI's regulatory reporting obligations would be properly considered. The FSA would expect these senior managers to have been more focused on the need for the Firm to consider the UK regulatory implications arising from the Tourre Wells Notice.

Conclusion

4.55 The FSA considers that GSI has breached Principle 11 because it failed to disclose to the FSA the fact of the Tourre Wells Notice.

4.56 For the reasons set out above, the Tourre Wells Notice was information of which the FSA would reasonably expect notice in accordance with Principle 11.

4.57 The FSA acknowledges that the Principle 11 breach in this case was not deliberate, but inadvertent; however, it is nevertheless a serious breach in view of:

(a) the seniority and experience of the GSI managers who were aware of the Tourre Wells Notice;

(b) the seriousness of the allegations made in the Tourre Wells Notice;

(c) the obvious regulatory implications for GSI arising from the Tourre Wells Notice, namely that it was information which was reasonably material to an assessment of Mr Tourre's fitness and propriety to carry out a controlled function; and

(d) the stature, resources and reputation of GSI.

4.58 Consequently, although the breach in this case was not deliberate and does not reflect adversely on the integrity of GSI or the individuals concerned, the FSA nevertheless considers it to be a serious breach of Principle 11, driven by significant breaches of Principles 2 and 3, which should attract a substantial fine.

5. SANCTION

5.1 The FSA's policy on the imposition of financial penalties and public censures is set out in the FSA's Decision Procedure & Penalties manual ("DEPP") and EG. In determining the financial penalty proposed, the FSA has had regard to this guidance.

5.2 Since the majority of GSI's relevant conduct occurred before the introduction of the new penalty regime on 6 March 2010, the FSA has applied the penalty regime that was in place prior to 6 March 2010.

5.3 The principal purpose of a financial penalty is to promote high standards of regulatory conduct by deterring firms who have breached regulatory requirements from committing further contraventions, helping to deter other firms from committing contraventions and demonstrating generally to firms the benefits of compliant behaviour.

5.4 For the reasons set out above, the FSA considers that GSI breached Principles 2, 3 and 11. In determining that the financial penalty is appropriate and proportionate in this case, the FSA has considered all the relevant circumstances. The FSA considers the following factors to be particularly important.

Deterrence (DEPP 6.5.2G(1))

5.5 GSI is a premier financial institution with significant operations in the United Kingdom and globally. It has very significant financial resources at its disposal to ensure that its internal procedures and external reporting systems and controls are fit for purpose and compliant with FSA rules. The FSA considers there to be a need to send a strong and robust message to the industry that the processes in place in order to enable a firm to interact appropriately with the FSA are of paramount importance in ensuring that firms pay due regard to their regulatory obligations and that they are fully compliant with the UK regulatory regime. Systems and controls must be adequate in all areas of a firm's business.

Seriousness and impact of the breach (DEPP 6.5.2(2))

5.6 The FSA has had regard to the seriousness of the breaches including the nature of the requirements breached, the duration and frequency of the breaches and whether the breaches revealed failings in the firm's systems and controls. The FSA considers GSI's breaches of Principles 2, 3 and 11 to be particularly serious for the following reasons:

(1) Throughout the Relevant Period, there were a number of key events relating to the SEC Investigation, aspects of which were known to certain senior managers at GSC and GSI, including approved persons, and which either individually or cumulatively should have been communicated to GSI Compliance so as to enable it to consider GSI's regulatory reporting obligations and whether an appropriate notification needed to be made to the FSA. Nevertheless, relevant

information relating to the SEC Investigation was not communicated to GSI's compliance function with the result that GSI Compliance did not consider GSI's regulatory reporting obligations. The inability to achieve effective internal communication in relation to high-impact regulatory matters with cross jurisdictional implications is unacceptable in a firm of GSI's size, resources and sophistication. Whilst it was not unreasonable for the individuals involved to assume that the matter would be properly handled (since the legal department was aware of it), the fact that this failure of communication occurred in spite of a number of senior GSI managers being aware of certain aspects of the SEC Investigation and the Tourre Wells Notice is disappointing;

(2) As a consequence of the Principle 11 breach, Mr Tourre was able to continue to perform a controlled function for several months without the FSA being able to consider the impact of the information contained in the Tourre Wells Notice on his fitness and propriety to do so (i.e. the fact that the SEC had alleged that Mr Tourre had committed serious violations of US securities law in connection with Abacus);

(3) There were inadequate policies, procedures, risk management systems and controls in place at GSI to ensure that its compliance and regulatory reporting obligations were satisfactorily met; and

(4) There was a failure by GSI in this case to engage properly with its UK regulatory obligations, such that there was an unacceptable risk that such obligations would not be considered at all.

The extent to which the breach was deliberate or reckless (DEPP 6.5.2(3))

5.7 Although the FSA considers that the circumstances of GSI's breaches of the FSA's Principles are serious, the FSA does not consider that GSI intentionally or recklessly breached the FSA's Principles and does not consider that the breaches reflect adversely on the integrity of GSI or any of the individuals concerned.

The size, financial resources and other circumstances of the firm (DEPP 6.5.2(5))

5.8 In deciding on the level of penalty, the FSA has had regard to the size of the financial resources of GSI. GSI is a member of the GS Group which is one of the world's premier financial institutions. GSI is required to have in place systems and controls around the internal reporting and escalation of relevant information sufficient to ensure that it fully complies with its regulatory reporting responsibilities.

5.9 The FSA has no evidence to suggest that GSI is unable to pay the financial penalty. For the 13 months ended 31 December 2009 its trading profit (broadly equivalent to turnover) was $11.2 billion, and its profit before taxation was $4.8 billion. As at 31 December 2009, GSI's net assets were $16.4 billion.

The amount of profits accrued or the loss avoided (DEPP 6.5.2(6))

5.10 GSI did not profit from the breaches.

Conduct following the breach (DEPP 6.5.2(8))

5.11 The FSA understands that GSI is in the course of reviewing its internal policies and procedures around the internal communication of regulatory matters and that a number of changes have already been made.

Disciplinary record and compliance history (DEPP 6.5.2(9))

5.12 GSI has not previously been the subject of FSA enforcement action.

Other action taken by the FSA (DEPP 6.5.2(10))

5.13 In determining the level of financial penalty, the FSA has taken into account penalties imposed by the FSA on other authorised persons for similar behaviour. However, the FSA has also had regard to the principal purpose for which it imposes sanctions, namely to promote high standards of regulatory conduct.

Conclusions

5.14 The FSA considers that the seriousness of GSI's breach of Principles 2, 3 and 11 merits a very substantial financial penalty. In determining the proposed financial penalty, the FSA has considered the need to send a clear message to the industry of the need to ensure that larger firms with a presence in multiple jurisdictions and subject to multiple regulatory regimes have adequate systems and controls in place to ensure that relevant information is shared appropriately and in a timely fashion within their global legal and compliance functions, not only to ensure that the potential impact of overseas regulatory investigations is duly considered and local regulatory obligations are duly complied with, but also to ensure that the business of the firm can be properly organised and controlled. While it is appropriate to organise a firm in such a way that its compliance function is responsible for making regulatory notifications, the FSA expects the firm's senior managers, who become aware of a matter which they ought reasonably to appreciate has regulatory implications, to focus on the need for the firm to comply with its regulatory reporting obligations and to ensure that those responsible for considering the firm's reporting obligations are properly informed of the information they need to know. Senior management must take responsibility for ensuring that the firm has effective systems in place to enable it to communicate promptly and appropriately all information of which the FSA would reasonably expect notice. Communication failures arising as a consequence of group structures or procedural deficiencies will neither excuse nor mitigate failures by firms to comply with that responsibility.

5.15 The FSA considers, taking into account the applicable Stage 1 discount for early settlement, that a financial penalty of £17.5 million is appropriate.

6. DECISION MAKERS

6.1 The decision which gave rise to the obligation to give this Final Notice was made on behalf of the FSA by the Settlement Decision Makers.

7. IMPORTANT

7.1 This Final Notice is given to GSI in accordance with section 390 of the Act.

Manner of and time for Payment

7.2 The financial penalty must be paid in full by GSI to the FSA by no later than 23 September 2010, 14 days from the date of this Final Notice

If the financial penalty is not paid

7.3 If all or any of the financial penalty is outstanding on 24 September 2010, the FSA may recover the outstanding amount as a debt owed by GSI and due to the FSA.

Publicity

7.4 Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the FSA must publish such information about the matter to which this notice relates as the FSA considers appropriate. The information may be published in such manner as the FSA considers appropriate. However, the FSA may not publish information if such publication would, in the opinion of the FSA, be unfair to GSI or prejudicial to the interests of consumers.

FSA contacts

7.5 For more information concerning this matter generally, GSI should contact Greg Brandman (020 7066 3032) or Jonathan Baker (020 7066 1352) at the FSA.

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Tracey McDermott
Head of Department
FSA Enforcement and Financial Crime Division