McKinsey & Company statement on Eskom

17 October 2017

Over the past four months our Global General Counsel, Jean Molino, conducted a thorough investigation into the claims of wrongdoing levelled against McKinsey & Company regarding our work at Eskom since 2015 that involved Regiments Capital and Trillian. She was assisted by two law firms, Norton Rose Fulbright in consultation with Morrison & Foerster. The investigation included collecting 2.4 million emails; reviewing hundreds of thousands of documents, including contracts, invoices, payments, telephone, personal email, and financial records; and conducting over 60 interviews. Now, as this investigation nears completion, we are in a position to speak with additional certainty about these matters.

Dominic Barton, McKinsey & Company's Global Managing Partner, said:

> "As a firm, we take these issues very seriously. We deplore corruption and we will cooperate fully with relevant authorities and any official inquiries and investigations into these matters. We are sorry for the distress this matter has caused the people of South Africa, our clients, colleagues, alumni, and others.
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> "We acknowledge that there are more than just legal issues at stake, and that many have raised – sometimes with significant emotion – concerns about our broader practices in, and commitment to, South Africa. We assure you that we hear you. We are taking a hard look at all of our practices in the country to ensure that we are not just compliant with the law and free of any form of corruption, but also that we are seen as a constructive partner in building a better future for South Africa. This is our, and my personal, commitment to you."

In summary, our findings from the investigation are that we have never served the Gupta family or any companies publicly linked to the Gupta family; we have never had a contract or supplier development partnership with Trillian, although we did work alongside Trillian for several months at Eskom; Trillian failed our due diligence in March 2016 after repeatedly refusing to provide details about its ownership; and we terminated all discussions with Trillian and informed Eskom that Trillian would not be our supplier development partner. That said, we should not have started working alongside Trillian in December 2015 before we had completed our due diligence and had answers to our questions.

We also found violations of our professional standards. Where we found issues, we disciplined individuals in line with our procedures and made improvements to our processes. Vikas Sagar, a partner, has decided to leave our firm. Others have been sanctioned or have left the firm. We became aware of one other potential professional standards issue, unrelated to Eskom, which we are in the process of investigating; we will take action as appropriate.

Tom Barkin, McKinsey's Global Chief Risk Officer, said:

> "The allegations against us have been painful. We have been focused for the last four months on getting the facts straight. This has taken longer than we had hoped because we wanted to be thorough.
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> "There are things we wish we had done differently and will do differently in the future, but we reject the notion that our firm was involved in any acts of bribery or corruption related to our work at Eskom and our interaction with Regiments or Trillian.

> "We were not careful enough about who we associated with, did not understand fully the agendas at play, and should not have worked alongside Trillian, even for a few months, before completing our due diligence. The behaviours of some individuals fell short of our standards. Some of our processes were inadequate and we have acted to reinforce compliance and improve them. We did not communicate appropriately to Advocate Budlender. We are embarrassed by these failings and we apologise to the people of South Africa, our clients, our colleagues, and our alumni, who rightly expect more of our firm.
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> "Our investigation was based on the information to which we had access; we would ask that anyone who may have additional relevant facts to contact our General Counsel so we can further enhance our understanding of these events and take all appropriate actions."[1]

We include below further detail of our investigation and the actions we are taking.

Our findings

We launched our internal investigation after we became aware of a letter sent by McKinsey on 9 February 2016 that inaccurately characterised our relationship with Trillian. Our investigation focused on our work at Eskom since 2015 that involved Regiments Capital and Trillian.

Based on the investigation, we can make the following conclusions:

1. McKinsey has never served the Gupta family nor any companies publicly linked to the Gupta family.
2. McKinsey has never made payments directly or indirectly to secure contracts, nor have we aided others in doing so.
3. McKinsey did not introduce Trillian to Eskom nor vice versa.
4. McKinsey has not made payments to Trillian.
5. McKinsey never had a contract with Trillian, although we worked alongside them for a few months at Eskom.
6. McKinsey's 9 February 2016 letter did not provide authorisation for Eskom to pay Trillian as the conditions set out in the letter had not been met.
7. Trillian failed our due diligence and we terminated discussions with them about a supplier development partnership in March 2016. We believe that Trillian withheld information from us about its connections to a Gupta family associate. We informed Eskom of this decision by letter on 30 March, having previously flagged our concerns to Eskom about Trillian's continued failure to disclose its beneficial ownership.
8. McKinsey did not authorise any payments made by Eskom to Trillian, and any payments by Eskom to Trillian were made by Eskom after McKinsey informed Eskom that Trillian failed our due diligence.

We note that a recent letter from Bowmans, Eskom's outside counsel, of 4 October 2017, reaches the same conclusions as we do on points 5-8 above.

We have concluded that we made several errors of judgment and process:

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[1] Jean Molino can be reached at jmolino@mckinsey.com

- Some of our administrative processes were not followed. For example, a letter sent to Eskom in February 2016, even conditionally authorising invoicing or payment, should not have been issued for a party with whom we did not have a subcontract. Whilst Eskom has conceded it did not rely on this letter for payment, the letter was inaccurately drafted and insufficiently reviewed. We found no evidence of bad faith in the drafting of this letter.
- In our eagerness to be responsive to the challenges Eskom faced, we mobilised our teams too quickly and began working alongside employees from Trillian in late 2015, before we later rejected a partnership with them in March 2016. Whilst our risk processes ultimately worked, we should have completed them sooner. We should not have begun to work alongside Trillian before we had completed our due diligence and without a contract in place. Had we fully understood Trillian's ownership structure at the time, we would not have considered working with them.
- We failed to engage adequately with Advocate Budlender. When we became aware that a letter McKinsey issued in February 2016 contradicted a statement we had previously made, we initiated our investigation. We thought it would have been premature for us to answer Advocate Budlender's questions while we were ourselves gathering the facts. We recognise this created the impression that we were avoiding Advocate Budlender's questions. This was not our intention, and we have apologised to Advocate Budlender.

The actions we are taking

As we reflect on our findings, we are taking four steps to address issues that have arisen.

We have set aside our full fee for the Turnaround Programme for repayment.

Eskom has been a client of McKinsey since 2005, and we stand by our work at the company. We believe our work on the Turnaround Programme created substantial value by helping to improve operating performance and contain costs. Our work involved, amongst other things, helping to increase plant availability, reduce reliance on expensive diesel generators, reduce contractor claims on the 'new build' programme, and deliver procurement savings. In addition, we built internal capabilities, including helping to scale Eskom's project management skills and setting up a contracts management organisation. Transformation work of this type is a staple of our firm globally.

Eskom has now advised us that it believes it violated procurement regulations and its internal procedures in the formation of the contract, and that decisions it took with respect to the contract may have been taken without proper authorisation. These requirements were solely Eskom's responsibility. McKinsey entered into the contract and performed its work in good faith.

Our contract with Eskom for the Turnaround Programme was approved by Eskom. It explicitly required Eskom to obtain the necessary approvals or consents required by the terms of the Public Finance Management Act. We were advised by Eskom on 5 February 2016 that it had received National Treasury approval and we have reviewed Eskom's Steering Committee minutes from February 2016 that confirm that fact.

Eskom now contends the contract should be held invalid because Eskom did not, in fact, receive the necessary approvals. We want this issue resolved and we have no interest in benefiting from an allegedly invalid contract.

To provide reassurance to the citizens of South Africa, we will support a review by the High Court of the validity of the Turnaround Programme contract. McKinsey will pay back the fee in full if the Court determines Eskom acted unlawfully. We invite Eskom and Trillian to submit themselves to this process too. In the expectation it will be repaid, we have already set aside the full fee McKinsey earned on the Turnaround Programme in a ring-fenced account ready to comply with the Court's decision.

We have suspended our work for state-owned companies (SOCs) in South Africa until further notice.

We will commit, as a condition of engaging with SOCs in the future, to greater transparency with the National Treasury and relevant shareholder departments, so they have a full understanding of the work we are undertaking, the value we will bring, and our contracting arrangements. We will ask SOCs for detailed documentary evidence that they have all the appropriate approvals in place before we begin work.

Furthermore, McKinsey will not begin any SOC work in South Africa until it has been thoroughly reviewed and formally approved by a newly formed and independent South Africa SOC Risk Committee. This committee will set a very high bar for impact and the quality of the contracting process.

We are improving how we work with supplier development partners. We will only work with our own approved supplier development partners. We will not start work with a supplier development partner until due diligence is complete and a contract is signed.

We have instituted a rigorous process to identify and vet potential new supplier development partners for our firm. Sixteen firms have been shortlisted for legal and financial due diligence. We will devote significant resources to helping the firms we finally select, and others vetted through the same process, grow into self-sustaining black-owned consulting firms.

We will strengthen the governance and capabilities of our South African office. We have asked Tom Barkin, a member of our Global Operating Committee and our Global Chief Risk Officer, to take on oversight of the implementation of these changes to our South African office.

We are upgrading our finance, legal, and compliance teams and are taking steps to strengthen, and improve adherence to, our administrative processes. We will also, for the future, put in place a more rigorous approach to our SOC client engagement, contracting, monitoring, and compliance processes.

Our commitment to South Africa

McKinsey has had a continuous presence in South Africa for more than 21 years. In late 1995, soon after South Africa held its first democratic elections, a group of five consultants established our office. We have over 250 people in our South Africa office, more than 60% of whom are black South Africans. We thank our people and alumni, and we are hugely grateful to them.

We do not want this episode to affect our commitment to South Africa. We intend to redouble our efforts to be an active, positive, and responsible member of the community. We will take steps to build on our contributions to date and engage directly with a group of leading South Africans to guide us. We will communicate more on this in the coming months.

Georges Desvaux, Managing Partner of McKinsey Africa, and Saf Yeboah-Amankwah, Managing Partner of McKinsey South Africa, said:

> “We know that we need to rebuild trust in our firm in South Africa. Our clients have been very patient with us throughout our investigation, and we know that it will take time and effort to restore our reputation. We sincerely appreciate the support we have received from clients, alumni, our people, and McKinsey’s global partnership. We are committed to bringing the best of what we have to offer to South Africa, to continue to advocate for the country and the entire continent, and to play our part to help build a stronger South Africa.”

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