Congress of the United States
Washington, DC 20510

December 20, 2018

Mr. Kevin Sneader
Global Managing Partner
McKinsey & Company
55 East 52nd Street, 21st Floor
New York, NY 10022

Dear Mr. Sneader:

We write regarding our concerns about McKinsey & Company's conflicts of interest—undisclosed until September 2018—as the firm simultaneously advises Puerto Rico's Financial Oversight & Management Board and "has millions of dollars riding on the outcome" of this advice.[1] McKinsey holds $20 million or more of Puerto Rico's bonds, "creat[ing] a potential conflict of interest between McKinsey's client"—the Oversight Board—"and McKinsey itself, which wants to make as much money as possible on the bonds."[2]

Three things are clear about these conflicts of interest: (1) McKinsey, as a consultancy, has paved the way for many of Puerto Rico's creditors to receive handsome payouts; (2) McKinsey, as a creditor, is poised to benefit significantly; and (3) McKinsey's disclosures have been opaque or non-existent.

According to a September 2018 New York Times report, McKinsey has collected $50 million advising the Oversight Board on Puerto Rico's fiscal plans and budgets, "drafting a blueprint for the island's fiscal affairs over the next decade," while holding "at least $20 million—and possibly considerably more—of" Puerto Rico's bonds[3]—the values of which are directly affected by those same fiscal plans and budgets that McKinsey has been designing and evaluating. Moreover, McKinsey appears not to have disclosed this fact, and the information only became public when "[a]ffiliates of McKinsey revealed their investments in filings in federal court," under a different name, and buried "among nearly 165,000 bankruptcy claims."[4] These conflicts and the failure to disclose them raise serious questions about McKinsey's decisions and actions, and about whether the company is in compliance with its services agreement with the Oversight Board.

Since November 2016, when the firm was hired by the Oversight Board as its strategic consultant, McKinsey has had immense responsibility for conducting technical work for the Oversight Board on matters related to the island's debt, as well as on decisions about cuts to government services provided to the Puerto Rican people. The firm has a significant influence on the process. "McKinsey's services are, according to many, both central and indispensable to

[1] New York Times, "McKinsey Advises Puerto Rico on Debt. It May Profit on the Outcome," Mary Williams Walsh, September 26, 2018, https://www.nytimes.com/2018/09/26/business/mckinsey-puerto-rico.html.
[2] *Id.*
[3] *Id.*
[4] *Id.*

the Oversight Board's work," wrote a neutral, court-appointed fee examiner who spoke with the Oversight Board's general counsel and executive director, as well as with McKinsey personnel working on the project.[5]

The firm's initial scope of work for the Oversight Board included: "Fiscal Plan Framework and Stress Testing: McKinsey will develop a framework and approach for the Board to evaluate and certify fiscal plans and annual budgets presented to the Board, stress test the revenue, expenditure and balance sheet of the Government public finances."[6] The original scope of work also included: "Build a debt sustainability model as required for the certification of the Fiscal Plan,"[7] "Based on debt sustainability analysis from other workstreams, developing a creditor engagement strategy across all creditor groups,"[8] and "Identify and assemble structural reforms."[9]

The scope of work also indicates that McKinsey is involved in bondholders' claims, stating that in order to develop the "Litigation [f]ramework and [s]trategy[,] McKinsey will work with Board counsel to build a baseline assessment of legal proceedings and litigation, develop a framework and guidelines to enable the Board to develop a strategy for managing existing claims (e.g. Covina [*sic*] related claims and amounts due to contractors and taxpayers), and then put in place a robust framework for evaluation of potential litigation risk and trade-offs that will support the Board in developing its debt restructuring and stakeholder engagement strategy."[10] All of this work is central to how the Oversight Board will handle bondholder claims.

Though McKinsey's original contract with the Oversight Board has been updated and revised multiple times, the consultancy's work has remained crucial to the Oversight Board's approach to Puerto Rico's debt, and more generally, to the island's economic future, and the scope of work for the Oversight Board has remained expansive.[11] The fee examiner wrote recently that "the parameters of McKinsey's work … are both broad and dynamic,"[12] and that "McKinsey's work is not only necessary but essential to the administration of the Title III cases"[13]—the proceedings for adjusting Puerto Rico's debts. And McKinsey charges lucrative fees for its Puerto Rico services, having collected more than $50 million.

In September 2018, the New York Times reported that MIO Partners, a McKinsey subsidiary that manages funds for the company's current and former employees, runs three hedge funds that

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[5] Fee Examiner's Third Interim Report on Professional Fees and Expenses (February 1, 2018–May 31, 2018), filed October 31, 2018, pp. 10–11.
[6] Contract between McKinsey & Company, Inc. and the Financial Oversight and Management Board for Puerto Rico, November 27, 2016, Attachment 1, p. 5, https://drive.google.com/file/d/1qeH3RM1Ic0q0N0qLb8fa9o-s-la_3AZ3/view.
[7] *Id.*
[8] *Id.* at p. 6.
[9] *Id.* at p. 5.
[10] *Id.* at p. 6.
[11] Contract between McKinsey & Company, Inc. and the Financial Oversight and Management Board for Puerto Rico, September 1, 2018, Exhibit A, https://drive.google.com/file/d/1xRRLnxH5RWWGten23w97uV6uorlPlR7T/view.
[12] Fee Examiner's Third Interim Report on Professional Fees and Expenses (February 1, 2018–May 31, 2018), filed October 31, 2018, p. 14.
[13] *Id.* at pp. 13–14.

are seeking payment of $20 million on their holdings of Puerto Rican COFINA bonds[14]—which appear to be the same bonds whose claims McKinsey was tasked with helping the Oversight Board to develop a strategy for managing, per its initial scope of work.[15] This $20 million would represent a significant profit for McKinsey, as the bonds were purchased at much lower prices; for instance, one of the MIO Partners funds "could more than double its investment" of $4.5 million.[16] The New York Times also reported that Whitebox Advisors, which manages funds for McKinsey's retirement plans and for other clients, holds more than $140 million of Puerto Rican bonds through multiple investment funds, including Pandora Select, which has held McKinsey money.[17] Whitebox Advisors is a member of the Cofina Senior Bondholders Coalition, which represents a group of bondholders.[18] And Whitebox "has been actively trading Cofina bonds, more recently increasing its total holdings to almost $170 million as of last November."[19]

If the news report is accurate, McKinsey is helping to determine how much money will be available to creditors, even though McKinsey is itself a creditor and stands to benefit from funds being available for debt service. And indeed, the fiscal plans—for which McKinsey's work has been critical—provide for a large sum to be made available to creditors: Puerto Rico's latest certified Fiscal Plan reserves more than $17 billion over the next six years for possible debt service payments.[20] This does not even include the COFINA restructuring deal, which provides extremely generous recoveries for holders of those bonds, such as McKinsey, at the same time that it imperils Puerto Rico's long-term economic prospects.[21]

McKinsey's role in providing for debt service is especially troubling because funds available to creditors come at the expense of rebuilding the island and providing services to the people of Puerto Rico, who had a poverty rate exceeding 44% even before Hurricanes Irma and Maria devastated the island and killed thousands.[22] It is also troubling because McKinsey, as a vendor of the Oversight Board, has agreed to "scrupulously avoid any conflict, real or perceived, direct or indirect, between their own individual, professional, or business interests and the interests of the Board."[23] To the extent that this potential conflict—real or perceived—could create doubt about whether the Oversight Board is prioritizing the needs of the people of Puerto Rico and

[14] New York Times, "McKinsey Advises Puerto Rico on Debt. It May Profit on the Outcome," Mary Williams Walsh, September 26, 2018, https://www.nytimes.com/2018/09/26/business/mckinsey-puerto-rico.html.
[15] Contract between McKinsey & Company, Inc. and the Financial Oversight and Management Board for Puerto Rico, November 27, 2016, Attachment 1, p. 6, https://drive.google.com/file/d/1qeH3RM1Ic0q0N0qLb8fa9o-s-la_3AZ3/view.
[16] New York Times, "McKinsey Advises Puerto Rico on Debt. It May Profit on the Outcome," Mary Williams Walsh, September 26, 2018, https://www.nytimes.com/2018/09/26/business/mckinsey-puerto-rico.html.
[17] *Id.*
[18] PROMESA Title III, Fifth Supplemental Verified Statement of the COFINA Senior Bondholders' Coalition, April 27, 2018, Exhibit A, https://cases.primeclerk.com/puertorico/Home-DownloadPDF?id1=NzMxNTUy&id2=0.
[19] Centro de Periodismo Investigativo, "McKinsey: Puerto Rico Bondholder and Fiscal Board's Lead Adviser," Luis J. Valentín Ortiz, December 13, 2018, http://periodismoinvestigativo.com/2018/12/mckinsey-puerto-rico-bondholder-and-fiscal-boards-lead-adviser/.
[20] Financial Oversight and Management Board for Puerto Rico, Fiscal Plan for Puerto Rico, October 23, 2018, Exhibit 84, p. 140, https://drive.google.com/file/d/17ca0ALe7vpYn0jEzTz3RfykpsFSM0ujK/view.
[21] Bloomberg Opinion, "Puerto Rico Needs a Better Debt Deal," Antonio Weiss, Brad W. Setser, and Desmond Lachman, October 8, 2018, https://www.bloomberg.com/opinion/articles/2018-10-08/puerto-rico-needs-a-better-debt-deal.
[22] U.S. Census Bureau, "Quick Facts: Puerto Rico," July 1, 2017, https://www.census.gov/quickfacts/pr.
[23] Oversight Board Vendor/Consultant/Representative Code of Conduct, Appendix B, September 1, 2018, p. 3, https://drive.google.com/file/d/1xRRLnxH5RWWGten23w97uV6uorlPlR7T/view.

whether the Oversight Board is acting fairly, it appears to be at odds with the Oversight Board's interests—and with McKinsey's contractual obligations. Such a potential conflict also appears to be at odds with the Oversight Board's interests because it increases the litigation risk that the Oversight Board faces.

Equally troubling is McKinsey's lack of disclosure of its dual roles in the restructuring of Puerto Rico's debt. The New York Times report indicates that the Oversight Board "became aware of the firm's bond holdings" only "[a]fter The New York Times contacted McKinsey with questions about its investments."[24] Because of a gap in PROMESA, the law that established the Oversight Board and its debt restructuring, McKinsey was not legally required to disclose these potential conflicts.[25] McKinsey has exploited this gap. For example, according to the New York Times, "In most other bankruptcies, McKinsey would have been required to disclose any Puerto Rican investments it had via Whitebox,"[26] the hedge fund that manages McKinsey retirement money. But because McKinsey has filed only a three-page certification with the Oversight Board, rather than the thousands of pages of certifications and documents that needed to be filed by the creditors' consultants, the full extent of McKinsey's potential conflicts of interest remain unknown to the public and the Board.

The Oversight Board's initial contracts with McKinsey took a surprisingly lax approach to potential conflicts of interest and allowed your company to skirt disclosure. Those contracts state that they "shall not conflict McKinsey from serving the Government of Puerto Rico or any stakeholders to the work."[27] These contracts also state that "McKinsey is not able to advise or consult with the [the Oversight Board] about McKinsey's serving the [Oversight Board's] competitors or other parties," which seemingly includes "clients with potentially conflicting interests."[28] It is not clear whether McKinsey views *itself* as a "client[] with potentially conflicting interests."

McKinsey and the Oversight Board entered into a new contract shortly before the New York Times report was published.[29] This new contract states that McKinsey "shall not take actions during the term of this Agreement or any Project Assignment that would constitute or could create the appearance of a conflict of interest with the Board's mission or the work performed by

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[24] New York Times, "McKinsey Advises Puerto Rico on Debt. It May Profit on the Outcome," Mary Williams Walsh, September 26, 2018, https://www.nytimes.com/2018/09/26/business/mckinsey-puerto-rico.html.
[25] This belief, though common, is not universally held. See, e.g., New York Times, "Justice Dept. Says McKinsey Hid Dual Roles to Profit From Bankruptcy," Mary Williams Walsh, November 30, 2018, https://www.nytimes.com/2018/11/30/business/mckinsey-bankruptcy-disclosures.html.
[26] New York Times, "McKinsey Advises Puerto Rico on Debt. It May Profit on the Outcome," Mary Williams Walsh, September 26, 2018, https://www.nytimes.com/2018/09/26/business/mckinsey-puerto-rico.html.
[27] Contract between McKinsey & Company, Inc. and the Financial Oversight and Management Board for Puerto Rico, November 27, 2016, p. 3, https://drive.google.com/file/d/1qeH3RM1Ic0q0N0qLb8fa9o-s-la_3AZ3/view; Contract between McKinsey & Company, Inc. and the Financial Oversight and Management Board for Puerto Rico, September 12, 2017, p. 3, https://drive.google.com/file/d/1iV82ACFcYQfgtCq02v8rk19nx-g4_VA7/view.
[28] Contract between McKinsey & Company, Inc. and the Financial Oversight and Management Board for Puerto Rico, November 27, 2016, p. 2, https://drive.google.com/file/d/1qeH3RM1Ic0q0N0qLb8fa9o-s-la_3AZ3/view; Contract between McKinsey & Company, Inc. and the Financial Oversight and Management Board for Puerto Rico, September 12, 2017, p. 2, https://drive.google.com/file/d/1iV82ACFcYQfgtCq02v8rk19nx-g4_VA7/view.
[29] Contract between McKinsey & Company, Inc. and the Financial Oversight and Management Board for Puerto Rico, September 1, 2018, https://drive.google.com/file/d/1xRRLnxH5RWWGten23w97uV6uorlPlR7T/view.

the Contractor for the Board."[30] This provision had not been included in McKinsey's previous contracts. This new contract also does not include the previous contracts' language about how they "shall not conflict McKinsey from serving the Government of Puerto Rico or any stakeholders to the work." And the new contract has another provision that was not included in previous contracts: "Use of 'Inside,' Confidential Information or Third-Party Information in making any investment is absolutely prohibited, and Contractor represents and warrants that Contractor will comply with all applicable securities laws and regulations."[31]

Moreover, the new contract included an appendix, the Vendor/Consultant/Representative Code of Conduct, which requires vendors like McKinsey to "scrupulously avoid any conflict, real or perceived, direct or indirect, between their own individual, professional, or business interests and the interests of the Board."[32] While the new contract represents a step in the right direction in terms of guarding against potential conflicts, it highlights the serious deficiencies in the previous contracts.

This is not the first time that questions about McKinsey's potential conflicts and its lack of disclosure have been raised in the company's restructuring work. In 2016, the U.S. trustees—who are part of the Department of Justice—for a pair of chapter 11 cases objected to McKinsey's bids to work on those cases due to the consultancy's failure to disclose adequately its potential conflicts of interest.[33] In May of this year, restructuring specialist Jay Alix sued McKinsey for conflicts of interest in its work on some bankruptcy cases, claiming that the consulting firm had "knowingly and intentionally submitted false and materially misleading declarations under oath."[34] In June of this year, the Wall Street Journal reported that according to court and regulatory filings, a McKinsey "retirement fund held investments that gave it a financial interest in the outcome of six bankruptcy cases in which the company also was serving as an adviser."[35] More legal challenges to McKinsey's potential conflicts and its lack of disclosure were put forward within the last two months.[36] Such consistent secretiveness is not normal. According to an analysis of all chapter 11 bankruptcy cases in which McKinsey has participated, the company "routinely discloses far fewer names and descriptions of connections than other advisers."[37]

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[30] *Id.* at p. 4.
[31] *Id.* at p. 3.
[32] Oversight Board Vendor/Consultant/Representative Code of Conduct, Appendix B, September 1, 2018, p. 3, https://drive.google.com/file/d/1xRRLnxH5RWWGten23w97uV6uorlPlR7T/view.
[33] Wall Street Journal, "Bankruptcy Watchdogs Say McKinsey Disclosures Are Inadequate," Tom Corrigan And Jacqueline Palank, May 17, 2016, https://www.wsj.com/articles/bankruptcy-watchdogs-say-mckinsey-disclosures-are-inadequate-1463516707.
[34] New York Times, "McKinsey Hid Conflicts of Interest From Courts, Lawsuit Says," Mary Williams Walsh, May 9, 2018, https://www.nytimes.com/2018/05/09/business/jay-alix-mckinsey-lawsuit.html.
[35] Wall Street Journal, "McKinsey Investments Weren't Disclosed in Bankruptcy Cases," Gretchen Morgenson and Tom Corrigan, June 19, 2018, https://www.wsj.com/articles/mckinsey-investments-werent-disclosed-in-bankruptcy-cases-1529423138.
[36] New York Times, "Justice Dept. Says McKinsey Hid Dual Roles to Profit From Bankruptcy," Mary Williams Walsh, https://www.nytimes.com/2018/11/30/business/mckinsey-bankruptcy-disclosures.html; Wall Street Journal, "Justice Department Chides McKinsey in Another Bankruptcy Case," Tom Corrigan, December 15, 2018, https://www.wsj.com/articles/justice-department-chides-mckinsey-in-another-bankruptcy-case-11544901946.
[37] Wall Street Journal, "McKinsey Is Big in Bankruptcy—and Highly Secretive," Gretchen Morgenson and Tom Corrigan, April 27, 2018, https://www.wsj.com/articles/mckinsey-is-big-in-bankruptcyand-highly-secretive-1524847720.

In light of the importance of McKinsey's work for the Oversight Board, the importance of this work for deciding the economic futures of millions of U.S. citizens, and the questions surrounding McKinsey's apparent conflicts of interest, I ask that you respond to these following questions no later than January 8, 2019:

1. Did McKinsey make the Oversight Board aware of all Puerto Rican bonds in which the firm or its affiliates maintained an interest?
    a. If so, when were these disclosures made?
    b. If not, why not?
    c. Please provide a list, including value and terms, of all Puerto Rican bonds held by the firm and its affiliates, and the date(s) of any of their transactions in these bonds.

2. When McKinsey initially bid to do work for the Oversight Board, did the firm's personnel discuss these holdings with anyone inside or outside the firm and develop processes and procedures to protect against conflicts of interest?
    a. Please describe any such discussions, and provide copies of all communications related to them.
    b. Please provide a copy of the processes and procedures developed to address these conflicts.

3. The public is able to see the holdings of the McKinsey Master Retirement Trust,[38] as well as the list of Puerto Rico's creditors.[39] But the sophisticated McKinsey personnel working for the Oversight Board would more easily be able to make the connection between the two.
    a. How do you know that McKinsey employees working for the Oversight Board did not make any decisions on the basis of the fact that their personal retirement savings and those of their colleagues could be directly affected by their work?
    b. McKinsey reportedly told Centro de Periodismo Investigativo, a San Juan-based investigative journalism outlet, that its "consultants … do not have knowledge of MIO third party managers or specific investments."[40] How is this consistent with the fact that specific investments in Puerto Rican bonds by MIO's hedge funds are publicly disclosed in the PROMESA Title III database?

4. Does McKinsey do business with any other of Puerto Rico's creditors?
    a. If so, please provide a list of all such creditors, their holdings in Puerto Rican bonds, and the nature of the relationship between McKinsey and the creditor(s).
    b. Has McKinsey disclosed these relationships to the Oversight Board? If so, when?
    c. Did any of the McKinsey staff that advised or provided services to these creditors also advise or provide other services to the Oversight Board?
    d. Has McKinsey developed processes and procedures developed to address any conflicts of interest that may arise with regard to these relationships?
        i. If so, please provide a copy of these processes and procedures.

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[38] McKinsey Master Retirement Trust, Form 5500, Schedule of Assets Held for Investment, filed October 10, 2018.
[39] PROMESA Title III database, Commonwealth of Puerto Rico (17-03283), https://cases.primeclerk.com/puertorico/Home-Index.
[40] Centro de Periodismo Investigativo, "McKinsey: Puerto Rico Bondholder and Fiscal Board's Lead Adviser," Luis J. Valentín Ortiz, December 13, 2018, http://periodismoinvestigativo.com/2018/12/mckinsey-puerto-rico-bondholder-and-fiscal-boards-lead-adviser/.

5. The Contractor Services Agreement signed by McKinsey with the Oversight Board states that McKinsey "shall scrupulously avoid any conflict, real or perceived, direct or indirect, between their own individual, professional, or business interests and the interests of the Board."[41] Do you believe that McKinsey's role advising the Oversight Board and the fact that the company or its affiliates have holdings in Puerto Rican bonds violates this agreement?
    a. If no, why not?
    b. If yes, why has McKinsey continued to maintain these business conflicts?
    c. Please provide any internal communications related to compliance with this provision.

6. The Oversight Board's Vendor Conflict of Interest Disclosure Certification states: "In the event … that the Vendor does not disclose potential conflicts of interest and they are discovered by the Board, the Vendor will be barred from doing business with the Board."[42]
    a. Does McKinsey believe that it has abided by this provision in its certification?
    b. If so, is this based on McKinsey's belief that its contract with the Oversight Board obviated any need to "disclose potential conflicts of interest," or is it instead based on McKinsey's belief that there do not exist even "*potential* conflicts of interest" (emphasis added)?

7. Have any McKinsey employees or affiliates who have done work for the Oversight Board been aware of McKinsey's Puerto Rican bond holdings prior to the September 26, 2018, New York Times article?
    a. Have these holdings been mentioned in any communications (written or oral) by or with McKinsey employees working for the Oversight Board?
    b. If so, please provide copies (if written) of all such communications.

8. While PROMESA was being drafted, did McKinsey employees or personnel communicate with anybody in either the Executive Branch or the Legislative Branch?
    a. If so, what were their roles and the nature of the communications?
    b. Did they have any involvement in ensuring that consultants to the Oversight Board would not face disclosure requirements similar to those faced by others, including companies providing services to Puerto Rico's creditors?

9. According to the New York Times, McKinsey's spokesperson "acknowledged that McKinsey had attended some meetings with creditors."[43]
    a. What creditor meetings did McKinsey personnel attend?
    b. In what capacity did McKinsey personnel attend these meetings?
    c. Which McKinsey personnel attended these meetings? And what are their roles—both at McKinsey, and in the meetings?

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[41] Oversight Board Vendor/Consultant/Representative Code of Conduct, Appendix B, September 1, 2018, p. 3, https://drive.google.com/file/d/1xRRLnxH5RWWGten23w97uV6uorlPlR7T/view.
[42] Oversight Board Vendor/Consultant/Representative Code of Conduct, Appendix C, September 1, 2018, p. 1, https://drive.google.com/file/d/1xRRLnxH5RWWGten23w97uV6uorlPlR7T/view.
[43] *Id.*

d. Has McKinsey leveraged its work for the Oversight Board to help McKinsey's business relationships with Puerto Rico's creditors (e.g., in marketing materials, sale pitches, or other conversations with potential clients)?
e. Does the September 1, 2018, contract impose any new or different obligations on McKinsey—with respect to avoiding conflicts of interest or the appearance of conflicts of interest—than its previous contracts did?
    i. If so, why were these obligations newly imposed?

10. In October 2016, the Oversight Board released a request for proposal (RFP) for strategic consulting services. McKinsey was ultimately hired for this work. The RFP said: "Please state if you have any conflict of interest or potential appearance of conflict of interest in taking this engagement by virtue of your firm's current or prior engagements with other parties."[44] What was McKinsey's response to this request?

11. In response to the report of McKinsey's potential conflict of interest, the Oversight Board has commissioned an investigation, and a report will be released by the end of the year.[45] Does McKinsey plan to reimburse the Oversight Board—which is funded out of Puerto Rico's budget—for the cost of the investigation and report?

12. What steps does McKinsey plan to take to improve transparency around its work for the Oversight Board while it is a creditor of Puerto Rico?

13. Does McKinsey view its relationship to Puerto Rico's Oversight Board as a fiduciary one? To whom does McKinsey believe it has assumed fiduciary obligations during its work for the Oversight Board?

Sincerely,

Elizabeth Warren
United States Senator

Nydia M. Velázquez
Member of Congress

Cc:

Governor Ricardo Rosselló, Governor of Puerto Rico
Natalie A. Jaresko, Executive Director, Financial Oversight and Management Board

[44] Financial Oversight and Management Board for Puerto Rico, Request for Proposal: Strategic Consulting Firm, October 20, 2016, p. 3, https://drive.google.com/file/d/1ahH7EPmcUU18s4pNSWq4JR9N7QWnB3kX/view
[45] Centro de Periodismo Investigativo, "McKinsey: Puerto Rico Bondholder and Fiscal Board's Lead Adviser," Luis J. Valentín Ortiz, December 13, 2018, http://periodismoinvestigativo.com/2018/12/mckinsey-puerto-rico-bondholder-and-fiscal-boards-lead-adviser/.