November 11, 2017 – Statement of David Robert Fine

STATEMENT OF DAVID ROBERT FINE

Introduction:

My name is David Robert Fine, and I am a Senior Partner at McKinsey & Company ("McKinsey") based in London.

I appreciate the opportunity to appear before you today and answer your questions. These issues are of immense importance to all of us at McKinsey, including in a very real sense the more than 250 people employed in our South Africa office. As a South African who has dedicated a large part of my career to improving the functioning of South African businesses and government so that they work better for all of the people in this country, I have felt deeply the allegations that have been made in recent months involving McKinsey and state-owned entities that I and others at McKinsey have served.

As I will go into in greater detail in a moment, I have worked with Transnet since 2005 and was the Senior Partner responsible for that relationship between 2007 and 2013. It was and is my strong belief that the extensive work McKinsey performed at Transnet over the years delivered great value and made significant contributions to Transnet's operations, and I would be grateful for the opportunity to discuss some of that with you today.

While I have not served Eskom and so am not able to discuss that relationship with the same degree of personal knowledge, I am obviously aware of the allegations made relating to our firm's contracts with Eskom. McKinsey recently released a statement that clarified the nature of our work alongside Trillian and noted, among other things, that our extensive review to date found that McKinsey never made payments directly or indirectly to secure contracts, nor did we aid others in doing so. I have not seen anything that would contradict this.

Before turning to the substance of my remarks, let me say at the outset that I am fully committed to seeing that your inquiry into these matters is thorough and complete and to cooperating fully with you throughout this process. Even as your work and the work of other governmental authorities remains ongoing, McKinsey has made clear that we are currently reviewing our own actions in this matter to ensure that we promptly identify areas in which we should improve our risk policies and practices and will make any necessary improvements without compromise or delay.

Background:

McKinsey & Company is a global management consulting firm committed to helping institutions in the private, public, and social sectors achieve lasting success. McKinsey was founded in Chicago in the 1920s and has grown, almost entirely organically, into a truly global firm. Today, we have over 30,000 employees from 122 countries who speak 136 languages. Despite that scale, we remain a privately-owned partnership, owned and governed by our partners worldwide.

For 90 years, our primary objective has been to serve as our clients' most trusted external advisor. With consultants in over 120 cities in over 60 countries, across industries and functions, we believe that we bring unparalleled expertise to clients anywhere in the world. Our focus is on forming long-lasting relationships of trust with our clients. The vast majority of our work involves repeat business for existing clients.

McKinsey has had a continuous presence in South Africa for more than 21 years. Despite significant local demand, our firm took a principled decision not to work in South Africa prior to 1994 on the belief that any activity that might have aided the Apartheid regime would have been incompatible with our values.

In late 1995, soon after South Africa held its first democratic elections, a group of five consultants established our office in Johannesburg. I first joined McKinsey and that office later that year in September 1995, which made me the very first South African consultant to work for McKinsey in South Africa. After being elected a Partner in 2002 and then Senior Partner in 2008, I was selected to lead the Johannesburg office from 2010 to 2014.

In 2014, I was offered a promotion in the form of an opportunity to lead McKinsey's Public and Social Practice in the CIS, Eastern Europe, Middle East and Africa regions. In 2016, I was further promoted to global leader of McKinsey's Public and Social Sector Practice, my current position, which required relocating from South Africa. In this current position, I advise clients in a range of industries including the public sector, banking, transport and logistics, mining, utilities, and oil and gas.

Today, McKinsey's presence in South Africa has grown so that it employs over 250 people in our South Africa office, more than 60% of whom are black South Africans. We invest heavily in our people and their development. 39 nationalities are represented among our consultants in South Africa. We have delivered over 1,000 projects in South Africa, and a further 1,400 across Africa.

As part of its work in South Africa, McKinsey has a long history of providing pro bono consulting support to organisations and projects that both develop black South African talent and give back to black South Africans. To give some examples of which I am particularly proud:

- In 2012, we established the Social Advancement Foundation (SAF), a non-profit organisation that supports disadvantaged communities by providing consulting services and financial donations in healthcare, education and welfare. McKinsey's Johannesburg office contributes 26% of its annual profits to the SAF.
- The two-year McKinsey Leadership Programme (MLP) was created as an unrivalled springboard to a high-impact career for exceptional black South Africans with strong leadership profiles and distinctive academic and professional experience. Since January 2016, 28 future young black South African leaders were part of the programme. Those who have participated have gone on to establish successful careers in leading South African organisations.
- Additionally, the McKinsey Leadership Academy (MLA) supports and trains previously disadvantaged individuals, many of whom have disabilities. In 2016, 15 learners graduated with a Higher certificate in Business Management (NQF level 5), of which two took up permanent positions within McKinsey.
- McKinsey was awarded the Top Empowered Socio-Economic Development Award in 2015 at the annual Oliver Empowerment Awards. In 2016, we received the Legends of Empowerment and Transformation award.

Having spent nearly 20 years growing this office, I have a tremendous stake in its accomplishments and the team we have built and a great deal of concern for how certain of McKinsey's actions have been portrayed. I hope to spend the balance of my statement giving an overview of some of the work we performed and to give context for the topics that I understand we will be discussing today.

<u>McKinsey's Work for Transnet (2005-2016):</u>

McKinsey began working for Transnet in 2005 and worked continuously for Transnet for four CEOs and over thirty senior executives until 2016. As you know, Transnet is South Africa's state-owned rail and ports company, whose primary shareholder is the Department of Public Enterprises. As stated in public figures, Transnet employs on the order of 60,000 people (as of March 2017), and its activities create or sustain some 200,000 to 300,000 jobs in the wider South African economy, making it one of the most important employers in South Africa. Additionally, the role it plays with respect to rail and port infrastructure makes it a critical actor in the country's overall economy.

All McKinsey projects with Transnet followed a typical governance process which served to ensure accountability of delivery. This included weekly progress reviews with Group Finance executives. In addition, a steering committee for each project was typically set up with relevant line executives. We also supported our clients with documentation to ensure relevant approvals were obtained from relevant board and executive committees e.g., Group capital and investment committee (CAPIC) and Board Acquisition and Disposals Committee (BADC). Finally, we provided documentation when necessary to ensure the relevant approvals were obtained from the Department of Public Enterprises and National Treasury.

<u>2005-2011: Vulindlela Project and Other Smaller Projects</u>

McKinsey's relationship with Transnet began when McKinsey won a tender in 2005 to work on turnaround project known as the "Vulindlela" project. Drawing on McKinsey's considerable rail and port experience, the project focused on ways to reduce Transnet's central costs, increase divisional revenue, and improve operational performance. Through our work on this project – a four-year program that involved nearly 100 South African McKinsey consultants, 94 international consultants and over 140 full-time Transnet employees – we were able to make a significant positive impact on Transnet. As confirmed by Transnet's internal (Ernst & Young), these impacts included:

- Improving Transnet's annual operating profit by R5.6b per annum
- Increasing the availability of locomotives from 83% to 87%
- Increasing the availability of wagons from 85% to 95%
- Improving throughput in Durban harbour by 36%
- Successful partnership with Letsema Consulting as our supplier development partner (more details to follow)

Between 2008 and 2011, McKinsey also began working on a series of smaller projects for Transnet, including: a Ports Regulatory Strategy, an Enterprise Performance Management project, some smaller strategies for the Commercial and Strategy Organisation, and some senior leadership workshops for several operating divisions including Transnet Port Authority and Transnet Freight Rail. But up until 2011, McKinsey did not work on so-called "capital projects" (that is, the purchase, construction, expansion or maintenance of infrastructure or other assets) for Transnet.

<u>2012: McKinsey Support for Transnet's New "Market Demand Strategy"</u>

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Beginning in 2012, McKinsey began undertaking new and additional types of projects for Transnet. These projects were intended to address weaknesses of Transnet that were causing reverberations for the broader economy. As you will recall, as of 2011 South Africa's economic growth had remained strong and infrastructure was seen to be essential to continued GDP growth. South Africa, however, had not fully benefitted from the commodity boom due to under-capacity in rail and port infrastructure – essentially Transnet was unable to transport South Africa's commodities to market.

Upon examination, it became clear these challenges had their origins in the fact that the pace, quality and cost effectiveness of Transnet's capital projects had declined. Up until this point, Transnet had developed and invested in capital projects only when customers first confirmed their demand. This led to delays in project delivery as customers generally prefer not to commit up front to financing large infrastructure projects.

Following a change in Government policy towards the objectives of the 'Developmental State'- and under the leadership of the new CEO at the time, Brian Molefe -- Transnet decided to embark on a new strategy (known as the "Market Demand Strategy" or "MDS") to stimulate demand by investing in infrastructure projects without confirmed orders from customers. Such a strategy requires detailed projections of freight demand based on realistic assumptions of global growth and demand.

In 2011-2012, McKinsey helped Transnet launch the Market Demand Strategy. In the years that followed, McKinsey supported Transnet on key pillars of the MDS until March 2016. Among other changes required by the strategy, McKinsey's work included: developing projections for the amount of commodities Transnet might need to transport (based on McKinsey's understanding of the global commodities markets and proprietary models); improving Transnet's capital project expenditure; and increasing Transnet's operational performance. Amongst others, the impact of our work in this period includes saving Transnet of over R100bn in capital expenditure. This was reflected directly in the annual budgets. Additional performance monitoring activities, a new pricing strategy and operational efficiency initiatives all contributed to greater volume and accountability for delivery.

The MDS also required Transnet to procure new locomotives and improve its rail capacity in other ways to meet expected demand. At the time, long-term projections for freight capacity required in South Africa were looking promising for a number of reasons. These included opportunities to export additional coal, manganese and chrome to Asia; strong growth expected in domestic freight sectors like iron ore, coal and cement; and the fact that significant number of containers then transported on South Africa's roads could be transported by rail.

Because I understand that Transnet's acquisition of locomotives in March 2014 ("the 1064 locomotive transaction") is of particular interest to you, I have included a detailed summary of that transaction as an appendix to this statement. A key point to highlight is that McKinsey ceased advising Transnet on locomotives in February 2014 and had no involvement in advising Transnet in relation to the awarding of the tender in March 2014, the selection of the suppliers, or in how the locomotive prices were determined.

Unfortunately, in 2015, several years after the MDS was developed, the economic situation in South Africa and abroad changed. Demand for commodities fell significantly due to unexpected external factors. In particular, the Chinese economy experienced an unprecedented slow-down in 2015, and because China accounts for 45-55% of steel and coal consumption, this slow-down had a substantial effect on global commodity demand, commodity prices, and ultimately on the demand for South Africa mining export that help drive demand for freight capacity. In addition, several external factors negatively impacted Transnet's performance including community unrest in the Phalaborwa channel, flash flooding due to unseasonal rains, and massive failure of the tippler at Majuba.

These changes had major implications for Transnet in that it posed significant balance-sheet risks, required the company to rapidly reduce its capital spending and improve operating profit. This meant that McKinsey's work for Transnet over this latter period focused predominantly on reducing spend on capital projects, improving volume delivery and reducing non-essential operating costs. McKinsey's last engagement with Transnet ended on 8 April 2016.

McKinsey's Work with Supplier Development Partners at Transnet

McKinsey's presence in South Africa is based on a commitment to supporting the development of the country and its people, including developing the skills and capabilities of the next generation of leaders. McKinsey & Company South Africa has achieved B-BBEE Level 1 contributor status under the latest Codes of Good Practice and invests 26% of its annual South African profits for the direct benefit of historically disadvantaged South Africans. Before describing our work with development partners at Transnet, it is important to make three framing points at the outset:

- First, on all the projects where we worked with Supplier-Development partners at Transnet, in line with our B-BBEE commitments, we supported the development of these organisations through working on joint or parallel teams, providing on-the-job training, formal training workshops, dedicated coaching and feedback sessions, and having joint leadership structures.

- Second, all of our Supplier-Development partners were paid by Transnet directly and not by McKinsey. This was to ensure that Transnet and not McKinsey benefited from B-BBEE supplier spend. As a prime contractor, McKinsey was expected to review the work completed by our sub-contractors and provide assurance to Transnet that the work had been adequately completed. But the payments went directly to the Supplier-Development partner.

- Third, in addition to typical Supplier Development requirements of B-BBEE, in 2011 Transnet required at least 30% of its spend with consultants to be allocated to South African Black owned companies. This was based on the Department of Public Enterprises directives related to the Preferential Procurement Policy Framework Act (5/2000).

All of the Supplier Development partnerships with which I was involved reflected a genuine commitment and effort by McKinsey to meet and exceed the B-BBEE requirements in South Africa and to do so in the spirit that these requirements were intended – to provide opportunities for historically disadvantaged South Africans to participate meaningfully in the economy. While I appreciate there are current allegations to the contrary (in particular, Bianca Goodson née Smith's testimony before this Committee), those allegations do not accord with what I observed during my more than two decades at McKinsey. In my experience, McKinsey always took our supplier development very seriously and were committed to building local black owned businesses. Bianca Goodson's testimony before this Committee, about McKinsey's approach to supplier development at Eskom, is inconsistent with my views and experiences. I have no personal knowledge of whether the statements made by Ms. Goodson, and attributed to Lorenz Jüngling (a former partner), occurred or not. However, such behaviour would be completely against our values and beliefs about Supplier Development.

McKinsey's Work with Letsema

Supplier development was a key objective for McKinsey from the very beginning of its relationship with Transnet, and a requirement for Transnet's procurement, during the Vulindlela Programme (2005-2008). At that time, McKinsey partnered with a small consulting company called Letsema Consulting. I managed the Letsema Relationship, alongside my Partner, Norbert Doerr.

Over the course of the Vulindlela Programme, McKinsey helped Letsema become a strong and vibrant company that could compete with McKinsey and conduct independent work at Transnet. The process of developing Letsema was not without its challenges (at times, McKinsey consultants needed to be reminded to be patient and in particular consultants from outside South Africa needed to be trained on the importance of supplier development) but, in my view, the challenges we faced in developing Letsema were normal for a Supplier Development partnership, where the aim is to help small, black-owned companies develop skills and capabilities they do not already possess.

McKinsey partnered with Letsema Consulting from 2005 until 2012. By 2012, Letsema's turnover had grown to a point that exceeded B-BBEE supplier development guidelines. In addition, Letsema had grown to a size whereby they were competing with McKinsey for work. While in many respects this was a success story given the goals of supplier development, it did give rise to conflict. In addition, a professional conflict issues arose in 2012 during the contract award to McKinsey (described in the appendix) when Letsema was identified as working with General Electric – a potential bidder for supplying locomotives to Transnet.

McKinsey's Decision to Partner with Regiments

From 2012 to 2016, Regiments Capital Partners ("Regiments") became our Supplier Development Partner at Transnet. It is important to stress that McKinsey did not introduce Regiments to Transnet. Rather, Regiments had been suggested to us by Transnet as a possible B-BBEE partner to consider in late 2012, based on: they were already a registered supplier for Transnet; and the positive regard for its prior work for Transnet's Treasury department (a prior engagement that Regiments highlighted in a company profile in July 2012 – see Annexure A).

In the course of deciding whether to work with Regiments in 2012, McKinsey conducted a basic level of due diligence that included the following:

- I personally reviewed documentation provided by Regiments on their work for a number of SOCs and Public Sector institutions in South Africa, including Transnet (for whom they were already an approved supplier).

- I personally reviewed the resumes of the owners, which I thought were impressive (Litha Nyhonyha was from at Ernst & Young and had established Thebe Investment Holdings, Niven Pillay had two degrees from Princeton, and Eric Wood had a Masters of Management from WITS cum laude).

- I reached out to personal contacts in the business world about Regiments and received positive feedback about both Litha Nyhonyha and Eric Wood. In addition to this feedback, we took into account that Anoj Singh, then Transnet's CFO, had told us that Regiments' work at Transnet's Treasury Department had been well regarded.

Based on an internet search I conducted, I came across an article in which Regiments was discussed as having profited from a contentious deal with the City of Johannesburg. McKinsey raised this issue directly with Regiments, and we were told that Regiments' work had been conducted on an at-risk basis and that the City was contesting their fees.

I was the Senior Partner responsible for the Transnet relationship at the time we engaged Regiments, and I am not aware of any requirement -- stated or unstated -- for McKinsey to partner with Regiments in order to work at Transnet.

McKinsey's Work with Regiments

McKinsey first worked with Regiments in January 2013 on a project at Transnet to support the company in implementing the MDS strategy discussed above. Vikas Sagar led the original negotiation with Regiments and continued to be the primary point of contact between Regiments and McKinsey. Over the years of our work with Regiments, we developed a constructive working relationship, partnering on various projects. We often worked in integrated teams and held working sessions to jointly develop the solution for the client.

During this time period (2013 to early 2014) most projects were related to capital optimisation (in other words, helping Transnet ensure effectiveness and cost-effectiveness of its infrastructure spending). As with Letsema, the beginning of the relationship with Regiments was challenging and the McKinsey teams were initially unhappy with Regiment's performance and the day-to-day leadership. But as with Letsema, we took steps to improve our working relationship, including engaging external facilitators to work with the joint leadership teams to resolve our differences.

In my experience, Regiments added value to our engagements including by bringing capabilities in financial modelling and funding analysis, a core competency from their investment banking experience that was critical for a number of initiatives. Regiments also added consultants who performed well, including through their subsidiary Burlington Consultants.

Ongoing Challenges and the End of McKinsey's Relationship with Regiments

In addition to the diligence performed at the outset, McKinsey took steps over the course of the relationship to ensure that its work with Regiments accorded with our policies and standards.

- In July 2014, allegations were published in the Mail & Guardian (http://mg.co.za/article/2014-07-24-the-house-of-graft-and-lies) about alleged improper conduct by Niven Pillay (who had been our main Regiments contact up until that point). In response, McKinsey wrote to Regiments asking for Mr. Pillay to be separated from all projects with McKinsey and for written that Regiments is in compliance with regulations including the South Africa Prevention and Combatting of Corrupt Activities Act, US FCPA, and UK

Bribery Act. McKinsey ultimately decided to continue the relationship only after we received confirmation from Regiments on 28 August 2014 that: (1) "the allegations in the press are baseless," (2) Regiments had policies for "the promotion of honest and ethical behavior" and a "corporate governance framework specifically address[ing] issues such as bribery, corruption, conflict of interest and disclosure of interest"; and (3) Mr. Pillay "step down from the Executive Committee of the Consortium" and Eric Wood would "assume the lead role on the part of Regiments." Moreover, I consulted with the Transnet CFO and CPO and was advised by Anoj Singh that Transnet was also seeking confirmation from Regiments of its compliance with relevant anti-corruption regulations. In the wake of these discussions, Mr. Wood became our principal contact, and the relationship with Regiments and the quality of its work improved for a period of time (Annexure B).

- In the middle of 2015, there was rising concern about the Regiments working arrangements within McKinsey. The quality of Regiments employees being deployed declined, and there was a concern that they could not keep up with commitments. In one case the delivery was so poor that McKinsey needed to staff one of Regiments' projects with McKinsey personnel and claim payment from them. McKinsey Partners serving Transnet raised these issues regularly with Mr. Wood and frustration with their performance built up towards the end of 2015.

- In late 2015, at a meeting of the Transnet Client Service Team, the McKinsey leadership team agreed to look into other partnerships. McKinsey partners had raised additional questions about Regiments, including about: their beneficial ownership, their values, their impact orientation, their B-BBEE transformation credentials, given that their senior consultants and Mr. Wood did not reflect South African demographics. Around the same time, we heard from Mr. Sagar that Regiments had proposed splitting in two: Regiments Capital, with its financial advisory business, and Trillian, that would grow its management consultancy arm. My partners and I saw this as a potential solution to the capability concerns we had raised.

Nevertheless, the concerns only grew. In February 2016, our concerns were heightened after an article was published by London-based outlet Africa Confidential that alleged that Mohammed Bobat (a Regiments Director appointed as an advisor to the Minister of Finance in December 2015) was connected to the Gupta Family. On 15 February, McKinsey sought clarification of Mr Bobat's relationship with Regiments and Trillian and their relationship with politically exposed persons referenced in the article (Annexure E). While McKinsey received a letter from Bianca Goodson née Smith on 26 February (Annexure F) claiming that Mr Bobat had ceased to be employed by Regiments in December 2015, I noted at the time that Mr Bobat's LinkedIn profile described him as a Regiments Director.

On 23 February 2016, Vikas Sagar and I wrote to Transnet (Annexure C) confirming that we would end our relationship with Regiments, for reasons that included: questions about their performance, the rate of their transformation, and recurring issues raised in the media (which they declined to address with us). The letter was also explicit that we would not work with Trillian unless they pass a detailed due diligence. Within days, I initiated a review of our work at Transnet that involved external legal advisors, a process that was later handed over to the Africa Office Leadership and McKinsey's General Counsel. On 17 March 2016, Vikas Sagar and I met with Litha Nyhonyha and Niven Pillay and mutually agree to end our relationship with Regiments. This was confirmed in writing on 18 March 2016.

The above developments reflect that my McKinsey colleagues and I were put in the in position of having to respond in real time to new information that was coming to light about a firm with which we had worked for several years. In assessing the speed of our actions, it is important to separate what is known now from what was known then. In particular, certain claims currently being raised in the media relate to things that I simply had no knowledge of at the time:

- First, I am aware of recent media reports alleging that Regiments paid a portion of its fees received through work with McKinsey to companies including Albatime, Forsure and Fortime (companies the journalists suggest are linked to the Gupta family). At no time, however, was I aware of any such payments.

- Second, I am also aware from media reports that Mr Pillay has said "[Moodley's company] Albatime … took us into a relationship with McKinsey and got paid a commission for that ..." As far as I am aware, this is categorically incorrect. I note that Mr. Moodley himself is quoted in the same article confirming that "I don't know McKinsey, …" (http://amabhungane.co.za/article/2017-10-23-the-mckinsey-dossier-part-5-how-transnet-cash-stuffed-gupta-letterboxes)
- Third, during the preparation of this submission, I have recently been made aware of two 2014 responses to Transnet RFPs for a coal project and to support Transnet's New Multi-Product Pipeline project (NMPP) that include references to Albatime, Homix and Accompany Advisory as companies Regiments intended to sub-contract. It appears these sections of our proposals were copied and pasted from Regiments Capital. I had no knowledge of these documents at the time but can confirm that only Accompany Advisory were involved in any project with which McKinsey was involved.

McKinsey's Due Diligence of Trillian

McKinsey has previously explained in a public statement that although McKinsey worked alongside Trillian for a few months at Eskom, we never had a contract with Trillian. The statement further explained that Trillian failed our due diligence and we terminated discussions with them about a supplier development partnership in March 2016. We now believe that Trillian withheld information from us about its connections to a Gupta family associate.

As noted, I have not served Eskom and so cannot speak from personal knowledge of many of the events relevant to these matters. It should also be noted that at that time, unlike now, State Owned Entities were not considered McKinsey public sector clients and did not fall under Public-Sector Risk policies. Eskom and related projects were not within my formal mandate to review.

In early 2016 I became aware of a substantial working relationship between McKinsey and Trillian. When I enquired about Trillian with external contacts, they raised significant concerns. During a February 2016 Partner meeting, I and other McKinsey partners raised serious concerns about Trillian's B-BBEE status and their ultimate beneficial ownership. Consequently, the South African office initiated a due diligence of Trillian with an external party. I therefore engaged in McKinsey's due diligence process with respect to Trillian given my strong concerns about Trillian.

McKinsey wrote to Trillian several times during February and March 2016, requesting details of Trillian's corporate structure and ultimate beneficial ownership. Trillian failed to provide this information. In addition, Mr. Sagar and I met with Eric Wood on 5 March 2016 to discuss the split of Trillian from Regiments and asked again who the shareholders/ board members of Trillian would be and received concerning answers. On 14 March 2016, I participated in a McKinsey Global Risk Committee discussion on the proposed Supplier-Development partnership with Trillian at Eskom as the Leader of the Public Sector in the EEMA region (the Commonwealth of Independent States (CIS), Eastern Europe, Middle East, Turkey, Pakistan and Africa). The committee reviewed the results of our due diligence process and decided that we should terminate discussions with Trillian. The next day, on 15 March 2016, McKinsey wrote to Mr. Wood informing him of this decision. McKinsey also wrote to Eskom on 30 March 2016 to inform Mr. Singh of this decision (Annexure G).

<u>**Lessons learned and personal reflections**</u>

These events have led to no shortage of self-reflection from McKinsey as a firm and for me personally. McKinsey holds itself to a higher standard than strict legalities, and as a firm we take great pride in the contributions we have made to the government and people of South Africa. It has been immensely difficult to be associated with companies and people who are now widely believed to be involved in State Capture.

In the interest of being as forthcoming as possible with the Committee, there a few points that I would like to emphasise before closing.

First, while with the benefit of hindsight I certainly wish we would have ended our association with Trillian sooner, I am heartened that our due diligence process prevented what could have been an even more serious matter for the firm. The decision to first consider working with Trillian and our subsequent decision to terminate our relationship with Trillian was the subject of a healthy and sometimes heated debate within our firm, especially in the South African office. Many partners believed very strongly that we should not associate McKinsey with Trillian and that by so doing we would risk bringing McKinsey into disrepute. There were others, however, who believed that the paramount consideration was that we not abandon Eskom, an important South African State-Owned Enterprise, in its hour of need because of suspicions and allegations that were unproven. Additionally, some colleagues were concerned about the size of the contract for McKinsey. There was genuinely felt discomfort and debate. In the end, McKinsey's governance processes took the decision to end our association with Trillian. That is a positive thing, but my view now is that we should have put clearer guidelines in place for the Partners managing the work at Eskom to ensure that we avoided the association risk while deliberations were happening.

Second, while our investigation found no evidence of illegality, McKinsey has previously acknowledged -- and I wholeheartedly agree -- we should have done some things differently.

In particular, we were not careful enough with whom we associated with. Had we known that Trillian was owned by Mr. Essa (who is widely believed to be a business associate of the Gupta family), which is now publicly reported, we would not have worked with them. It is my view now with the benefit of hindsight that Trillian deliberately withheld information about their ultimate beneficial ownership from McKinsey (Annexure Eric Wood email 14 March 2016). While we terminated the discussions with Trillian, I regret that we did not move even more quickly when media reported potential links between Trillian and the Gupta family in 2016. We should not have worked alongside Trillian, even for a few months, before completing our due diligence and without a contract. While our risk process ultimately worked, we should have completed it sooner.

Among other lessons learned from these events:

1. Some of our processes were inadequate. I and McKinsey's South African office leadership were not aware of the letter sent to Eskom on 9 February 2016. This letter inaccurately characterised our relationship with Trillian and was a mistake. My Partners should not have prepared such a letter authorising, even conditionally, payment for an entity with which we did not have a contract. Eskom has confirmed it did not rely on this letter to make any payment to Trillian.
2. We did not communicate appropriately to Advocate Budlender, a deeply respected advocate in South Africa. However, Advocate Budlender was acting on behalf of Trillian and requested confidential information about McKinsey's clients. This was of great concern internally in McKinsey given our legal agreements with our clients. While we terminated the discussions with Trillian, I regret that we did not proactively investigate in detail in 2016 when media reported potential links between Trillian and the Gupta family.
3. I was not party to negotiations with Eskom on the "at-risk" engagement on the Turnaround programme. It is public knowledge that McKinsey worked on the turnaround programme at its own risk. McKinsey invested substantial resources (at its peak 108 consultants plus an additional 16 specialists/experts and 13 members of the leadership team from around the world) with no guarantee of any payment by Eskom. In recent discussions with Partner colleagues who were involved in the negotiation process, I understand it was never the intention for McKinsey to profit excessively from the eleven months of work at Eskom. However, I wish to make my personal points of view clear:
    a. McKinsey provided value for money for Eskom on the Turnaround Programme. Based on my discussions with my colleagues I understand this was independently verified by Oliver Wyman which is consistent with an McKinsey's review.
    b. However, in my view, we should have capped our fee structure and the total fees in absolute terms. While we do big programmes around the world, in my view, it was unlikely that Eskom had the management capacity and depth to absorb this much change in a sustainable way. These are of course judgements of mine that may differ with my colleagues.
    c. Even though the fees were an agreed percentage of savings and the benefits to Eskom were large, uncapped fees would be perceived negatively. We should have been more sensitive to the country's and Eskom's economic situation.

    McKinsey's Public Sector practice is now reflecting deeply how we structure these engagements in future in terms of contractual terms and conditions.
4. It was Eskom's responsibility to secure National Treasury approval for the Turnaround Programme. It turns out Eskom failed to do this. We should have insisted that Eskom confirm in writing Treasury's approval for the project and we should not have begun the project without that written confirmation.
5. In this specific case, the Turnaround Programme used metrics agreed with Eskom to trigger performance-related payments to McKinsey. I understand these were negotiated at great length between McKinsey and Eskom and the implementation levels used were broadly in line with our standard approach for at-risk projects globally. I also understand that some colleagues

of mine were concerned about whether we would be paid. In hindsight, we are exploring ideas like very rigorous stage-gating for such risk-based arrangements to make sure that the organisation can absorb our work and have comfort that the benefits are sustainable. In the case of Eskom, this would have given the South African public greater comfort that McKinsey had delivered sustainable impact through our work.

6. Recently the Shareholders Council of McKinsey met to review our risk policies related to SOE's. We resolved to subject SOE's to the Public Sector risk process in circumstances where SOE's are subject to public procurement laws. This means that today, Eskom would be subjected to McKinsey Public Sector risk review.

Lastly, I want to highlight one thing we are doing to move forward from these events by clarifying McKinsey's position on repaying the fees earned on the Turnaround Programme. Eskom has said that they acted without the required treasury approval and they contend that the contract was therefore invalid. McKinsey does not want to benefit from an invalid contract.

Therefore, McKinsey's Partners have agreed that the money paid by Eskom to us should be returned to South Africa. We avail ourselves to have any discussions with the appropriate authority, inclusive of Eskom and National Treasury, to find the appropriate mechanism to effect this commitment. I fully support McKinsey's decision to set aside the full amount with the intention to pay all of it back to South Africa.

Closing

Thank you for the work you are doing. I want to reiterate the importance of these matters and the seriousness with which they are being taken by McKinsey. I was born and raised in this country, my family still lives here, and I cannot overstate the significance of the inquiry in which you are engaged to the people of South Africa. Without belaboring the point, we all have a stake in understanding what happened and learning from these experiences. I look forward to answering your questions and hope that I am able to assist you in your inquiry.

November 11, 2017 – Statement of David Robert Fine

APPENDIX: SUMMARY OF 1064 LOCOMOTIVE TRANSACTION

1. A summary of McKinsey's work on this transaction is intended for clarity.
2. On 15 January 2013, a consortium led by McKinsey won a tender to provide advisory services to Transnet on their planned locomotives acquisition. The RFP was GSM/12/05/0447. The consortium had submitted the tender in May 2012.
3. The Consortium initially consisted of five parties: McKinsey (prime contractor), Letsema Consulting (Supplier Development Partner, with experience at Transnet in Locomotive component procurement), Utho/Nedbank (deal structure and funding), Advanced Railway Technologies (ART provided technical assessment of locomotive fleet and requirements). Transnet asked McKinsey to use Webber Wentzel as legal advisors.
4. The Letter of Intent from Transnet indicated that the total value of this tender would be R35.2 million, excluding VAT.
5. There were four primary workstreams, which were intended to start in March 2013 and conclude in October 2013. The workstreams were:
    1) McKinsey & Company would be responsible for validating the business case, to include projections for the volume of commodities Transnet could transport, validate that the procurement of 1064 locomotives was viable financially (Transnet had projected 1064 would be required), and conduct scenario planning to inform contracting.
    2) Letsema would be responsible for programme Management, to monitor overall progress against timelines and ensure proper governance.
    3) Utho/Nedbank, Webber Wentzel, and McKinsey would provide transaction advisory services and procurement execution, to minimise financial risk for Transnet and ensure suppliers deliver on their commitments.
    4) ART and McKinsey would provide technical evaluation and optimisation by assessing the lifecycle costs of suppliers short-listed by Transnet.
6. However, in 2012, Transnet raised a conflict issue about Letsema, who were serving General Electric Locomotives, Transnet felt this was a conflict of interest. In May 2013, shortly after awarding the tender to the consortium, Nedbank indicated it that it wanted to participate in the financing of the transaction and therefore no longer wanted to participate in the advisory part of the engagement.
7. Transnet suggested that Regiments Capital had the advisory skills of Nedbank, the programme management experience of Letsema (through their relationship with Burlington Consultants), and a strong track record at Transnet, should join the consortium in their place.
8. Mr Sagar raised this suggestion with the Transnet client-service team at McKinsey. After a discussion amongst our partners and some due-diligence (Annexure A), we decided to accept this suggestion as we thought that Regiments would bring the required skills and knew how to work with the Transnet. At no time did I feel compelled to use Regiments Capital
9. The work initially proceeded according to the agreed timelines.

10. From early 2013 to the end of April 2013, McKinsey facilitated the development of the business case, to determine whether the acquisition of 1064 locomotives was financially viable. This was done by analysing commodity trends across the freight system and the corresponding locomotive requirements. The approach optimised delivery flexibility so that supply timing could reflect changes in the volumes of commodities Transnet transported.
11. The recommendations McKinsey made in the business case were explicit and signed off by Transnet's Executive Committee ('Exco') and Board in the first half of 2013, namely:
    a. Without locomotive procurement, the shortfall between locomotive capacity and market demand would rise to almost 112 million tons by 2021/2022, i.e. a 59% shortfall in capacity.
    b. The projections of the likely future volumes of commodities Transnet could transport were the most sensitive variable for the business case. Since the global financial crisis in 2008, McKinsey's standard practice is to advise our clients to ensure their capital investment plans are able to scale back or accelerate to better match volume movements. We included this advice to Transnet on its capital expenditure programme, including the 1064 Locomotive Transaction. Therefore, the procurement process proposed included flexibility in the contracts so that the number of locomotives could be adjusted downwards or upwards if necessary.
    c. Local supplier content was important and possible. Our calculations showed that 50% local supplier content would probably add only 2% to the price and create about R68 billion in economic impact for South Africa.
    d. The likely capital expenditure ('Capex') required for the 1064 locomotives would be R38.6 billion over a 7-year period, including the costs of hedging in the business case on page 38 of Annexure D, and South African and US inflation included in the business case of US 2.2.% per annum, SA 5.2% per annum. Locomotive cost estimates were provided by Transnet freight Rail based on recent locomotive acquisitions combined with expert input from Advanced Railway Technologies. They estimated each diesel locomotive would cost around R25 million and each electric locomotive, around R34 million).
    e. Using likely efficiency improvements and projecting past volume performance at Transnet, we recommended that Transnet might only require the 1064 locomotives beyond the business case timeframe of seven years. This was because Transnet would still require to procure between 60-80 locomotives per annum to maintain its locomotive fleet.
    f. Detailed recommendations on procurement security and governance, given the size of the transaction. This included a secure data room with controlled access
    g. McKinsey did not propose any locomotive costs.
12. After completing the validation of the business case in April 2013, McKinsey tried to start up our team to prepare for the procurement execution phase of the project. However, Transnet did not provide McKinsey with access to Transnet Freight Rail's ('TFR') data, which was essential for McKinsey to support Transnet on this element of the project. Mr Singh committed over the course of the second half of 2013to resolve the matter with TFR CEO Siyabonga Gama, but remained unsuccessful.

13. Transnet also experienced serious delays in the second half of 2013 in terms of the work it had committed to perform as part of this project and only completed their work by the end of 2013. In particular:
    1) The Transnet RFP for potential locomotive suppliers was delayed
    2) Transnet did not secure the necessary internal approvals within agreed timelines
    3) DPE and National Treasury approvals were not submitted in time
14. McKinsey was not involved in the Technical, Financial or B-BBEE assessment of bidders. McKinsey played no role in identifying, scoring/assessing or awarding bidders.
15. As a result of these delays, and because McKinsey was not given access to essential data, we were unable to progress to the next step of the project – procurement execution.
16. In January 2014, Transnet told us it wanted to complete the locomotive procurement process more rapidly than originally intended so revised the scope of work for the project. McKinsey expressed concern about the revised scope and timing. The delays and proposed shortened procurement timing meant that there were few negotiation levers left, given the time available to Transnet. We therefore felt that our value-add would be very limited.
17. McKinsey took the following actions:
    a. 31 January 2014 - we wrote to Anoj Singh, describing what we would require in order to complete the work in the revised timing. The note set out the specific information and access to key personnel we would require in order to meet the deadlines.
    b. 4 February 2014 - after one week of work, a pattern of delays and lack of response thereto, we wrote to Transnet to withdraw from the project. (Annexure D)
18. On 5 February 2014 it was agreed in a meeting between Mr Singh and Mr Sagar that McKinsey would transfer the remaining contract to Regiments. According to Mr Singh, Regiments was required to provide the financial advice required as per the 'transaction advisory' workstream in order to complete the locomotive procurement.
19. After McKinsey withdrew from the project, I am aware that Transnet signed a three-year locomotive acquisition contracts with four manufacturers, for 1064 locomotives at a total cost of around R54 billion (including contingencies) on 17 March 2014, which compares with the original R38.6 billion. When McKinsey asked Transnet about these changes, Mr. Singh said that Transnet had done new calculations based on funding costs, exchange rates and inflation and had come to the conclusion that it was better to secure the deal they did.
20. McKinsey had no involvement in advising Transnet in relation to the awarding of this tender nor on how the locomotive prices were determined after 4 February 2014
21. McKinsey had no involvement in the currency hedging and interest rate derivatives, which Regiments Capital advised Transnet to purchase and which are discussed in (the OCCRP article of date 03 Nov 2017 – https://www.occrp.org/en/28-ccwatch/cc-watch-indepth/7215-guptas-nedbank-skillfully-extract-money-from-south-african-state-firm)
22. McKinsey & Company was paid R8.4 million (excluding VAT) for its work on the Locomotive Business Case.

23. I have no knowledge of how the cost of the Locomotives Advisory Contract (RFP GSM/12/05/0447) increased to over R200 million as reported in the media (http://amabhungane.co.za/article/2016-09-16-xhow-to-eat-a-parastatal-like-transnet-chunk-by-r600m-chunk).

24. As mentioned above, projections of the commodity volumes Transnet would transport decreased in 2015. As a result, in 2016, McKinsey supported Transnet for six weeks to identify options for how Transnet might engage with the locomotives manufacturers so that the timing of locomotive deliveries was better aligned with the new projections and financial constraints.

25. McKinsey provided these options to Transnet but were not part of any of the discussions with the OEM's and any subsequent agreements.