DISCLOSURE REQUIREMENTS FOR REORGANIZATION CONSULTANTS UNDER THE BANKRUPTCY CODE

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INTRODUCTION

The United States Bankruptcy Code ("the Code") is a central part of American jurisprudence, allowing the honest but unfortunate debtor an opportunity at a fresh start. In order to properly effectuate this purpose, the Code imposes a variety of requirements intended to preserve the fair and unmarred administration of the estate. Arguably, the most salient of these obligations is the Code mandated disclosure requirements on all professionals retained by the estate, which strives to ensure that estate assets are divided in a transparent manner and without influence from potential conflicts of interest.

Today, the Code's professional disclosure requirements have found themselves intertwined in controversy as a result of entrance into the bankruptcy advisory field by McKinsey & Company ("McKinsey"), one of the world's premier global consulting companies.[1] McKinsey is under scrutiny for allegedly failing to make adequate disclosures of its outside interests, giving rise to concerns that the company could be influenced by conflicts and wrongfully employed as advisers to the estate. Leading the charge behind these allegations is Jay Alix, founder of AlixPartners—a dominant company and competitor of McKinsey in the turnaround and restructuring consulting industry.[2] Due in part to Jay Alix's allegations and the RICO claims[3] he brought against McKinsey in the Southern District of New York, the Department of

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1 McKinsey & Company first entered the bankruptcy advisory field in 2001. Since 2010, the company has operated in the bankruptcy advisory field directly through "McKinsey RTS," the firms restructuring division. *See About RTS*, MCKINSEY & COMPANY, https://www.mckinsey.com/business-functions/rts/how-we-help-clients/about-rts (last visited Apr. 19, 2020).

2 In order to obtain the required standing needed to challenge McKinsey's disclosure practices in chapter 11 cases, Jay-Alix created the investment company, Mar-Bow Value Partners. Mar-Bow Value Partners obtains standing by purchasing creditor claims in the bankrupt companies for which McKinsey acts as a reorganization consultant. *See* Mary Williams Walsh & Emily Flitter, *McKinsey Faces Criminal Inquiry Over Bankruptcy Case Conduct*, N.Y. TIMES (Nov. 8, 2019), https://www.nytimes.com/2019/11/08/business/mckinsey-criminal-investigation-bankruptcy.html (discussing the pending federal criminal investigation faced by McKinsey and efforts of Jay Alix to challenge McKinsey's practices in court).

3 Jay Alix alleged insufficient disclosure practices that harmed his interests in the following thirteen bankruptcies: *In re* Hayes Lemmerz Int'l, Inc., No. 01-BR-11490 (Bankr. D. Del. filed Dec. 5, 2001) ("*Hayes Lemmerz*"); *In re* UAL Corp. (*United Airlines*), No. 02-BR-48191 (Bankr. N.D. Ill. filed Dec. 9, 2002) ("*United*"); *In re* Mirant Corp., No. 03-BR-46590 (Bankr. N.D. Tex. filed July 14, 2003) ("*Mirant*"); *In re* Lyondell Chem. Co., No. 09-BR-10023 (Bankr. S.D.N.Y. filed Jan. 6, 2009) ("*Lyondell*"); *In re* Harry & David Holdings, Inc., No. 11-BR-10884 (Bankr. D. Del. filed Mar. 28, 2011) ("*Harry & David*"); *In re* AMR Corp., No. 11-BR-15463 (Bankr. S.D.N.Y. filed Nov. 29, 2011) ("*AMR*"); *In re* AMF Bowling Worldwide, Inc., No. 12-BR-36495 (Bankr. E.D. Va. filed Nov. 13, 2012) ("*AMF*" or "*AMF Bowling*"); *In re* Edison Mission Energy, No. 12-BR-49219 (Bankr. N.D. Ill. filed Dec. 17, 2012) ("*Edison Mission*" or "*Edison Mission Energy*"); *In re* NII Holdings, Inc., No. 14-BR-12611 (Bankr. S.D.N.Y. filed Sept. 15, 2014) ("*NII Holdings*"); *In re* The Standard Register Co., No. 15-BR-10541 (Bankr. D. Del. filed Mar. 12, 2015) ("*Standard Register*"); *In re* Alpha Natural Resources, Inc., No. 15-BR-33896 (Bankr. E.D. Va. filed Aug. 3, 2015) ("*ANR*" or "*Alpha Natural Resources*"); *In re* SunEdison, No. 16-BR-10992 (Bankr. S.D.N.Y. filed Apr. 21, 2016) ("*SunEdison*"); *In re* GenOn Energy, Inc., No. 17-BR-33695 (Bankr. S.D. Tex. filed June 14, 2017) ("*GenOn*").

Justice's United States Trustee Program opted to investigate.[4] In February 2019, after conducting an evaluation of McKinsey's practices, the United States Trustee Program entered into a settlement with McKinsey, in which the company agreed to pay $15 million to remedy past inadequate disclosures of connections.[5] Despite the allegations and settlement, McKinsey continues to maintain that its disclosure practices are adequate and legal.[6] This begs the question of what is the scope of required disclosures by a debtor's professionals.

In an attempt to answer that question, this Note focuses on the disclosure requirements imposed on professionals retained by the estate—specifically those imposed by 11 U.S.C. § 327(a) and Federal Rules of Bankruptcy Procedure Rule 2014 ("Rule 2014"). Further, this Note highlights the importance of disclosure requirements and argues that companies such as McKinsey and other advisory professionals, should be held to the same traditional standard of disclosure imposed by the Bankruptcy Code. Part I outlines the processes of retaining estate professionals and delves into the relevant code provisions that impose disclosure requirements on such professionals. Next, Part II analyzes the disclosure requirements imposed on professionals acting outside of the bankruptcy process, and the importance of such requirements in their respective fields. Finally, Part III will discuss an ultimatum for McKinsey and others operating as reorganization consultants moving forward to ensure that sufficient disclosure standards are maintained and upheld—adopt a cognizable solution or leave the bankruptcy consulting industry.

I. THE RETENTION OF PROFESSIONALS & DISCLOSURE REQUIREMENTS

Section 327 governs the retention of professional persons by the bankruptcy estate.[7] In relevant part, section 327(a) states,

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[4] *See* Mary Williams Walsh, *McKinsey Will Return $15 Million in Fees Over Disclosure Failures*, N.Y. TIMES (Feb. 19, 2019), https://www.nytimes.com/2019/02/19/business/mckinsey-bankruptcy-settlement.html.

[5] *See* Press Release, Dep't of Justice: Office of Public Affairs, U.S. Trustee Program Reaches $15 Million Settlement with McKinsey & Company to Remedy Inadequate Disclosures in Bankruptcy Cases (Feb. 19, 2019), https://www.justice.gov/opa/pr/us-trustee-program-reaches-15-million-settlement-mckinsey-company-remedy-inadequate.

[6] Subsequent to McKinsey's settlement with the Department of Justice, it was recently reported that McKinsey is under a federal criminal investigation in an effort to further determine whether McKinsey's bankruptcy unit improperly failed to disclose investment interests in the bankrupt companies it has advised. *See* Gretchen Morgenson & Rebecca Davis O'Brien, *McKinsey Bankruptcy Unit Faces Criminal Probe*, WALL STREET J. (Nov. 19, 2019), https://www.wsj.com/articles/mckinsey-bankruptcy-unit-faces-criminal-probe-11573512656; *see also* Walsh & Flitter, *supra* note 2.

[7] Although this note discusses retention specifically under 11 U.S.C. § 327(a), it is important to note that there is a dispute as to whether certain professionals may be retained under 11 U.S.C. § 363(b) rather than section 327. *See In re* First Merchants Acceptance Corp., No. 97-1500 JJF, 1997 WL 873551, at *5 (Bankr. D. Del. Dec. 15, 1997) (denying Debtor's motion to retain assistance under section 363(b) ruling the disinterested requirement of section 327 was not satisfied); *In re* Nine W. Holdings, Inc., 588 B.R. 678, 691, 695 (Bankr. S.D.N.Y. 2018) (stating debtors may rely on section 363(b), rather than section 327(a), when seeking authorization for professional retention); *In re* Brookstone Holdings Corp., 592 B.R. 27, 28–29

> except as otherwise provided in this section, the trustee,[8] with the courts approval, may employ one or more attorneys, accountants, appraisers, auctioneers, or other professional persons, that do not hold or represent an interest adverse to the estate and that are disinterested persons to represent or assist the trustee in carrying out the trustee's duties under this title.[9]

As such, section 327(a) imposes two requirements on professionals seeking retention: (1) they have no adverse interest to that of the estate; and (2) they are acting as a disinterested person.[10] While the term "adverse interest" is not defined by the code,[11]

(Bankr. D. Del. 2018) (applying section 363(b) in determining whether the retention of professionals for store-closing liquidations should be authorized). Proponents of retention under 11 U.S.C. § 363(b) rely on the language of the statute, which in pertinent part states "[t]he trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate . . . ." 11 U.S.C. § 363(b) (2018). Ultimately, retention under § 363(b) may be preferred by professionals due to the less onerous requirements. *See* Eli Blechman & Leslie Liberman, *To Retain (Under Section 327(a) or 363(b) of the Bankruptcy Code) or Not to Retain? Retention of Liquidation Consultants in Bankruptcy Cases*, WEIL BANKR. BLOG (Mar. 22, 2019), https://business-finance-restructuring.weil.com/professionals/retain-under-section-327a-or-363b-of-the-bankruptcy-code-or-not-to-retain-retention-of-liquidation-consultants/. Recently, in September 2018, the United States Bankruptcy Court for the District of Delaware attempted to help define the scope of who qualifies as a "professional" within the scope of each provision, stating,

> a "professional" is limited to those occupations which control, purchase or sell assets that are important to reorganization, is negotiating the terms of a plan of reorganization, has discretion to exercise his or her own personal judgement, and whether he or she contributes "some degree of special knowledge or skill."

See In re Heritage Home Group LLC, No. 18-11736 (KG), 2018 WL 4684802 at *3 (Bankr. D. Del. Sept. 27, 2018) (holding the consultant, whose responsibilities did not "constitute an intimate role in the Debtors' plans[,]" need not be retained formally pursuant to section 327(a) and could be retained instead through section 363(b)). Ultimately, because the specific professionals that this Note focuses on are most often retained under 327(a), this Note will not discuss section 363(b) retention further.

[8] Subject to 11 U.S.C. § 1107(a), a debtor in possession has the same rights of a trustee. *See* 11 U.S.C. § 1107(a) ("Subject to any limitations on a trustee serving in a case under this chapter, and to such limitations or conditions as the court prescribes, a debtor in possession shall have all the rights, other than the right to compensation under section 330 of this title, and powers, and shall perform all the functions and duties, except the duties specified in sections 1106(a)(2), (3), and (4) of this title, of a trustee serving in a case under this chapter.").

[9] *See id.* § 327(a).

[10] *Id.* ("[T]he trustee, with the court's approval, may employ . . . professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons . . . .").

[11] Despite not being defined by the Code, courts have generally accepted the definition of an adverse interest to be:

> (1) possession or assertion of an economic interest that would tend to lessen the value of the bankruptcy estate; or (2) possession or assertion of an economic interest that would create either an actual or potential dispute in which the estate is a rival claimant; or (3) possession of a predisposition under circumstances that create a bias against the estate.

Dye v. Brown (*In re* AFI Holding, Inc.), 530 F.3d 832, 845 (9th Cir. 2008); *see* Rome v. Braunstein, 19. F.3d 54, 58 n.1 (1st Cir. 1994); *see also In re* Roberts, 46 B.R. 815, 826–27 (Bankr. D. Utah 1985), *aff'd in part, rev'd and remanded in part on other grounds*, 75 B.R. 402 (D. Utah 1987).

11 U.S.C. § 101(14) provides a definition of what it means to be a "disinterested person."[12] The Code defines a disinterested person as someone who

> (A) is not a creditor, and equity security holder, or an insider; (B) is not and was not within the 2 years before the date of filing of the petition, a director, officer, or employee of the debtor; and (C) does not have an interest materially adverse to the intertest of the estate of or any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor or for any other reason.[13]

Subsection C of the provision acts as a "catch-all" and has been interpreted by the courts to be "broad enough to include anyone who in the slightest degree might have some interest or relationship that would even faintly color the independence and impartial attitude required by the Code and Bankruptcy Rules."[14]

Giving teeth to the retention requirements imposed by section 327(a), Rule 2014 requires that an application for employment disclose "all of the [applying professional's] *connections* with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee."[15] Notably, courts have drawn an important distinction between section 327(a) and Rule 2014—the requirements of Rule 2014 "are more-encompassing than those governing the disinterestedness inquiry under section 327."[16] This distinction owes its existence to the term

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[12] 11 U.S.C. § 101(14).

[13] *Id.*

[14] *In re* BH & P, Inc., 949 F.2d 1300, 1308 (3d Cir. 1991); *see also In re* AFI Holding, Inc., 530 F.3d at 837–38 (adopting the broad application of the Bankruptcy Code's "catch-all" provision).

[15] FED. R. BANKR. P. 2014 (emphasis added). Section A of the Rule in its entirety reads as follows:

> An order approving the employment of attorneys, accountants, appraisers, auctioneers, agents, or other professionals pursuant to § 327, § 1103, or § 1114 of the Code shall be made only on application of the trustee or committee. The application shall be filed and, unless the case is a chapter 9 municipality case, a copy of the application shall be transmitted by the applicant to the United States trustee. The application shall state the specific facts showing the necessity for the employment, the name of the person to be employed, the reasons for the selection, the professional services to be rendered, any proposed arrangement for compensation, and, to the best of the applicant's knowledge, all of the person's connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee. The application shall be accompanied by a verified statement of the person to be employed setting forth the person's connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee.

Id.

[16] *In re* Leslie Fay Companies, Inc., 175 B.R. 525, 536 (Bankr. S.D.N.Y. 1994); *see also In re* Granite Partners, L.P., 219 B.R. 22, 35 (Bankr. S.D.N.Y. 1998) ("The scope of disclosure is much broader than the scope of disqualification.").

"connections," which is not defined by the Code, but is consistently interpreted by the courts to be more broad than the "materially adverse" language imposed by section 327.[17] Accordingly, "[*a*]*ll* facts that may have any bearing on the disinterestedness of a professional must be disclosed."[18]

Furthermore, under Rule 2014, the professional who is seeking retention has the onus and burden of full disclosure placed squarely on his shoulders.[19] This is important as the courts place their trust in professionals, assuming that they will act honestly and police themselves in a manner that allows the courts to rely on their disclosure statements when determining whether the professional is qualified under section 327.[20] At no time does this burden shift from the professional to the other parties in interest, as Rule 2014 does not intend to "condone a game of cat and mouse where the professional seeking appointment provides only enough disclosure to whet the appetite of the [US trustee], the court or other parties interest, and then the burden shifts to those entities to make inquiry in an effort to expand the disclosure."[21] Courts routinely stress that it is the duty of the bankruptcy court, not the professionals, to determine which connections rise to the level of an actual conflict or pose the threat of a potential conflict.[22] Additionally, while Rule 2014 does not expressly require supplemental disclosure as the case continues, courts have determined that section 327 implicitly imposes such a duty of continuing disclosure even after retention is approved.[23] Ultimately, the purpose of such requirements is to ensure that the integrity of the bankruptcy system is preserved through conflict free professionals.[24]

Finally, the potential consequences that stem from a violation of either of these provisions illustrates the importance of adhering to the requirements of section 327 and Rule 2014. Under 11 U.S.C. § 328(c), a court may deny allowance of compensation for a professional person if it is determined that he is not

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[17] *In re* Leslie Fay, 175 B.R. at 536 ("[W]hile retention under section 327 is only limited by interests that are 'materially adverse,' under Rule 2014, 'all connections' that are not so remote as to be *de minimus* must be disclosed."); *see In re* Olsen Indus., Inc., 222 B.R. 49, 60 (Bankr. D. Del. 1997) ("A court may find a disclosure violation without holding that it would have found the [professional] not disinterested given timely and complete disclosure."); *see also In re* BH & P Inc., 949 F.2d at 1314 (stating each prong of section 327(a) is satisfied when a person is found to be disinterested under section 101(14)).

[18] *In re* Leslie Fay, 175 B.R. at 533 (emphasis added).

[19] *In re* Granite Partners, L.P., 219 B.R. at 34–35.

[20] *Id.* at 35 ("The professional's duty to disclose is self-policing.").

[21] *In re* Matco Elecs. Grp., Inc., 383 B.R. 848, 854–55 (Bankr. N.D.N.Y. 2008).

[22] *See* Miller Buckfire & Co. v. Citation Corp. (*In re* Citation Corp.), 493 F.3d 1313, 1321 (11th Cir. 2007) ("Rule 2014 requires a professional to disclose all of its relevant connections in its disclosure so that the bankruptcy court can determine if there are any conflicts or potential conflicts."); *see also* Rome v. Braunstein, 19 F.3d 54, 59 (1st Cir. 1994) (noting the decision whether a specific disclosure is pertinent to the professionals eligibility "should not be left to counsel, whose judgement may be clouded by the benefits of the potential employment").

[23] *See In re* Granite Partners, L.P., 219 B.R. at 35.

[24] *Id.*; *see* United States v. Gellene, 182 F.3d 578, 588 (7th Cir. 1999) ("The Code reflects Congress' concern that any person who might possess or assert an interest or have a predisposition that would reduce the value of the estate or delay its administration ought not have a professional relationship with the estate."); *Rome*, 19 F.3d at 58 ("These statutory requirements—disinterestedness and no interest adverse to the estate—serve the important policy of ensuring that all professionals appointed pursuant to section 327(a) tender undivided loyalty and provide untainted advice and assistance in furtherance of their fiduciary responsibilities.").

disinterested.[25] Even more seriously, although rarely acted upon,[26] criminal charges may be brought against an attorney for submitting a materially false Bankruptcy Rule 2014 affidavit.[27] Such severe punishment evidences "Congress' attempt to criminalize all possible methods by which a debtor or any other person may attempt to defeat the intent and effect of the Bankruptcy Code . . . ."[28] If the foregoing analysis reveals anything, it is this—proper disclosure under section 327 and Rule 2014 is *mandatory*, not permissive.

II. CONFLICT DISCLOSURE PRACTICES IMPOSED IN OTHER FIELDS OF BUSINESS

Upon an initial review of the disclosure requirements imposed by the Bankruptcy Code one may get the impression that the Code's requirements are harsh or overbearing on professionals seeking retention. In fact, this argument is raised by McKinsey itself, as the company implicitly argues that it would be too burdensome, difficult, and costly for it to disclose each of its connections.[29] However, when

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25 11 U.S.C. § 328(c).

> Except as provided in section 327(c), 327(e), or 1107(b) of this title, the court may deny allowance of compensation for services and reimbursement of expense of a professional person employed under section 327 or 1103 of this title if, at any time during such professional person's employment under section 327 or 1103 of this title, such professional person is not a disinterested person, or represents or holds an interest adverse to the interest of the estate with respect to the matter on which such professional person is employed.

Id.

26 The only individual that has ever been criminally charged with making a materially false Bankruptcy Rule 2014 affidavit was John Gellene, an ex-Milbank partner associated with the Bucyrus-Erie Bankruptcy in 1994. *See* Ronald R. Peterson, *Criminal Liability for the Bankruptcy Petitioner*, *in* ATTORNEY LIABILITY IN BANKRUPTCY 305, 306 (Corinne Cooper & Catherine E. Vance eds., A.B.A. 2006); *see also* Paul M. Barrett, *How Ex-Millbank Partner Gellene Ended Up on Trial Over a Conflict*, WALL STREET J. (Feb. 23, 1998), https://www.wsj.com/articles/SB888188381575881500.

27 *See Gellene*, 182 F.3d at 585–91. In *Gellene*, John Gellene was charged under sections 152(3) and 1623 of title 18 of the United States Code. Pertinently, section 152(3) states, "[a] person who—(3) knowingly and fraudulently makes a false declaration, certificate, verification, or statement under penalty of perjury . . . in relation to any case under title 11; . . . shall be fined under this title, imprisoned not more than 5 years, or both." 18 U.S.C. § 152(3) (2012). Similarly, section 1623 provides:

> (a) Whoever under oath (or in any declaration . . .) in any proceeding before or ancillary to any court or grand jury of the United States knowingly makes any false material declaration or makes or uses any other information, including any book, paper, document, record, recording, or other material, knowing the same to contain any false material declaration, shall be fined under this title or imprisoned not more than five years, or both.

Id. § 1623. Additionally, it should also be noted that section 1746 of title 28 of the United States Code states that a bankruptcy professional's declarations pursuant to Rule 2014 are made under the penalty of perjury. *See* 28 U.S.C. § 1746 (2018).

28 *Gellene*, 182 F.3d at 586–87.

29 Symposium, *Professional Fees in Bankruptcy*, 29 AM. BANKR. INST. L. REV. (forthcoming 2021) (on file with American Bankruptcy Institute Law Review) [hereinafter Symposium, *Professional Fees in Bankruptcy*]. It should be noted, however, that McKinsey maintains that the company adhered to all disclosure protocols in

analyzing the disclosure requirements imposed on other professionals outside of bankruptcy, such a conclusion cannot be reached. Throughout the business world, disclosure is mandated on professionals in a variety of different fields and in a variety of different manners. Regardless of its form, it is evident that disclosure is stressed and mandated in order to maintain the fundamental principles of transparency and fairness.

One business concept that relates closely to the idea of a chapter 11 reorganization is a management buyout ("MBO"). Put simply, an MBO is a corporate finance transaction where the existing management team of a company acquires financing in an effort to buy out the current business owners.[30] In such a transaction, managers play an interesting dual role, acting as fiduciaries to their shareholders while at the same time acting as acquirers of the company.[31] Similar to professionals retained by a debtor in chapter 11, these managers have the ability to directly affect the value of the company and the value received by shareholders and creditors. As such, similar to the Code, federal securities laws have imposed distinct disclosure requirements that apply to MBOs, specifically when an MBO is a "going private transaction."[32] One such rule, Rule 13e-3,[33] is designed to cover transactions that are not done at arms-length, as they have the potential for abuse and overreaching.[34] Rule 13e-3 requires that the managers leading the transaction must disclose "the purposes of the going private transaction, the basis on which the filer has drawn its conclusions on whether the transaction is fair to the target's unaffiliated security holders, and the content of any fairness opinion received from the issuer's financial adviser."[35] The rule is a direct attempt by the Securities and Exchange Commission ("SEC") to

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a sufficient manner. *See* Walsh, *supra* note 4 ("[T]he settlement did not require McKinsey to admit that its disclosures were insufficient or noncompliant, and did 'not in any way constitute an admission of liability or misconduct by McKinsey . . . .'"). Additionally, McKinsey has gone to the lengths of proposing its own disclosure protocol. The proposal, referred to as the "Houston Disclosure Protocol," which was created in the Westmoreland Coal Bankruptcy Case, will be discussed in further detail later in this Note, but it essentially acts as McKinsey's attempt to lighten the disclosure requirements imposed by the Code. *See* McKinsey Recovery & Transformation Services U.S., LLC's Eighth Status Report in Accordance with Order on Joint Motion in Furtherance of Mediation Agreement [Dkt. 1427] at 1, *In re* Westmoreland Coal Co., No. 18-35672 (DRJ) (Bankr. S.D. Tex. 2018) [hereinafter Houston Disclosure Protocol].

30 *See Management Buyout (MBO) Management using leverage to buy their company from shareholders*, CORP. FIN. INST., https://corporatefinanceinstitute.com/resources/knowledge/finance/management-buyout-mbo/ (last visited Apr. 19, 2020).

31 *See* Iman Anabtawi, *Predatory Management Buyouts*, 49 U.C. DAVIS L. REV. 1285, 1298 (2016) (explaining, on one hand, managers are "obligated to obtain the best deal possible for the company and its shareholders," but, on the other hand, are looking to "obtain the best possible deal for the prospective new owners of the company, which include itself").

32 *See* Nancy L. Sanborn, Phillip R. Mills & Saswat Bohidar, *Going Private Transactions: Overview*, DAVIS POLK & WARDWELL LLP (2010), https://www.davispolk.com/files/uploads/davis.polk.going.private.pdf ("'Going private' is a term used to describe a transaction (or series of transactions) with a controlling stockholder or other affiliated person(s) that reduces the number of stockholders of a public company, allowing the company to terminate its public company status and related reporting obligations under the Securities Exchange Act of 1934 . . . .").

33 17 C.F.R. § 240.13e-3(a)(3) (2015).

34 Anabtawi, *supra* note 31, at 1311–13.

35 *Id.* at 1311.

address the concerns about self-dealing in MBO transactions; it imposes on managers a level of accountability that the Bankruptcy Code also seeks to impose on its professionals in ensuring that their interests are not adverse to those of the estate.[36]

Another area of the financial services industry where the SEC has stressed the importance of disclosure is in stockbroker transactions. The SEC recently articulated a new standard of conduct for broker-dealers under the Securities Exchange Act of 1934, which applies when broker-dealers engage in making recommendations to customers regarding any security transaction or investment strategy involving securities.[37] The standard, referred to as "Regulation Best Interest" is designed to, in part,

> address conflicts of interest by establishing, maintaining, and enforcing policies and procedures reasonably designed to identify and fully and fairly disclose material facts about conflicts of interest, and in instances where [it has been] determined that disclosure is insufficient to reasonably address the conflict, to mitigate or, in certain instances, eliminate the conflict.[38]

Regulation Best Interest takes steps to effectuate this purpose by expanding the definition of a conflict of interest to include "an interest that might incline a broker-dealer—consciously or unconsciously—to make a recommendation that is not disinterested."[39] Furthermore, the standard continues to broaden disclosure requirements by explicitly requiring broker-dealers to provide "'full and fair' disclosure of material facts, rather than requiring broker-dealers to 'reasonably disclose' such information."[40] While admittedly the standard imposed by Regulation

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[36] *Id.* at 1311–13. Similar to relief allocated by the Bankruptcy Code's fraud provisions, if the SEC believes that a company has violated Rule 13e-3, it may take action against the company either administratively or in federal court.

[37] *See* Regulation Best Interest: The Broker-Dealer Standard of Conduct, Exchange Act Release No. 34–86031, 84 Fed. Reg. 33318, 33319 (July 12, 2019) (to be codified at 17 C.F.R. pt. 240) ("Regulation Best Interest enhances the broker-dealer standard of conduct beyond existing suitability obligations, and aligns the standard of conduct with retail customers' reasonable expectations . . . .").

[38] *Id.*

[39] *Id.* at 33325.

[40] *Id.* at 33326.

> The Disclosure Obligation requires the disclosure of *all* material facts related to the scope and terms of the relationship with the retail customer. The material facts identified in Regulation Best Interest are the minimum of what must be disclosed. Similar to what was proposed, broker-dealers will need to disclose in writing prior to or at the time of a recommendation any material facts that relate to the "scope and terms of the relationship." As to what constitutes a "material" fact related to the "scope and terms of the relationship," the standard for materiality for purposes of the Disclosure Obligation is consistent with the one the Supreme Court articulated in *Basic v. Levinson*. Specifically, a fact is material if there is "a substantial likelihood that a reasonable shareholder would consider it important." In the context of Regulation Best Interest, the standard is the retail customer, as defined in the rule.

Id. at 33347.

Best Interest is not as broad as the "connections" standard imposed on reorganization consultants retained under section 327, pursuant to Rule 2014, the new standard's goal of enabling consumers to make complete and informed decisions about a recommendation runs parallel to the Code's goal that the court is presented with all the information it needs to determine whether a professional is sufficiently disinterested.[41]

Finally, as an additional comparison, we can look to the disclosure requirements imposed on investment advisers when entering into soft dollar arrangements. A soft dollar arrangement involves a money manager using client brokerage commissions to purchase research that helps that manager make investment decisions.[42] Such agreements, and the use of "soft dollars" in general, are typically scrutinized by the investing public, as many hold the belief that brokerage companies operating on the buy-side should use their own profits to pay for research expenses, rather than use investor profits.[43]

In part due to this scrutiny, when engaged in soft dollar arrangements advisers must comply with all federal law disclosure requirements.[44] Currently, advisers adhere to such disclosure requirements by delivering Form ADV to each of their clients upon retention and each year after that.[45] Form ADV, acting the main disclosure document used by advisers, contains a variety of information including soft dollar disclosures describing to and alerting clients of the existence of any soft dollar agreements.[46] However, despite the disclosure requirements and the existence

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[41] *See id.* at 33365. Regulation Best Interest only requires broker-dealers to "disclose material facts about the scope and terms of the relationship or conflicts of interest." *Id.* at 33366. However, Bankruptcy Rule 2014 requires the professional seeking retention to disclose "all of the person's connections with the debtor, creditors, any other party in interest . . . ." FED. R. BANKR. P. 2014(a).

[42] *See CFA Institute Soft Dollar Standards: Guidance for Ethical Practices Involving Client Brokerage*, CFA INST. CTR. FOR FIN. MKT. INTEGRITY (Nov. 2004), https://www.cfainstitute.org/-/media/documents/code/other-codes-standards/soft-dollar-standards-corrected-2011.ashx; *see also* Brendan Biffany, Note, *Fixing Soft Dollars Is Not That Hard: A Consent and Reporting Framework for Regulating Client Commission Arrangements*, 68 DUKE L.J. 141, 148–49 (2018) ("[Soft dollar] agreements take one of two general forms. In the first iteration the adviser and broker might agree that when the adviser sends trades to the broker, the broker will credit the adviser's account with soft dollar credits . . . . As the adviser trades with the broker, his soft dollar credit balance increases. Later the adviser can exchange the accumulated balance for research and brokerage services provided by the broker. The second form is for the broker, in advance, to provide credits to pay a portion of the adviser's research bill with an independent research provider. In return, the adviser agrees to send the broker future trades at premium commission rates.").

[43] *See* James Chen, *Soft Dollars*, INVESTOPEDIA (Feb. 13, 2020), https://www.investopedia.com/terms/s/softdollars.asp (explaining brokerage companies have turned to using "hard dollars" because the use of "soft dollars" is frowned upon to pay expenses).

[44] *See* Biffany, *supra* note 42, at 152.

[45] *See id.* at 152–53 (expressing how financial advisers meet the federal disclosure requirements).

[46] *See id.* Biffany explains that soft dollar disclosures include three general statements:

> First, advisers must explain that they benefit when they use client brokerage commissions to obtain research or brokerage services because they do not have to pay for those products themselves. Second, advisers must disclose that they have an incentive to select a broker based on their own interest in receiving research, rather than the client's interest in receiving the most favorable execution terms. And third, advisers must disclose the

of Form ADV, the SEC has found that advisers often fail to adhere to the rules and make insufficient disclosures to their clients.[47] The SEC's concern with these insufficient disclosures is markedly similar to the concerns of bankruptcy courts when addressing professionals utilizing their clients to unjustly enrich themselves.[48] Similar to the repercussions a professional faces for failure to adequately disclose in a bankruptcy case, an investment adviser can too be subject to administrative proceedings against him or her if the SEC determines that soft dollars have been used by the adviser without adequate disclosure. While it is argued that more disclosure may be needed when it comes to soft dollar agreements, it is clear that the disclosure requirements that are in place attempt to remedy some of the same concerns held by the Bankruptcy Court.

III. THE "MCKINSEY PROBLEM"

Throughout his crusade against McKinsey and the company's disclosure practices, Jay Alix consistently alleges that McKinsey knowingly conceals its disqualifying conflicts of interest in chapter 11 cases where the company acts as an adviser.[49] In reference to such allegations, the court in *Alix v. McKinsey & Co.* noted that, "if true . . . the [alleged] facts are indeed concerning."[50] While the allegations have never been proven in court,[51] in April of 2018, the Wall Street Journal ("the Journal") published an eye-opening report detailing the findings of its investigation into McKinsey's disclosure practices.[52] In the report, the Journal analyzed McKinsey's disclosure filings in each of the thirteen chapter 11 cases in which

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> fact that they may cause clients to pay commissions greater than those charged by discount brokers in order to receive soft dollar benefits.

Id. at 153–54 (citations omitted).

47 *See id.* at 156 (noting the SEC has found that a majority of investment advisers who participate in soft dollar arrangements are not providing "meaningful disclosures" about them to clients).

48 *See id.* at 157 ("[S]oft dollars provide an avenue for advisers to use client commissions to unjustly enrich themselves. Inadequate disclosure requirements contribute to these abuses.").

49 *See* Objection of Mar-Bow Value Partners, LLC, a Creditor, to the Debtor's Application for Approval of the Employment of McKinsey Restructuring And Transformation Services U.S., LLC at 4, *In re* Westmoreland Coal Co., No. 18-35672 (DRJ) (Bankr. S.D. Tex. 2018) [hereinafter Objection of Mar-Bow Value Partners] ("Either McKinsey RTS or its parent . . . has served as a professional for Chapter 11 debtors in thirteen previous cases. In those cases, McKinsey and McKinsey RTS filed a total of 39 disclosure declarations. Each of those 39 disclosure declarations concealed multiple connections and was false."); *see also* Alix v. McKinsey & Co., 404 F. Supp. 3d 827, 829 (S.D.N.Y. 2019) ("Alix brings this lawsuit because he believes that McKinsey has won bankruptcy-consulting business at the expense of AlixPartners by filing incomplete or misleading Rule 2014 disclosure statements.").

50 *McKinsey & Co.*, 404 F. Supp. 3d at 829–30.

51 Jay Alix's RICO claim against McKinsey & Co. was dismissed for failure to satisfy RICO's proximate clause standard; the Court never reached the issue of whether or not McKinsey's disclosure practices were adequate. *See id.* at 830. Jay Alix is currently challenging McKinsey's retention using the same allegations in *In re Westmoreland Coal Co.*, No. 18-35672 (DRJ) (Bankr. S.D. Tex. 2018). *Id.* at 831.

52 *See generally* Gretchen Morgenson & Tom Corrigan, *McKinsey Is Big in Bankruptcy—and Highly Secretive*, WALL STREET J., https://www.wsj.com/articles/mckinsey-is-big-in-bankruptcyand-highly-secretive-1524847720?mod=article_inline (last updated Apr. 27, 2018, 1:29 PM).

McKinsey had participated as a restructuring adviser,[53] concluding that the company "routinely discloses far fewer names and descriptions of connections than other advisers."[54]

In these disclosures, McKinsey initially identified by name a mere total of fifty-nine connections to participating parties in those thirteen cases—in comparison, the other fourty-five bankruptcy professionals involved in such cases, named more than 15,000 connections in total.[55] The chart attached in Appendix A, created by the Journal, exemplifies the stark contrast of such disclosure practices: "[o]n average, McKinsey reported five such relationships per case compared with the other firms' disclosures of 171 connections each."[56] Depicting the disclosure data further, the chart attached in Appendix B, also created by the Journal, offers a visual on exactly what McKinsey's disclosure numbers looks like as juxtaposed to other professionals.[57]

A. Organizational Structure

In order to determine why McKinsey's disclosures are more barren in relation to other professionals, it is important to look at their current organizational structure. According to their website, McKinsey employs over 30,000 people in 130 cities around the world.[58] Due in part to its vast operations around the globe, the company brings in a revenue of $10 billion a year.[59] Specifically, the company operates through a variety of subsidiaries. Two of the subsidiaries that are important to understand while analyzing the controversy surrounding their disclosure documents include McKinsey RTS and MIO Partners, Inc. ("MIO").[60] As mentioned earlier, McKinsey RTS functions as the firm's corporate restructuring and turnaround arm and, as such,

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[53] *See* cases cited *supra* note 3.

[54] Morgenson & Corrigan, *supra* note 52, at 2.

[55] *See id.*

[56] *Id.*

[57] *See id.* at 4 ("In the Edison Mission Energy bankruptcy in 2012, McKinsey listed no relationships. Akin Gump Strauss Hauer & Feld, a law firm representing unsecured creditors, named and described 368 connections—not an unusual number for a large firm in a major bankruptcy.").

[58] *See About Us*, MCKINSEY & COMPANY, https://www.mckinsey.com/about-us/overview (last visited Apr. 19, 2020).

[59] *See McKinsey & Company*, FORBES, https://www.forbes.com/companies/mckinsey-company/#207135724c1d (last updated Dec. 17, 2019).

[60] McKinsey RTS is a direct wholly-owned subsidiary of McKinsey & Company, Inc., United States. McKinsey & Company, Inc., United States is a direct wholly-owned subsidiary of McKinsey Holdings, Inc., which is a direct wholly-owned subsidiary of McKinsey & Company, Inc. MIO Partners, Inc., is also a wholly owned subsidiary of McKinsey & Company Inc. *See* Objection of Mar-Bow Value Partners, *supra* note 49, at 8–12; *see also Who We Are*, MIO PARTNERS, https://www.miopartners.com/ public/who-we-are/ (last visited Apr. 19, 2020) (explaining MIO is a subsidiary of McKinsey and a registered investment adviser regulated by the SEC, providing investment options and advice to McKinsey pension plans, and to current and former McKinsey partners); *Reset. Transform. Sustain*., MCKINSEY & COMPANY, https://www.mckinsey.com/business-functions/rts/how-we-help-clients (last visited Apr. 19, 2020) (RTS is: "a special unit of McKinsey that delivers a proven approach for transformational change to clients seeking radical, rapid, and sustainable performance improvement" with over 200 specialists, $100+ billion of CFO-certified value creation, thirty plus industries, in sixty-nine countries).

McKinsey RTS is the subsidiary retained as a professional in many of the chapter 11 cases at issue.[61] MIO on the other hand, functions as McKinsey's investment arm, providing "investment options and advice to McKinsey & Company's pension plans and to current and former McKinsey partners."[62] On behalf of the company's current and former employees, MIO manages over $12 billion in assets across public and private markets.[63]

Jay Alix, and others criticizing McKinsey's disclosure statements, argue that because of the closely related nature of the two subsidiaries, they are in fact "one firm."[64] As such, the argument proceeds that under section 327 and Rule 2014, McKinsey RTS must disclose all connections of MIO in addition to its own connections.[65] McKinsey vehemently rejects this argument, stating that MIO Partners is a separately operating subsidiary that is designed to be disinterested.[66] McKinsey further states that its board of directors, which oversees MIO, has delegated the responsibility to make investment decisions to the professional staff of MIO, who in turn engage and supervise third-party managers who make investment decisions under their own discretion.[67] In its application for retention in the Westmoreland Coal bankruptcy, McKinsey admitted that MIO had not been asked to search for connections to potential parties in interest.[68] This is consistent with the pattern of actions influencing McKinsey's sparse disclosure statements that the company has relied upon when acting as an adviser in the other chapter 11 cases.[69]

B. Houston Disclosure Protocol

In response to the criticism received from Jay Alix and the U.S. Trustee, McKinsey proposed a new bankruptcy disclosure practice to the court in *In re*

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[61] *See Reset. Transform. Sustain.*, MCKINSEY & COMPANY, https://www.mckinsey.com/business-functions/rts/how-we-help-clients (last visited Apr. 19, 2020) (describing RTS's relationship with McKinsey and discussing its specialists in corporate restructuring and distressed turnarounds).

[62] *Who We Are*, MIO PARTNERS, INC., https://www.miopartners.com/public/who-we-are/ (last visited Apr. 19, 2020).

[63] *See What We Do*, MIO PARTNERS, INC., https://www.miopartners.com/public/what-we-do/ (last visited Apr. 19, 2020); *see* Debtors' Application for Entry of an Order Authorizing the Retention and Employment of McKinsey Recovery & Transformation Services U.S., LLC as Performance Improvement Advisors to the Debtors *Nunc Pro Tunc* to the Petition Date at 52, *In re* Westmoreland Coal Co., No. 18-35672 (DRJ) (Bankr. S.D. Tex. 2018) [hereinafter Debtors' Application for Retention] ("It manages assets for . . . pension plans sponsored by McKinsey in which current and former McKinsey employees participate.").

[64] Objection of Mar-Bow Value Partners, *supra* note 49, at 19. Arguing for this proposition, Alix relies on the following main points: MIO only exists to serve the affiliates of McKinsey; McKinsey RTS's practice leader is also a general partner of McKinsey & Company; MIO shares in the profits of McKinsey as a whole including the profits generated by McKinsey RTS. *Id.*

[65] *See id.*

[66] *See* Debtors' Application for Retention, *supra* note 63, at 18.

[67] *See id.* at 52.

[68] *See id.* at 53.

[69] *See* Objection of Mar-Bow Value Partners, *supra* note 49, at 4.

Westmoreland Coal.[70] Central to the proposal, referred to as the Houston Disclosure Protocol ("the Protocol"), is McKinsey's belief that restructuring advisers should be able to limit the amount they reveal regarding potential conflicts.[71] Namely, the proposal limits disclosure requirements by: (A) defining the term "Connections;"[72] (B) allowing professionals to exclude connections that the professional seeking retention does not have actual knowledge of, or deems to be "*De minimus*;"[73] and (C) by providing for different classifications of "Connections" suggesting different disclosure treatment for each classification.[74]

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[70] *See* Houston Disclosure Protocol, *supra* note 29. The Court, when discussing the proposed protocol, expressly stated that it would not approve the protocol and exchange the disclosure standard imposed on professionals seeking retention in a chapter 11 case:

> THE COURT: So am I going to be curious to read it? Absolutely. Am I going approve it? Absolutely not. You know, the standard is what the standard is. I'm assuming that the protocol will simply be a mechanism, if you will, on how compliance is hoped to be achieved. So I'm going to read it. I'm going to go through it. I may have some comments about it. I don't know what I am going to do with it. I haven't seen it. But in terms of whether or not that changes the required standard under the applicable rules, it does not.

Mar-Bow Value Partners LLC's Response to McKinsey's Protocol at 4, *In re* Westmoreland Coal Co., No. 18-35672 (DRJ) (Bankr. S.D. Tex. 2018) [hereinafter Mar-Bow Response to McKinsey's Protocol] (citing Hearing Transcript, *In re* Westmoreland Coal, No. 18-35672, Apr. 16, 2019, 41: 12-16, 42: 8-18).

[71] *See* Morgenson & Corrigan, *supra* note 52 ("Restructuring advisers should be able to limit how much they reveal about potential conflicts of interest in large bankruptcy cases, a role typically left to federal judges, according to a new protocol on bankruptcy practices drafted by consulting firm McKinsey & Co.").

[72] In the context of section 327 and Rule 2014, McKinsey's protocol defines a "Connection" as "an association or relationship with an IPL Party that a reasonable person might find bears on whether the Proposed Professional 'holds or represents an interest adverse to the estate' and is 'disinterested' under section 327 and section 101(14), based on the facts of a particular bankruptcy case." *See* Houston Disclosure Protocol, *supra* note 29, at 3. An "IPL Party" is defined as "the persons or parties listed on an IPL." *Id.* An "IPL" references the "Interested Party List," which means "a list of parties with Connections to the debtors' estate (other than de minimus connections)." *Id.*

[73] *Id.* at 1. McKinsey's protocol defines the term "*De minimus*" as "a known Connection between a Proposed Professional and an IPL Party (other than an Indirect Connection)." *Id.* at 3.

[74] *See id.* at 1–2. McKinsey's protocol provides for a somewhat complicated classification system of Connections. The protocol starts by distinguishing between "(a) Retained Affiliates, which the Protocol classifies as generating Direct Connections of the Proposed Professional, and (b) Unretained Affiliates (including AMAs), which the Protocol classifies as generating Indirect Connections." *Id.* at 1. "Direct Connections" are defined as "a known Connection between a Proposed Professional and an IPL Party (other than an Indirect Connection)." *Id.* at 3. "Indirect Connections" are defined as an Immediate Indirect Connection [defined as a "known Connection between an IPL Party and a Proposed Professional's Unretained Affiliate (including an AMA)"] or a Remote Indirect Connection [defined as a "known Connection arising from a relationship between a Proposed Professional's Unretained Affiliate (including an AMA) and a third party, which third party, in turn, has a Connection with an IPL Party."]. *Id.* at 3–4. The Final piece of the puzzle is the definition of "AMA" which:

> means an affiliate or division of a Proposed Professional that is actively engaged in managing or owning financial investments. For clarity, AMA does not refer to assets that might be held through investment vehicles or to such investment vehicles, e.g., mutual funds, but does refer to the entity managing such investment vehicles, i.e., a mutual fund manager.

Id. at 3. The Protocol provides for four different sub levels of AMAs. *See id.* at 5.

As expected, the Protocol was met with much scrutiny by Jay Alix and Mar-Bow Partners.[75] Alix's objections stem from the central proposition that McKinsey's protocol "illegally constrict[s] the disclosures that Rule 2014 requires of it" and, as such "improperly limits the information that the Court critically needs to evaluate McKinsey's conflicts of interest and qualifications to serve as a professional under 11 U.S.C. § 327."[76] First, Alix attacks the "restrictive definition" of the term connection.[77] He argues that because the definition essentially only requires adherence to sections 327 and 101(14) of the Code, the definition ignores that "[t]he disclosure requirements of Rule 2014(a) are broader than the rules governing disqualification."[78] Next, Alix takes issue with the proposition that McKinsey, and other potential professionals, would be able to exclude connections that are not actually known to the estate, excusing connections that reasonable investigations should have disclosed but did not.[79] Alix prudently points out that Rule 2014 requires disclosure of "all connections," regardless of whether or not they are de-minimus.[80] He asserts that a standard to the contrary would promote "negligence, willful blindness, and even bad faith."[81]

Finally, Alix contends that by allowing McKinsey or another professional to restrict its disclosure in the manner provided for, a professional would be able to hide their investment connections from the court.[82] Jay Alix points to the complex scheme that the Protocol sets up to determine first, what type of connections must be disclosed and then second, which "type" of AMA a professionals investment connection would fall under.[83] Regardless of its complexity, once again Alix points to the Code itself, which, through section 327, has been interpreted to provide that disqualification is *mandatory* if the professional seeking retention holds an equity interest in the debtor or an interested party.[84]

IV. THE SOLUTION—ADHERE TO THE REQUIREMENTS IMPOSED BY THE CODE

As discussed throughout this Note, the Code imposes disclosure requirements on professionals seeking retention through section 327 and Rule 2014. Essentially, the requirements imposed by these provisions can be summed up in 3 major points: a professional seeking retention must (1) not hold an interest adverse to the estate; (2)

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75 *See, e.g.*, Mar-Bow Response to McKinsey's Protocol, *supra* note 70, at 1 ("This response demonstrates that in substantial and illegal ways, McKinsey's protocol dangerously obstructs the Court's ability to carry out its responsibility to preserve the integrity of its process.").

76 *Id.*

77 *Id.*

78 *Id.* at 9 (quoting *In re* Am. Int'l Refinery, Inc., 676 F.3d 455, 465 (5th Cir. 2012)).

79 Mar-Bow Response to McKinsey's Protocol, *supra* note 70, at 10–14.

80 *Id.* at 12 (emphasis omitted); *see also* FED. R. BANKR. P. 2014.

81 Mar-Bow Response to McKinsey's Protocol, *supra* note 70, at 12.

82 *Id.* at 10–14 (arguing McKinsey's protocol allows a professional to manipulate its disclosure obligations for excusing disclosures for connections the professional is "willfully blind" to).

83 *Id.*

84 *Id.* at 23.

be disinterested as defined by section 101(14); and (3) disclose all connections (a term consistently held to have broader meaning than that of a general conflict) for the court to have adequate information to make a decision determining whether or not such a professional is fit to serve the estate. Despite their breadth, these requirements have proven to be achievable, as numerous professionals have abided to them for years. For McKinsey to abide by the rules it does not need to recreate them, the company simply needs to follow them. Two ways McKinsey can adhere to the requirements imposed is through the creation and adoption of a centralized conflict checking system or the establishment of a truly isolated restructuring LLC.

A. Centralized Conflict Checking System

A clear view into the conflict-checking procedure that McKinsey currently employs is obtainable by analyzing the company's application for retention in the Westmoreland Coal bankruptcy case.[85] There, as in other cases, McKinsey immediately stresses its protection of client confidentiality and the resulting business practices that it does not adhere to as a result.[86] One such general business practice that McKinsey does not employ is a centralized conflict checking database.[87] Instead, McKinsey has a global database for record keeping purposes.[88] In an effort to check for conflicts, McKinsey searches this database, which encompasses information regarding McKinsey RTS and its affiliates that provide consulting services (notably this *does not* include MIO).[89] The company also reviews billing records and the list of clients identified in McKinsey's financial records as clients of McKinsey RTS.[90] Additionally, McKinsey surveys members of its "Service Team"[91] by email.

This disclosure process is insufficient to determine all of the connections McKinsey may have with the bankruptcy estate. Rule 2014, as mentioned numerous times, requires the disclosure of *all connections* of the professional seeking retention.[92] A global consulting behemoth like McKinsey, who is involved in

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[85] *See* Debtors' Application for Retention, *supra* note 63, at 48–70.

[86] *Id.* at 48 ("Because of its practice of serving clients with overlapping or competing interests, [McKinsey RTS and its consulting affiliates] do not have in place any centralized conflicts identification process, and instead have a global database of clients and engagements performed for those clients, which is kept principally for record keeping purposes and does not contain detailed descriptions of the client support.").

[87] *See id.* Mar-Bow in its response to McKinsey's Protocol asserts that "McKinsey is the only professional in large chapter 11 cases that claims it does not have a conflicts-checking database." *Id.* at 27.

[88] *See id.* at 48.

[89] *See id.* at 49 (stating McKinsey's global client database "covers clients of McKinsey . . . and all affiliates that provide consulting services"); *see also id.* at 52 ("MIO Partners is operated separately and distinctly from McKinsey's consulting services.").

[90] *Id.* at 49.

[91] The Service Team is defined as including "(a) the directors, officers and employees of McKinsey RTS US, and (b) certain consultants borrowed from affiliates of McKinsey RTS US for the purpose of serving the Debtors in these Chapter 11 cases." *Id.* at 36.

[92] *See* FED. R. BANKR. P. 2014 (explaining "all of the person's connections with the debtor, creditors, and any other party in interest, their respective attorneys and accountants, [and] the United States Trustee" must be disclosed).

"helping organizations optimize their application hosting, network, and end-user environments to operate effectively and efficiently at scale," has no reason to lack a functional conflict checking database.[93] Despite having the clear ability and expertise to implement such a routine conflict-checking system, McKinsey simply may not want to because it understands that its conflicts would be plentiful and result in frequent disqualification. However, McKinsey should not be able to decide that it does not have to play by the rules just because it does not want to. All major law firms, financial service companies and business advisers operating in industries that require adherence to conflict of interest rules routinely employ conflict-checking databases—McKinsey should be no different.

B. Truly Isolated LLC

Evidence of a second troubling trend employed by McKinsey when seeking professional retention can again be found in its application in *Westmoreland Coal*. There, McKinsey asserts that MIO and RTS are two distinct and separate subsidiaries and that "because of such separateness . . . McKinsey RTS US has not asked MIO Partners to search for connections to the Potential Parties in Interest."[94] As discussed above, there are arguments as to whether the two subsidiaries are functionally different or apart of the same firm. Regardless, the following is clear: (1) MIO is established to manage assets for pension plans sponsored by McKinsey that current and former McKinsey employees participate in, while also offering private investment vehicles in which McKinsey partners can invest;[95] and (2) employees working as advisers in the chapter 11 cases come from *both* McKinsey RTS and other affiliate McKinsey subsidiaries.[96]

These two facts reveal a major issue with McKinsey's level of disinterestedness. First, the fact that the company operates its investment/retirement fund on behalf of its employees implies that its employees know where their money is being invested.[97] In fact, Jay Alix asserts that much of this information is public and thus available to all employees.[98] Furthermore, by employees moving across subsidiaries—even if the MIO employees are specific to MIO as asserted by McKinsey—the line becomes blurred between the different subsidiaries giving rise to a stronger presumption of

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[93] *How We Help Clients*, MCKINSEY DIGITAL, https://www.mckinsey.com/business-functions/digitial-mckinsey/how-we-help-clients/digital-strategy (last visited Apr. 19, 2020); *see also* Mar-Bow Response to McKinsey's Protocol, *supra* note 70, at 31.

[94] Debtors' Application for Retention, *supra* note 63, at 53.

[95] *See id.* at 52.

[96] *See id.* at 36 ("Members of the Service Team are employed by McKinsey RTS US and McKinsey & Company, Inc. United States and other affiliates that provide consulting services."). For a definition of "Service Team," see *supra* note 91.

[97] *See* Symposium, *Professional Fees in Bankruptcy*, *supra* note 29.

[98] *See* Objection of Mar-Bow Value Partners, *supra* note 49, at 14.

disinterestedness.[99] If McKinsey truly wanted to appear and act as a disinterested party in chapter 11 cases, the company should establish a separate LLC to conduct all of its bankruptcy consulting business without any potential influence from MIO investment holdings and without any employee crossover with the other McKinsey subsidiaries.

CONCLUSION

Contrary to the assertions of McKinsey and other professionals seeking retention, when taken together, section 327, Rule 2014, and the case law interpreting these provisions paint a clear picture of what is required of professionals. Admittedly, the picture that results may be a broad painting and one that requires a wide variety of disclosure action from a professional seeking retention, but ultimately that is the point. The Bankruptcy Code seeks to fulfil its paramount goal in ensuring the unmarred administration of bankrupt estates operating in chapter 11. As realized elsewhere in the business world, such a goal is best served by imposing strict disclosure requirements in an effort to minimize conflicts and potential self-dealing. No new disclosure procedures minimizing the requirements already imposed by the Code are needed to further effectuate this purpose. If McKinsey, or any other professional, can't accept the current requirements imposed by section 327 and Rule 2014, they would be better off operating in a different industry.

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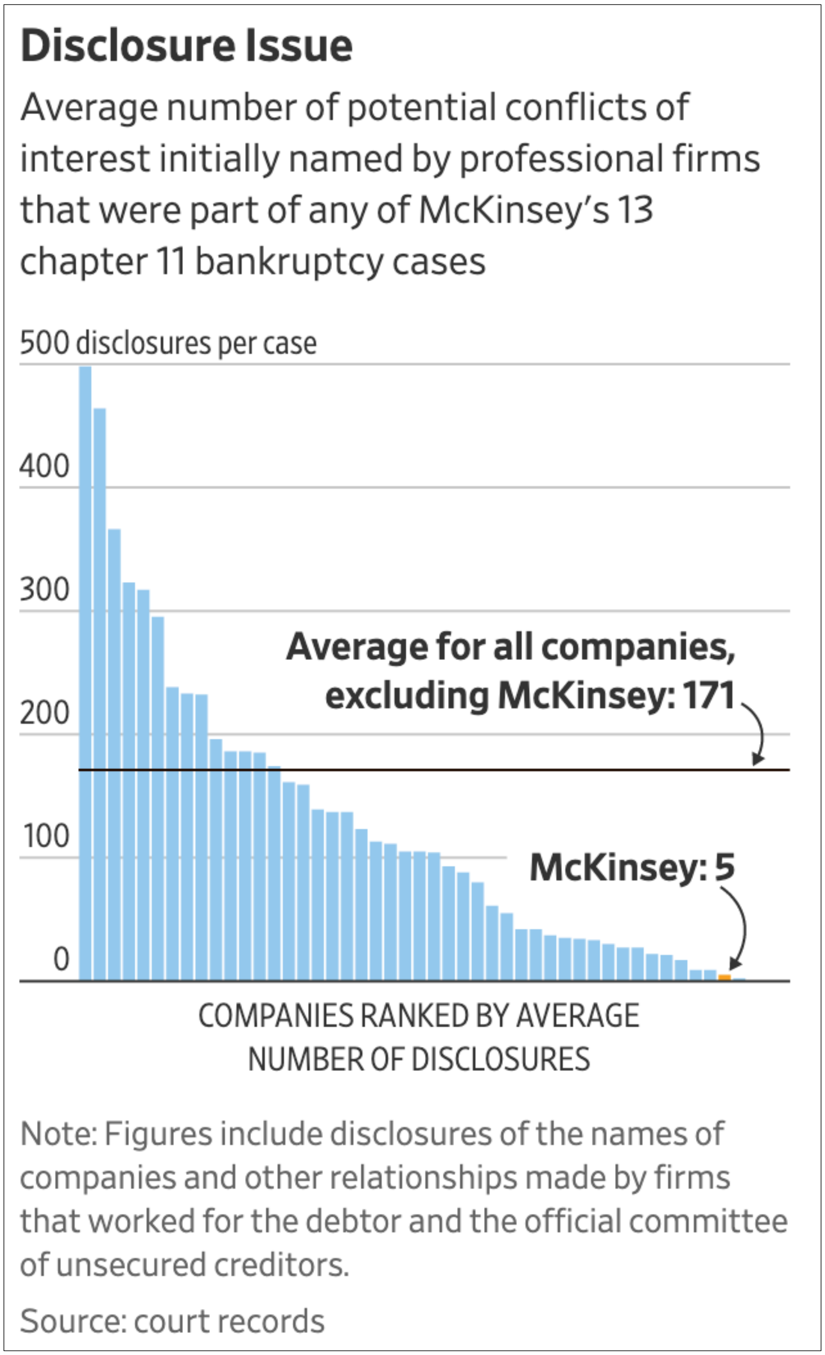
[99] The head of the bankruptcy consulting group is also a partner in main McKinsey. *See Our People: Practice Leaders*, MCKINSEY & COMPANY, https://www.mckinsey.com/business-functions/rts/our-people (last visited Apr. 19, 2020); *see also* Symposium, *Professional Fees in Bankruptcy*, *supra* note 29.

APPENDIX A



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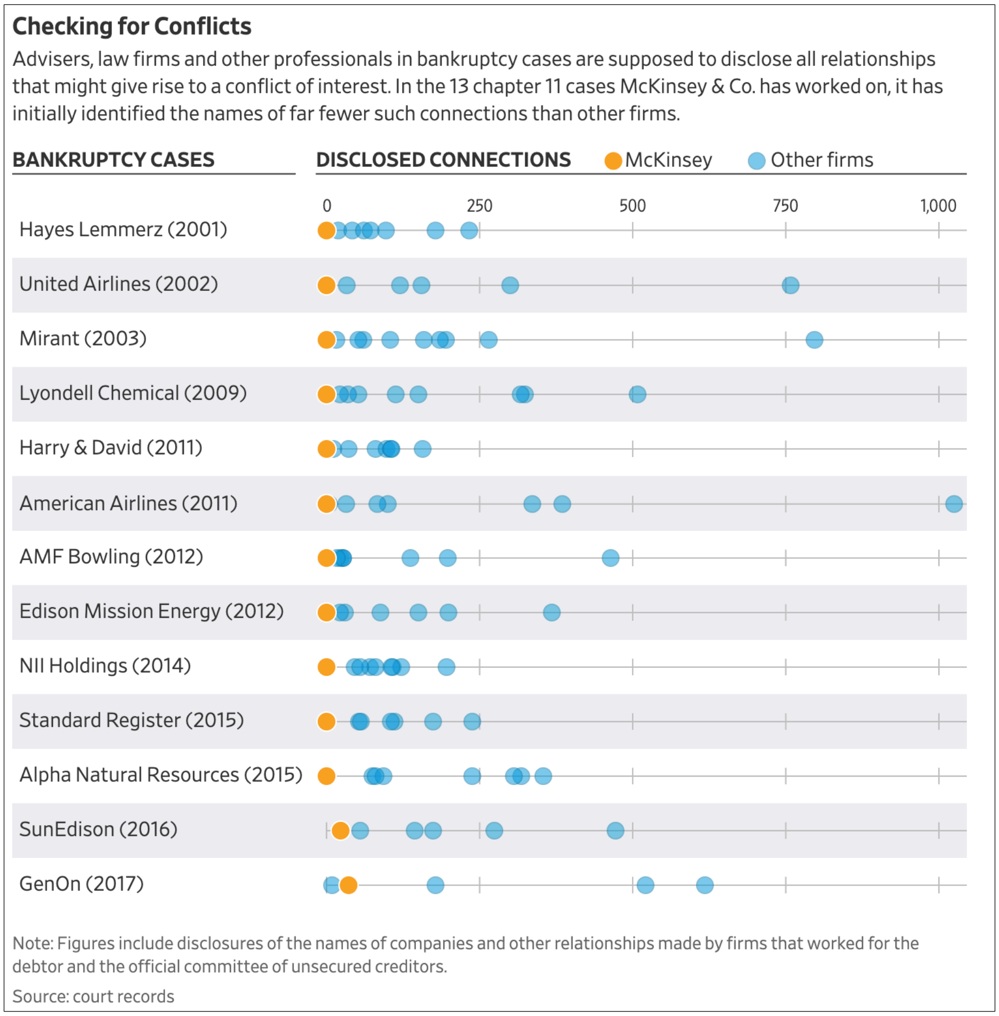
APPENDIX B



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