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Koch Industries, Inc. Strategic Corporate Research Report

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Koch Industries, Inc. Strategic Corporate Research Report

Abstract

[Excerpt] With its 2005 purchase of paper giant Georgia-Pacific, Koch Industries became the largest privately-held corporation in North America. Originally started as an oil production and refining firm in the first half of the twentieth century, Koch now has major operations in petroleum, chemicals, energy, fibers and polymers, minerals, fertilizers, chemical technology equipment, forest and consumer products, ranching, trading, and securities and finance. The company, based in Wichita, Kansas, employs 80,000 people in sixty countries worldwide.

Koch's oil operations are run primarily through the Flint Hills Resources family of subsidiaries, which has a production capacity of about 800,000 barrels of crude oil daily. Another one of Koch's major ventures, synthetic textiles, operates through the company's wholly-owned subsidiary, INVISTA, which produces both consumer and commodity textiles. Koch's newest project, forest and consumer products, operates through Georgia-Pacific, which remains an independent but wholly-owned subsidiary of Koch Industries.

Keywords

Koch Industries, globalization, corporations, capitalism

Comments

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Office of Labor Education Research
Cornell ILR School

Koch Industries, Inc.

Strategic Corporate Research Report

**Patrick Young, Ed Yoo, Robert Wesley Hannah,
Iris Packman, and Jordan Wells**

Under the supervision of

**Kate Bronfenbrenner
Labor Education Research
Cornell University
School of Labor and Industrial Relations**

June 2006



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1. Executive Summary¹

1.1 Description of Firm and its Operations

With its 2005 purchase of paper giant Georgia-Pacific, Koch Industries became the largest privately-held corporation in North America. Originally started as an oil production and refining firm in the first half of the twentieth century, Koch now has major operations in petroleum, chemicals, energy, fibers and polymers, minerals, fertilizers, chemical technology equipment, forest and consumer products, ranching, trading, and securities and finance. The company, based in Wichita, Kansas, employs 80,000 people in sixty countries worldwide.

Koch's oil operations are run primarily through the Flint Hills Resources family of subsidiaries, which has a production capacity of about 800,000 barrels of crude oil daily. Another one of Koch's major ventures, synthetic textiles, operates through the company's wholly-owned subsidiary, INVISTA, which produces both consumer and commodity textiles. Koch's newest project, forest and consumer products, operates through Georgia-Pacific, which remains an independent but wholly-owned subsidiary of Koch Industries.

1.2 Profit Centers

Of Georgia-Pacific's four major operating segments, two major profit centers drive their operations. These two segments, Consumer Products and Building Products, comprise nearly 80 percent of their day-to-day operations. Ironically, their paper segment has lost a great deal of prominence, as they now focus on paper derivatives and building products to generate their profits. Paper comes in at around 9 percent of their operations, while Packaging is at 16 percent.

According to Georgia-Pacific's last 10-K report filed in 2005, just prior to their sale to Koch industries, their Consumer Products division, both domestic and international, made over \$7 billion in net sales in 2004, and Building Products was close behind with about \$6.8 billion in net sales.

Koch's petrochemical side is driven by the Flint Hills Resources subsidiary, where the main centers of operation are Corpus Christi, Texas; Pine Bend, Minnesota; and North Pole, Alaska. The Minnesota location is the main profit center, drawing in approximately \$800 million in annual sales.²

1.3 Growth Plan

Koch's 2004 acquisition of INVISTA and its 2005 acquisition of Georgia-Pacific seem to mark a major deviation from the company's history as an energy and commodities conglomerate. All signs indicate, however, that they are serious about these projects and plan to stay in these consumer product industries. After an interview with Charles Koch, *Financial Times* reporter

¹ This report was conducted by a team of undergraduate researchers under the supervision of Kate Bronfenbrenner. Administrative support for the project was provided by Tamara Lovell. This project was fully funded by the United Steel Workers.

² Dunn and Bradstreet report, Flint Hills Resources

Jeremy Grant noted that Koch was looking to expand into “value added” markets.

This newfound interest in consumer products does not mean that the company plans on leaving its new acquisitions untouched. In an interview for an Atlanta newspaper, Georgia-Pacific CEO Joe Moeller dropped hints that the company may be spinning off its consumer products division. Also, before the takeover, Georgia-Pacific was undergoing a major process of upgrading machinery in its consumer products division to increase productivity and reduce workforce. Under Koch’s leadership there is no indication that this has stopped or slowed appreciably. On the INVISTA side the company is making major investments, although not in its original US and EU facilities. INVISTA has just invested \$100 million in China to double its capacity in that region.

Koch’s new interest in consumer products does not mean that the company is going to be ignoring its interests in the oil industry. Koch has announced major projects in Alaska and Minnesota and is currently working to get approval for a new pipeline project that would increase the company’s capacities for bringing Canadian crude to its Pine Bend refinery. Additionally, the company is pursuing smaller projects in increasing capacity for refining and transportation at a number of refineries and terminals in the Corpus Christi, Texas area, the Minnesota region, and at the Netherlands refinery. The Alaska project entails a partnership to bring low-sulfur gasoline to the Alaskan market.

In an interview with the president of Koch Materials, several acquisitions are discussed. “In 2004, Koch completed more than \$7 billion in acquisitions, picking up an Alaska refinery from the Williams Co., chemical intermediates asset from BP, the pulp and paper business of Georgia-Pacific, and INVISTA, formerly DuPont Textiles & Interiors. Additionally, the company invested in the Tran Alaska Pipeline System, while its Koch Financial affiliate invested in Channel Re, a reinsurance company. Koch also expanded its refining facility in the Netherlands by \$15 million to boost capacity from 65,000 barrels a day to 80,000 barrels a day. On the other hand, Koch’s Materials Co. division put portions of its U.S. asphalt business up for sale in October 2004. “Our asphalt business is profitable,” said Rob Witte, president of Koch Materials, “but we recognize that other companies with different strategies may place a higher value on certain assets or businesses than we do.” The company found a buyer in Holly Western Asphalt Company, who paid \$22 million for a 51 percent interest in NK Asphalt Partners in February 2005. The same month, Koch set aside \$14 million to design and build an oil hydrotreater at its Navajo Refining Company in New Mexico, part of a larger company strategy for clean fuels. The project, expected to be complete by 2006, seems a sign that Koch is truly committed to cleaning up its act.”³

1.4 Key Decision Makers

There is no question that CEO and Chairman of the Board, Charles Koch, is running the show at Koch industries. Charles and his brother David (an executive vice president) each own half of the company and maintain strong control of the operations. The company’s management philosophy,

³ Obtained from the website Vault, http://vault.com/companies/reports/coreport_main.jsp? (vault-koch-snapshot) Accessed May 2006.

Market-Based Management, which demands that each employee acts as an individual entrepreneur, is something that CEO Charles Koch pursues almost fanatically. While Market-Based Management puts an emphasis on pushing decision making down to the lowest levels, it is clear that this does not mean that managers have the final say in their decision making—a strong hierarchy remains in place, and managers at the top have no problem pushing their vision down the decision-making chain.

Nearly all of the company's top executives have been with the company for most of their careers, and it is clear that Charles Koch rewards loyalty. David Robertson is President of the parent company and has been with Koch Industries since he graduated from college in the mid 1980s. He replaced Joe Moeller who became president of Koch's newest and biggest project, Georgia-Pacific. Moeller is also a career Koch employee, having started with the company in 1966. At INVISTA Jeff Walker was appointed CEO after the DuPont buyout. Walker has been with Koch subsidiaries for over 20 years. Charles Koch's brother David, a chemical engineer by training, runs the Koch Industries Chemical Group and is an executive vice president at the parent company.

When Koch acquired Georgia-Pacific, as with INVISTA, the company cleaned house among top managers. Among Georgia-Pacific's current fourteen executive officers, nine are from Koch or its subsidiaries; and only five—the company's business unit leaders and chief financial officer—have been allowed to stay through the takeover.

1.5 Key relationships

The most important relationship for Koch Industries is the tie between the Koch family, the company, and the conservative party. In addition to supporting a number of right-wing and libertarian think-tanks, including the Cato Institute, the majority of the companies' political donations go to the Republican Party. These occur both directly and through 527 Committees such as the Republican Governor's Association, Americans for a Republican Majority, and the Majority Leader's Fund.⁴ Not only does money bring them together, but Koch Industries is also connected through family and professional ties to the Republican Party. The Koch brothers' cousin Bobby Koch, for example, is married to Doro Bush, the younger sister of President Bush. Two government workers, Elizabeth Stolpe, the Associate Director of the White House Council on Environmental Quality, and Alex Behler, the Pentagon's Assistant Deputy Undersecretary of Defense for Environment, Safety and Occupational Health, were both formerly employed by Koch. Also, Bush's former Deputy Director of Political Affairs, Matt Schlapp, now works for Koch on government relations. These political connections do pay off, such as in 2000, when the company faced \$352 million in EPA fines that were subsequently dropped to a plea bargained small fine upon George Bush's inauguration. Also, the company has better access to securing lucrative timber rights for its paper subsidiaries.

Koch's most important financial relationship is with Citigroup. Financially, the company relied on Citigroup to provide an \$11 billion dollar loan to initialize the \$21 billion buyout of Georgia-Pacific. Deutsche Bank, Bank of America, and J.P. Morgan were among those that financed the

⁴ Ibid.

transaction as co-underwriters.⁵ Additionally, Koch has relied on Goldman Sachs for advice during the deal, as well as in past transactions. Subsidiary Flint Hills Resources has a \$510 million revolving credit line from a syndicate of banks led by Bank One in 2004.⁶

Koch Industries, acting on a free market model of purchasing, usually does not form long term core bonds with suppliers. Georgia-Pacific also avoids being dependent on any single provider. Thus its largest lumber supply source, Plum Creek Timber Company, represents only 6 percent of its total lumber supply. In the recycled paper sector, Georgia-Pacific obtains paper pulp from its subsidiary Harmon Associates, acquired in 2000 as part of the Fort James Corporation. The company does have several customers that are more significant, including Wal-Mart Stores Inc., Costco Wholesale Corp., Sam's Choice Wholesale, Carrefour SA, The Home Depot, Inc., Lothey's Companies Inc., Royal Ahold N.V., Target Corp., Sysco Corp., Kroger Co., Unisource, US Foodservice and Staples Inc.⁷ Although no company holds nearly a monopoly, together those businesses represent one quarter of GP's profit,⁸ and the loss of any one would be a large blow to the company.⁹

Koch has key relationships to several other companies in various fields. Flint Hills Resources, for example, is investing \$23 million in a low-sulfur gasoline project directed by the Tesaro Corp. in Alaska. But most importantly is its growing trade with China. Paper subsidiary Harmon is a part of a joint venture called Water Lily with the Chinese company PACCESS, through which it hopes to gain great access into the country.¹⁰ The fact that INVISTA is also investing large amounts of money in China—\$100 million in a production facility in Foshan, Guangdong Province of China for the manufacturing of (Lycra®) and commodity (Elaspan®) fibers¹¹—shows that Koch's growing ties with China, on the trade and investment front, are extremely important to the companies' future plans.

2. Introduction

2.1 Basic information

Koch Industries, Inc.
4111 I. 37th St. North
Wichita, KS 67220-3203
Phone: 316.828.5500
Fax: 316.828.5739
www.kochind.com

Koch Industries, Inc. is a private sector, privately-held, for-profit employer.

⁵ "Georgia-Pacific launches \$11B acquisition loan, outlines upfront fees," *GoldSheets* (Loan Pricing Corporation) January 10, 2006.

⁶ Loan Pricing Corporation, "Flint Hills Resources," DealScan, April 15, 2004.

⁷ Georgia-Pacific, op. cit.

⁸ Georgia-Pacific, op. cit.

⁹ Georgia-Pacific, op. cit.

¹⁰ Obtained from Harmon Associates website, <http://www.eharmongp.com/homeabout.html>, Spring 2006.

¹¹ Ibid.

2.2 Company history

2.2.1 The Birth of a Giant

In 1940 Fred C. Koch co-founded Wood River Oil & Refining Company, a small refinery near St. Louis. Koch, an MIT educated engineer, got his start in the oil industry when he developed a more efficient process for refining oil in 1928. Because of patent law suits and other pressure from the major oil companies of the time, Koch took his process to the Soviet Union where he spent years pushing his system. Koch quickly became disenchanted with the Soviet Union and Stalin's brand of Communism and returned home. Back in the United States Fred Koch became a staunch anti-communist and a founding member of the John Birch Society. His libertarian principles have provided the company with an ideological direction for more than sixty years. In 1947 Koch purchased the Rock Island refinery in Oklahoma, proceeding to fold the company's purchasing and gathering network into Rock Island Oil and Refining.¹²

In 1967, after Fred Koch's death, his son Charles Koch took control of the company, renaming it Koch Industries. Under Charles' leadership the company began a series of acquisitions, adding petrochemical and oil trading service operations, among other operations.¹³

In the early 1980s Charles' younger brothers Frederick and William made a power play attempting to take control of the company. Charles, the oldest Koch brother and president of the company, and his younger brother David were able to fight off the takeover attempt, firing William and buying out the two brothers for just over \$1 billion dollars following a law suit in 1983. After the deal was closed, Frederick and William claimed that they had been shortchanged in the deal and the matter stayed in court all the way until 1988 when the US Supreme Court refused to hear the brothers' appeal.¹⁴

Throughout the 1980s and 1990s the company continued its rapid expansion. In 1981 the company purchased a large oil refinery in Corpus Christi, Texas. Koch Industries expanded its pipeline system, buying the Bigheart Pipe Line in Oklahoma in 1986 and two more systems from Santa Fe Southern Pacific in 1988. In 1991 the company bought Ashland Oil subsidiary Scurlock Permian's marine terminal, pipelines, and gathering system. The next year Koch Industries bought United Gas Pipe Line, extending the company's pipeline system from Texas to Florida. In 1997, in an effort to strengthen the company's engineering services capacity, Koch bought Glitsch International from engineering giant Foster Wheeler. That same year Koch also acquired natural gas processor and transporter, USX-Delhi Group.¹⁵

In 1998 Koch took a major step outside the oil industry with the purchase of Purina Mills, the largest producer of animal feed in the United States. Through 1998 and 1999, low livestock prices forced Koch to lay off several hundred employees and sell its feedlots, and in 1999 Purina Mills declared bankruptcy. Later that same year, Koch took another, more successful stab at diversifying their holdings when it formed a joint venture with the Saba family forming KoSa,

¹² Obtained from the company website, www.kochind.com, accessed May 14, 2006.

¹³ ibid

¹⁴ Hoover's Online, "Koch Industries." www.hoovers.com accessed May 14, 2006.

¹⁵ www.kochind.com

which purchased Hoechst's Trevira polyester unit. Then, in 2004 the company acquired synthetic fabric producer INVISTA from Dupont and merged it with KoSa, taking on the INVISTA brand name.¹⁶

Today, Koch Industries employs 80,000 workers in sixty countries in industries which include trading, petroleum, chemicals, energy, fibers, intermediates and polymers, minerals, fertilizers, chemical technology equipment, pulp and paper, ranching, and securities and finance.¹⁷

2.2 Georgia-Pacific Buy Out

In 2004 Koch entered the pulp industry, purchasing two of Georgia-Pacific's non-integrated pulp mills for \$610 million. Then in 2005 talks of a buyout began. In September of that year, Koch announced that it would pay GP's shareholders \$48 per share to close the deal—a 27 percent premium over the highest share price in the last five years, totaling \$13.2 billion. In addition, Koch agreed to assume \$7.8 billion in GP debt, bringing the total cost of the transaction up to \$21 billion.¹⁸ The deal constituted the largest acquisition in Koch's history and put the company in significant debt. Citigroup provided the initial loan of \$11 billion to make the deal happen, and Koch contributed \$2.2 billion in cash up front.¹⁹

The buyout has faced some resistance from two stock holders and some bond holders who filed a class-action law suit against GP's board and Goldman Sachs, who provided advice to the company during the deal. The suit argues that Goldman Sachs, who has done business with Koch Industries in the past, has a conflict of interest and that the deal was unfair to shareholders.²⁰ Resistance from bond holders in a takeover deal is not entirely unexpected. While shareholders often relish the idea of a takeover because of the premium on stock prices that is associated with such a transaction, huge increases in new debt cuts the price of a company's bonds.²¹

Observers noted that Koch's investment in the highly extractive logging industry makes perfect sense, as their political influence gives the company a comparative advantage in securing rights to clear cut for lumber. Scott Silver, executive director of the environmental group Wild Wilderness, pointed out that Koch's purchase of GP "completes the circle...the ideologues running the land management agencies are the product of the think tanks created by, and funded by, the Koch family...Those ideologues are now in a position to permit Koch's newest acquisition, Georgia-Pacific, to further rape and pillage the public's lands."²²

¹⁶ Hoover's Company History, Accessed April 3, 2006.

¹⁷ www.kochind.com/industry/default.asp

¹⁸ Securities and Exchange Commission documents on sale of Georgia-Pacific to Koch Industries: Exhibit (a)(1)(A), November 17, 2005; Schedule 14D-9, ; Schedule TO; Form 8-K Current Reports, December 20, 2005, December 20, 2005, and December 23, 2005.

¹⁹ "Koch to reinvest in G-P manufacturing," www.paperloop.com, accessed January 2006

²⁰ Ibid

²¹ "Control Freaks," The Economist, March 18, 2006.

²² Berkowitz, Bill, "The powerful Koch boys from Kansas." <http://www.workingforchange.com/article.cfm> accessed February 9, 2006.

2.3 Growth Structure

Koch's "Market-Based Management" system has established a series of subsidiaries and mini-economies strewn out in a complex web to generate profit. This unique blend of libertarian politics with a seemingly non-hierarchical business practice sets up each new project as an independent subsidiary. Free market ideals aside, however, it is clear that even with this complex network of subsidiaries, control still rests strongly at the top of the company. Because of the company's private ownership, Koch management insists, the company is able to concentrate on long-term growth by investing 90 percent of its profit back into its subsidiaries.

3. Operations

3.1 Paper Operations

3.1.1 Overview

Since the vast majority of Koch Industries' paper products operations are found in its recent acquisition, Georgia-Pacific, this segment of the report will focus on Georgia-Pacific. Koch's investment in this company is interesting because they chose to take over a company in what many consider a "faltering industry."²³ Georgia-Pacific, as well as its competitors such as International Paper and Kimberly Clark, have all recently been involved in restructuring programs that have involved divestitures and significant downsizing. International Paper, for example, has divested 6 million acres of logging property,²⁴ as well as divested five business units.²⁵

Judging from this analysis, it seems that Koch is taking something of a risk investing in Georgia-Pacific. It is also clear that there is a significant probability that Koch may resell Georgia-Pacific, or sell off its components piece by piece. As was mentioned earlier in this report, there is no current indication that this is imminent, as Koch's activities with its new acquisition seem to indicate that it is trying to integrate Georgia-Pacific into its corporate structure.

Georgia-Pacific until 2005 was a for-profit, publicly-held employer. However, when it was taken over in a merger with Koch Industries in late 2005, it ceased to become a publicly-held company as Koch became the majority shareholder. Koch "purchased" Georgia-Pacific for \$21 billion, and the purchase was completed in December of 2005.²⁶ As a result of this merger, Koch Industries became the largest privately-held employer and company in the United States. However, Georgia-Pacific's headquarters remain based at

Georgia-Pacific Corporation
133 Peachtree Street, N.E.
Atlanta, Georgia 30303

²³ Irwin, Stephanie, "MeadWestvaco move shouldn't be surprising; ANALYSIS: Company has been cutting to compete for years," *Dayton Daily News*, February 19, 2006, D7.

²⁴ Lexis story

²⁵ Irwin, Stephanie, op. cit.

²⁶ Dun and Bradstreet Report, 2006.

3.1.2 Products

If you ever wandered into a public restroom or the restroom down the hall from you in your office building and ever contemplated the origins of the paper towels/toilet paper, or even perhaps the dispenser in which these items are housed, it is highly probable that the Georgia-Pacific Corporation manufactured the paper towel that you used to dry your hands, and the mechanism you used to dispense the paper towel.

Georgia-Pacific specializes in all elements of paper products and paper production. It defines its business in four segments: Consumer Products, Building Products Manufacturing, Packaging, and Bleached Pulp and Paper.²⁷ These four segments cover everything from pulping chips and lumber and processing to manufacturing particle board, plywood, and also chemicals such as formaldehyde and artificial resins.

The company's most profitable segment, Consumer Products, is the source of 42 percent of its operations and revenue. In North America, Georgia-Pacific has about 30 percent of the market share for consumer tissues, and their brand Dixie is responsible for most of this. Other principal commercial brands in this category are Quilted Northern and Angel Soft bath and facial tissues; BigFold and Signature towels; Preference, Acclaim and Envision brands of folded, hardwound roll and perforated roll towels, bath and facial tissue; Compact, HACCP Guardian, MAX 3000, enMotion (dispensers), SofPull, and Cormatic controlled usage dispensing systems for a range of towel, tissue, soap, air freshener and toilet seat cover products; Easy Nap, Essence, Impressions, MORNAP, and Preference brands of dispenser or single-service napkins; and ShopMaster, DynaMAX, TuffMate, and TaskMate wipers.²⁸

Georgia-Pacific's second most profitable segment is Building Products and Manufacturing. This broad segment runs the gamut of building products, including the chemicals used for bonding boards as well as various kinds of lumber. More specifically, their products include wood panels such as plywood, oriented strand board and industrial panels; lumber; gypsum products; and chemicals.²⁹

In light of their recent merger with Koch Industries, this segment, the chemical side in particular, may be at some risk for spinoff or divestiture by Koch. Although this might be in conflict with Koch's rather interesting espousal of in-company competition, the risk of divestiture is still there. Koch's other chemical subsidiary, INVISTA, makes many of the same chemicals that Georgia-Pacific manufactures, including some of the resins as well as substances like formaldehyde.³⁰ The possible affected plants will be listed later.

The company's third most profitable area is their packaging segment, which produces mostly cardboard and corrugated boxes for packaging. They also make plastic packaging (boxes), and

²⁷ Georgia-Pacific, op. cit.

²⁸ Georgia-Pacific, op. cit.

²⁹ Georgia-Pacific, op. cit.

³⁰ Westervelt, Robert, "Koch to Acquire Georgia-Pacific for \$21 Billion," *Chemical Week Associates*. November 23, 2005.

high graphics packaging. These boxes can be used for both shipping purposes and point of sale usage. Their main subsidiary in this division is their Color-Box company.³¹

Georgia-Pacific's bleached pulp and paper segment has become their least profitable segment, and leading up to their merger with Koch Industries they were making heavy divestitures in this part of their operations. Coincidentally (at least on paper), two of the pulp processing facilities that were divested by Georgia-Pacific in 2003 were, in fact, sold to Koch Industries. This segment produces mostly office paper, pulp, bleached board, and bleached and unbleached Kraft paper. The bleached board usually ends up in boxes for commercial food products, and the Kraft paper is for packaging bags.³²

3.1.3 Workforce

As of 2005 Georgia-Pacific employed approximately 55,000 people. About 22,000 of these employees are members of unions. The unions representing the workers are as follows: GMP, IAM, IBB, IBEW, IBT (including GCIU), ILWU, LIUNA, OPEIU, SEIU, UBC, UFCW, UMW, USW (including both former USWA and former PACE), as well as multi-union facilities.³³

| | Number of Unionized Workers | Percentage of Total |
|----------------------|---|----------------------------|
| USW | 10,849+ (54 locations) | 34.0 percent |
| USWA | 640+ (5 locations) | 2.0 percent |
| PACE | 10,209+ (49 locations) | 32.0 percent |
| IBT (including GCIU) | 4,384 (45 locations) | 13.7 percent |
| Other | 4,883+ (27 locations - IAM, UFCW, LIUNA, IBB, GMP, ILWU, UBC) | 15.3 percent |
| Multiple | 11,800+ (36 locations - GMP, IBB, LIUNA, IBT, PACE, IAM, SEIU, UFCW, USWA, IBEW, GCIU, OPEIU, UMW) | 37.0 percent |
| Total | 31,916 | 100 percent |

³¹ Georgia-Pacific, op. cit.

³² Georgia-Pacific, op. cit.

³³ Data provided by the AFL-CIO Collective Bargaining Department from its UNICORE database.

The largest unionized facilities are in the southeastern United States, with a 2,500 worker facility in Atlanta, GA; a 2,000 worker facility in Pennington, AL; and a 1,200 worker facility in Palatka, FL. The predominant organizing unions have been the former PACE and the IBT.³⁴ One identifiable worker issue seems to be health and safety. In 2002 there was a major accident concerning worker exposure to hydrogen sulfide gas at a Georgia-Pacific plant.³⁵ There are also various OSHA violations that will be addressed later on in this report, which have occurred with enough frequency to warrant concern by the union as well as a Republican-run OSHA.

A major worker concern for the past several years in Georgia-Pacific has been the increased frequency of plant closures and layoffs that have been associated with the company's restructuring prior to the takeover. In 2005 alone, Georgia-Pacific laid off over 1100 workers from plants in Plattsburgh, NY; Wauna and Halsey, Oregon; and Epic, Michigan.³⁶ Workers have been laid off and plants closed from all major segments in Georgia-Pacific, with the paper and pulp mills being hit the hardest. This restructuring program may be a potential stumbling block in collective bargaining; Koch may use Georgia-Pacific's restructuring as leverage.

3.1.4 Facilities

Georgia-Pacific's facilities are spread out across the country and tend to be concentrated in the southeast, including Georgia, Florida, and Mississippi. Its largest facilities are in Atlanta, GA, with 8,500 workers, Green Bay, WI, with 3,000 workers, and another in Atlanta, GA, with 2,500 workers.³⁷ For a complete list of facilities and locations, consult the appendix, section 9.1.1.2. Georgia-Pacific's last acquisition before merging with Koch Industries was of the Fort James Company.³⁸ However, aside from this acquisition there were no other gains in property by this company. Most of the change in ownership has been to divest, again mostly in the pulp and paper segment.

There have been some plant closings, as Georgia-Pacific was restructuring even before Koch took over in 2005. Starting in 2003, Georgia-Pacific began to close plants across all of its various segments due to what they called "excess capacity." Several plants that produced products for its Dixie brand were closed, as well as plants that created building supplies such as particle board, as well as some chemical plants, especially ones that created urea formaldehyde resins. Increased operating costs were cited as being the major reasons.³⁹

More recently plants in Bangor, Maine and Green Bay, Wisconsin have closed due to this restructuring process, and the company is planning to sell a hardwood plywood plant in Savannah, GA.⁴⁰ Although Georgia-Pacific's significant global presence would suggest that all

³⁴ Data provided by the AFL-CIO Collective Bargaining Department from its UNICORE database.

³⁵ http://www.csb.gov/completed_investigations/docs/CSB_GeorgiaPacificFINAL.pdf, accessed Spring 2006.

³⁶ Degross, Rene, "Georgia-Pacific to cut 1100 jobs." *Atlanta Journal Constitution*. October 5, 2005, 1C.

³⁷ Data provided by the AFL-CIO Collective Bargaining Department from its UNICORE database.

³⁸ Zaporta, Maria, "Atlanta loses corporate leader; Subsidiary status takes some of the shine off Fortune 500 company known for community efforts." *Atlanta Journal Constitution*. November 14, 2005, 6A.

³⁹ Williams, Charles, "Plant closure leaves town in limbo," *The (Charleston) Post and Courier*, June 16, 2003, 17E.

⁴⁰ Obtained from <http://galenet.galegroup.com/servlet/BCRC> accessed on (BCRC-atlanta-5-6-06).

of this work is being outsourced or moving overseas, the nature of the restructuring, as well as the intent (downsizing), point to outsourcing as not being the major cause. Indeed, industry analysts have shown that it is not profitable for paper companies to ship raw materials overseas to be processed in more high tech, cheaper facilities and then shipped back. The cost incurred would be too great.⁴¹ The plants that have been closing are the older plants that would cost too much to upgrade, which is a reflection of this trend in Georgia-Pacific to upgrade machinery and production to cut costs.⁴²

3.1.5 Raw Materials/Suppliers

Georgia-Pacific depends mostly on lumber for its raw materials. The majority of these purchases are made from independent contractors and suppliers, and these are mainly based in the southeast United States. As a rule, the company is careful not to rely too heavily on one supplier for all its needs, and the largest percentage supplied is 6 percent by Plum Creek Timber Company. However, due to their reliance on natural resources, Georgia-Pacific's production is affected by natural disasters like forest fires and soil erosion. In their last filing with the SEC in 2005, Georgia-Pacific outlined a limited supply of timber being available to them due to heavy rainfall in the southeast region of the United States.

Georgia-Pacific also uses recycled fiber and pulp to make its products. Most of this is obtained through its subsidiary, Harmon Associates. Harmon, which was acquired in 2000 as part of the Fort James Corporation,⁴³ acquires recycled pulp mostly through a bidding process. A global subsidiary, Harmon caters to markets in over 20 different countries, and even created a joint venture called Water Lily with the Chinese company PACCESS to open the Chinese market to them.⁴⁴ This auction-based system, according to Harmon, "allows suppliers and buyers to connect at a fair, market-based price."⁴⁵ This bidding process undoubtedly facilitates supplying recycled fiber and pulp from overseas, and Harmon's aggressive forays into Mexico and China seem to underscore "facilitation."

3.1.6 Customers and Clients

Georgia-Pacific's main customer base is comprised of major mass retailers, warehouse club stores and supermarket chains in both North America and Europe. They are significant customers across one or more of Georgia-Pacific's operating segments. They include Wal-Mart Stores Inc., Costco Wholesale Corp., Sam's Choice Wholesale, Carrefour SA, The Home Depot, Inc., Lothey's Companies Inc., Royal Ahold N.V., Target Corp., Sysco Corp., Kroger Co., Unisource, US Foodservice and Staples Inc.⁴⁶

The company freely admits, however, that they face strong competition for contracts with these companies. Although they don't receive more than 10 percent of their business from each of their

⁴¹ Trotter, Bill, "GP's mill's future analyzed," *Bangor Daily News*, March 21, 2006, A1.

⁴² Williams, Charles, "Plant closure leaves town in limbo," *The (Charleston) Post and Courier*, June 16, 2003, 17E.

⁴³ Dun and Bradstreet Report 2006.

⁴⁴ Obtained from Harmon Associates website, <http://www.eharmongp.com/homeabout.html>, Spring 2006.

⁴⁵ Ibid.

⁴⁶ Georgia-Pacific, op. cit.

customers, they are careful to note that any loss of business from any of these suppliers may result in serious fiscal difficulties for the company.⁴⁷ Although Wal-Mart may not be the best pressure point, Georgia-Pacific's major consumer brands customers may be a point of influence if they can be leveraged in the right way. In their 2005 financial statements, Georgia-Pacific noted that 23 percent of their business came from companies such as the ones mentioned above.⁴⁸

3.2 Petroleum Operations

3.2.1 Overview

The petrochemical industry has been a focus of Koch Industries since 1940.⁴⁹ Several Koch subsidiaries are involved, although the petrochemical backbone is Flint Hills Resources, based in Wichita, Kansas. Flint Hills operates two central refineries, in Corpus Christi, Texas and Pine Bend, Minnesota. It also runs a refinery in North Pole, Alaska, and has a multitude of satellite offices. Flint Hills Resources named its former-EVP Brad Razzok as its new president and chief executive in early 2006.⁵⁰ Another subsidiary, Koch Supply and Trading, deals more in the logistical side, trading in both crude oil and refined petroleum products, in addition to metals, chemicals, and other areas. Lastly, in the pipeline field, Koch uses the Koch Pipeline Company to operate thousands of miles of pipelines throughout the country, and also through the Koch Capital Investments Company, which is an investor in Colonial Pipeline Company, operator of the largest-volume refined products pipeline in the world. (section 9.1.1.3 for Koch Industry subsidiaries).

Overall, the petrochemical field is continually expanding. All the refinery sectors in the United States are in the process of expanding, either in terms of production capacity or distributive capacity.

3.2.2 Products

Flint Hills Resources is Koch's key center of petrochemical production, refining base oils, fuels, and other petrochemical-related products. On the distribution side, it markets gasoline, jet fuel, diesel, heating oil, and other fuels. Blue Planet® "environmentally friendly" gasoline is produced by FHR, as well as Arctic Diesel® gasoline. FHR also owns pipelines, some operated by Koch Pipeline Company. It also owns 50 percent of base oil producing Excel Paralubes.⁵¹ From its plant in Corpus Christi, it produces chemical intermediates to be used in the production of polyester resins, and automotive, agricultural, and consumer products. Lastly, it produces up to 4 billion pounds per year of commodity chemicals.⁵²

⁴⁷ Georgia-Pacific, op. cit.

⁴⁸ Georgia-Pacific, op. cit.

⁴⁹ Obtained from Koch Industries website <http://www.kochind.com/industry/petroleum.asp>, accessed Spring 2006.

⁵⁰ Obtained from <http://galenet.galegroup.com/servlet/BCRC>, accessed on (BCRC-oil-1-9-06).

⁵¹ Obtained from Koch Industries website <http://www.kochind.com/newsroom/>, accessed April, 2006

⁵² Obtained from Koch Industries website <http://www.kochind.com/industry/petroleum.asp>, accessed April, 2006.

Koch Industries is also invested in the pipeline industry, owning some 4,000 miles of pipeline within the United States under its Koch Pipeline Company subsidiary. Operating in conjunction with Flint Hills Resources and Koch Supply and Trading, it moves oil from terminals to refineries in Flint Hills areas of operation in Minnesota and Texas through the South Texas Pipeline (Corpus Christi), Wood River Pipeline (St Louis to Minnesota), and the Minnesota Pipeline (common-carrier pipeline, Minnesota area). Moving oil from refineries to terminals for distribution, it uses the Wisconsin Pipeline (from Minnesota refineries to distribution terminals in Wisconsin), MSP Airport Line (jet fuel to the Minneapolis/ St Paul airport), Texas Pipeline System (Corpus Christi to San Antonio, Austin, Waco, and Dallas/ Ft Worth), and the DFW Airport Line, which delivers jet fuel from a Ft Worth terminal to the Dallas/ Ft Worth airport.

Lastly, KPC also operates pipelines within the Corpus Christi facility, operates Koch Supply and Trading's Rotterdam refinery in the Netherlands, and runs a propane distribution pipeline in Wisconsin and Minnesota. Proposed is the MinnCan Project, an expansion of the Minnesota Pipeline System.

Through a subsidiary, Koch Alaska Pipeline Company, Koch Pipeline Company owns a 3 percent interest in the Trans Alaska Pipeline System.

In addition to refining and transportation, a large part of Koch Industries focuses on marketing petrochemical products. This is done through Koch Supply and Trading, LLC, which works in close juxtaposition with Flint Hills Resources, often trading for crude oil to be used by FHR, or marketing its finished product. Although this study focuses on their petrochemical side, KS+T also provides global trading and risk management in natural gas, liquid gas, steel, industrial and precious metals, chemicals and more. It also provides logistical and technical management services, as well as market research, derivative transactions, and price hedging in terms of risk management.⁵³

3.2.3 Workforce

Of Koch Industries' 80,000 employees, approximately 4,000 are involved in petrochemicals, with over 3,000 in Flint Hills Resources, and approximately 350 in each of Koch Pipelines and Koch Supply and Trading. (See section 9.1.1 Facilities Listing, with employee numbers.)

There is extremely limited union membership at Koch; the unions representing petrochemical and other Koch industries are IBT (including GCIU), UW, CWA, and USW (including the former USWA and former PACE).⁵⁴

The largest unionized facilities are the 2,000 worker plant in Wichita, KS, organized by the CWA and IBT; and the 775 worker Kocell LLC plant in Brunswick, GA, organized by USW (formerly organized by PACE). The largest organizers appear to be the USW and the IBT. (See section 9.1.1.1 Koch Industries (Non Georgia-Pacific) UNICORE.)

⁵³

Obtained from Koch Industries website <http://www.kochind.com/newsroom/fact> accessed April

2006.

⁵⁴

Data provided by the AFL-CIO Collective Bargaining Department from its UNICORE database.

| | Number of Unionized Workers | Percentage of Total |
|----------------------|------------------------------------|----------------------------|
| USW | 1,332 (5 locations) | 36.5 percent |
| USWA | 15 (1 location) | 0.4 percent |
| PACE | 1,317 (4 locations) | 36.1 percent |
| IBT (including GCIU) | 271 (4 locations) | 7.4 percent |
| Other | (50+) (2 locations – ORG, UW) | 1.4 percent |
| Multiple | 2,000 (1 location – CWA, IBT) | 54.7 percent |
| Total | 3,653 | 100 percent |

Although there are no readily apparent worker issues, the company's environmental problems have led to many indictments, including the 2000 ninety-seven-count indictment after the cover-up of a Benzene leak from the Corpus Christi refinery. Koch Industries reportedly requires employees themselves to pay for fines related to environmental infractions. Although in the plea bargain for the Corpus Christi case the company and the four employees related were not charged, there may be some worker issues regarding environmental concerns.⁵⁵

On a blog discussing Koch as an employer, some comments were "managers are inept, but vicious in terms of firing employees on a whim," "very high turnover, emails are searched," "market-based management doesn't work," "overly-tight security; employees treated like cattle," "low compensation."⁵⁶

3.2.4 Facilities

The main refining locations are in Corpus Christi, Texas, and Pine Bends, Minnesota. Surrounding both of those refineries is a number of lesser facilities dedicated to the operations and distribution relating to those two sites.

The Texas facility produces gasoline, diesel, jet fuel, and other petroleum products, with up to 300,000 barrels of oil refined daily.⁵⁷ It also produces 4 billion pounds per year of commodity chemicals (paraxylene, cumene, benzene, toluene, etc), to be marketed from the Wichita, KS and

⁵⁵ <http://www.publicintegrity.org/oil/report.aspx>, accessed April 2006.

⁵⁶ Obtained from the website VAULT, http://vault.com/community/mb/mb_main.jsp, accessed May 2006. (vault-discussion-employers)

⁵⁷ <http://www.fhrrfuels.com/refineries/refineries.asp>, accessed April 2006.

Singapore offices.⁵⁸ The Minnesota refinery also produces gasoline, diesel, and jet fuel, as well as asphalt products. It refines up to 290,000 barrels of crude oil per day, meeting approximately 60 percent of the energy and fuel needs of WI and MN. 700 workers are employed full-time and 200 additional jobs are contracted out.⁵⁹

Additionally, the company operates a refinery in North Pole, Alaska, which is capable of refining 220,000 barrels of oil per day. It produces gasoline, diesel, jet fuel, heating oil, and asphalt, for both local markets and international distribution. Flint Hills also has two terminals in Alaska, in Fairbanks and Anchorage. The Anchorage terminal can store 700,000 barrels, and has a pipeline to the Port of Anchorage to facilitate bulk fuel transfers. Overall, there are about 175 Flint Hills employees in Alaska.⁶⁰

In Canada, Flint Hills operates a crude oil terminal in Hardisty, Alberta that supplies the Pine Bend facility. The company's Canadian headquarters are in Calgary, Alberta.

In Rotterdam, the Netherlands, a Koch Supply and Trading subsidiary, Koch HC Partnership B.V., operates a refinery that produces jet fuel, gas oil, and residential fuels. It is currently expanding its refining capacity to 80,000 barrels per day, after which it will mostly process crude oil instead of condensates. This facility operates in conjunction with the London Supply and Trading office.

Several of Koch Supply and Trading's facilities are located near the refineries, and in part work to distribute those refined products. In the Houston, Texas office, the focus is on distribution for Flint Hills' Texas refineries, as well as regional and global trade in crude oil and other fuels. The traders work closely with traders in Flint Hills for effective distribution, and the primary trading partners here are in North and South America. In Wichita, Kansas, the office operates to serve the Pine Bend refinery, and it is also the central Supply and Trading hub from which other branches operate.

In St. James, Louisiana, Supply and Trading also owns a terminal that can store three million barrels of crude oil. It also handles liquid nitrogen and feedstock. This facility is operated by the Koch Pipelines Company, and it was unaffected by the hurricane.

In London, England the office trades in crude oil, refined products, feedstock, hydrocarbons, steel and other metals, with the feedstock coming from the KS+T Rotterdam refinery. It also provides hedging services for airline and utility companies. This office primarily deals with Europe, but also Africa, the remains of the Soviet Union, and the Middle East.

Koch Supply and Trading also has offices in Manhattan, NY, where it trades primarily in energy derivatives and precious and industrial metals; in Singapore, where it trades in crude oil, petroleum products, chemicals, and precious and industrial metals primarily in Asia and

⁵⁸ <http://www.kochind.com/industry/petroleum.asp>, accessed April 2006.

⁵⁹ <http://www.fhrfuels.com/refineries/refineries.asp> accessed April 2006.

⁶⁰ Obtained from company website <http://www.fhr.com/newsroom/fact.aspx>, accessed April 2006.

Australia; in Mumbai, India, where trades in crude oil and refined petroleum products with mostly state-owned companies in India; and in Moscow, Russia, trading in crude oil, refined petroleum products, and other commodities. A Russian subsidiary, Koch Risk Management Services, is listed on the St. Petersburg Currency Exchange.

Most development is happening within the United States, primarily in the Texas region. In the Waco, Texas terminal, storage capacity is being expanded by 40 percent in 2006 (providing an array of fuels, including low sulfur gasoline and diesel, for retail customers who provide fuel to Central Texas communities such as Waco, Temple, Killeen, Bryan, College Station and Corsicana, among others). Elsewhere in Texas, Flint Hills will build a jet fuel storage and distribution operation in Bastrop County that will serve the Austin-Bergstrom International Airport. Once the Bastrop setup is operating in 2006, the company says it will use its current jet fuel tanks at its East Austin terminal for additional gasoline and diesel storage, and might expand the terminal's truck-loading rack capacity. The company says it will increase the amount of gasoline and diesel it carries on its pipeline by 30,000 barrels a day to serve the Central Texas market.

In St James, Louisiana, Koch Supply and Trading is expanding the crude oil and fuel oil terminal by 1.5 million barrels in storage capacity (for a total of 5 million barrels capacity). The project is expected to be completed in 2007. The St. James terminal, with direct Mississippi River access, is connected to several key U.S. receipt and delivery points, including Capline Pipeline, which delivers more than 1 million barrels of crude per day to the Midwest. The terminal is also connected to the Louisiana Offshore Oil Port (LOOP), which handles 13 percent of all waterborne foreign crude oil imports (1.2 million barrels a day), and connects to more than 40 percent of U.S. refining capacity by pipeline.

At its Minnesota refinery, the company is increasing refining capacity by 50,000 barrels per day, and increasing pipeline to its Wisconsin market by 10,000 barrels per day. The MinnCan project will follow the existing Minnesota pipeline for the northern half, but in the south will divert so as to avoid residential and commercial areas. Terminating at the FHR refinery in Rosemount, MN, it will provide a direct connection to the Marathon Petroleum Company's St. Paul Park Refinery.

In Alaska, Koch is investing \$23 million to supply Alaska customers with low sulfur fuels. Tesoro Corp. has started a \$45 million project to construct a distillate desulfurization unit at its Kenai Refinery. Flint Hills will contribute \$15 million for that project and will receive up to 6,000 barrels daily of low sulfur gasoline and diesel.

Lastly, in Rotterdam, the Netherlands, the refinery is being expanded to a capacity of 80,000 barrels per day (up from 65,000 barrels per day). The refinery now has the capability to process either condensates or a high proportion of crude oil.

3.2.5 Raw Materials / Suppliers

At the Minnesota refinery, most of the crude oil that Flint Hills processes comes from the Canadian province of Alberta from the Canadian crude oil supply group of Flint Hills, and travels via pipeline to the refinery. The refinery can also receive crude oil from another pipeline

that runs south to Wood River, Illinois (across from St. Louis, Missouri), where it connects with other crude oil pipelines from the Gulf of Mexico (including Koch Supply and Trading's St. James terminal.) Flint Hills is able to obtain Caribbean crude oil (from Mexico and Venezuela) or from anywhere in the world through this pipeline.

Most of the pipeline operations come from Koch Pipeline Company, although Williams Energy Partners also provides pipeline connections to Supply and Trading in Corpus Christi, Texas, as well as supply services to Supply and Trading in Galena Park, Texas. Among those known, the Tyumen Oil Company (TNK) sold oil to Koch's Corpus Christi facility.⁶¹

The Kingston cogeneration plant, run by the Northland Power Income Fund, supplies steam to Koch in a power contract that runs until 2017.⁶²

In Suriname in 2000, Koch Industries' Canadian subsidiary signed a twenty-year production-sharing contract with the state-owned oil company Staatsolie Maatschappij Suriname N.V. (Staatsolie) regarding the 140,000 acre tract in the Wayomba area.⁶³

3.2.6 Customers / Clients

The Pine Bend facility supplies a majority of the jet fuel used at the Minneapolis/St. Paul International Airport. It also supplies the "earth-friendly" gasoline "Blue Planet" to the "Holiday Station Stores" (gas stations), of which there are approximately 125 stations across MN and WI. The Corpus Christi refinery produces commodity chemicals that are marketed by Koch offices in Wichita, KS and Singapore.⁶⁴ Fuels are shipped via pipeline to Dallas/Forth Worth, and along the way supply San Antonio, Austin, Waco, and Dallas. A second pipeline flows to Waco, TX. The jet fuel from this refinery supplies the Austin-Bergstrom International Airport.⁶⁵

In Alaska about 60 percent of the refined fuel goes to the aviation market. Both the airport of Anchorage and that of Fairbanks are primarily supplied by Flint Hills. A pipeline extends from the Anchorage facility to the Port of Anchorage to facilitate bulk fuel transfers to vessels docked there.⁶⁶

4. The Industry and Competitors

Koch is a highly diversified company and as such operates in a myriad of different industries, including energy and utilities; animal production; plastic and fiber manufacturing; lumber, wood production, and timber operations; paper and paper product manufacturing; and packaging and container manufacturing.⁶⁷ Certainly no firms operate in all of the same industries as Koch, but

⁶¹

http://www.norexpetroleum.com/norex_vs_alfa/facts_and_evidence/phil_murray_declaration/declaration_eng.pdf, accessed May 2006.

⁶² <http://galenet.galegroup.com/servlet/BCRC>, accessed (BCRC-finance-4-06)

⁶³ <http://minerals.usgs.gov/minerals/pubs/country/2000/9520000.pdf> (usgs-suriname) accessed Spring 2006.

⁶⁴ <http://www.kochind.com/industry/petroleum.asp>, accessed Spring 2006.

⁶⁵ <http://www.fhrfuels.com/refineries/refineries.asp>, accessed Spring 2006.

⁶⁶ <http://www.fhr.com/newsroom/fact.aspx>, accessed Spring 2006.

⁶⁷ Hoover's Online, "Koch Industries." www.hoovers.com, accessed May 14, 2006.

in almost all of the company's ventures they are embedded in highly competitive industries. For the purposes of understanding Koch, its positioning and direction, perhaps the two most important industries to understand are energy and utilities, and paper and paper product manufacturing.

4.1 Energy and Utilities

The energy industry today is among the most profitable, most widely watched markets in the world. Oil and gas are commodities traded on global markets, so prices fluctuate with global trends. Fueling the oil industry and oil prices right now are the rapid industrialization in China and huge instability in the Middle East. As China enters the industrial world, the emerging giant is driving an unprecedented rise in demand for the world's most hotly traded resource. At the same time instability in the Middle East and natural disasters around the world are choking, or at least destabilizing, supply.

With energy prices high right now, oil companies worldwide are investing more in upstream exploration and production, but these ventures will not yield an increase in supply for several years. It is for that reason that some of the world's largest oil companies are acting more conservatively through this most recent investment frenzy. Chevron Texaco and ExxonMobil are cooling down for fear of overproducing and causing oil prices to collapse. High prices and improving technologies are, however, driving production in the oil sands of Canada. There has always been a huge supply of crude oil in the region, but high prices and lower extraction costs are just now making production profitable.⁶⁸

The major players in the oil industry are the biggest companies in the world: ExxonMobil, Chevron Texaco, Royal Dutch Shell, Conoco Philips, and BP. In comparison, Koch Industries is tiny (ExxonMobil's 2005 sales were \$328 billion in comparison to Koch's \$80 billion),⁶⁹ but there are many fortunes to be made in the oil industry, and with Koch's vertically integrated system and notoriously low production costs it looks like they will be able to hold their own in the energy industry for some time to come.

4.2 Paper and Paper Product Manufacturing

The paper industry is a highly cyclical industry that is just now recovering from a long downturn that started at the turn of this century. The industry, which is highly dependent on postal rates and advertising expenditures nationwide, moves quickly in response to general economic indicators. Over the past several years, nearly every company in the industry (Georgia-Pacific included) has gone through an expensive restructuring. As companies have consolidated through a series of mergers and buyouts, mill closings have become more and more common.

⁶⁸ Obtained from Mergents Online, The North American Oil and Gas Sectors, 2003-2005, <http://www.mergentonline.com/compsearch.asp>, accessed Spring 2006.

⁶⁹ Hoover's Online. "Koch Industries." www.hoovers.com, accessed May 14, 2006.

Koch subsidiary Georgia-Pacific is a major player in the industry, ranking second in sales world wide to International Paper. It ranks comfortably above its US competitors Weyerhaeuser, Kimberly-Clark, and Boise-Cascade, which fill out the 3, 4, and 5 slots on the US list.⁷⁰

5. Financial Analysis

Financial information on Koch Industries is very scarce, since the company is privately held and goes to great lengths to keep its finances secret. The best source is Standard & Poor's, which only hints at the company's finances, along with those of its Flint Hill Resources subsidiary.⁷¹

S&P does not provide a complete analysis of the Koch Industries, Koch Resources, or Flint Hills, even though it rates their debt. Rather, it supplies only a "summary analysis" that leaves out the financial models that usually accompany its ratings. Either S&P has agreed to Koch's demands for privacy or Koch has not provided the information. In any case, this is hardly surprising, given the rating agency's dependence on the companies it rates.

As of May 19, 2006, S&P rated Koch Resources A+/Stable/A-1 and Flint Hills Resources A/Stable/A-1. These ratings are down one step from early November 2004, due to the \$21-billion Koch acquisition of Georgia-Pacific. Koch Resources went to A+ from AA+, while Flint Hills Resources went from A+ to A. S&P says the Koch rating reflects "superior credit strength that rests on the company's strong business position as a diversified concern with interests in energy, chemicals, minerals, real estate, and financial services. The ratings are based on Koch Resource's excellent profitability measures and very conservative financial policies. Diverse operations enable it to maintain very strong financial performance, smoothing the volatility of individual segments over time."

S&P rates Flint Hills separately from Koch because Koch separated Flint Hills from the rest of its operations. Nonetheless, S&P recognizes that Flint Hills remains an important source of earnings and cash flow for Koch, which still owns 100 percent of the subsidiary. S&P has a very positive assessment of Flint Hills operations. It notes that the "segment's results typically exceed industry norms."⁷²

Flint Hills Resources' credit quality is supported by profitable and cash flow-producing refinery operations, especially at the company's flagship Pine Bend plant, even in extreme downturns. The quality of the operations is based on locational advantages, complex plant configurations that provide feedstock flexibility, and efficient operations. An integrated system of crude and product pipeline assets around the refineries further enhance the credit profile by providing a stable revenue stream in downturns. Acquisitions (a half-interest in Excel Paralubes, a base lube oil facility in Louisiana, and a refinery in Alaska) have added to Flint Hills' operational strength.⁷³

⁷⁰ Ibid.

⁷¹ Standard & Poor's report in a .ZIP file included with this report's supporting documents

⁷² Todd Shipman, "Summary: Koch Resources LLC," *Standard & Poor's Ratings Direct*, March 28, 2006.

⁷³ John Thieroff, "Industry Report Card: U.S. Oil and Gas," *Standard & Poor's Ratings Direct*, January 12, 2006.

The risks at Flint Hills, according to S&P, are its dependence on the volatile oil refinery business, the concentration of its business in three plants, its lack of retail operations, and the prospect of competition.⁷⁴ S&P asserts that Flint Hills Resources receives “limited support” from Koch Industries. For example, it does not guarantee FHR's financial and counterparty obligations.⁷⁵

According to data from Loan Pricing Corporation, Flint Hills Resources had revenue of \$666.6 million in 2003. This data comes from a sheet listing the terms of the a \$510 million revolving credit line given to Flint Hills Resources by a syndicate of banks, led by Bank One, on April 14, 2004.⁷⁶ However, this seems much too low given Koch’s total revenue is estimated near \$40 billion that year, and Flint Hills Resources was and still is a significant contributor to Koch.

As for Koch Resources, the “primary subsidiary of Koch Industries,” S&P expressed some concern about the Georgia-Pacific acquisition, noting that it “represents a large commitment of financial and managerial resources. This large commitment could strain the parent's ability to maintain an absolute level of separation between and among the various affiliates.” On the other hand, S&P speaks highly of Koch. “The Koch influence and pedigree is vital to the credit quality of both rated entities.” It also notes that Koch has a very conservative financial policy and that its financial performance “fluctuates between good to very robust through all market cycles.”⁷⁷

6. Command and Control

6.1 Management

Georgia-Pacific Management⁷⁸

| | |
|---------------------------|--|
| Joseph (Joe) W. Moeller | President, CEO, and Director |
| Jim Hannan | EVP, Chief Administration Officer |
| Bill R. Caffey | EVP, Operations Excellence and Compliance, and Director |
| James E. Jim Bostic Jr. | EVP Environmental, Government Affairs, and Administrative Services |
| Danny W. Huff | EVP Finance and CFO |
| David (Dave) J. Paterson | EVP Building Products |
| Michael (Mike) C. Burandt | EVP, North American Consumer Products |
| George W. Wurtz III | EVP, President, Pulp and Paper |
| Ronald (Ronnie) L. Paul | EVP, Wood Products |

⁷⁴ Todd A. Shipman, “Summary: Flint Hills Resources LLC,” *Standard & Poor’s Ratings Direct*, March 28, 2006.

⁷⁵ Todd A. Shipman, “Research Update: Ratings on Koch Industries and Sub Are Lowered; Off Watch, Outlook Stable,” *Standard & Poor’s Ratings Direct*, December 23, 2005.

⁷⁶ Loan Pricing Corporation, “Flint Hills Resources,” DealScan, April 15, 2004.

⁷⁷ Todd Shipman, “Summary: Koch Resources LLC,” *Standard & Poor’s Ratings Direct*, March 28, 2006.

⁷⁸ Hoover’s Online. “Koch Industries.” www.hoovers.com, accessed May 15, 2006.

| | |
|--------------------|--|
| Charles G. Koch | Chairman, CEO |
| David H. Koch | EVP, Director |
| Jeff Gentry | EVP, Director, President, Koch Mineral Services, LLC |
| David L. Robertson | President, Director, COO |
| Ron Vaupel | VP, Business Development |
| Rich Fink | EVP, Director |
| John C. Pittenger | SVP Corporate Strategy |
| Steve Feilmeier | CFO and Director |
| Chris Wilkins | Director of Corporate Compliance |
| Dale Gibbens | VP, Human Resources |
| Richard Dinkel | Controller |
| Patti Parker | Communication Coordinator and Public Affairs |
| Marsha Seekens | VP, Sales and Marketing |
| David May | Treasurer |
| Mark Holden | General Council |

6.1.1 Shakeup in Management after Georgia-Pacific Takeover

Immediately following Koch's purchase of paper giant Georgia-Pacific, several top managers moved up the command chain in Koch or across to top spots in GP. The level of the executives involved in the shift reflects Koch's interest in Georgia-Pacific and its strategic importance to the company. According to a company press release, more than a dozen Koch employees are moving over to Georgia-Pacific.

Joe Moeller, former President and COO of Koch, was moved to President and CEO of Georgia-Pacific. Moeller was replaced by Dave Robinson as President and COO of Koch. Koch executive vice president for operations, Bill Caffey, left his spot at Koch and on its Board to become executive vice president at Georgia-Pacific. Caffey also took a seat on GP's Board. At Koch, Caffey was replaced by Jim Mahoney, who was previously the executive vice president of operations for Flint Hill Resources.

Before the buyout, Mark Holden and Tye Darland held twin positions as co-general counsel for the company. Following the acquisition, Darland was named GP's general counsel and Holden was named senior vice president and general counsel at Koch.⁸⁰

On the Georgia-Pacific side, Moeller brought an entourage of managers from Koch and its subsidiaries to help himself, Caffey, and Darland in managing the paper giant. Jim Hannan left his position as president of INVISTA Intermediates to become executive vice president and chief

⁷⁹ Hoover's Online. "Koch Industries." www.hoovers.com, accessed May 14, 2005.

⁸⁰ Koch Industries Press Release: "Koch Industries Announces New Leaders; Georgia-Pacific acquisition results in promotions for key employees." January 3, 2006.

administrative officer at GP. Julie Brehm and Philip Ellender also left INVISTA for slots as senior vice president at GP; and Mark Leutters and David Park also left spots with the parent company to come on board as senior vice presidents. In all, nine of the company's fourteen executive officers came from Koch companies; four were from INVISTA. Of the five GP holdovers, four—Mike Burandt, Steve Klinger, Dave Paterson, and Bill Shultz—are senior business unit leaders and one, Tyler Woolson, is the company's Chief Financial Officer.⁸¹

It seems like major house cleaning at Georgia-Pacific stopped with the company's top officers. Although the business units were restructured as of January 6, 2006, all of the business unit leaders are longtime GP employees, as are virtually all of the company's business presidents and other key officers.⁸²

6.1.1.1 Charles Koch

Charles Koch was born on November 1, 1935 in Wichita, Kansas, son of Fred Koch, MIT educated engineer, oil industry entrepreneur and conservative political activist (Fred Koch was a founding member of the anti-communist John Birch Society). Charles followed in his father's footsteps, studying engineering at MIT where he earned his bachelors degree in 1957 and then two master's degrees, one in mechanical (nuclear) engineering in 1958 and the other in chemical engineering in 1959.⁸³

After MIT Charles worked for two years as an engineer for Arthur D. Little, Inc. before going to work as a vice president at his father's Koch Engineering Company, Inc. in 1961. When his father died in 1967, Charles took control of Koch Industries and has been at the head of the family company ever since.⁸⁴

Today, Charles Koch is Chairman and CEO of Koch Industries, Inc., and he sits on the board of the company's largest subsidiaries, Georgia-Pacific, INVISTA, and Entergy-Koch.

Charles is a notoriously intense businessman. Well known for his twelve-plus-hour days in the office followed by hours of work at home, he proposed to his wife, Liz, over the phone. *Fortune* magazine reports "she could hear him flipping his calendar to find a time for the wedding."⁸⁵ And he demands the same from his employees; executives at Koch Industries are expected to work on Saturday mornings, and he routinely schedules meetings that stretch into Saturday evening. Koch is also known for being an intense and aggressive negotiator. One lawyer who had worked with Charles was quoted saying "in a fifty-fifty deal, he keeps the hyphen."⁸⁶ Charles Koch's approach to building the company has been a mix of free market principles and fierce competition with the company encouraging each department and business segment to act as an individual profit-maximizing entity. The approach, which he has termed "Market-Based

⁸¹ Obtained from Georgia-Pacific website, <http://www.gp.com/center/news/news.asp?NewsID=4618>, Spring 2006.

⁸² <http://www.gp.com/center/newsroom/executives.html>, Spring 2006.

⁸³ http://www.kochind.com/newsroom/bio_detail.asp?ID=1, Spring 2006.

⁸⁴ Ibid.

⁸⁵ O'Reilly, Brian, "The Curse on the Koch Brothers." *Fortune* Magazine, February 17, 1997, obtained from http://money.cnn.com/magazines/fortune/fortune_archive/1997/02/17/222188/index.htm, Spring 2006.

⁸⁶ Ibid.

Management,” is something that Koch has written and lectured extensively on, pursuing it almost fanatically.

At one point Koch pushed his Market-Based Management so far that he attempted to require employees to negotiate over the price of intra-company goods and services. That scheme fell through when the cost of negotiating became prohibitively high, but Koch still requires his managers to pay market prices when trading supplies in bulk and to negotiate the share of the overhead each pays.⁸⁷

Koch’s zest for libertarian principles has led him to become a leading activist advocating free market solutions in the US and global community. In 1977 he was the co-founder of the Cato Institute, a leading libertarian think-tank based in Washington, DC. Then in 1984 Charles and his brother David commissioned future Koch Industries VP, Richard Fink, to found Citizens for a Sound Economy, a public advocacy organization touting similar free market principles and advocating privatization and deregulation, particularly in environmental issues. Koch is also Chairman of the Institute for Humane Studies, the Claude R. Lambe Foundation, the Charles G. Koch Charitable Foundation, and a board member at the Mercatus Center at George Mason University, and a major donor to the Atlas Economic Research Foundation and the Lock Institute.⁸⁸ *Fortune* Magazine reports that Charles Koch seriously considered purchasing *Time* or *Newsweek* to “proselytize for a political revolution in the U.S.”⁸⁹

6.1.1.2 David H. Koch

David H. Koch and his estranged twin, William, were born on May 3, 1940. David and William followed their father and brother Charles to MIT where they both earned bachelor’s and advanced degrees in engineering. While William stayed at MIT to study for a PhD, David went to work as a process design engineer for Amicon Corporation, then Arthur D. Little Inc., Haicon International, Inc., and then finally he joined his brother, Charles, at Koch Industries in 1970.⁹⁰

David is an Executive Vice President and member of the board of directors at Koch Industries. A chemical engineer by training, David Koch is the CEO and director of Koch Chemical Technology Group, LLC, which is a wholly-owned subsidiary of Koch Industries. The Chemical Technology Group includes Koch-Glitsch, LP (Wichita, KS); Koch Membrane Systems (Wilmington, MA); Koch Engineering Company Ltd. (Agincourt, Ontario, Canada); Koch Heat Transfer Company, LP (Houston, TX); Unifin International (London, Ontario, Canada); John Zink Company (Tulsa, OK); and OPD Inc. (Houston, TX).

In addition to his work with Koch Industries, David Koch is on 20 non-profit boards, including many libertarian and free market think tanks, most notably the Cato Institute, Citizens for a Sound Economy, the Reason Foundation, and the Aspen Institute. In addition to producing free market research, many of these organizations, namely the Earthwatch Institute and the Reason

⁸⁷ *Forbes Magazine*, “Mr. Big,” March 13, 2006.

⁸⁸ Obtained from www.exxonsecrets.org (Greenpeace and theyrule.net), accessed Spring 2006.

⁸⁹ O’Reilly, Brian, op. cit.

⁹⁰ http://www.kochind.com/newsroom/bio_detail.asp?ID=2, accessed Spring 2006.

Foundation, fund junk science denying the existence and severity of global climate change.⁹¹

In contrast to his brother Charles, whose primary interest is the family business, David takes participation in free market politics much more seriously. In 1980 David Koch was vice presidential candidate from the Libertarian Party under Ed Clark. Koch contributed \$1.6 million to his own campaign, which earned about 1 million votes. The Clark-Koch presidential bid, which ran on a platform of "low tax liberalism," remains the most successful presidential attempt in the history of the Libertarian Party.⁹² The general campaign strategy, devised by campaign manager and founding president of the Cato Institute, Ed Crane, was to appeal to affluent social liberals.

Although the platform and the campaign were hugely successful by libertarian party standards, Clark, Koch, and Crane were not without opposition within the party. Clark's and Koch's more ideological opponents accuse Koch of buying the vice presidential nomination, which appears to be just what he did. In 1979 Koch sent a memorandum to the nominating committee offering \$500,000 if he received the nomination. The Koch family's influence within the party, widely and not so affectionately termed "the Kochtopus," allegedly used its pet think tank, the Cato Institute, and millions of dollars in donations to control the party from 1976 to 1983.⁹³ Then in 1983, at the Libertarian Party national convention, the party essentially pushed out the Kochtopus, opting for a more "ideologically pure" candidate. Shortly after the 1983 convention David Koch and his Cato Institute cronies moved away from the party, choosing to concentrate more on funding research and pressuring the Republican Party.⁹⁴

Today David is very much a political activist, working extensively with and giving large sums of money to free market think tanks and NGO's. In 1999 he sat on a committee with secretary of the interior-to-be Gale Norton, advising George W. Bush on developing a conservative "environmentalism for the twenty-first century."⁹⁵ Interestingly, he all but stopped donating money through his philanthropy entity, the David H. Koch Charitable Foundation, in 2002. For the 2000 fiscal year, the Foundation distributed \$4.8 million, but in 2001 that dropped to \$2.8 million and \$13 thousand in 2002. This trend is particularly interesting because his brother's foundation, The Charles G. Koch Charitable Foundation, continued to distribute \$3 million in 2003, about the same amount as the Foundation distributed in 1999.⁹⁶ Contributions from both foundations went to a predictable mix of libertarian think tanks and fine arts foundations chronicled thoroughly in the "Outside Stakeholders" portion of this report.

In 1996 David married Julia Flesher, just six months after meeting her on a blind date. Julia, 22 years David's junior, had previously been working as a \$200-a-week assistant to the New York City fashion designer Adolfo before meeting her husband. In a 1998 *New York Times* article, David acknowledged that he had a long history of dating women in "glamour jobs." He was quoted saying, "you know, I went out with a lot of them over the years...they have the right

⁹¹ Obtained from www.exxonsecrets.org (Greenpeace and theyruule.net), accessed Spring 2006.

⁹² http://en.wikipedia.org/wiki/David_H._Koch, accessed Spring 2006.

⁹³ Paul, Mark. "Seducing the Left: The Third Party That Wants YOU." *Mother Jones*, May, 1980, obtained from <http://en.wikipedia.org/wiki/Neoliberalism>, accessed Spring 2006.

⁹⁴ <http://en.wikipedia.org/wiki/Neoliberalism>, accessed Spring 2006.

⁹⁵ <http://www.albionmonitor.com/0307a/galenorton2.html>, accessed Spring 2006.

⁹⁶ 2004 IRS 990 forms for the David H. Koch and Charles G. Koch Charitable Foundations.

social skills, savoir-faire and intelligence.” Before meeting his wife, Julia, he also dated Blaine Beard, now Blaine Trump.⁹⁷

David and Julia Koch have been prominent New York City socialites in recent years, and their extravagant parties have been covered extensively on “who’s who” blogs. In 2003 the couple sold their Fifth Avenue apartment, previously owned by Jackie Onassis-Kennedy, to move into a \$17 million, eighteen-room duplex from the Japanese Consulate. Their reason for moving: the \$10 million Fifth Avenue apartment was not big enough to throw a proper party. Before the move the couple kept a spare apartment at the U.N. Plaza for entertaining.⁹⁸

6.1.1.3 David L. Robertson

Dave Robertson is the President and Chief Operating Officer of Koch Industries. He serves on the board of Koch Industries, the Koch Chemical Technology Group, and Flint Hills Resources. Before taking the top management position with the company Robertson, a career Koch employee, spent five years as president of the company’s oil and resources industry subsidiary, Flint Hills Resources. Before taking that position, Robertson supervised the down-sizing at Purina Mills through 1999.⁹⁹

In contrast to the Koch brothers, notably little is known about Dave Robertson. Robertson is younger than most managers and has strikingly little work experience. He graduated from college in 1984, went straight to work with Koch Industries, and has worked there ever since.

Robertson’s political activity has been relatively unremarkable. According to the Center for Responsive Politics, he has given \$25,000 in political contributions over the past 3 election cycles. Twenty thousand dollars went to the Koch Industries Political Action Committee and five thousand went to individual candidates, all of whom are Republican.¹⁰⁰ In addition to his political contributions, David and his wife Kathy are listed as members of Emporia State University’s “Regents Club” for donating between \$5,000 and \$50,000 in 2004.¹⁰¹

6.1.1.4 Joseph (Joe) W. Moeller

Joe Moeller is the President and CEO of Georgia-Pacific, and he sits on the board of directors at Koch Industries and Georgia-Pacific. He also sits on the board of directors at Entergy-Koch LP, and Velocita Corp, both joint ventures with publicly-held corporations. Moeller is a lifetime Koch employee; who came to work with the company just after graduating from the University of Tulsa in 1966. Before moving to the Georgia-Pacific side, Moeller held the slot of President

⁹⁷ Yazigi, Montique P., “Non-Stop New York Glamour Girls” *The New York Times*, April 5, 1998, obtained from <http://members.aol.com/nonstopny/wedlock/meetglam.htm>, accessed Spring 2006.

⁹⁸ *New York Metro*, “People,” obtained from http://newyorkmetro.com/nymetro/news/people/columns/intelligencer/n_9428/, accessed Spring 2006.

⁹⁹ Obtained from company website, http://www.kochind.com/newsroom/bio_detail.asp?ID=4, accessed Spring 2006.

¹⁰⁰ Obtained from the The Center for Responsive Politics’ website, www.opensecrets.org, accessed Spring 2006.

¹⁰¹ Obtained from Emporia State University website, <http://www.emporia.edu/saf/news/spotlight/honorroll-2003-2004.pdf>, accessed Spring 2006.

and COO at the parent company.¹⁰² It is not clear whether the move to Georgia-Pacific is a promotion, a demotion or a lateral move, but given his status in the company it seems clear that he will have relative autonomy as the head of the paper giant.

Moeller came into the company on the petroleum side, working first in marketing for the Koch Refining Company and eventually moving up that chain to vice president in charge of the company's refining products group in 1980. Then in 1992 he became president of the Koch Petroleum group and in 1995 president of Koch Industries International. It is notable that Moeller was the one who initiated the company's initial expansions into international markets and established Koch's first operations in Canada. He became the fourth president of Koch Industries in 1999 and then stepped down to take the top spot at Georgia-Pacific, just after the takeover.¹⁰³

6.1.1.5 Richard Fink

Richard Fink is an executive vice president at Koch Industries and a member of the company's board of directors. When he officially went on the Koch payroll is not exactly clear, but it is clear that he has been closely tied to the Koch brothers since the early 1980s. An economist by training, Fink has worked extensively in researching, packaging, and promoting free market ideology. According to SourceWatch, he has long advocated that conservative grant makers invest in university programs, think tanks, and implementation groups. They write "using Friedrich Hayek's models of the production process, he shows that to influence policy, you must first develop the intellectual 'raw materials;' then develop these into policy 'products' and finally 'market' and 'distribute' them to 'consumers.'"¹⁰⁴

Fink started his academic career at Rutgers University, where he founded the Center for Market Processes. Then in 1981 he became an assistant professor of economics at George Mason University, bringing along his Center for Market Processes. The Center for Market Processes eventually became the Mercatus Center, and Fink is still a board member. In 1984 Fink became the founding president of Charles Koch's new think tank, Citizens for a Sound Economy.

Rich Fink is Charles and David Koch's pet academic. Today, in addition to his position with the company, Fink is on the board of the Progressive Policy Institute, the Institute for Humane Studies, the Mercatus Center, and the Center for Public Choice, and has also been a trustee and former president of the Charles G. Koch Foundation and the Claude R. Lambe foundation. He is also on the Board of Visitors at George Mason University.¹⁰⁵

6.2 Board of Directors

Koch Industries is run by both a traditional Board of Directors, which has seven members and oversees the general operations of the company, and a twenty-member "Discovery Board,"

¹⁰² Hoover's Online. "Koch Industries." www.hoovers.com, accessed May 14, 2006.

¹⁰³ Hoover's Online. "Koch Industries." www.hoovers.com, accessed May 14, 2006.

¹⁰⁴ Obtained from SourceWatch, http://www.sourcewatch.org/index.php?title=Rich_Fink, accessed Spring 2006.

¹⁰⁵ *ibid.*

which meets quarterly to discuss strategy.¹⁰⁶

| | |
|--------------------|---|
| Charles G. Koch | Chairman and CEO |
| David H. Koch | EVP and Director |
| Jeff Gentry | EVP and Director; President, Koch Mineral Services, LLC |
| David L. Robertson | President, COO, Director |
| E. Pierce Marshall | Director |
| Sterling Varner | Director |
| Steve Feilmeier | CFO and Director |
| Rich Fink | EVP and Director |

¹⁰⁷

6.3 Business Strategy and Growth Plan

Koch Industry's roots are in the oil industry: pipelines, refineries, and power plants. Certainly the company has always maintained diversified holdings, but these ventures were historically "extra curricular" activities. Since the mid 1990s, however, the company has shifted serious resources into other industries, making big-ticket purchases and major ventures.

The first of these came with the purchase of Purina Mills in 1998, which went bust in 2000. That same year, however, Koch entered into textiles, taking part in a joint venture to purchase Hoechst's Trevira polyester unit. This endeavor proved more profitable than the Purina Mills purchase, and in 2004 Koch proceeded to take full control of the joint venture and take over Du Pont's synthetic fibers subsidiary, INVISTA, for \$4.2 billion. (See section 2.2 Company History.) In addition to marking a shift out of the oil industry, the Financial Times noted that the INVISTA venture "gives Koch a way to diversify from largely commodity-based businesses into more 'value-added' areas."¹⁰⁸

The purchase of Georgia-Pacific is Koch's largest step outside of the oil industry. It is clear that Koch is taking this project seriously, as they have moved several of their top managers, including former President and COO Joe Moeller, over to Georgia-Pacific to keep an eye on the company.

A simplistic analysis of Koch's industrial positioning would describe Koch as an oil company that is heavily diversified into other industries. Perhaps a more accurate description of Koch is that it is in the business of making money. Each of Koch's acquisitions constitutes a move either to acquire more capacity in the company's profitable segments or to make more profit out of existing segments by purchasing more pieces of the production line.

One other major shift that has been caused by the company's purchase of Georgia-Pacific is its public profile. The Koch billionaires have worked hard to keep themselves out of the public eye, but their high-profile purchase of GP has pushed them into the spotlight. GP's status as a heavily indebted company also opens the company up to creditor scrutiny. Koch had been debt free since

¹⁰⁶ Grant, Jeremy, "The private empire of Koch Industries." *Financial Times*. January 30, 2004.

¹⁰⁷ Hoover's Online. "Koch Industries." www.hoovers.com, accessed May 14, 2006.

¹⁰⁸ Grant, Jeremy, op. cit.

1983, but the buyout put it \$11 billion in the hole, and the company acquired \$8 billion in old debt from GP.¹⁰⁹

The Kochs attribute much of the company's success to its status as a privately-held firm. Rather than pushing for quick profits to pacify shareholders, Koch is able to concentrate on long-term growth, even if it does not pay off right away. Charles Koch told the *Financial Times* "to survive and prosper long term, you have to create value, not the illusion of value." The newspaper went on to comment that "Koch's private status means it can risk some losses as it experiments...unlike publicly listed competitors that must answer quarterly to shareholders."¹¹⁰

6.3.1 Georgia-Pacific Strategy

Before the takeover, Georgia-Pacific was in the middle of a major restructuring project aimed at upgrading mills to make them more efficient and require less labor. That practice is still underway, bringing upgrades and layoffs as predicted. Industry analysts have, however, predicted that following the takeover, Koch would spin off Georgia-Pacific's consumer products. President and CEO, Joe Moeller discussed Koch's plans following the takeover in the question and answer exchange they provided to the *Atlanta Journal and Constitution*:

Q: Industry analysts think the company consumer products business will be spun off by Koch. Are any such discussions under way?

A: There are a lot of opportunities in this industry... G-P has always had a practice of continually reviewing assets for strategic fit. That practice will continue.¹¹¹

6.3.2 INVISTA Strategy

In January of 2005 INVISTA announced a global reorganization of its apparel operations. The shift brings a new focus in production, leadership, and sales in Asia, splitting the continent into two operating regions, one in China and Hong Kong and the other encompassing the rest of Asia. INVISTA Apparel president Bill Ghitis insists that shifting production to Asia is necessary for the long term profitability of the INVISTA apparel operations. In a company press release he says "with the increasing size, scope and complexity of the Asia markets, it is vital to the long-term success of our business to increase our focus and leadership in this region..."¹¹²

The announcement follows the September 2004 announcement that INVISTA would invest over \$100 million in a new production facility in Foshan, Guangdong Province of China. The project, which is expected to be completed sometime this year, will increase production capabilities in both branded (Lycra®) and commodity (Elaspan®) fibers. The relative impact of the capital improvement is huge—the Foshan facility will double the company's capacity in the region.¹¹³ Not surprisingly, the new interest in Asia has been marked by the hemorrhaging of production

¹⁰⁹ Arndt, Michael, "Koch: Very Private, and a Lot Bigger." *Business Week*, November 16, 2005

¹¹⁰ Grant, Jeremy, op. cit.

¹¹¹ "New Georgia-Pacific CEO takes in unfamiliar industry like sponge." *Atlanta Journal and Constitution*, February 23, 2006.

¹¹² http://www.invista.com/news/2005/pr_050117_globalspandex.shtml, accessed Spring 2006.

¹¹³ Ibid.

capacity in North America and Europe. Layoffs have been relatively widespread at most of the company's facilities, and in an interesting move, in January the company announced that it would be selling its production capabilities (not its factory or machines) from its Brockworth Lycra factory in the UK to Nilit, an Israeli nylon production firm.¹¹⁴

In 2005 the company also sold off its 100-branch group of subsidiaries working under the brand name The Environmentalists. Before being sold off as franchises to former branch managers, The Environmentalists had been operating in installing and maintaining commercial carpets. INVISTA spokespeople commented that the operations were spun off to allow the company to focus more on producing carpets. "We believe that these transactions will allow INVISTA to be more focused on its core businesses of providing innovative product and services through the Antron® family of brands."¹¹⁵

6.4 Stockholders

Koch brothers Charles and David are the principle owners of Koch Industries. They, with brothers William and Frederick, inherited the majority of their money from their father, Fred Koch. As noted above, Charles and David bought out William and Frederick in a hotly contested deal in the early 1980s.

Aside from activities in Libertarian politics and free market think tanks, Koch Industries is the primary interest of both Charles and David Koch. The brothers are not likely to sell off their interest in their father's business under any circumstances. When asked about ownership succession, 70 year old Charles Koch told Forbes Magazine that his only son, 28-year-old Chase is "going to be a significant stockholder someday." Forbes quoted Charles saying that shares in Koch Industries "will be offered to the public 'literally over my dead body.'"¹¹⁶

6.5 Lenders

Because of two heavily leveraged buyouts, both Koch Industries and its new subsidiary, Georgia-Pacific, are heavily indebted companies. Before the buyout, GP alone had \$7.8 billion in debt. In order to facilitate the purchase of GP, Koch received an \$11 billion loan from Citigroup. While Citigroup will remain a major player, the mammoth bank will have the opportunity sell some of its interest in Koch.

Several analysts have been watching the company in order to keep track of its credit rating, as its bonds are traded on public markets. Standard and Poor's had listed Koch's long term credit rating as AA+ before the merger but predicted that it would be downgraded because of the debt accumulated during the merger. Georgia-Pacific had been rated BB+ but is expected to fall at least one notch.¹¹⁷

¹¹⁴ "Job pledge in Invista sell-off" *The Gloucester Citizen*, January 31, 2006.

¹¹⁵ http://www.invista.com/news/2005/pr_050629_sale_thei.shtml, accessed Spring 2006.

¹¹⁶ *Forbes Magazine*. "Mr. Big," March 13, 2006

¹¹⁷ Bank Loan Report, "Koch/Georgia-Pacific Merger To Generate \$11B in Loan Facilities." *SourceMedia Inc.* Vol. 20, No. 45.

In addition to Citigroup, other banks participating in the Georgia-Pacific financing as co-underwriters included Deutsche Bank, Bank of America, and J.P. Morgan.¹¹⁸ Most of the money in the financing deal went to Georgia-Pacific, making it one of the largest obligors in the institutional (non-bank) loan market.¹¹⁹ Koch refused to guarantee GP's outstanding unsecured bonds, causing the bonds to drop precipitously before the completion of the deal. In other words, existing GP bondholders were put at greater risk through the Koch acquisition, while shareholders reaped a premium for their shares.¹²⁰ Moody's looked poorly on the deal and downgraded Georgia-Pacific debt.¹²¹ It is worth noting that the banks sold the debt mostly to other institutions, such as hedge funds and mutual funds, a relatively new phenomenon in the debt markets.¹²²

7. Outside Stakeholders

7.1 Safety and health

Like most large companies in the dangerous construction, manufacturing, oil refining, and meat processing industries, Koch's health and safety record is far from spotless. The company and its subsidiaries have hundreds of OSHA violations over the past ten years, many of them containing serious fines, logout/tagout practices, and repeat or willful violations. Amputations and deaths have occurred, although Koch's overall safety ratings are on par with others in their industries. (See section 9.3 OSHA Violations.)

7.1.1 Trends in Health and Safety Violations

In the residential and industrial construction industries, most of Koch's violations were for fall protection equipment, lack of training, and actual falls. A recent incident with Koch Homes involved a worker crushed at a private home construction site in Maryland, causing an amputation. In Texas City a worker was killed at a Koch Specialty Plant Services site due to faulty ladders and fall protection equipment. The 2004 average rate of non-fatal injuries in construction was 6.2 percent and for roofing, 7.9 percent.¹²³

For the plastics and furniture manufacturing segment, the violations were for improper protective equipment, faulty machines, and hazardous electrical wiring. The most common OSHA violations for these industries in 2005 were control of hazardous energy, chemical exposure, and

¹¹⁸ "Georgia-Pacific launches \$11B acquisition loan, outlines upfront fees," *GoldSheets* (Loan Pricing Corporation) January 10, 2006.

¹¹⁹ "Citigroup preps \$14.8B financing for Koch/Georgia-Pacific," *GoldSheets* (Loan Pricing Corporation), November 17, 2005.

¹²⁰ Christine Richard, "Holders of Corporate Bonds Seek Protection From Risk," *Wall Street Journal*, December 17, 2005; Shayna Stoyko, "Long Bond Price Moves Higher As Investors Anticipate Auction," *Wall Street Journal*, February 7, 2006.

¹²¹ "Ratings: Georgia-Pacific proposed term loans, revolver rated Ba2; corporate rating lowered to Ba3 (Moody's)," (Moody's Press Release), *Gold Sheets* (Loan Pricing Corporation), January 6, 2006.

¹²² Serena Ng, "M&A Boom Propels Surge in Leveraged Loans," *Wall Street Journal*, April 26, 2006.

¹²³ US Department of Labor. Table: Incidence Rate and Number of Nonfatal Occupational Injuries by Industry, 2004. OSHA. www.osha.gov, accessed 1 May, 2006.

faulty personal protective equipment.¹²⁴ These are the types of OSHA violations that Koch faced in the same period. Overall, the injury rates were 7.1 and 5.8 percent, respectively, in 2004.¹²⁵

For the oil/petrochemical processing plants, violations at Koch were mostly for employee exposure to harmful chemicals and spills. In 2005, the most frequent OSHA violations for the industry were in chemical exposure and hazardous energy control. Benzene and asbestos exposures, although in smaller numbers, were also reported.¹²⁶ At Koch Materials Company in Cleves, Ohio, ten workers were struck by hot asphalt at the petroleum refinery; in Rosemount Indiana at a Koch Petroleum Group plant, other workers were exposed to benzene, a highly carcinogenic gas.¹²⁷

In paper mills and processing, industry violations in 2005 involved problems with sawmills, noise exposure, control of hazardous energy/wiring, and powered trucks. This is consistent with the violations that Georgia-Pacific faced in the same period.¹²⁸ Paper manufacturing had an industry injury rate of 4.5 percent, while sawmills had an 8 percent rate in 2004.¹²⁹

In poultry and beef processing, Koch violations seemed the most egregious and include a \$65,000 amputation settlement, hefty fines for guarding exits and windows, inadequate protective equipment, and exposure to carbon monoxide gas. This is consistent with violations across the industry—many involved unsafe machinery and “guarding” of openings—although the amputations and inhumane conditions at the feed and poultry plants stand out at Koch. Industry-wide, the injury rate in beef cattle farming was 7.3 percent, in poultry processing 8.0 percent, and in animal food processing 6.3 percent for 2004.¹³⁰ (See section 9.3 OSHA Violations).

In an attempt to reduce injury rates, whether for cost reduction or for better PR, Koch has just renewed their January 2003 Strategic Partnership Program with OSHA (OSPP) to take on their health and safety problems through a “partnership” approach. As the OSHA website describes, “the OSHA Strategic Partnership Program (OSPP) moves away from traditional enforcement methods and embraces collaborative agreements” so that “OSHA serves mainly as a technical resource and facilitator” rather than an enforcer, relying on the “partners” to self-regulate their

¹²⁴ US Department of Labor. “Frequently Cited OSHA Standards by SIC Codes.” *OSHA*. <http://www.osha.gov/pls/imis/citedstandard.html>, accessed 1 May, 2006.

¹²⁵ US Department of Labor. Table: Incidence Rate and Number of Nonfatal Occupational Injuries by Industry, 2004. *OSHA*, www.osha.gov, accessed 1 May, 2006.

¹²⁶ US Department of Labor. “Frequently Cited OSHA Standards by SIC Codes.” *OSHA*. <http://www.osha.gov/pls/imis/citedstandard.html>, accessed 1 May, 2006.

¹²⁷ Benzene, used in manufacturing plastics, petroleum, and other chemicals, is a highly toxic substance and has been shown to cause cancer. According to OSHA: “With exposures from less than five years to more than 30 years, individuals have developed, and died from, leukemia. Long-term exposure may affect bone marrow and blood production. Short-term exposure to high levels of benzene can cause drowsiness, dizziness, unconsciousness, and death.” See the OSHA website: <http://www.osha.gov/SLTC/benzene/standards.html>, accessed 1 May, 2006.

¹²⁸ US Department of Labor, “Frequently Cited OSHA Standards by SIC Codes.” *OSHA*. <http://www.osha.gov/pls/imis/citedstandard.html>, accessed 1 May, 2006.

¹²⁹ US Department of Labor. Table: Incidence Rate and Number of Nonfatal Occupational Injuries by Industry, 2004. *OSHA*, www.osha.gov, accessed 1 May, 2006.

¹³⁰ US Department of Labor. Table: Incidence Rate and Number of Nonfatal Occupational Injuries by Industry, 2004. *OSHA*. www.osha.gov, accessed 1 May, 2006.

own goals and achievements. As the website makes clear, "the resulting agreement maximizes the use of non-OSHA resources to accomplish tasks such as training employees and developing site-appropriate safety and health management systems" and puts the employer in the role of establishing and maintaining a safe and healthy work environment because OSHA resources are too limited to fully accomplish these tasks on their own. Companies included in the 405 active OSPP agreements are Johnson & Johnson, the US Army, Ford, USPS, Ready Mix, and Koch Industries.¹³¹

The Koch-OSHA partnership covers over 450 employees in fourteen states and is committed to reducing workplace injuries, especially those related to ergonomics.¹³² The Koch subsidiaries that have signed on are limited to a handful of petrochemical and manufacturing firms. Participating segments of Koch are: Koch Business Holdings LLC; Aviation Hangar, Wichita, KS; Koch Carbon LLC, Chicago, IL and Corpus Christi, TX; the C. Reiss Coal Company, Green Bay, WI; Koch Mineral Services Office Complex, Wichita, KS; and Koch Nitrogen Company, Enid, OK, Beatrice, NE and Dodge City, KS.

According to the OSHA website, participation in this program has helped Koch to lower both their total case injury rates and their employee's average time away from work due to injury since joining the OSPP. Koch Executive VP Jeff Gentry remarked that "as a direct result [of the OSPP], our employees can better leverage health and safety knowledge across our companies and work toward continuous improvement. This has enhanced our knowledge systems and allowed us to develop clearer strategies for future improvements. We look forward to continuing to work together to reduce injuries." Tangible improvements include a contractor safety training course, an ergonomic awareness campaign, and enhanced working relations between Koch facilities and OSHA regional offices, as well as a focus on reducing injuries and illnesses, including ergonomic-related injuries at the participating Koch subsidiaries.¹³³ (See the appendix of Koch's 2005 EH&S Report.)

Georgia-Pacific transferred a significant amount of litigation to Koch along with its paper plants. As of September 30, 2005, the company was facing 57,400 suits for asbestos-related illnesses and had already spent \$945 million on asbestos litigation and compensation. Experts disagree on the overall impact of the suits and when these claims may dissipate. However, the companies did not hesitate to lobby against (failed) legislation in the Senate that would establish a \$140 billion trust fund for people suffering from nine levels of asbestos diseases, paid out in fixed amounts by both the companies and the insurers.¹³⁴

¹³¹ US Department of Labor. "Partnership: An OSHA Cooperative Program." *OSHA*. <http://www.osha.gov/dcsp/partnerships/index.html>, accessed 4 April, 2006.

¹³² US Department of Labor. "OSHA, Koch Industries Form Partnership." *OSHA Trade News Release*. 14 January 2003. http://www.osha.gov/pls/oshaweb/owadisp.show_document?p_table=NEWS_RELEASES&p_id=9979, accessed 4 April, 2006.

¹³³ US Department of Labor. *OSHA Trade News Release*. "OSHA, Koch Industries Renew Partnership." 24 March, 2006. accessed 1 April, 2006. http://www.osha.gov/pls/oshaweb/owadisp.show_document?p_table=NEWS_RELEASES&p_id=12100. Accessed 4 April, 2006.

¹³⁴ Peters, Andy, "Asbestos Cases Could Keep Koch Lawyers Busy," *Fulton County Daily Report*, 16 November, 2005.

7.2 Environmental

Koch is a chronic polluter and strongly denies any evidence of global warming. During the 1990s, Koch's pipelines were responsible for over 300 oil spills in six states (Alabama, Kansas, Louisiana, Missouri, Oklahoma, and Texas). More than 3 million gallons of oil was spilled. Carol Brown of the EPA fined Koch a record-breaking \$30 million in January of 2000, while also requiring the company to improve its leak-prevention programs and spend \$5 million on environmental projects.¹³⁵

In an April 2001 case, Koch Petroleum Group LP pled guilty to covering up environmental violations at Flint Hills Resources' (Koch subsidiary) oil refinery in Corpus Christi, Texas. The company had to pay \$10 million in criminal fines, plus \$10 million for local environmental improvement projects.¹³⁶

Koch claims to "...take a hands-on approach to philanthropy that furthers environmental preservation in areas where [their companies] operate." They list a litany of environmental organizations with which they have done work, presumably spending penalty money that was allotted for environmental projects.¹³⁷ While these collaborations seem to be legitimate environmental projects, some of the "environmental" organizations that Koch works with are bogus, such as the Earth Watch Institute and the Environmental Law Institute. Koch funds George Mason University's global warming denial research.

Koch is an outspoken supporter of opening up Alaska's ANWR for oil exploration and drilling. They also support developing natural gas sites in the Outer Continental Shelf, particularly in the Gulf of Mexico. The US Senate is currently considering legislation (introduced February 2006: S. 2253) that would open up more of this region for leasing to companies such as Koch.¹³⁸

As for possible green allies, it would be hard to come between Koch's money and environmental stewardship organizations like the Nature Conservancy, who want money, no matter who is paying. Wild Wilderness is an organization whose leader, Scott Silver, appeared in one or two articles; they are locally based in Oregon. Perhaps a more promising prospect might be Greenpeace, which is currently running a boycott against Kimberly-Clark, who trails GP closely in tissue products.¹³⁹

7.3 Regulatory / Legal

The Department of Justice reported in Fall, 2000, that Koch and four employees were indicted on ninety-seven counts of violating federal clean air and hazardous waste laws. The company was accused of purposefully releasing benzene fumes into the atmosphere and lying about it to Texas

¹³⁵ http://www.motherjones.com/news/special_reports/mojo_400/51_koch.html, accessed Spring 2006.

¹³⁶ "Koch's record a mixed history; new owner of G-P praised, prosecuted." *Bangor Daily News*. (Maine) November 16, 2005.

¹³⁷ www.kochehs.com, see appendix for list of organizations.

¹³⁸ <http://www.doi.gov/ocl/2006/S2253.htm>, accessed Spring 2006.

¹³⁹ www.conservatree.com/paper/PaperTypes/tissueconsumer.shtml; www.greenpeace.org

regulators. If convicted, the company could have faced as much as \$352 million in fines. After Bush took office, however, eighty-eight counts were dropped and US Attorney General Ashcroft offered the company a plea bargain. Koch admitted falsifying documents and paid a relatively small fine.¹⁴⁰

Besides having to deal with the EPA for its egregious violations in the past, Koch has cozier relationships with other agencies such as the Minerals Management Service, a part of the Department of the Interior that manages minerals and other resources. The Director of MMS, “Johnnie” Burton, recently testified before the Senate Committee on Energy and Natural Resources with respect to S. 2253 and the Outer Continental Shelf Sale Area 181. He explained his agency’s strong support for the leasing of the Sale Area 181 to increase domestic natural gas production.¹⁴¹

7.3.1 Legal

Koch has had several significant and interesting cases in recent decades:

- The Koch brothers’ family feud resulted in Freddie and Bill suing David and Charles (along with the other Koch shareholders) for deflating the price of Koch Industries during the buy-out.¹⁴²
- Bill Koch also brought a suit on behalf of American Indians and the federal government, who were cheated over the course of many transactions with Koch Industries. Koch measured the amount of oil it was drawing in such a way as to draw slightly more oil than the company paid for. Over time, this amounted to millions in stolen oil (over \$230 million according to Bill Koch). In May, 2001, Koch agreed to pay \$25 million to the federal government for its cheating.¹⁴³
- In Southwest Pet Products vs. Koch Industries et al, Southwest Pet Products sued Koch for supplying them with contaminated dog food that killed several dogs.
- Koch retirees tried to bring an ERISA suit against the company, claiming that the company violated ERISA when it cut off their benefits. The retirees lost the case (2005 WL 3157590 (M.D.N.C.)).
- Celebrity Anna Nicole Smith went to the Supreme Court in a fight over the inheritance of J. Howard Marshall, a billionaire oil tycoon invested in Koch Industries, with his son, Pierce Marshall. The case came to Koch’s attention because, if successful, it would have made public the worth of Koch’s stock.
- Grynberg v. Koch, in which Jack Grynberg attempted to bring a second suit against the company for stealing natural energy sources from the federal government. His suit was dismissed essentially because it was a duplicate. Grynberg also owns a private energy company.

¹⁴⁰ Bill Berkowitz, “Finance-U.S.: The Biggest Company You Never Heard Of,” *IPS-Inter Press Service*, January 4, 2006.

¹⁴¹ <http://www.doi.gov/ocl/2006/S2253.htm>, accessed Spring 2006.

¹⁴² 275 B.R. 5, *; 2002 U.S. Dist. LEXIS 3766; also 203 F.3d 1202

¹⁴³ <http://www.cbsnews.com/stories/2000/11/27/60II/main252545.shtml>, accessed Spring 2006.

7.4 Community

7.4.1 Georgia-Pacific Community Relations

Atlantans considered Georgia-Pacific to be a great corporate citizen because of their leaders' involvement in civic affairs, their generous donations to local charities, and their hometown pride as an Atlanta company. As the president of the Metro Atlanta Chamber of Commerce explained of Georgia-Pacific, "they have been one of the best civic leaders in Atlanta year in and year out."¹⁴⁴ In 2004 alone, Georgia-Pacific gave \$2.6 million to Atlanta nonprofits, and thirty G-P executives hold over seventy board appointments within the greater-Atlanta area. Former CEO Pete Correll was a major civic participant in Atlanta, fighting for flag change, recognition of controversial governors in a racially tense environment, and donating to many charities. As a result, there is concern among the Atlanta community that Koch Industries, which is replacing most G-P leaders with their own Market-Based Management team, will not contribute to Atlanta in the same way.

The Koch brothers have been nationally recognized for their efforts. The Boy Scouts of America gave Charles Koch the "Distinguished Citizen Award."¹⁴⁵ In Brunswick, Georgia, Mayor Bradford Brown described the company as a "good corporate citizen," and in Perry County, Michigan, the president of the Board of Supervisors says that Koch is good for their community because the company built bleachers for the Little League and funded paper mill upgrades.¹⁴⁶ In Wichita, the Koch brothers have made personal as well as corporate contributions to the community. Charles gave \$6 million to Wichita State University to refurbish their basketball arena, sponsored the primate exhibit at the local zoo, and funded the free outdoor annual orchestra concert.¹⁴⁷ In keeping with their community focus, Koch sponsored the "Capital River Relief" project that committed celebrities and politicians to taking a few hours out of their weekends to pick up trash along the Potomac River in Washington, DC. Other sponsors of this April 2004 event included Alcoa, The Army of Corps Engineers, Caterpillar, Cargill, the National Fish and Wildlife Federation, the National Park Service, Pepco, and Whole Foods.¹⁴⁸

7.4.2 Community Issues with Koch

However, the Atlantans' fears about the Koch brothers may be justified, as the libertarian family is concerned mainly with individual rights, deregulation, and privatizing public goods. According to the report *Koch's Low Profile Belies Political Power*, published by the Center for Public Integrity, "Koch's chief political influence tool is a web of interconnected, right-wing think tanks and advocacy groups funded by foundations controlled and supported by the two

¹⁴⁴ Saporta, Maria, "Georgia-Pacific Deal: Atlanta Loses Corporate Leader," *The Atlanta Journal-Constitution*. 15 November 2005, pg 6A.

¹⁴⁵ Mercatus Institute, "Charles Koch," <http://www.mercatus.org/people.php/145.html?menuid=1>, accessed 14 April, 2006.

¹⁴⁶ Trotter, Bill. *Bangor Daily News*. 16 November, 2005.

¹⁴⁷ Hirschman, Dave. "Koch watches over Wichita." *The Atlanta Journal-Constitution*. 5 November 2005, 1A.

¹⁴⁸ Environment Writers, "Koch Industries Leads 'Team up to Clean Up' Coalition of Local, National Sponsors for 2005 Capital River Relief," *Business Wire*, 22 March, 2005.

Koch brothers."¹⁴⁹ The three major foundations through which Koch has channeled over \$120,000,000 in donations since 1986 are the Charles G. Koch Foundation, the David H. Koch Charitable Foundation, and the Claude R. Lambe Charitable Foundation. Major recipients include the Cato and Locke Institutes, both libertarian organizations advocating environmental deregulation, corporate rights, and a right-wing political agenda.¹⁵⁰ (See section 9.4 Political Contributions.)

The Koch brothers' favorite beneficiary is George Mason University in Virginia, where they have donated over \$23 million since 1985.¹⁵¹ The two departments to which they direct their gifts are the Institute for Humane Studies and the Mercatus Center. The former provides named scholarships for libertarian students and encourages studies of the free market. Koch EVP Richard Fink sits on the university's Board of Visitors and is a visiting professor of economics for the school.¹⁵² On the Board of Directors at the Mercatus Center are Charles Koch and Richard Fink, as well as Edwin Meese, former US Attorney General. The Center focuses on lobbying the Office of Management and Budget (OMB), and for the 2001 review of the Clean Air Act, put forth more comments than any other group.¹⁵³ They effectively influenced Bush's review of the "New Source Review" stipulation in the Act so that factories expanding their machinery would work with the Environmental Protection Agency (EPA) for tailored deadlines for bringing the equipment up to current emissions standards.¹⁵⁴ Mercatus director Wendy Gramm, wife of Sen. Phil Gramm (R-TX), leads the research and lobbying for reassessing 44 federal regulations regarding public health and air pollution. These included standards of smog, soot, SUV and large truck emissions, tailpipe emissions, and diesel fuel, making it clear that, as the Clean Air Trust noted, "Gramm would like to pull the plug on virtually every effective air pollution cleanup measure adopted in recent years."¹⁵⁵ The Mercatus lobbying for Koch has paid off—in 2005, Koch's Flint Hills refinery was presented with the "Clean Air Award" by the EPA.¹⁵⁶ The Clean Air Trust says it best: "Koch basically rents [George Mason] University's name to give a patina of credibility to Wendy Gramm's anti-environmental agenda."¹⁵⁷

The Koch brothers also finance a range of "nonpartisan" value-driven institutions like the Aspen, Locke, and Reason Institutes. On their boards of trustees sit powerful international political figures, academics, and activists. For example, the Aspen Institute, located in Colorado, has a seemingly harmless mission to "foster enlightened leadership and open-minded dialogue... to promote nonpartisan inquiry and an appreciation for timeless values."¹⁵⁸ Leading the organization is CEO Walter Isaacson who is also Chairman of the Board for Teach for America.

¹⁴⁹ Center for Public Integrity. *Koch's Low Profile Belies Political Power*. www.cpi.org, 14 July, 2005.

¹⁵⁰ www.mediatransparency.org/funderprofile.php?funderID=9, accessed Spring 2006.

¹⁵¹ Media Transparency, "Koch Family Foundations," www.mediatransparency.org/funderprofile.php?funderID=9, accessed 4 April, 2006.

¹⁵² CPI. *Koch's Low Profile Belies Political Power*. www.cpi.org, 14 July, 2005.

¹⁵³ Clean Air Trust. "Wendy Gramm: Clean Air Villain of the Month." January 2002, obtained from <http://www.cleanairtrust.org/villain.0102.html>, accessed 11 April, 2006.

¹⁵⁴ 2001 Press Releases. "Opportunities Exist to Fix Ailing New Source Review Process." *Mercatus Center*. 8 August, 2001. <http://www.mercatus.org/article.php/128.html>, accessed 3 May, 2006.

¹⁵⁵ Clean Air Trust. Op. cit. <<http://www.cleanairtrust.org/villain.0102.html>, accessed 11 April, 2006.

¹⁵⁶ Koch Industries. *2005 Environmental Health & Safety Progress Report*. www.kochind.com, accessed Spring 2006.

¹⁵⁷ Clean Air Trust, op. cit.

¹⁵⁸ Aspen Institute. www.aspeninstitute.org, accessed 11 April, 2006

Other powerful leaders include John Riggs, the Executive Director for the Program on Energy, Environment, and the Economy who was the Assistant Acting Secretary for Policy and International Affairs at the US Department of Energy (1993-1995) and previously staffed the US House Subcommittee on Energy and Power. In keeping with the nonpartisan mission, Aspen Emeritus Trustee John Clarke is also the Senior Vice President of Exxon Corporation. While David Koch is also a trustee, so too are Madeline Albright, Prince Bandar Bin Sultan of Saudi Arabia, Her Majesty Queen Noor of Jordan, and SEIU president Andy Stern.

Another Koch brainchild is *Freedomworks*, formerly *Citizens for a Sound Economy (CSE)*, launched by Richard Fink, and David and Charles Koch in 1984. The two brothers have since donated about \$12 million.¹⁵⁹ According to a report published by the Center for Public Integrity, *Freedomworks* is the “most incestuous” of all the Koch foundations.¹⁶⁰ The co-chairman of *FreedomWorks*, Boyden Gray, was council to President Bush Sr. and to the Presidential Task Force on Regulatory Relief during the Reagan administration. In 1999, CSE sponsored an amicus brief for suspending air quality regulations that had been issued by Clinton in 1997. They also drafted a bill for Senator Bob Dole, the Comprehensive Regulatory Reform Act of 1995, which would have allowed companies being sued by the government for noncompliance to cite previous under-enforcement as a means of egress from prosecution. In application, this would mean that Koch, a company that was at the time facing suits from both the EPA and the Coast Guard for an oil spill, could cite earlier instances when other companies were not prosecuted to avoid paying damages in their current situation. Thankfully, this bill failed in the House, but the Koch brothers were not deterred from pursuing their agenda. Citizens for Responsibility and Ethics in Washington filed a complaint in 2000, alleging that CSE violated campaign funding laws by giving scripts to members for phone-banking Oregon residents about voting for Ralph Nader in hopes of dividing the liberal vote.¹⁶¹

7.4.3 Potential Allies

As a result of their libertarian spin, Koch faces opposition mostly from national environmental watchdogs and corporate monitoring groups such as Wild Wilderness, Clean Air Watch, the Center for Public Integrity, the National Committee for Responsive Philanthropy, and People for the American Way.

7.5 Political

Maintaining connections within the federal government, heavy lobbying through Koch-funded institutions, major campaign contributions, and pseudo-research groups allow the company to leverage the government on issues, mostly environmental, and to win legislation favorable to their industries. The family keeps a close circle of political luminaries: Charles and David’s cousin, Bobby Koch, while once a staffer for Democratic House Majority Leader Dick Gephardt, is also married to Doro Bush, younger sister of President George W Bush. They were married in

¹⁵⁹

Berkowitz, Bill, op. cit.

¹⁶⁰

Center for Public Integrity. Koch's Low Profile Belies Political Power. 15 July, 2004.

¹⁶¹

Ibid.

1992, with Clinton's blessing, at Camp David.¹⁶² And as the Clean Air Trust explains, "Charles Koch is a major mover and shaker in reactionary political circles...[he] doles out millions of dollars each year to reactionary groups."¹⁶³

7.5.1 Political Contributions

Both Georgia-Pacific and Koch are friends of the Republican Party and of institutions lobbying in their favor. Nationally, Georgia-Pacific endorsed a right-wing agenda and donated exclusively to the Republican Party in 2002, while two thirds of their political funds supported Republicans in 2002.¹⁶⁴

The Center for Public Integrity explains that "Koch's chief political influence tool is a web of interconnected, right-wing think tanks and advocacy groups funded by foundations controlled and supported by the two Koch brothers."¹⁶⁵ Koch has one Political Action Committee, Kochpac, which is funded by Koch employees and their families. Koch also sponsors three major 527 Committees (groups that permit unlimited donations to candidates to influence elections and are tax exempt): the Republican Governor's Association, Americans for a Republican Majority, and the Majority Leader's Fund.¹⁶⁶ Accordingly, in the 2006 election cycle, 94 percent of Koch's campaign donations went to Republicans, as did 84 percent in 2004. Second only to Exxon, Koch is the largest donor in the oil and gas industry and spends millions each year in lobbying efforts.¹⁶⁷ (See section 9.4 Political Contributions.)

7.5.2 Top Management in Politics

Koch leadership also has intimate connections to the national government. President Bush's former Deputy Director of Political Affairs Matt Schlapp is the current Executive Director of Federal Government Affairs for Koch, while former Koch in-house lobbyist Elizabeth Stolpe is now the Associate Director of the White House Council on Environmental Quality. Another former Koch executive, Alex Beehler, is involved in committees affecting Koch's industries. He works in the Pentagon as the Assistant Deputy Undersecretary of Defense for Environment, Safety and Occupational Health through the Defense Department. (See section 9.4.3 Key Leaders in Politics.)

8. Conclusion

8.1 Profit Center

With Koch's heavily diversified interests, it is impossible to attribute its profit center to just one industry. The introduction of Georgia-Pacific introduces the possibility of those related products

¹⁶² Meacham, Joan. "Hill Climbers." *Washington Monthly*. June 1993.
http://www.findarticles.com/p/articles/mi_m1316/is_n6_v25/ai_13816704/pg_2, accessed 24 April, 2006.

¹⁶³ *Clean Air Trust*, op. cit.

¹⁶⁴ Open Secrets. "Soft Money Donors for Georgia-Pacific." www.opensecrets.org, accessed 14 April, 2006.

¹⁶⁵ *Center for Public Integrity*, Koch's Low Profile Belies Political Power, 15 July, 2004.

¹⁶⁶ *Ibid.*

¹⁶⁷ Media Transparency. "Koch Family Foundations." <http://www.mediatransparency.org/kochaggregate.php>, accessed 3 May, 2006.

becoming the new profit center for the company. For Georgia-Pacific, consumer and building products together bring in nearly \$14 billion in annual net sales. There is the good chance, however, of Koch selling off at least the consumer products half of the company.

In the petrochemical division, Flint Hills Resources accounts for much of the profit, both in refining oil and in distribution (in pipelines and in the general market).

8.2 Growth plans

With major oil projects coming to term in Minnesota and Alaska, it seems clear that Koch will not be shying away from its historic roots in the oil industry. Increased capacity in Canadian oil will likely be a huge cash cow if crude prices stay high and refining technology improves substantially. This does not, however, mean that the company will be staying exclusively in oil. Koch's relatively new acquisitions in synthetic textiles and paper will be major strategic focuses as the company makes a major effort to build serious capacity in new markets.

Koch's synthetic textile subsidiary INVISTA will be following the rest of the textile industry to Asia as the company closes many of its US facilities and sells capacity in its EU facilities while investing \$100 million to double the firm's capacity in China. Similarly, big changes are happening at Georgia-Pacific. Although the company was already undergoing an extensive and expensive restructuring, Georgia-Pacific CEO Joe Moeller is sending thinly veiled hints that the Koch subsidiary will be undergoing even bigger changes, namely selling off its consumer products division.

8.3 Key decision makers

The primary decision makers at Koch industries are principle owners Charles and David Koch. The Koch brothers, who inherited half of the company from their father and purchased the other half of the company from their estranged brothers, are both on the company's top management team. Older brother Charles is the chairman of the board of directors and CEO, and younger brother David is executive vice president looking after the company's chemical operations.

Outside of the family, it is clear that the Koch brothers reward loyalty to the company. Nearly all of the company's top executives are career Koch employees. New president and COO David Robertson went to work with the company just after graduating from college, as did former President Joe Moeller, who just left the top spot on Koch's management team to run Georgia-Pacific. The company's management philosophy, "Market-Based Management," is a unique form of free market management under which each manager would theoretically have the freedom to act autonomously in seeking value for the company. While this philosophy is something that CEO Charles Koch pursues aggressively, it seems that top managers have no problem pushing their ideas down the decision making ladder.

8.4 Key relationships

The most important relationship for Koch Industries is the tie between the Koch family, the company, and the conservative party. In addition to supporting a number of right-wing and

libertarian think-tanks, including the Cato Institute, the majority of the companies' political donations go to the Republican Party. These occur both directly and through 527 Committees such as the Republican Governor's Association, Americans for a Republican Majority, and the Majority Leader's Fund.¹⁶⁸ Not only does money bring them together, but Koch Industries is also connected through family and professional ties to the Republican Party. The Koch brothers' cousin Bobby Koch, for example, is married to Doro Bush, the younger sister of President Bush. Two government workers, Elizabeth Stolpe, the Associate Director of the White House Council on Environmental Quality, and Alex Behler, the Pentagon's Assistant Deputy Undersecretary of Defense for Environment, Safety and Occupational Health, were both formerly employed by Koch. Also, Bush's former Deputy Director of Political Affairs, Matt Schlapp, now works for Koch on government relations. These political connections do pay off, such as in 2000, when the company faced \$352 million in EPA fines that were subsequently dropped to a plea bargained small fine upon George Bush's inauguration. Also, the company has better access to securing lucrative timber rights for its paper subsidiaries.

Koch's most important financial relationship is with Citigroup. Financially, the company relied on Citigroup to provide an \$11 billion dollar loan to initialize the \$21 billion buyout of Georgia-Pacific. Deutsche Bank, Bank of America, and J.P. Morgan were among those that financed the transaction as co-underwriters.¹⁶⁹ Additionally, Koch has relied on Goldman Sachs for advice during the deal, as well as in past transactions. Subsidiary Flint Hills Resources has a \$510 million revolving credit line from a syndicate of banks led by Bank One in 2004.¹⁷⁰

Koch Industries, acting on a free market model of purchasing, usually does not form long term core bonds with suppliers. Georgia-Pacific also avoids being dependent on any single provider. Thus its largest lumber supply source, Plum Creek Timber Company, represents only 6 percent of its total lumber supply. In the recycled paper sector, Georgia-Pacific obtains paper pulp from its subsidiary Harmon Associates, acquired in 2000 as part of the Fort James Corporation. The company does have several customers that are more significant, including Wal-Mart Stores Inc., Costco Wholesale Corp., Sam's Choice Wholesale, Carrefour SA, The Home Depot, Inc., Lothey's Companies Inc., Royal Ahold N.V., Target Corp., Sysco Corp., Kroger Co., Unisource, US Foodservice and Staples Inc.¹⁷¹ Although no company holds nearly a monopoly, together those businesses represent one quarter of GP's profit,¹⁷² and the loss of any one would be a large blow to the company.¹⁷³

Koch has key relationships to several other companies in various fields. Flint Hills Resources, for example, is investing \$23 million in a low-sulfur gasoline project directed by the Tesaro Corp. in Alaska. But most importantly is its growing trade with China. Paper subsidiary Harmon is a part of a joint venture called Water Lily with the Chinese company PACCESS, through which it hopes to gain great access into the country.¹⁷⁴ The fact that INVISTA is also

¹⁶⁸ Ibid.

¹⁶⁹ "Georgia-Pacific launches \$11B acquisition loan, outlines upfront fees," *GoldSheets* (Loan Pricing Corporation) January 10, 2006.

¹⁷⁰ Loan Pricing Corporation, "Flint Hills Resources," DealScan, April 15, 2004.

¹⁷¹ Georgia-Pacific, op. cit.

¹⁷² Georgia-Pacific, op. cit.

¹⁷³ Georgia-Pacific, op. cit.

¹⁷⁴ Obtained from Harmon Associates website, <http://www.eharmongp.com/homeabout.html>, Spring 2006.

investing large amounts of money in China—\$100 million in a production facility in Foshan, Guangdong Province of China for the manufacturing of (Lycra®) and commodity (Elaspan®) fibers¹⁷⁵—shows that Koch's growing ties with China, on the trade and investment front, are extremely important to the companies' future plans.