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How Canada made the Koch brothers rich

By Bruce Livesey

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The attacks were nasty.

In the winter of 2011, Karen Kleiss, a reporter with the *Edmonton Journal*, wrote a story about how Koch Industries Inc. had hired a lobbyist in Alberta. The story provided background on the Wichita, Kansas-based energy conglomerate, its presence in Alberta, and its American billionaire owners, Charles and David Koch.

Kleiss reported at the time that no one from Koch Industries addressed her questions. Nevertheless, after her story appeared, Koch Industries went on the offensive. On their website, kochfacts.com – and in vivid red type – they lashed out at Kleiss's article, claiming it was "slanted," that it "parroted partisan political rhetoric and other distortions" and that its coverage of the Koch brothers registering a lobbyist in Alberta was a "purported story." The Koch Industries representative summed up by saying:

"There is a place for opinion on the op-ed pages, on blogs, and on Twitter. It does not belong on the news pages of an objective journal."

What the paragraph-by-paragraph rebuttal did not dispute was Kleiss's assertion that Koch industries is "an American energy conglomerate owned by two powerful billionaire brothers who help fund the Tea Party and climate change denial movements in the U.S."

The attack was so strong that Lucinda Chodan, editor-in-chief of the *Journal* at the time, felt compelled to write a lengthy response to Koch defending her reporter's work. The company replied by taking further potshots at the newspaper and at Kleiss's judgment.

Around the same time, a similar scenario was playing out after Reuters ran a story entitled "Koch Brothers Positioned To Be Big Winners If Keystone XL Pipeline Is Approved," that also detailed Koch's holdings in Canada. It discussed how the Koch brothers would benefit if the Keystone XL pipeline was built.

Written by David Sassoon, a journalist who runs InsideClimate News— a Brooklyn, NY-based, Pulitzer prize-winning website that covers climate change issues— the Reuters piece eventually elicited a ferocious response from Koch's PR department. The company accused Sassoon of publishing "falsehoods" and of being an "environmental activist," and Reuters of printing "advocacy journalism."

Koch Industries even took out ads via Facebook and Google with a photo of Sassoon under the headline “David Sassoon’s Deceptions.”

Once again, a Reuters editor had to intervene with a lengthy letter to Koch defending their use of Sassoon’s reporting. These attacks went on for some months. Today, Kleiss and Sassoon refuse to discuss these events.

But at that time Koch Industries’ campaigns against the media were not unusual. Their website, KochFacts, criticized reporting in *The New York Times*, *The New Yorker*, *Mother Jones*, Forbes.com, *The Washington Post* and Bloomberg's *Markets Magazine.*

By 2011, the Koch brothers – currently the sixth richest people in the world, with US$42.3-billion apiece – were attracting attention because of their efforts at influencing the US political system, helping foster the Tea Party movement, and attacking attempts to curb climate change. They were also emerging as political kingmakers: two weeks ago, the brothers were in the news for endorsing Scott Walker, the governor of Wisconsin, as their choice for the Republican presidential nominee (Walker is well-known for his attacks on labour rights in his state).

Koch Industries, the second-largest private company in the US, has become infamous for playing hardball.

Yet the broadsides on articles linking the Koch brothers to Canada might have had another purpose: to direct prying eyes away from their company’s history in this country. After all, few people know how Canada and its oil riches have been central to creating their vast fortune.

And what a fortune it is: today, Koch Industries is a global behemoth with annual sales of US$115-billion and a presence in 60 countries and employing more than 100,000 people worldwide. It has invested US$70-billion in capital expenditures over the past 12 years. They produce a wide range of products, and not only from the 750,000 barrels of oil they process every day: fertilizers, drywall, windowpanes, carpets, Brawny paper towels, Dixie cups, chemicals, and fibre optics.

As it turns out, Koch Industries also controls anywhere from 1.1 million to as much as two million acres of Alberta’s oil sands – or the equivalent of around 4,500 square kilometers – thereby guaranteeing the company’s prosperity for decades to come. The value of their oil sands holdings is in the tens of billions of dollars.

“You can say a lot of things about the Koch brothers, you can have a lot of criticisms – but what you cannot say is that they're stupid business people,” remarks Mike Casey, campaign manager of NextGen Climate, a Virginia-based environmental group founded by American hedge fund manager Tom Steyer. “They're very smart, they play for the long-term… And that's why they're invested in tar sands to such a huge huge extent.”

Refining Canadian oil creates the Kochs' fortune

Koch was founded by Fred C. Koch, who was born in Texas in 1900. He trained as an engineer at MIT and invented a new thermal cracking process that turned crude into gasoline. Koch made a fortune in the 1930s by helping Stalinist Russia upgrade its oil fields. He eventually moved to Wichita, Kansas, and founded an engineering company that formed the basis of what would become Koch Industries.

Fred and his wife had four sons – Frederick, Charles and two twins, David and William – who would be shaped by their father's strong anti-government views. In the late 1950s, Fred was an early member of the John Birch Society, a far-right conspiracist political organization and an antecedent of the Tea Party movement. He wrote a best-selling pamphlet on the evils of communism, influenced by his time spent in the Soviet Union.

One of Fred's smartest business decisions was to purchase a one-third stake in the Pine Bend refinery in Minnesota, which had been built in 1955, and was refining 25,000 barrels of Canadian crude every day. The Kochs also began buying and selling mineral leases in the tar sands as far back as the late 1960s, according to David Sassoon.

Of Fred's four children, three would enter the family business – Charles, who was groomed to run the company, and the twins, Bill and David (the eldest, Frederick, had no interest in the company). After Fred died in 1967, Charles took over as CEO, and his first big move was to buy outright control of the Pine Bend refinery for US$30.5-million. In his 2007 book *The Science of Success,* Charles refers to the Pine Bend purchase as "one of the most significant events in the evolution of our company" and that "this acquisition brought new capabilities to Koch Industries and led to many new opportunities."

At the time of Fred's death, the company was closing in on annual sales of US$250-million and had about 650 employees. "I think you could certainly say that the Pine Bend refinery – people in the company referred to it as 'our cash cow'," relates Daniel Schulman, author of *Sons of Wichita,* a book about the Koch brothers published last year.

"And the Pine Bend refinery essentially helped to fuel its investments in all of these other (areas)… It basically pushed them into chemicals. In the 1980s they bought a facility in Corpus Christi, Texas, that is one of their major (refineries). They bought another Texas plant. My understanding is that it was the massive profits generated at Pine Bend through refining this really heavy Canadian fuel that enabled them to make these investments."

In fact, the importance of refining Canadian oil at Pine Bend was revealed due to a bitter lawsuit that tore the Koch family apart. By the early '80s, the Koch brothers had split into two warring factions, with Charles and David on one side and Bill and Frederick on the other. This divide led to Bill and Frederick selling their share in Koch Industries to their brothers for US$800-million in 1983.

But soon Bill felt he'd been ripped off in this deal – that Charles and David had deliberately undervalued the company's assets. In 1985, Bill sued them over this issue, accusing his brothers of fraud.

Key issues in the lawsuit were the value of Pine Bend and Koch's holdings in Alberta.

"The location of that refinery in the Midwest meant they had a monopoly in that market – that's why it was so valuable," says Schulman.

Court documents show that by 1982, Koch Industries as a whole was valued at US$1.5-billion and earning US$309-million in net profits (another valuation put it at between US$1.6-billion and US$2.3-billion). An expert witness hired by Bill put the value of Pine Bend alone at about US$660-million.

Another expert witness for the plaintiffs put the value of Pine Bend as high as US$1.2-billion by the summer of 1983. In court motions, Bill and Frederick claimed that "(Charles and David) hid from the selling shareholders their actions and plans to increase the capacity of the Pine Bend Refinery… and to gain access to greater volumes of low-priced Canadian crudes."

The court records suggest Pine Bend was the most valuable single asset the company owned – and its revenues came almost entirely from refining Canadian oil, which it was designed specifically to do (by 1985, the refinery was refining 152,000 barrels a day, and generating US$115-million in net profits for the company). Eighty per cent of the crude Pine Bend was refining was coming from Canada by 2010.

The lawsuit also revealed the extent of the company's oil reserves in Alberta. Notes by Bill from board meetings in the early '80s said: "Canada at this moment looks very encouraging" while Charles was saying "reserves in Canada fantastic but worth only 10 cents" – due to the low price of oil at that time.

In 1999, the court battle between the brothers finally went to trial in Kansas where the jury ruled in favour of Charles and David. By then, Pine Bend was refining 285,000 barrels a day and had turned Koch Industries into the world's number-one exporter of oil from Canada, ahead of Mobil and Amoco.

Today, Pine Bend refines around 320,000 barrels a day of primarily Canadian oil – and covers 1,000 acres with 16 kilometres of roads. Canadian sour crude travels through a network of pipelines that begin in Hardisty, Alberta, where the Kochs own an oil terminal with 670,000 barrels of capacity. The Kochs also control a 864-kilometre pipeline system that distributes its Pine Bend products to customers.

"They've made untold millions from that refinery from Canadian oil, for many decades now," says Kert Davies, executive director of the Climate Investigations Center in Washington, DC. At times it's refined as much as one quarter of the 1.3 million barrels of oil exported from Canada to the US per day.

But Pine Bend also has a troubling environmental legacy. By the late '90s, the company was being investigated by the EPA and FBI for illegally dumping millions of gallons of ammonia-laced wastewater and 600,000 gallons of fuel into the Mississippi River from the refinery.

Allegations arose that Koch had tried to hide its environmental crimes by dumping the pollutants at night and falsifying records.

Kochs developing their tar sands holdings

While the Kochs bought up leases to the oil sands, most of this land has remained untouched. This might soon change.

This winter I travelled to Fort McKay, Alberta, a hamlet of 700 citizens that hugs the Athabasca River, a half hour's drive north of Fort McMurray. It's home to the Fort McKay First Nation band.

A cluster of small, neat houses, this community is famous for being located at ground zero of the oil sands – whose manifestations are visible from the river's bank. A Syncrude refinery lies a few kilometres down the road, belching out smoke all day long. Tailings ponds of polluted water surround the community.

"Every which way there is an open pit mine or proposed mine," says Dan Stuckless, the band's environment and regulatory manager. "We are at a point where we are 70 per cent leased on the territory here."

Long ago, in order to combat the poverty plaguing the community, the band decided to strike deals with oil companies wanting to build projects on their land in order to garner some of the bounty. Fort McKay is now a prosperous community with new homes, schools and community centres. Band members also work in the oil patch.

One company currently negotiating with the band is Koch Oil Sands Operating ULC (KOSO), one of seven subsidiaries Koch operates in Canada. Run out of an obscure set of offices in a downtown Calgary tower, KOSO has submitted plans to build a 60,000 barrel per day bitumen extraction project on the band's land. Called Dunkirk, the Koch project will steam bitumen from underground, costing as much as $2.4-billion to construct. "Their staff have been transparent, really professional and really worked with the community," says Stuckless, who leads the talks with KOSO.

As oil sands projects go, the Dunkirk proposal is of medium size. But its importance lies in that it suggests a dramatic change in Koch Industries' strategy.

Historically, Koch made its fortune not in exploring and drilling for oil, but in the transportation and refining part of the business – and then converting it into other products (like jet fuel or asphalt). In contrast, Dunkirk indicates the company is planning to develop their oil sands holdings themselves.

In fact, since 2011, KOSO has applied to Alberta's energy regulator to drill dozens of exploratory wells on their land, and build at least one other in situ bitumen recovery project – called the Gemini Oil Sands Project.

If true, it might explain why the Koch brothers want the Keystone XL pipeline built, why the oil sands are a critical asset to the company's future—and why they are taking such an active role in American politics.

Kochs fund both climate denial and a political machine

The wealth generated by refining Canadian oil not only helped the Koch brothers expand their empire, but gave them cash to pursue their ideological ambitions.

Following in the footsteps of their father and his John Birch Society roots, Charles and David began setting up and financing right-wing foundations, front groups and political lobbying organizations – often called the "Kochtopus" by critics.

Today, this network consists of at least 17 different organizations, including the Cato Institute, Americans for Prosperity and the Heritage Foundation.

"We have never in all of our research uncovered a set of organizations that has funding as concentrated in a structure as complicated as the Koch network," says Robert Maguire, an investigator with the Center for Responsive Politics, a Washington, DC-based non-partisan organization that tracks political spending."Because the network is so buried under convoluted financial flows, we can't figure out exactly how much money is pouring into it."

Some of this political spending has been aimed at changing the debate on climate change by suggesting it does not pose a threat to the planet. In 2009, with the Tea Party in ascendancy, and groups like the Koch-backed Americans for Prosperity becoming a force against climate change laws, Kert Davies, Greenpeace's research director at the time, began an investigation into the Kochs' funding of scientists and groups who deny the existence of global warming. "We started to take a deeper look at the Kochs and the money was enormous," he recalls.

In a 2010 report, Greenpeace said the Kochs had spent US$25-million between 2005 and 2008 on groups that questioned the existence of global warming (compared to US$9-million by Exxon during the same time period). "With climate change, the science is the engine that pulls the policy train along," explains Davies. "And for decades now, in many different forms, the (oil) industry has attacked the science. Everybody has heard 'there's uncertainty' or 'it's not as bad as you think,' [or] 'might not be happening at all' — all different flavours of climate denial. The Kochs were funding some of the most preeminent institutions carrying on this denial campaign."

"The impacts, many scientists are saying they're happening sooner and harder than we thought they would ten, 20 years ago... The fact that we have been slowed down not only by the Kochs but by many in the fossil fuel industry funding disinformation campaigns… has cost us years, cost us decades."

Greenpeace's most recent research shows that since 1997, the Kochs have spent a total of US$79-million to groups that deny climate change science.

Some of that cash has come north to Canada – specifically to the Fraser Institute. As first revealed by the *Vancouver Observer*, tax records show that since 2007, the Fraser Institute, one of Canada's oldest conservative think tanks, has pocketed a total of US$765,000 from one of Charles Kochs' foundations.

"Multiple generations of Fraser Institute staffers and donors and board members have had links to the federal Conservative Party," says Rick Smith, executive director of the Broadbent Institute, a liberal think tank. "There's no doubt that the Fraser Institute's aggressive denial of climate change, you can see resonating in Harper government policy."

Given that the Kochs' companies generate huge quantities of greenhouse gases, this expenditure is no surprise. But it also has a direct bearing on their plans for the oil sands.

For instance, the Kochs' Dunkirk project will be using in situ technology – whereby the bitumen is steamed out of the ground. Yet Erin Flanagan, an oil sands analyst with the Pembina Institute, says "when you compare in situ drilling and open pit mining, in situ is actually 2.5 times more greenhouse-gas damaging per barrel than a barrel through mining."

And then there is the Keystone XL pipeline, which would connect the oil sands to the Gulf of Mexico. Koch Industries claims they have no financial stake in, or party to the design and construction of Keystone – even producing a YouTube video to this effect. And it's true the company has booked no capacity on the pipeline, should it ever be built.

These denials ring a little hollow to some: after all, the tar sands are the world's third largest source of oil and the Kochs control at least 1.1 million acres of it. "The Koch brothers are very interested in the Keystone XL pipeline going through," insists Mike Casey of NextGen Climate. "They'll tell you that they're not, but the reality is that they understand that it's a key piece of enabling infrastructure for tar sands development. Without a major pipeline, the tar sands do not get developed."

Indeed, the oil industry is desperate to build pipelines for two reasons: cost and capacity. "Pipelines are going to replace rail over the long term and will be a cheaper option for these (oil sands) projects," explains Sam La Bell, an oil analyst with Veritas Investment Research, a Bay Street equity research firm. "From that point of view, it will probably cost you from $8 to $12 a barrel on a pipeline, whereas you will pay up to $20 a barrel for rail. It's the cheaper option."

In fact, the financial industry has pointed to the cost difference as being critical. In a 2013 Royal Bank of Canada (RBC) report on Keystone, they said if it does not go ahead "oil sands projects slated for start-up in the 2014-16 timeframe are likely to proceed at a much slower pace or be deferred." A Goldman Sachs report the same year said if Keystone was not approved, supply to the U.S. of oil sands fuel begins to level off.

Moreover, transporting bitumen by rail has its limits. "With rail capacity, we will be at capacity by 2017 and 2018," says La Bell. "So, in other words, all of the takeaway capacity – rail and pipelines – would be used up by that point. Beyond 2017 we need longer term options to pan out" – in other words, pipelines like Keystone.

In short, Koch will be hampered in exploiting their oil sands holdings if Keystone and other pipelines are not approved. As Casey says: “They're not holding 1.1 million acres of tar sands for conservation purposes.”

Which is one reason the Kochs have perhaps invested so heavily in backing the pro-Keystone Republican Party.

In 2012, for example, Koch-affiliated organizations raised US$404-million during the US election cycle. This past US midterm, they spent US$290-million to help Republicans win control of the Senate. The Republicans’ first order of business was to introduce a bill in the Senate on Keystone, which was passed in January (Obama vetoed it).

This winter, it was revealed that the Kochs and their billionaire friends plan to spent US$889-million on the 2016 election cycle – or more than double what the Republican National Committee spent in 2012.

“I think they are doubling down on their efforts to change the balance of power in the U.S.,” says Schulman. “They are funding really their own political party.”

The *National Observer* contacted a Koch Industries spokesperson multiple times for comment on the issues raises in this article. The company did not respond.

Meanwhile, as the Koch brothers continue to make headlines over their political ambitions, the evidence suggests that behind their veil of secrecy lies a plan to continue profiting from Canada’s oil.

As Mike Casey says: “These are business people and they invest politically to advance a business agenda and financial agenda, and they're not in the tar sands because they like the look of the landscape.”