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Secret Owners of Cato Institute Surface as Oil Billionaires Move to Take Control

Koch Brothers, Worth $50 Billion, Sue Widow Over $16.00 of Nonprofit's Stock

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With the Koch brothers, it's all about control. They reign over the largest private oil company in the U.S. with estimated revenues of $100 billion. They wield power over a sprawling network of nonprofit front groups with unbridled influence over everything from the Tea Party to economics professors at publicly funded universities. Forbes lists their personal wealth as $25 billion each. They own mansions in the toniest towns in America. And last week, in a decidedly Scrooge-esque maneuver, they filed a lawsuit against a widow who lost her husband to a stroke a mere four months ago over stock she inherited in the Cato Institute worth a measly $16.00.

The lawsuit, filed in the District Court of Johnson County, Kansas (the State where Cato was incorporated and home to Charles Koch) has opened up a nasty can of worms. Unknown to the public at large, the Cato Institute, a stronghold of free market, libertarian writers and speakers, has been privately owned by a handful of men for 35 years, notwithstanding its receipt of hundreds of millions of dollars in donations — which the wealthiest 1 percent have used as tax deductions to lower their tax tab to Uncle Sam; in itself a neat maneuver to shrink government.

The can of worms is this: the Internal Revenue Service warns that charitable organizations like the Cato Institute, organized as a 501(c)(3) "must not be organized or operated for the benefit of private interests,and no part of a section 501(c)(3) organization's net earnings may inure to the benefit of any private shareholder or individual."

Unfortunately for Cato, two of their owner-shareholders, Edward (Ed) Crane, long serving President, and William Niskanen, long serving Chairman and former husband of the widow being sued, have received millions in compensation from the Institute: a total of over $1.86 million in just tax years 2008, 2009, and 2010.

Crane has served at Cato for over 35 years, Niskanen for 26 years until his death in October of 2011, suggesting their cumulative compensation would be an extremely large benefit to private shareholders, an eventuality expressly disallowed for 501(c)(3)s by the IRS. This could potentially subject Cato to significant back taxes and require donors to file amended tax returns to remove the nonqualified deductions.

The original Cato Five, who signed a “Shareholders Agreement” on January 26, 1977 were: Charles Koch, George Pearson, Roger MacBride, Murray Rothbard, and Edward Crane.

Pearson became an employee of Koch Industries; MacBride was the Presidential nominee of the Libertarian Party in 1976; Rothbard became a libertarian icon. A 1981 issue of The Libertarian Forum, a newsletter edited by Rothbard, charged Crane and Charles Koch with illegally grabbing his shares of Cato and barring him from attending future Board meetings in order to consolidate their control. The details of Cato having owners and the extent of their control over the nonprofit has not found its way into mainstream media until now.

Rothbard, who died in 1995, summed up the episode as follows: “Let each and every one of you, dear readers, consider this crucial question: How many fellow libertarians would you trust to guard your back in an ambush?... As a friend and long-time libertarian observed in reply: ‘Ambush, hell. How many libertarians would you allow in the same room with you and trust not to poison your food?’ ”

According to the current lawsuit, a revised version of the 1977 agreement was consummated in 1985 and “...the four persons owning the shares of Cato were Plaintiff Charles Koch, defendant Crane, William A. Niskanen, and George Pearson. Each owned 16 shares of Cato’s capital stock that he had purchased for $1.00 per share. Plaintiff David Koch became a shareholder of Cato in 1991 when Cato issued 16 shares of its capital stock to him...In 2008, George Pearson ceased to be a shareholder of Cato when he tendered his 16 shares of capital stock to the Corporation and the Corporation purchased the stock for the $16.00 that Pearson had originally paid for it. After Cato’s purchase of Pearson’s shares of stock, four shareholders of Cato remained: Plaintiffs Charles Koch and David Koch, Defendant Crane, and William Niskanen...” each constituting “a 25% voting interest in the Corporation.”

So for two decades, scores of Ph.D.s, student interns and research fellows have been pumping out OpEds, research papers, and burning the midnight oil to espouse the principles of freedom without knowledge that they were toiling for a corporation that was 50% owned by two oil billionaires.

The Koch brothers’ stated incentive for the lawsuit is to force Niskanen’s widow, Kathryn Washburn, to relinquish her shares to Cato, as spelled out in the Shareholders Agreement. That would leave only three shareholders, making the Koch brothers the majority shareholders and, under the Shareholders Agreement, allowing them to oust Crane and retire his shares or split his shares between themselves.

Crane issued a public statement last week calling the action a “hostile takeover.” Jason Kuznicki, a research fellow at the Cato Institute, posted a statement from an anonymous blogger that was less kind: “This is the height of irrational greed. It is greed because [Charles] Koch has had it in for Crane for years for whatever slight he felt and is doing this to feel good. It is irrational because he will destroy something he claims to value in order to seek that vengeance…Charles Koch—you suck.”

Irrational is probably not a good fit for what’s playing out. Greed and control would more aptly apply. This is a pivotal Presidential election year. Charles Koch predicted 2012 would be the “mother of all wars” to his wealthy pals at his secret fundraising confab. He’s just making good on that promise.

A Cato Senior Fellow, Jerry Taylor, shared an insider’s take with a blogging friend, Jonathan Adler, on what is motivating the Kochs. Taylor gave permission to Adler to share his statement. “The answer was given in early November of last year when David Koch, Richard Fink (he of many Koch hats), and Kevin Gentry met with Cato board chairman Bob Levy. They told Bob that they intended to use their board majority to remove Ed Crane from Cato and transform our Institute into an intellectual ammo-shop for Americans for Prosperity and other allied (presumably, Koch-controlled) organizations.” Americans for Prosperity is the Koch funded money funnel to the Tea Party.

The Cato Shareholders Agreement gives tight control to the owners, according to the document attached to the lawsuit: “…each of the undersigned [shareholders] shall vote his stock in the Corporation so long as he is a stockholder in such a way as to assure that each of the undersigned is elected to the position of a Director on the Board of Directors of the Corporation.”

Cato Board Chairman, Robert A. Levy, responded to my query as to the appropriateness of a tax subsidized organization having private owners as follows: “The key question for us is whether the persons who will elect our board are those who for 35 years have operated the Cato Institute as a non-partisan, non-aligned, independent source of libertarian views on key policy questions, or individuals who might be perceived as controlled by, affiliated with, or responsive to, Charles and David Koch’s many political and corporate interests.”

Koch control was on display last Thursday at Cato according to Taylor: “Last year, they used their shares to place two of their operatives – Kevin Gentry and Nancy Pfotenhauer – on our board against the wishes of every single board member save for David Koch. Last Thursday, they used their shares to force another four new board members on us (the most that their shares would allow at any given meeting)…To make room for these Koch operatives, we were forced to remove four long-time, active board members, two of whom were our biggest donors.” The four new Koch appointees were: Charles Koch, attorney Ted Olson, Fox News analyst Andrew Napolitano, and Koch family friend Preston Marshall.

I asked a Cato spokesperson to comment on what had taken place last Thursday. Her response was: "The makeup of the board is the subject of a legal dispute about which we've been advised not to comment any further."

Is Taylor's characterization of these new Koch appointments as "operatives" fair? Kevin Gentry is Vice President for Strategic Development at the Charles G. Koch Charitable Foundation. He's on the Koch payroll.

Nancy Pfotenhauer has served Charles Koch in a dizzying array of incarnations. Pfotenhauer was previously a lobbyist for Koch Industries in their Washington, D.C. office. In 2009 her media firm, Media Speaks Strategies, was paid $175,000 by the Koch funded Americans for Prosperity Foundation. KochFacts.com, a web site set up by the Kochs, carries an interview with Pfotenhauer in April 2011 in which she is identified as the "Koch family spokesperson." She is or was on the Koch payroll.

Ted Olson wrote an OpEd for the Wall Street Journal on February 1 of this year defending the Koch brothers against charges from the Obama campaign and likening the attacks to Joe McCarthy and Nixon's enemies list. At the end of the OpEd, he notes that he's on the Koch Industries payroll.

Preston Marshall is a director of the Institute for Energy Research, funded by Koch foundations and Exxon. Gentry, Pfotenhauer, Napolitano, Marshall, and another Cato Board Member, Ethelmae Humphreys, have all attended one or more of the secret confabs hosted by Charles Koch to plan "the mother of all wars."

This secret deal is reminiscent of another secret deal exposed 10 months ago that created a media maelstrom. As Kris Hundley reported in the St. Petersburg Times, Charles Koch had pledged $1.5 million to hire faculty at Florida State University's (FSU) economics department. Details only leaked out in 2011. Hundley writes: "Under the agreement with the Charles G. Koch Charitable Foundation, however, faculty only retain the illusion of control. The contract specifies that an advisory committee appointed by Koch decides which candidates should be considered. The foundation can also withdraw its funding if it's not happy with the faculty's choice or if the hires don't meet 'objectives' set by Koch during annual evaluations."

Escaping less media scrutiny at that time was that the $1.5 million from Koch was actually a matching grant to the southern banking giant, BB&T's, own $1.5 million grant which made Objectivist Ayn Rand's book, *Atlas Shrugged,* required reading in an ethics and economics course.

Koch's money strings at FSU pales in comparison to the $30 million the Koch foundations have pumped into George Mason University's (GMU) economics programs. Much of the details concerning how much control Charles Koch has at GMU nonprofits remains a tightly guarded secret. Both FSU and GMU are publicly funded institutions.

So what we have at Cato today is essentially the same illusion of fair dealings behind a dark curtain of control based on secret contracts. Cato has over $52 million in assets, according to its 2010 tax filing with the IRS. The Koch brothers, if the court rules in their favor, could spend $16.00 to acquire 16 shares of stock for $1 each from Niskanen's widow, and end up controlling $52 million in assets. That's not so much a hostile takeover as it is the most adept arbitrage maneuver in history. Ayn Rand's hedge funds pals must be whooping it up. Unfortunately for the Kochs, because the lawsuit has exposed to the IRS the controlling owners of the 501(c)(3) and their significant compensation, the Kochs could end up with growing lawsuits and a hefty tax tab. It may be that they've bought themselves a pig in a poke as they like to say in the heartland.

Pam Martens *and* ***Russ Martens*** *maintain an archive dedicated to the abject corruption of this financial era at www.WallStreetOnParade.com. They have no security position, long or short, in any company mentioned in this article. Pam Martens is a contributor to Hopeless: Barack Obama and the Politics of Illusion, forthcoming from AK Press. She can be reached at pamk741@aol.com*