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Koch Brothers Flout Law Getting Richer With Secret Iran Sales

By Asjylyn Loder and David Evans - Oct 3, 2011
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In May 2008, a unit of Koch Industries Inc., one of the world's largest privately held companies, sent Ludmila Egorova-Farines, its newly hired compliance officer and ethics manager, to investigate the management of a subsidiary in Arles in southern France. In less than a week, she discovered that the company had paid bribes to win contracts.

"I uncovered the practices within a few days," Egorova- Farines says. "They were not hidden at all."

She immediately notified her supervisors in the U.S. A week later, Wichita, Kansas-based Koch Industries dispatched an investigative team to look into her findings, Bloomberg Markets magazine reports in its November issue.

By September of that year, the researchers had found evidence of improper payments to secure contracts in six countries dating back to 2002, authorized by the business director of the company's Koch-Glitsch affiliate in France.

"Those activities constitute violations of criminal law," Koch Industries wrote in a Dec. 8, 2008, letter giving details of its findings. The letter was made public in a civil court ruling in France in September 2010; the document has never before been reported by the media.

Egorova-Farines wasn't rewarded for bringing the illicit payments to the company's attention. Her superiors removed her from the inquiry in August 2008 and fired her in June 2009, calling her incompetent, even after Koch's investigators substantiated her findings. She sued Koch-Glitsch in France for wrongful termination.

Obsessed with Secrecy

Koch-Glitsch is part of a global empire run by billionaire brothers Charles and David Koch, who have taken a small oil company they inherited from their father, Fred, after his death in 1967, and built it into a chemical, textile, trading and refining conglomerate spanning more than 50 countries.

Koch Industries is obsessed with secrecy, to the point that it discloses only an approximation of its annual revenue -- $100 billion a year -- and says nothing about its profits.

The most visible part of Koch Industries is its consumer brands, including Lycra fiber and Stainmaster carpet. Georgia- Pacific LLC, which Koch owns, makes Dixie cups, Brawny paper towels and Quilted Northern bath tissue.

Charles, 75, and David, 71, each worth about $20 billion, are prominent financial backers of groups that believe that excessive regulation is sapping the competitiveness of American business. They inherited their anti-government leanings from their father.

Abolishing Social Security

Fred was an early adviser to the founder of the anti- communist John Birch Society, which fought against the civil rights movement and the United Nations. Charles and David have supported the Tea Party, a loosely organized group that aims to shrink the size of government and cut federal spending.

These are long-standing tenets for the Kochs. In 1980, David Koch ran for vice president on the Libertarian ticket, pledging to abolish Social Security, the Federal Reserve System, welfare, minimum wage laws and federal agencies -- including the Department of Energy, the Federal Bureau of Investigation and the Central Intelligence Agency.

What many people don’t know is how the Kochs’ anti- regulation political ideology has influenced the way they conduct business.

A Bloomberg Markets investigation has found that Koch Industries -- in addition to being involved in improper payments to win business in Africa, India and the Middle East -- has sold millions of dollars of petrochemical equipment to Iran, a country the U.S. identifies as a sponsor of global terrorism.

The ‘Koch Method’

Internal company documents show that the company made those sales through foreign subsidiaries, thwarting a U.S. trade ban. Koch Industries units have also rigged prices with competitors, lied to regulators and repeatedly run afoul of environmental regulations, resulting in five criminal convictions since 1999 in the U.S. and Canada.

From 1999 through 2003, Koch Industries was assessed more than $400 million in fines, penalties and judgments. In December 1999, a civil jury found that Koch Industries had taken oil it didn’t pay for from federal land by mismeasuring the amount of crude it was extracting. Koch paid a $25 million settlement to the U.S.

Phil Dubose, a Koch employee who testified against the company said he and his colleagues were shown by their managers how to steal and cheat -- using techniques they called the Koch Method.

Refused to Falsify

In 1999, a Texas jury imposed a $296 million verdict on a Koch pipeline unit -- the largest compensatory damages judgment in a wrongful death case against a corporation in U.S. history. The jury found that the company's negligence had led to a butane pipeline rupture that fueled an explosion that killed two teenagers.

Former Koch employees in the U.S. and Europe have testified or told investigators that they've witnessed wrongdoing by the company or have been asked by Koch managers to take what they saw as improper actions.

Sally Barnes-Soliz, who's now an investigator for the State Department of Labor and Industries in Washington, says that when she worked for Koch, her bosses and a company lawyer at the Koch refinery in Corpus Christi, Texas, asked her to falsify data for a report to the state on uncontrolled emissions of benzene, a known cause of cancer. Barnes-Soliz, who testified to a federal grand jury, says she refused to alter the numbers.

"They didn't know what to do with me," she says. "They were really kind of baffled that I had ethics."

Koch's refinery unit pleaded guilty in 2001 to a federal felony charge of lying to regulators and paid $20 million in fines and penalties.

Corporate Cultures

"How much lawless behavior are we going to tolerate from any one company?" asks David Uhlmann, who oversaw the prosecution of the Koch refinery division when he was chief of the environmental crimes unit at the U.S. Department of Justice. "Corporate cultures reflect the priorities of the corporation and its senior officials."

Koch Industries declined to make either Charles Koch, who lives near corporate headquarters in Wichita, or David Koch, who lives in New York, available for interviews.

Melissa Cohlmia, Koch's director of corporate communications, said in an e-mailed statement that the company has developed a good relationship with environmental regulators and now complies with all rules. Cohlmia says the company has learned lessons from past mistakes, including the improper payment scheme that Koch outlined in its letter filed in French court.

'Steps to Correct'

"We are proud to be a major American employer and manufacturing company with about 50,000 U.S. employees," she wrote. "Given the regulatory complexity of our business, we will, like any business, have issues that arise. When we fall short of our goals, we take steps to correct and address the issues in order to ensure compliance."

Cohlmia says Koch fired the employees and sales agents involved in the illicit payments and strengthened internal controls.

Regarding sales to Iran, she wrote, “During the relevant time frame covered in your article, U.S. law allowed foreign subsidiaries of U.S. multinational companies to engage in trade involving countries subject to U.S. trade sanctions, including Iran, under certain conditions.”

Koch has since stopped all of its units from trading with Iran, she says.

Lobbying Washington

The Koch brothers have vaulted into the American political spotlight in recent years. Koch Industries has spent more than $50 million to lobby in Washington since 2006, according to the Center for Responsive Politics, a nonpartisan group that tracks political donations. The company opposed derivatives regulation and greenhouse gas limits.

The brothers have backed a foundation that has trained thousands of Tea Party activists. The Tea Party, a popular movement whose name stands for Taxed Enough Already, has grown into a potent force in national politics. Sixty representatives of Congress, out of a total of 435, identify themselves as Tea Party members. Virtually every Republican candidate for president -- including Texas Governor Rick Perry and Minnesota Congresswoman Michele Bachmann -- has solicited the group’s support.

Integrity and Compliance

Koch Industries’ political action committee, KochPAC, donated $50,000 to Texans for Rick Perry last year for his gubernatorial campaign, according to the Texas Ethics Commission. It has also donated to support Bachmann’s congressional campaigns, Federal Election Commission records show.

The company tells all of its employees around the world that its top two values, which it calls Guiding Principles, are integrity and compliance. Koch Industries and its subsidiaries have won 436 awards for safety, environmental excellence, community and customer service and innovation since January 2009, Cohlmia says.

The U.S. Occupational Safety and Health Administration has recognized several of the company’s units for their commitment to the workplace, the company says. Koch Industries has also supported charitable causes in Wichita and beyond, including the Kansas Special Olympics and Big Brothers Big Sisters. The company has also helped enlistees in the U.S. Army Reserve.

Koch Industries has donated millions of dollars to the Nature Conservancy, the Red Cross, the Salvation Army and victims of the March 11 earthquake and tsunami in Japan.

Reputation is Critical

David Koch has contributed more than $135 million to cultural institutions, including Lincoln Center for the Performing Arts in New York and the Smithsonian's National Museum of Natural History.

Koch Industries zealously guards its public image.

"A company's reputation is critical to how it will be treated by others and to its long-term success," Charles Koch wrote in "The Science of Success: How Market-Based Management Built the World's Largest Private Company" (Wiley, 2007). "We must build a positive reputation based on reality, or others will create one for us based on speculation or animus and we won't like what they create."

The illicit payments uncovered by Ludmila Egorova-Farines raised the specter of a new blow to the company's effort to improve its reputation following criminal convictions and civil penalties.

Avoiding Scandal

The company wanted to avoid a bribery scandal similar to that of Siemens AG (SIE), says Ged Horner, a managing director at Koch-Glitsch in the U.K. from 2002 until he retired in 2010.

"The only thing that would seriously impact the profitability and continuity of Koch Industries was a compliance issue," Horner says.

In November 2006, the U.S. Department of Justice and German prosecutors opened an investigation into bribery by Munich-based Siemens, Europe's largest engineering company. Siemens and three of its subsidiaries pleaded guilty in December 2008 to charges of violating the U.S. Foreign Corrupt Practices Act from 1998 to 2007.

Siemens paid $1.6 billion in penalties, admitting it had paid bribes to companies in Argentina, Bangladesh, Iraq and Venezuela.

"Koch decided that if it could happen to Siemens, it could happen to them," Horner says.

Koch Chemical Technology Group, a Koch Industries subsidiary run by David Koch, hired Egorova-Farines in April 2008 for the newly created position of compliance and ethics manager for Europe and Asia.

French Investigation

The division, which makes distillation, pollution control and water filtration equipment, recruited her from accounting firm PricewaterhouseCoopers LLP, where she was a consultant for four years on integrating corporate cultures after mergers. As soon as she joined Koch, the company flew her to Wichita to attend an internal compliance conference, she says.

The company then asked her to investigate Koch-Glitsch in France because it had heard that managers were awarding salary increases inappropriately, Egorova-Farines says. The company never mentioned anything about improper payments for contracts when it gave her that assignment, she says. She declines to discuss the details of her findings, saying it would be unprofessional.

The specifics of illicit payments for contracts by Koch- Glitsch can be found in two French labor court cases. The complaints were brought separately by Egorova-Farines and Leon Mausen, business director of Koch-Glitsch France from 1998 to 2008.

Illicit Payments

Koch-Glitsch fired Mausen on Dec. 8, 2008, sending him a termination letter that described illicit payments from 2002 to 2008 in Algeria, Egypt, India, Morocco, Nigeria and Saudi Arabia. In the Middle East, Koch-Glitsch paid what the termination letter describes as an exceptionally high commission of 23 percent to one of its sales agents.

“A portion of that money was intended to pay a customer’s employee in order to secure the contract,” Koch wrote.

The customer was an unnamed Egyptian company that was partially owned by the state. Koch-Glitsch made similar payments to win other contracts with public and private companies in Egypt and Saudi Arabia, Koch wrote in its letter to Mausen.

Koch-Glitsch gave envelopes stuffed with cash to a Moroccan company, Koch wrote in its letter. Koch-Glitsch also made an improper payment to secure a contract with a Moroccan government organization, Koch wrote. The company made similar payments to an unnamed Nigerian government agency to win contracts, Koch wrote.

Koch Blamed Employee

Koch-Glitsch inflated its bid price to a private company in India in 2008, the letter said. A Koch employee explained the reason in an e-mail copied to Mausen and dated Feb. 6, 2008: “Add an extra 2 percent for a third person whose name I would rather give you only on the phone at this time.”

A Koch-Glitsch agent increased the commission paid to an Algerian agent in 2007 and 2008 to cover what Koch described as an unlawful payment to secure a deal with an unnamed French company.

Koch’s spokeswoman Cohlmia says Koch Industries acted firmly and decisively in response to what it had learned.

In its Dec. 8, 2008, termination letter to Mausen, Koch blamed him for the illegal payments. In July 2009, Mausen sued Koch for severance and performance pay in the Arles Labor Court in southern France.

On Sept. 27, 2010, the court said Mausen hadn’t acted on his own.

"It was not Mr. Mausen alone who was giving authorizations," the court wrote.

Company policy required approval from other Koch-Glitsch managers, including Christoph Ender, the president of Koch- Glitsch for Europe and Asia, the court said.

'Without Doing Due Diligence'

"Ender, manager of Koch-Glitsch France, as well as the controllers and auditors who were assisting him, allowed such business practices developed with Mr. Mausen to continue without doing due diligence in their reviews concerning the payment of commissions and the final beneficiaries of said commissions," the labor court wrote.

An appeals court in Aix-en-Provence issued a second ruling on June 14, 2011, saying the company couldn't justify terminating Mausen for the payment scheme because his managers had been aware of the practices for more than 60 days before he was fired. The court ordered Koch-Glitsch to pay Mausen 150,808 euros ($206,170).

Mausen declined to comment, beyond saying he disputed Koch's arguments in court. Ender, who is now a Koch-Glitsch executive in Wichita, didn't respond to requests for comment.

Koch's Cohlmia says Ender "had no knowledge of Mr. Mausen's misconduct at the time it occurred, as Mr. Mausen concealed it from him."

Initially On Track

As for Egorova-Farines, her career was initially on track after she exposed bribery. Koch Chemical promoted her to a permanent position after her trial period expired in mid-2008, court records show. She was dispatched to offices in Germany, Russia and Switzerland, she says.

"I worked hard to drive cultural change to make these units compliant," she says.

Egorova-Farines was hospitalized for seven weeks starting in February 2009, according to the decision in her lawsuit against Koch-Glitsch for wrongful termination.

The company fired her on June 16, 2009, saying later in court that she didn't have the skills she'd listed on her resume and that she had failed to share documents with others at the company, according to the court record. She contested Koch's arguments.

Court Ruling

Neither Egorova-Farines nor the labor court knew at the time that Koch had cited the company's six-year pattern of improper payments in its termination letter to Mausen, she says. The court ruled against her on Feb. 11. She filed an appeal two months later in Paris.

She said in court that Koch had harassed her and retaliated against her for uncovering the payment scheme. She asked to be reinstated in her Koch job and paid for the time she was out of work. Egorova-Farines, who was born in London, now runs a business practices consulting firm in Paris.

Koch's Cohlmia says the labor court found that the company treated Egorova-Farines fairly and provided her with chances to perform adequately.

The payments to win contracts documented by Koch investigators may violate U.S. law, says Sara Sun Beale, a professor at Duke Law School in Durham, North Carolina. She says Koch's termination letter to Mausen gives clear guidance to federal prosecutors.

'Smoking Gun'

"It sounds like a smoking gun," says Beale, who co- authored "Federal Criminal Law and Its Enforcement" (Thompson West, 2010). "It really should get the Justice Department's attention. When you have a smoking gun, you launch an investigation."

Such a probe would fall under the Foreign Corrupt Practices Act, a 1977 law that makes it illegal for companies and their subsidiaries to pay bribes to government officials and employees of state-owned companies.

Justice Department spokeswoman Laura Sweeney says the agency won't confirm or deny the existence of any investigation.

While Koch-Glitsch was conducting its internal probe of illicit payments for contracts, the U.S. government was investigating Koch's European unit on another front: sales to Iran.

On Aug. 14, 2008, investigators from the U.S. Department of Homeland Security met with George Bentu, who had worked as a sales engineer from 2001 to 2007 for Koch-Glitsch in Germany, Bentu says. In a four-hour interview at the U.S. consulate in Frankfurt, the officials asked about documents showing details of the company's trades with Iran, he says.

Legal Sidestep

Homeland Security spokeswoman Barbara Gonzalez declined to comment.

Internal company records show that Koch Industries used its foreign subsidiary to sidestep a U.S. trade ban barring American companies from selling materials to Iran. Koch-Glitsch offices in Germany and Italy continued selling to Iran until as recently as 2007, the records show.

The company's products helped build a methanol plant for Zagros Petrochemical Co., a unit of Iran's state-owned National Iranian Petrochemical Co., the documents show. The facility, in the coastal city of Bandar Assaluyeh, is now the largest methanol plant in the world, according to IHS Inc., an Englewood, Colorado-based provider of chemicals, energy and economic data.

Engineer Challenged Sales

“Every single chance they had to do business with Iran, or anyone else, they did,” Bentu, 46, says.

Bentu, a German engineer who earned his master’s degree in chemical engineering from Montana State University in Bozeman in 1990, joined Koch-Glitsch in 2001. His duties included drawing up bids for potential buyers of the company’s distillation equipment, which is used in making fuels, fertilizers, detergents and other products.

Bentu says he had been working at Koch-Glitsch in Viernheim, about 80 kilometers (50 miles) south of Frankfurt, for two months when he first saw an order destined for Iran. Concerned that the transaction might run afoul of U.S. law, Bentu asked his manager about it, he says. Bentu says his boss told him not to worry, that the company’s U.S. lawyers made sure the deals with Iran were legal.

U.S. companies have been banned from trading with Iran since 1995, when President Bill Clinton declared it a threat to national security. Iran supports Iraqi militants and Taliban fighters as well as terrorist groups, including Hamas and Hezbollah, according to the U.S. State Department.

Getting Around Ban

Koch Industries took elaborate steps to ensure that its U.S.-based employees weren’t involved in the sales to Iran, internal documents show.

Koch Industries may not have violated the law if no U.S. people or company divisions facilitated trades with Iran, says Avi Jorisch, a Treasury Department policy adviser from 2005 to 2008. That’s impossible to determine without a complete investigation, Jorisch says.

Internal Koch-Glitsch correspondence shows that the company coordinated with Koch Industries lawyers in the U.S. to make sure that American employees didn’t work on sales to Iran. Elena Rigon, now Koch-Glitsch compliance manager for Europe, based in Italy, in December 2000 addressed a memo outlining compliance guidelines to company managers in her region.

‘Axis of Evil’

In another e-mail, Rigon said all offices had to go through a checklist for each estimate quoted for materials headed to Iran.

“Your staff shall send this form to me since I have to send it to the lawyers in the USA as part of the compliance program,” Rigon wrote in the e-mail. “If somebody happens to find out that any U.S. persons are involved in this project or U.S. material is delivered to Iran you CANNOT quote.”

Rigon declined to comment.

“Koch-Glitsch had protocols in place that were consistent with applicable U.S. laws allowing such sales at the foreign subsidiary level,” Koch’s Cohlmia says.

In his annual State of the Union address on Jan. 29, 2002, in the wake of the 9/11 attacks in New York and Washington, President George W. Bush said that Iran was part of what he called the “Axis of Evil.”

A year later, in his Jan. 28, 2003, address to Congress, Bush said, “In Iran, we continue to see a government that represses its people, pursues weapons of mass destruction and supports terror.”

Soliciting Iranian Orders

The following day, Koch-Glitsch was sent a purchase order to supply petrochemical equipment for the Zagros plant, which was being designed and built by two engineering firms, Pidec in Iran and Lurgi in Germany, according to company documents.

On May 31, 2004, Koch-Glitsch secured another contract for 1.2 million Euros, to help expand the Zagros facility. The plant helped Iran turn its vast natural gas reserves into methanol, which is used for making plastics, paints and chemicals.

The Italian office of Koch-Glitsch sought work on other projects in Iran -- the expansion of the Abadan refinery, the country’s largest, and the development of South Pars, part of the world’s largest natural gas field, the documents show.

Koch-Glitsch told employees in 2006 that the company was winding down business in Iran, Bentu says. At that point, he says, his bosses still asked him to work on Iran bids. He says he told them he was no longer willing to sign off on such work, leading to arguments between Bentu and his managers.

‘Totally Betrayed’

Bentu says he felt dismayed because Koch Industries clearly tells all of its employees around the world that integrity is the company’s No. 1 value.

“You feel totally betrayed,” Bentu says. “Everything Koch stood for was a lie.”

Bentu, who was earning about 49,000 euros a year, says the company forced him out in April 2007 and paid him 25,000 euros severance.

In 2009, Bentu was interviewed as part of a probe by the Bundeskartellamt, the German antitrust agency. It was looking into whether Koch-Glitsch had collaborated with a rival, Montz GmbH, a smaller petrochemical equipment maker in nearby Hilden, to rig bids they made to supply products to companies.

In November 2010, Koch-Glitsch and Montz each paid 250,000 euros as part of a settlement with the regulator for sharing information from December 2002 to August 2008. The German regulator said the violations were a minor infraction. Koch- Glitsch closed its office in Viernheim in 2009, Bentu says. Several former employees went to work for Montz.

Guenther Frey, general manager for Montz, declined to comment.

Cohlmia says of the agency's ruling, "The decision did not find that Koch-Glitsch GmbH engaged in price fixing or any illegal behavior."

Felony Conviction

This wasn't Koch Industries' first brush with complaints of improper competition. In October 2000, the FBI secretly recorded the telephone calls of Troy Stanley Sr., director of textile staples at KoSa, then a Luxembourg company with its main office in Charlotte, North Carolina.

Koch Industries and a Mexican company established KoSa as a joint venture in 1998 to buy the Hoechst AG unit that produced polyester staples, which are used in making textiles. KoSa pleaded guilty in October 2002 to a felony charge of conspiracy to restrain trade and paid a $28.5 million fine.

Stanley pleaded guilty to one count of conspiring to restrain trade in December 2004 and was sentenced to one year of probation and a $5,000 fine.

'Anti-trust Conspiracy'

"Officers, directors, managers or employees participated in the conspiracy" between September 1999 and January 2001, KoSa admitted in the plea agreement.

The conspiracy began before KoSa bought the business and continued during its ownership, Stanley testified. Koch bought out its partner in 2001. The criminal activity occurred while Koch was a 50 percent owner.

During the next eight years, Koch Industries paid $76 million to settle antitrust claims brought by KoSa's customers, and $59 million in legal fees, according to court records. KoSa is now part of Koch's Invista unit.

A prosecution of KoSa by Canada's attorney general for price fixing followed in August 2003. KoSa pleaded guilty and paid a C$1.5 million fine.

Cohlmia says a KoSa subsidiary "unknowingly bought into an ongoing antitrust conspiracy." Once the company found out about the wrongdoing, it stopped the conspiracy and cooperated with the U.S. Justice Department, she says.

Benzene Emissions

The price-fixing convictions came after years of investigations, environmental lawsuits and fines that had plagued Koch's oil pipeline and refining divisions.

In April 1996, Koch environmental technician Sally Barnes- Soliz walked into the offices of Texas regulators in Corpus Christi and told them the company had lied about spewing benzene into the air.

Koch Refining Co. had recruited Barnes-Soliz in 1991 to work in the safety department at the company's Corpus Christi refinery. Barnes-Soliz, then 30, had earned a bachelor's degree in science and environmental health and a Master of Science in industrial hygiene at Colorado State University in Fort Collins.

"I loved that job," she says, describing how she helped protect plant workers and neighborhood residents from the many hazards at the refinery. "It's important to me that people are safe and their job is not the reason they die."

Federal rules in 1995 required the plant, one of two refineries Koch owns in Corpus Christi, to reduce benzene emissions to less than 6 metric tons a year. Benzene, a chemical compound refined from crude oil, was found to cause leukemia in 1928 by two Italian doctors who detected the cancer in a worker exposed to benzene for five years.

False Report

Four federal agencies -- the National Institutes of Health, the Food and Drug Administration, the Environmental Protection Agency and the Occupational Safety and Health Administration -- say that benzene is a cause of cancer.

On Jan. 6, 1995, Koch's refining unit informed the Texas Natural Resource Conservation Commission, or TNRCC, that it had installed a new anti-pollution device called a Thermatrix that used flameless heat to burn off the benzene. The machine lacked sufficient capacity for the job, Barnes-Soliz says, and refinery workers disconnected it within days.

"The refinery was just hemorrhaging benzene into the atmosphere," she says.

Three months after disconnecting the machine, Koch filed a quarterly report with Texas regulators, while concealing that it had violated the emission rules.

Pressured to Change

On Aug. 17, 1995, Koch Industries attorney Vincent Mietlicki wrote a memo to another company lawyer, Thomas Meek, saying the refinery had given the state incorrect information about its uncontrolled benzene emissions.

"I think it goes without saying that there is a need to correct our first quarterly report which is misleading and inaccurate," he wrote.

That December, a refinery manager asked Barnes-Soliz to tally the plant's annual benzene emissions for a report to state regulators, Barnes-Soliz says. She found 91 metric tons of uncontrolled benzene emissions, more than 15 times higher than what the rules allowed.

"I redid the calculation a lot of times," Barnes-Soliz says.

Those levels of emissions could increase the cancer risk to refinery employees and the public, she says. Barnes-Soliz reported the results in a document dated Jan. 4, 1996, to Mietlicki, the same lawyer who had written the memo calling out the inaccuracies in the quarterly report Koch filed with the state. She says Mietlicki and other Koch executives pressured her to lower the figures in her report.

Falsified Document

"There were a lot of meetings to try and get me to change the number," she says. "It was hard, but I held firm to my convictions."

Barnes-Soliz's bosses went around her. On April 8, 1996, Koch reported to Texas regulators that its Corpus Christi plant had uncontrolled emissions of 0.61 metric tons for 1995, or 1/149th the quantity she had found.

"When I saw they had actually falsified that document, I had no recourse but to notify the authorities," Barnes-Soliz says.

On April 18, 1996, on her lunch break, she drove to the state's TNRCC office and reported that Koch had lied about its benzene emissions. By the time Barnes-Soliz walked in, environmental regulators were already investigating Koch in Corpus Christi.

Oil Slick

The EPA had sued Koch Industries a year earlier for a series of pipeline leaks in several states, including one that left a 12-mile-long oil slick on Nueces and Corpus Christi bays in October 1994. Her statement triggered another probe by state regulators and the FBI.

During the next three years, investigators compiled evidence that included hundreds of internal memos about benzene emissions. In 1999, Koch's lawyers tried to stop prosecutors from using the documents in court.

Koch argued that records of the company's internal investigation regarding benzene rules were protected by attorney-client privilege. U.S. District Judge Janis Graham Jack in Corpus Christi rejected that claim, ruling that the privilege doesn't apply when used to help commit a crime or fraud. She singled out Mietlicki.

‘Front Man’

“The government has submitted evidence which indicates that Koch was intentionally using Mietlicki and his investigation and expertise in reference not to prior wrongdoing, but to future wrongdoing,” the judge wrote. “The February memo strongly suggests that Koch was using Mietlicki (and his investigation and expertise) as a ‘front man’ to impede the TNRCC from ascertaining the extent of its noncompliance.”

The February memo was sealed by the court.

A federal grand jury issued a 97-count indictment against Koch Petroleum Group, Mietlicki and three refinery managers on Sept. 28, 2000. Koch Petroleum Group pleaded guilty to a felony charge of lying to the government about its benzene emissions in April 2001.

Judge Jack fined Koch Petroleum $10 million and ordered that it pay another $10 million to fund environmental projects in south Texas. Koch earned $176 million in profit from the Corpus Christi plant in 1995, prosecutors told the court. The company said in a hearing that it would have cost $7 million to comply with the benzene emission regulation.

Koch Petroleum changed its name to Flint Hills Resources in 2002.

In the agreement to plead guilty, prosecutors dropped the charges against the four individuals.

‘Ultimately Collapsed’

Koch spokeswoman Cohlmia says the company reported its compliance issues to the state before a whistle-blower did so. She says the federal case was flawed, citing testimony by a prosecution expert witness.

“The government’s case ultimately collapsed after the company finally had an opportunity to challenge the government’s key expert witness,” she says.

Uhlmann, the federal prosecutor who led the probe, says Koch’s after-the-fact response is a public relations whitewash.

“The Koch case was a classic case of environmental crime, significant violations of law occurring alongside widespread efforts to conceal those violations, which Koch has admitted,” Uhlmann says. He now teaches at the University of Michigan Law School in Ann Arbor.

Empty Office

Mietlicki, who is now assistant principal at John Paul II High School in Corpus Christi, says he can’t comment on details of the case.

“I know all of my actions as a lawyer, throughout all my years of practice, were nothing but honest and truthful," he says.

After the company found out that Barnes-Soliz had tipped off state regulators, Koch stripped her of her responsibilities and moved her to an empty office with no tasks and no e-mail access, she says.

"They were pressuring me to quit," she says.

She left the company in July 1996. Barnes-Soliz sued Koch in January 1997, saying the company harassed and mistreated her after she became a whistle-blower. Koch settled the lawsuit in July 1999 for an undisclosed amount.

The Corpus Christi case was one of a series of challenges Koch Industries faced in the 1990s over environmental issues. In 1997, a company now owned by ConocoPhillips sued Koch for toxic waste dumping at a refinery in Duncan, Oklahoma.

'Replete With Evidence'

In March 1998, U.S. District Court Judge Vicki Miles- LaGrange in Oklahoma City ordered Koch to pay for 15 percent of the cleanup costs for dumping at the site between 1946 and 1953. That decision was upheld by the U.S. Court of Appeals for the 10th Circuit in May 2000.

"The record is replete with evidence Koch used unlined ditches, pits and ponds to dispose of hazardous waste at the site," the appeals court ruled, finding that Koch had tainted groundwater. "The pollution of any Oklahoma waters, including groundwater, has been prohibited by state statute since the early 1900s -- well before Koch's waste disposal activity at the refinery."

By March 2007, Koch Industries had paid just $440,899 and still owed $2.97 million for its share of the cleanup, Conoco told the court.

"Koch simply refuses to pay its share as ordered by this court," Conoco said.

Companies Settled

The two companies settled in February 2009. Terms weren't disclosed.

Cohlmia says, "We understand that appropriate remediation is occurring and Koch has met all of its obligations with respect to this matter."

A Koch unit in Rosemount, Minnesota, pleaded guilty in 1999 to two federal misdemeanors of violating the Clean Water Act and paid $8 million in fines and penalties. The company used fire hydrants to pump more than a million gallons of wastewater contaminated with ammonia onto the ground.

Koch also increased its dumping of wastewater on weekends when it didn't monitor discharges, circumventing the reporting requirement of its permit, the EPA said. Koch also admitted that it negligently released between 200,000 gallons (757 kiloliters) and 600,000 gallons of aviation fuel into a nearby wetland.

Cohlmia says the company cooperated with state and federal regulators to resolve the Rosemount issues and has met all of its obligations.

“In March, 1999, Koch Petroleum Group took full responsibility for past underlying discharges,” she says.

Koch Industries also spent much of the 1990s defending itself against what a U.S. Senate subcommittee called a widespread scheme to steal oil on Indian land.

Twin Brother

The Senate held hearings in May 1989 after Bill Koch, David Koch’s twin brother, told a U.S. Senate special committee on investigations that Koch Industries was stealing oil on American Indian reservations, cheating the federal government of royalties.

Bill Koch had a long-standing feud with his brothers after his failed attempt to take over the company in the early 1980s. He sold his shares in June 1983 and later lost a lawsuit claiming he’d been shortchanged.

The Senate committee sent investigators to Oklahoma to secretly observe oil companies, including Koch, buying crude on Indian land. The federal agents hid in ditches, crouched behind scrub cedars and ducked behind cows to avoid detection by Koch Oil’s purchasers, FBI agent Richard Elroy testified to the committee in May 1989.

‘Theft is Widespread’

The investigators caught Koch Oil’s employees falsifying records so that the company would get more crude than it paid for, shortchanging Indian families, Elroy said. Koch’s records showed that the company took 1.95 million barrels of oil it didn’t pay for from 1986 to 1988, according to data compiled by the Senate.

“The theft is widespread and pervasive, and these people are being horribly victimized,” Elroy testified.

Elroy told the committee that Charles Koch gave a deposition that said that no one could make exact measurements.

“There was a lot of uncertainty and tremendous variations,” Elroy quoted Koch as saying. The full deposition is sealed, which is committee policy.

The committee concluded in a November 1989 report that Koch Oil had engaged in a widespread, sophisticated scheme to steal millions of barrels of oil. The Senate referred the case to the Justice Department, which convened a grand jury that never indicted the company.

“We believe that our practices were consistent with industry practice,” Cohlmia says.

The Civil Trial

Bill Koch brought a lawsuit on behalf of U.S. taxpayers, claiming that Koch Industries’ scheme defrauded the government of royalties. The case came to trial in 1999. Former company employees testified that Koch Industries trained them to steal.

Phil Dubose, who worked for Koch Industries from 1968 to 1994, told the jury how the scheme worked.

“The Koch Method is to cheat the producer out of crude oil,” he said.

He testified that he was able to steal 2,000 barrels a month from one customer.

“You used every available tool to mismeasure the crude oil in Koch’s favor,” says Dubose, who is now retired.

Charles Koch testified in the trial, saying the company had the highest standards.

“By 1988, I thought we had developed the best measurement approach, controls and so on of any crude oil purchaser in the industry,” Koch said. “And that’s why we became the No. 1 crude oil purchaser in the United States.”

24,587 False Claims

Two days before Christmas 1999, the jury delivered the verdict: Koch Industries had made 24,587 false claims in buying oil, underpaying the U.S. government for royalties on Native American land from 1985 to 1989. Koch paid the U.S. $25 million to settle the case in 2001.

The Koch brothers, meanwhile, reached an agreement, with undisclosed terms, dropping all litigation against each other.

While the Koch brothers battled over oil, Koch Industries clashed with regulators over its failure to properly maintain its pipelines. In 1995, the EPA sued the company, saying poor maintenance resulted in corrosion that contributed to hundreds of spills.

The following year, before the EPA case was resolved, a leak in a Koch butane pipeline led to an explosion that killed two teenagers.

Burned Alive

On Aug. 24, 1996, Danielle Smalley and her high school friend and neighbor Jason Stone, both 17, smelled gas outside Smalley’s mobile home in rural Lively, Texas, 50 miles southeast of Dallas. The house had no telephone, so they decided to drive the Smalley family’s pickup truck to a neighbor’s home to call 911.

They never made it.

The truck stalled after the couple drove into a fog-like cloud, says Danielle's father, Danny Smalley, who watched them drive away. It was butane vapor, leaking from a corroded steel pipeline. Seconds later, as Danielle restarted the truck, the gas ignited into a fireball, burning Danielle and Jason to death.

Smalley's father sued Koch Industries in 1997 in the Kaufman County, Texas, district court for the wrongful death of his daughter.

'Definitely Responsible'

"I will tell you Koch Industries is definitely responsible for the death of Danielle Smalley," Bill Caffey, an executive vice president of the company, testified in a 1999 deposition during Smalley's lawsuit.

Caffey oversaw pipeline safety at the company. He testified that he thought the pipeline was safe before the explosion. Koch Pipeline Co., the unit that managed the Texas pipeline, knew the line had corroded and didn't fix it, an investigation by the National Transportation Safety Board concluded in November 1998.

The 570-mile-long pipeline carrying liquid butane from Medford, Oklahoma, to Mont Belvieu, Texas had corroded so badly that one expert, Edward Ziegler, likened it to Swiss cheese. The company didn't give 40 of the 45 families near the explosion site -- including the Smalley and Stone families -- any information about what to do in case of an emergency, the NTSB wrote.

Danny Smalley hired Ziegler, a third-generation oilman and certified safety professional, as an expert witness. Ziegler had previously been retained by Koch Industries as an expert witness in an unrelated case. Ziegler told the jury that he'd never seen a company disregard safety to this extent in his more than 25-year career.

'A Total Failure'

"This is an example of a total failure of a company to follow the regulations, keep their pipeline safe and operate it as the regulations require," Ziegler, who now operates his own pipelines, testified.

A memo forwarded by Caffey to another Koch executive vice president justified putting a 70-mile section of the pipeline back into operation after being closed for three years because it could earn more than $7 million in operating income a year.

"We were to work on reducing wasteful spending," Caffey said in his deposition.

In his 2007 book, Charles Koch didn't comment on the pipeline explosion. He did, however, offer this observation: "Our organization does not reward failure."

Koch Industries didn't penalize Caffey, the executive in charge of pipeline safety. The company doubled his annual bonus to $900,000 for 1996, the year the fatal blast occurred, according to court records. In his deposition, lawyers asked Caffey whether the disaster came up during his annual review.

'I Don't Believe'

"I don't believe we discussed that specifically in my review," he said.

Caffey, who stayed with Koch for a decade after the explosion and now runs the BB River Ranch in Comanche, Texas, says the explosion was a one-of-a-kind tragedy.

"I have never known any company executive more focused on compliance than Charles Koch," he says.

The state jury awarded Danny Smalley $296 million in its Oct. 21, 1999, verdict. The jury found that Koch Industries acted with malice because it had been aware of the extreme risks of using the faulty pipeline.

Smalley later settled for an undisclosed amount. Stone's family also settled. Danny Smalley used settlement money to start the Danielle Dawn Smalley Foundation for pipeline safety education. Large pipeline operators such as ExxonMobil Corp., BP Plc and Kinder Morgan Inc. -- and not Koch -- accept free services from the foundation, Smalley says.

'Never Forget'

"You see two children burned to death in front of you, you never forget that," he says. "I want to stop other parents from ever having to see that."

Cohlmia says Koch Industries used the lessons learned from the explosion to help avoid similar accidents. The company immediately accepted responsibility for the explosion, which was the only one of its kind, she says.

Three months after the Smalley verdict, Koch settled the five-year-old EPA case for pipeline leaks, along with a second EPA case brought in 1997. The company paid $35 million to resolve those cases, which covered more than 300 oil spills in six states.

For six decades around the world, Koch Industries has blazed a path to riches -- in part, by making illicit payments to win contracts, trading with a terrorist state, fixing prices, neglecting safety and ignoring environmental regulations. At the same time, Charles and David Koch have promoted a form of government that interferes less with company actions.

'Overall Concept'

"My overall concept is to minimize the role of government and to maximize the role of the private economy and maximize personal freedoms," David Koch told the National Journal in May 1992.

In his 2007 book, Charles Koch says his company had difficulty keeping up with changing government regulations and that it did eventually build an effective compliance program for 20 areas ranging from environmental to antitrust to safety regulations.

“We were caught unprepared by the rapid increase in regulation,” he wrote. “While business was becoming increasingly regulated, we kept thinking and acting as if we lived in a pure market economy.”

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