

**BASIS FOR IRS INVESTIGATION INTO WHETHER THE HEARTLAND  
INSTITUTE IS ELIGIBLE FOR TAX-EXEMPT STATUS UNDER  
SECTION 501(C)(3)**

This attachment sets forth the basis for the complaint against the Heartland Institute (“Heartland”) that it is participating in a political campaign on behalf of a candidate for public office in violation of IRC section 501(c)(3), as required in Section 4 of Form 13909.

**FACTUAL BACKGROUND**

Heartland is a section 501(c)(3) organization, whose purpose is to “discover, develop, and promote free-market solutions to social and economic problems.”<sup>1</sup> It is headquartered in Chicago and has a full-time staff of 40 and an annual budget of \$6 million. *Id.*

In November 2010, Scott Walker was elected governor in the state of Wisconsin and his party won majorities in both houses of the Legislature. In early February 2011, Governor Walker proposed a budget adjustment bill eviscerating public sector bargaining laws. The bill, which became known as Act 10, required public employees to pay more for pension and health insurance. It also prohibited bargaining over all terms and conditions of employment except for base wages, eliminated mandatory union dues and dues checkoff, and required annual recertification elections—none of which had anything to do with balancing the budget. Walker had never campaigned on these issues.

Over the next five months until Act 10 became effective on July 1, 2011, there were massive public protests throughout the state opposing the repeal of public sector bargaining rights. In July and August, there were nine recall votes conducted of state senators, both Republicans and Democrats, which resulted in two Republican senators being removed from office.

On November 15, the earliest date possible to file recall petitions,<sup>2</sup> a recall committee sponsored by an organization called United Wisconsin registered to begin circulating petitions seeking to recall Governor Walker, Lieutenant Governor Rebecca Kleefisch and four Republican senators who supported Governor Walker’s repeal of public sector bargaining rights.

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<sup>1</sup> <http://heartland.org/about>

<sup>2</sup> Under Wis. Stat. § 9.10, the governor cannot be recalled until he has held office for a year after his January 2010 swearing in and electors have 60 days in which to secure sufficient signatures.

On January 17, 2012, United Wisconsin filed an estimated 1 million signatures seeking the recall of Governor Walker. Under Wisconsin law, if 540,208 of these signatures are verified, a recall election must be conducted. Currently, it appears these petitions will be verified soon and an election would be held in May or June.

On February 16, 2012, a story appeared in the *Milwaukee Journal Sentinel* indicating that Heartland intended to spend \$612,000 during 2012 to promote a campaign called “Operation Angry Badger.”<sup>3</sup> This information was contained in two documents, Heartland’s 2012 Fundraising Plan and Heartland’s 2012 Budget, both of which had been provided to independent websites.<sup>4</sup> While a Heartland spokesperson claimed some of the documents discussing climate change were forged, he did not assert the 2012 Fundraising Plan and 2012 Budget documents were forged. n. 2, supra.

The 2012 Fundraising Plan, with the phrase “Confidential. Please do not circulate.” appearing on its cover page, described a new initiative called “Operation Angry Badger” designed to “excit[e] new donors to make the contributions needed to fund our programs.”<sup>5</sup> This program calls for direct intervention in the recall campaign of Wisconsin Governor Scott Walker on his behalf:

Wisconsin was the focus of national attention due to recall campaigns waged in 2011, and campaigns are taking place in 2012 against Gov. Scott Walker, Lt. Gov. Rebecca Kleefisch and three Republican senators who voted for Act 10, the landmark collective bargaining reform legislation adopted in 2011. We have been following the Wisconsin debate closely, reporting on it in *Budget & Tax News*, commenting in op-eds and LTEs and on blogs, doing television and radio interviews, and sending research and commentary to elected officials in Wisconsin and nationally.

The recall elections of 2012 amount to a referendum on collective bargaining reform at the state level, making them of *national* interest. Successful recalls would be a major setback to the national effort to rein in public sector compensation and union power. Heartland is the largest and most influential national free-market think tank in the Midwest, so we are in the right place and with the right resources to help defend and secure Wisconsin’s recent gains.

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<sup>3</sup> <http://www.jsonline.com/news/wisconsin/leaked-documents-detail-operation-angry-badger-u447pp9-139483133.html>

<sup>4</sup> Peter Gleick, a scientist affiliated with the Pacific Institute, later acknowledged he obtained these documents from Heartland under someone else’s name after being provided with other documents anonymously that named him [http://www.huffingtonpost.com/peter-h-gleick/the-origin-of-the-heartl\\_b\\_1289669.html](http://www.huffingtonpost.com/peter-h-gleick/the-origin-of-the-heartl_b_1289669.html)

<sup>5</sup> 2012 Fundraising Plan, p. 12, Attachment 1 to <http://www.desmogblog.com/heartland-insider-exposes-institute-s-budget-and-strategy>

We are contemplating five projects:

1. Recruit and promote superintendents who support Act 10
2. Explain the benefits of Act 10
3. Document the shortcomings of public schools in Wisconsin
4. Expose teacher pay in key districts
5. Create blogs that shadow small town newspaper coverage of the controversy

We anticipate that this project will cost about \$612,000. Maureen Martin, Heartland's legal counsel, will be the chief researcher and writer for this project. The anonymous donor has pledged \$100,000 toward this project. We are circulating a proposal to other potential funders.<sup>6</sup>

The Heartland 2012 Proposed Budget, whose cover page also bore the label, "Confidential. Please do not circulate.," provided more detail regarding Operation Angry Badger's tie-in to defeating the recall campaign:

Communications Budget (p. 22)

\$91,500 (annual cost)	<b>OPERATION ANGRY BADGER</b> A research and education project built to take advantage of the public interest in Wisconsin's Act 10 generated by recall elections that could take place. Publications Dept. budget includes printing and mailing three reports and brochures.
\$60,000 (breakout)	Design and place ads in 10 small newspapers reporting teacher salaries and benefits, 10 @ \$6,000.
\$31,500 (breakout)	HL staff will create and launch blogs allowing volunteers and allies to post information about Act 10 that their local newspapers aren't covering. Maintain for 6 months. \$ 1,500 Web site hosting, \$25/month x 10 sites x 6 months \$30,000 Web site promotion, \$500/month x 10 sites x 6 months ----- \$31,500 Total

Publication Budget (p. 27)

\$205,020	<b>OPERATION ANGRY BADGER</b> A research and education project built to take advantage of the public interest in Wisconsin's Act 10 generated by recall elections that could take place. Communications Dept. budget includes print ads and Web site projects.
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<sup>6</sup> *Id.* Pp. 13-14.

	<b><i>The Benefits of Wisconsin's Act 10</i></b>
\$3,500	Print, 5,000 @ \$0.70
\$5,640	Mail, 4,000 @ \$1.41
\$40,800	Brochure print, 120,000 @ \$0.34
\$48,000	Brochure mail, 120,000 @ \$0.40
	<b><i>How Good Are WI Schools?</i></b>
\$3,500	Print, 5,000 @ \$0.70
\$5,640	Mail, 4,000 @ \$1.41
\$40,800	Brochure print, 120,000 @ \$0.34
\$48,000	Brochure mail, 120,000 @ \$0.40
	<b><i>Are Wisconsin's Teachers Underpaid?</i></b>
	\$3,500 Print, 5,000 @ \$0.70
\$5,640	Mail, 4,000 @ \$1.41
	(Comm. Dept. will design and run print ads for local newspapers.) <sup>7</sup>

Since this disclosure, Heartland has not expressed any intention to eliminate Operation Angry Badger from its budget or to not implement it as prescribed.

## LEGAL ANALYSIS

### **I. Heartland is Engaged in Non-Exempt Operations Supporting the Walker Campaign.**

#### **A. Legal Standards.**

Section 501(c)(3) of the Code provides, in part, that an organization is exempt from federal income tax if it is organized and operated for charitable and educational purposes, provided that no substantial part of its activities is carrying on propaganda and that it does not participate in, or intervene in (including the publishing or distributing of statements) any political campaign on behalf of (or in opposition to) any candidate for public office.

The regulations implementing this provision establish two primary tests for determining whether an organization is exempt, one focusing on whether the formal organizational purposes are exempt, and the other on whether the operation's practices are consistent with exempt purposes. 26 CFR 1.501(c)(3)-1(a). Since the Service has already approved the tax exemption for the

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<sup>7</sup> 2012 Budget, Attachment 2 to <http://www.desmogblog.com/heartland-insider-exposes-institute-s-budget-and-strategy>

Heartland Institute, the organizational purposes prong has been met.

The analysis set forth below shows that Heartland's Operation Angry Badger violates the second operational test of these regulations. Section 1.501(c)(3)-(3)(i) provides that if an organization participates or intervenes, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office, it is an "action" organization. An "action" organization is not operated exclusively for one or more exempt purposes and, therefore, cannot be exempt under [section 501\(c\)\(3\) of the Code](#).

The prohibition against participation or intervention in a political campaign is absolute. Therefore, it is not material that the intervention is an insubstantial part of an organization's activities or that the other activities of the organization would, by themselves, support exemption under [section 501\(c\)\(3\) of the Code](#). See *United States v. Dykema*, 666 F.2d 1096, 1101 (7th Cir. 1981), cert. denied, 456 U.S. 983 (1982) and *Association of the Bar of the City of New York v. Commissioner*, 858 F.2d 876 (2nd Cir. 1988), cert. denied, 490 U.S. 1030 (1989).

Section 4955(d)(1) of the Code provides that the term "political expenditure" means any amount paid or incurred by a section 501(c)(3) organization in any participation in, or intervention in (including the publication or distribution of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Revenue Ruling 2007-41, 25 I.R.B.1421 (June 18, 2007) defines the distinction between issue advocacy and prohibited support of a campaign to require a consideration of substance over form:

Section 501(c)(3) organizations may take positions on public policy issues, including issues that divide candidates in an election for public office. However, section 501(c)(3) organizations must avoid any issue advocacy that functions as political campaign intervention. Even if a statement does not expressly tell an audience to vote for or against a specific candidate, an organization delivering the statement is at risk of violating the political campaign intervention prohibition if there is any message favoring or opposing a candidate.

The following factors must be considered in determining whether purported issue advocacy functions as support for a political campaign:

[1] Whether the statement identifies one or more candidates for a given

public office;

[2] Whether the statement expresses approval or disapproval for one or more candidates' positions and/or actions;

[3] Whether the statement is delivered close in time to the election;

[4] Whether the statement makes reference to voting or an election;

[5] Whether the issue addressed in the communication has been raised as an issue distinguishing candidates for a given office;

[6] Whether the communication is part of an ongoing series of communications by the organization on the same issue that are made independent of the timing of any election; and

[7] Whether the timing of the communication and identification of the candidate are related to a non-electoral event such as a scheduled vote on specific legislation by an officeholder who also happens to be a candidate for public office.

A communication is particularly at risk of political campaign intervention when it makes reference to candidates or voting in a specific upcoming election.

Nevertheless, the communication must still be considered in context before arriving at any conclusions.

Likewise, TAM 9609007, 1996 WL 87759 (IRS TAM) makes clear that all forms of direct or indirect campaign intervention fall within the ban:

M has argued that there must be more than evidence of bias in its fund raising letters for or against candidates running for public office in order for M to be found to have violated the section 501(c)(3) political intervention prohibition. However, in respect to this prohibition there is no "express advocacy" rule as was required by the Supreme Court in Buckley v. Valeo, 424 U.S. 1 (1976), and Federal Election Commission v. Massachusetts Citizens for Life, 479 U.S. 238 (1986), in regard to influencing federal elections under the jurisdiction of the Federal Election Commission. For purposes of section 501(c)(3), intervention in a political campaign may be subtle or blatant. It may seem to be justified by the press of events. It may even be inadvertent. The law prohibits all forms of participation or intervention in "any" political campaign.

Applying these standards here demonstrates that Operation Angry Badger functions as support for Governor Walker in his effort to defeat the recall campaign which was launched at the same time.

## **B. Operation Angry Badger Functions as Support for Governor Walker.**

### **1. Walker is a Candidate for Recall.**

As noted above, under Wisconsin law, a governor cannot be recalled prior to serving one year in office and since he assumed office in January 2011, the earliest a recall effort could be initiated was 60 days prior to this date since the law requires the signatures to be gathered within a 60-day period. If sufficient signatures are filed and verified, the Government Accountability Board directs a recall election. Wis. Stat. § 9.10.

A group called United Wisconsin initiated such an effort on November 15, 2011 and began gathering signatures. For purposes of this analysis, Walker must be considered a “candidate,” even though no recall election had been set in November. There is no question that by virtue of the filing of the petition to gather signatures to recall him from office, he was “proposed by others, as a contestant for an elective public office,” under Section 1.501(c)(3)(c)(1)(iii). That Walker considered himself a candidate is evidenced by his decision to run a campaign ad on November 14. n. 10, *infra*.

## **2. Operation Angry Badger is Intended to Intervene in the Walker Recall Campaign.**

Application of the remaining criteria reveals the explicit purpose of Operation Angry Badger was to assist Governor Walker in his attempt to defend his position from recall. Indeed, the Fundraising Proposal for Operation Angry Badger makes this political objective unequivocal:

Successful recalls would be a major setback to the national effort to rein in public sector compensation and union power. Heartland is the largest and most influential national free-market think tank in the Midwest, **so we are in the right place and with the right resources to help defend and secure Wisconsin’s recent gains.** (emphasis added)

Examination of the five specific projects proposed to implement Operation Angry Badger underscores its inherently political nature. The first two projects are to “recruit and promote superintendents who support Act 10” and to “explain the benefits of Act 10.” The reference to “superintendents” means superintendents of school districts. The proposal is to have superintendents explain the purported benefits of Act 10, such as additional flexibility to unilaterally establish working conditions and hours of operation, and introduce pay systems tied to student performance on tests. The proposed budget contemplates that these superintendents’ comments would be disseminated through brochures and mailings.

The projects to “document the shortcomings of public schools in Wisconsin” and to “expose teacher pay in key districts” are tied to another of Heartland’s priorities – to promote “education reform” which encourages the public funding of private for-profit schools through vouchers allowing parents to choose private schools.<sup>8</sup> On June 17, 2011, the Legislature enacted Governor Walker’s proposal to substantially expand a voucher program from Milwaukee to other cities.<sup>9</sup> Heartland’s proposal to publicize through brochures and mailings the shortcomings of public schools and to expose teacher pay (which really means to assert teachers are overpaid) is plainly intended to assist Walker’s recall campaign by defending his expansion of school privatization.

Perhaps the clearest evidence of Heartland’s political desire to use educational issues to promote Walker’s candidacy is found in Walker’s own ads, which dovetail neatly with Operation Angry Badger. On November 14, Walker’s campaign ran the following ad on statewide television stations following the Heartland theme of “explaining the benefits of Act 10” in an educational setting:

[School district official]: We were worried when the state budget was going to mean less money for our school district and we have 25 schools. But Governor Walker, he gave us options that reduced our biggest costs so that we could put more money back into our classrooms.

[Walker]: I’m committed to working together to create more jobs, to improve our schools, and to protect our seniors. You know, Wisconsin’s best days are yet to come. It won’t happen overnight but we are on our way.<sup>10</sup>

On December 6, the Walker campaign continued with the same theme that Act 10 was working in schools:

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<sup>8</sup> Heartland’s extensive work in privatizing schools is described on its website. <http://heartland.org/issues/education>

<sup>9</sup> [http://blogs.edweek.org/edweek/state\\_edwatch/2011/06/wisconsin\\_approves\\_voucher\\_expansion.html](http://blogs.edweek.org/edweek/state_edwatch/2011/06/wisconsin_approves_voucher_expansion.html) Wisconsin Superintendent of Schools Tony Evers described this law as follows: “Once again in the middle of the night, the majority party in the Assembly voted to expand taxpayer-funded vouchers for religious and private schools,” Evers said. “Wisconsin is now set to expand vouchers for private and religious schools, while making a catastrophic \$1.6 billion cut in funding for public schools.” *Id.*

<sup>10</sup> <http://www.youtube.com/watch?v=m0EfMhiE9E0>



[Teacher]: When the state budget passed in Madison a lot of us thought we might lose our jobs. We figured if we didn't get laid off, our class sizes would become unmanageable but that didn't happen. I don't agree with Governor Walker on everything but thanks to his budget reforms, hundreds of teachers like me still have their job.

[Walker]: I'm committed to working together to create more jobs, to improve our schools and to protect our seniors. Wisconsin's best days are yet to come. It won't happen overnight but we are on our way.<sup>11</sup>

Accordingly, there is no question that the second, third and fifth prongs of the Revenue Ruling 2007-41 test are met, indicating an intention to intervene on Walker's behalf by encouraging citizens to vote for Walker in the imminent recall election based upon his signature legislative achievements in Act 10 and the expansion of the school voucher program.

Likewise, consideration of the remaining Revenue Ruling 2007-41 factors weighs in favor of finding an intention to intervene in the campaign. Prior to launching Operation Angry Badger, Heartland had never before been involved in publicly promoting the benefits of Act 10 or school vouchers in Wisconsin. Thus, it cannot be said Operation Angry Badger is "part of an ongoing series of communications by the organization on the same issue that are made independent of the timing of any election." *Id.*

Nor can it be said this campaign was "related to a non-electoral event such as a scheduled vote on specific legislation by an officeholder who also happens to be a candidate for public office." Act 10 had already been passed on March 11, 2011, and became effective July 1 as had the voucher expansion. The Operation Angry Badger campaign focuses exclusively on the effects of this legislation. No similar legislation was or is currently pending.

Finally, while it may be true that the intended publicity campaign does not expressly "make reference to voting or an election," this is inconsequential. There is no question its actual goal, as stated in the Fundraising Proposal, is "to help defend and secure Wisconsin's recent gains" and that "(s)uccessful recalls would be a major setback to the national effort to rein in public sector compensation and union power." This makes clear that the way to defend Act 10 and the voucher reforms even under the disguised public face of this campaign is to re-elect Governor Walker.

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<sup>11</sup> <http://www.youtube.com/watch?v=r-bHIfsJV-E&list=UUEeJwPqSAkPNxIR-HZ89fvw&index=6&feature=plcp>

## CONCLUSION

Until such time as the U.S. Supreme Court's *Citizens United* decision is overturned, the donors to Heartland are free to donate as much as they desire to section 527 or "Super-PAC" entities to engage in independent spending to support Governor Walker. Instead, they are making taxpayer-subsidized deductible donations to the Heartland Institute to accomplish their blatantly partisan political objectives of defeating the proponents of Governor Walker's recall. The Service should use all of its enforcement powers to immediately enjoin these abuses and assess the maximum penalties for this affront to section 501(c)(3).

March 13, 2012