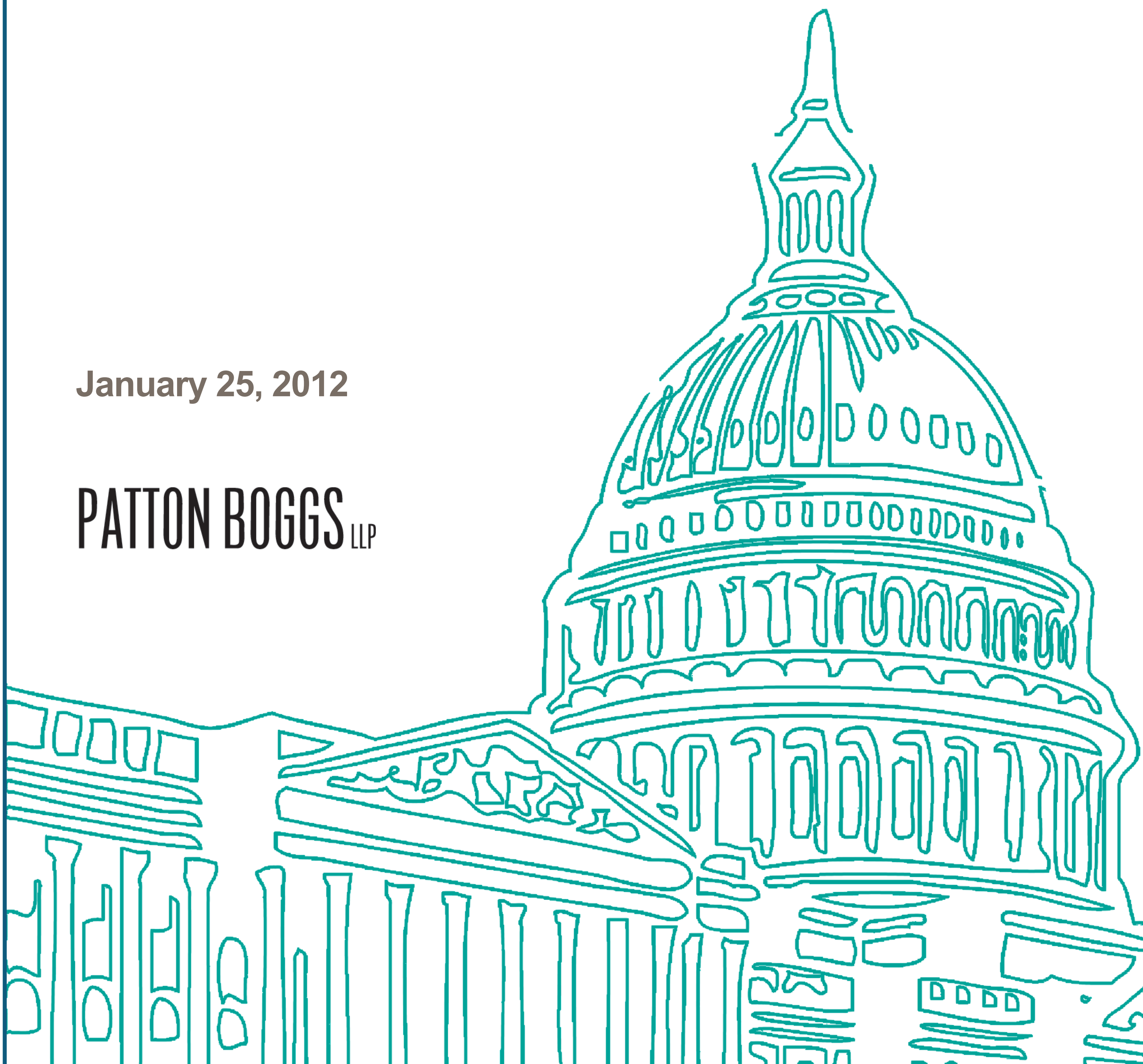
The State of the Union
and
The 2012 Presidential Election



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“[The President] shall from time to time give to the Congress Information of the State of the Union, and recommend to their Consideration such Measures as he shall judge necessary and expedient;”

Article 2, Section 3
U.S. Constitution

Introduction

In his State of the Union Address last year, President Barack Obama addressed Congress for the first time since the 2010 mid-term elections in which Republicans wrested control of the House from Democrats and weakened the Democratic majority in the Senate. Aware that American voters were increasingly fed up with Washington and with an eye on his own reelection prospects in 2012, President Obama indicated that he would pursue an ambitious agenda in 2011. He spoke of "our generation's Sputnik moment." He challenged the country to "win the future." And he reminded the Congress and the American public that as a nation "[w]e do big things."

That was then. This is now: We as a country may do big things, but politicians didn't do them in 2011. And they won't be doing them in the run up to the 2012 elections. The bulk of what they will be able to accomplish prior to the elections may be evident by February 29—the Wednesday at the stroke of midnight when the payroll tax holiday, unemployment insurance, and the "doc fix" expire unless extended further. As the parties seek to frame the narrative going into the November elections, they undoubtedly will push legislative proposals designed to appeal to core constituencies without much expectation that they will be enacted into law. In other instances, such as continuing the discussion on comprehensive tax reform, they will establish the parameters by which legislation is likely to move in 2013 or 2014, with potential far-reaching financial consequences for businesses in every sector of the economy, as well as for individual taxpayers. Meanwhile, fierce regulatory battles will continue, as the Administration continues to implement financial services reform, health care reform (the scope of which will depend in part on the Supreme Court), and its environmental agenda. Washington will be busy, but as with last year not much is likely to become law before November.

The first session of the 112th Congress is likely to be remembered as one of the least productive in decades. When the President signed into law the National Defense Authorization Act for FY 2012 on New Year's Eve, it became Public Law No. 112-81. Having fallen seven short of the 88 bills enacted in 1995, the first session of the 112th Congress produced the fewest number of bills signed into law since Congress formally began keeping track in 1947. With a flurry of signatures on January 3, the President helped this Congress eke out of last place with a total of 90 bills signed into law. Of those, 25 bills extended current law (*e.g.,* four separate bills were enacted to reauthorize the Federal Aviation Administration for a short period of time), 13 bills named a post office or a court house, and at least five bills were of a commemorative nature or provided for service appointments (*e.g.,* bills awarding the Congressional Medal of Honor and providing for citizen regent appointments to the Smithsonian Institution).

When the second session of the 112th Congress gathered last night for the President's State of the Union Address, it did so at a time when its approval rating had hit some of the lowest levels in nearly four decades. An ABC News/*Washington Post* poll released on January 16 found that just 13% of the American public approve of the job Congress is doing, while 84% disapprove—the worst numbers in that poll since 1974. Separately, a CNN/ORC International poll was even harsher—11% approval and 86% disapproval. But at least Congress has improved upon the 9% approval rating recorded in an October CBS News/*New York Times* poll.

Beyond agreeing to legislation to extend the payroll tax holiday, unemployment insurance, and the "doc fix" that Congress has enacted every year since 1997 to avoid steep cuts in the reimbursement rate for physicians who treat Medicare patients, little else is likely to get done before the November elections. The bar has been set so low that, as Senator Joe Manchin (D-WV) recently put it, "even a hard-charging fast-digging mole" couldn't find it. Then again, the bar could be even lower. In the run-up to the Civil War, on May 25, 1856, a House Member attacked abolitionist Senator Charles Sumner of Massachusetts on the Senate floor, beating him unconscious, three days after he addressed the Senate on the issue of whether Kansas should be admitted to the Union as a slave state or a free state.

On the short "must-do" list of other bills likely to be addressed in the next few months, Congress must pass legislation to enact a breakthrough compromise to reauthorize the Federal Aviation Administration and also must extend or reauthorize the nation's surface transportation programs. Before the year is out, it also must pass legislation to reauthorize current law to enable the Food and Drug Administration to continue its current programs for the review and approval of new drugs and medical devices. And in theory Congress should decide early in the year whether to extend corporate and individual tax breaks that expired at the end of last year and should by later in the year be able to move a series of appropriations bills since the overall top-line spending number was established last year as part of the Budget Control Act of 2011. But with both parties in full election mode, little else will get done until after the elections—when Congress must come to grips with the looming expiration of the Bush tax rates and the AMT "patch" and the potential impact of severe, automatic budget cuts triggered by the Budget Control Act of 2011, one half of which will be borne by the Pentagon.

Last night, in his third State of the Union Address, the President had the chance to lay out the case for his reelection to an audience of approximately 40 million Americans, an opportunity he won't get again until he gives his acceptance speech at the Charlotte Motor Speedway on September 6. Although nominally a report on the "state of the union," the speech served as the de facto opening of the 2012 campaign. The speech thus gave the President an opportunity to meld a report on an improving economy with his ambitions for the balance of this term and the second one he hopes to secure in November. And it gave him an opportunity to remind the American public how much business has been left unfinished by the current Congress.

As he prepares for reelection, the President faces enormous challenges given the state of the economy. Through December, the unemployment rate had hovered around 9.0% or higher throughout most of his first term. No President since President Franklin D. Roosevelt has faced the unemployment rate the President now faces (8.5%) going into a reelection campaign. In addition, the nation faces the potential for further economic dislocation if Europe were to implode over the debt crisis and the certainty of a huge spike in oil prices if the situation in Iran were to spin out of control. And if those risks were not enough of a potential drag on the economy, GDP is unlikely to increase fast enough to lower the unemployment rate substantially by November. And yet, and yet.

On January 26, 1982, President Ronald Reagan appeared before the 97th Congress to give his first State of the Union Address. With the prime rate of interest having reached an all-time high (21.5%) shortly after the 1980 election and the unemployment rate having reached 8.6% by the time he addressed Congress, his approval rating had fallen to 47%. President Reagan's popularity--and apparent reelection prospects--declined even further over the ensuing year. In March 1982, the Associated Press was reporting that "[m]ost Americans are turning against President Reagan because of concerns about the economy and hope he does not seek a second term." By the time he delivered his second State of the Union Address on January 25, 1983, unemployment had risen to 10.4% and his approval rating had fallen to 35%. But by January 1984 the economy had begun to turn around and the unemployment rate had fallen to 8%. The rest is history.

As President Obama's reelection campaign moves into overdrive in 2012, the press is likely to make frequent references not to Reagan but to President Harry S. Truman, an incumbent who succeeded in his 1948 presidential campaign by running against Republican Thomas E. Dewey and a "do nothing" Republican Congress. The President undoubtedly will adopt elements of the Truman model and will make frequent references to Teddy Roosevelt, echoing the speech he gave last month in Osawatomie, Kansas. But whatever the rhetoric, his actions and the narrative his campaign team ultimately develops are more likely to meld those of three Presidents of more recent vintage, especially if the economy continues to improve: President Bill Clinton, who, in addition to engaging in triangulation (positioning himself between the extremes of both parties), adopted a more conservative tone and used executive power and "small ball" issues to build the base that would carry him to reelection in 1996; President George W. Bush, who made the 2004 election largely about his opponent and who implemented a reelection campaign built around targeting a core base of voters--irrespective of party affiliation--and getting them to the polls in November; and, if the economy continues to improve, President Reagan, who ran on the optimistic theme that "[i]ts morning in America again."

The Clinton Precedent. Like President Bill Clinton before him, President Obama to a degree already has embraced "triangulation," as evidenced by the withering criticism he has received from both the right and the left, especially on foreign affairs issues. President Clinton adopted three other tactics that are looking increasingly familiar: (1) he adopted a more fiscally conservative tone, message, and proposals; (2) he sought to achieve consensus on "small-ball" bipartisan legislative proposals that connected with the American public (*e.g.,* school uniforms) rather than complex and controversial measures (*e.g.,* health care); and (3) he used his constitutional power to implement other elements of his agenda through Executive Orders and regulations (*e.g.,* firearms control) when he could not get Congress to act. Notwithstanding the 1994 elections in which voters repudiated the first two years of his presidency by giving Republicans control of Congress, Clinton cruised to reelection in 1996.

President Obama began implementing a similar strategy late in 2010 following an election in which House Republicans gained control of the lower chamber and Senate Republicans added six seats to their ranks. While Clinton's triangulation strategy conjures images of the 1996 State of the Union Address in which he declared that "[t]he era of big government is over," President Obama's embrace of triangulation became quite evident during the surprisingly productive lame-duck session in December 2010, when he was able to broker a bipartisan compromise to extend the Bush-era tax rates. In addition, with the support of the Republican establishment, he was able to achieve ratification of the New START Treaty. And in a move significant to his base, he persuaded Congress to repeal the military's "Don't Ask, Don't Tell" policy.

President Obama has also shown a willingness to triangulate in the field of foreign policy. In several ways, he has prosecuted the war on terror reminiscent of a conservative Republican not a liberal Democrat. He can (and will) take credit for giving the order that enabled Seal Team Six to kill Osama Bin Laden. Under his direction, drones have been used to kill much of the rest of the leadership of Al Qaeda, including 600 combatants since May 2010 alone. Then again, despite an explicit campaign promise, Guantanamo Bay remains fully operational today. And yet the President seized upon public dissatisfaction with the length of the war in Iraq by ordering the last remaining troops home at the end of 2011 and he has committed to ending the war in Afghanistan. In doing all of these things, he has taken flak from the extreme left and right, but seems to have connected with the majority of Americans in the middle.

He is now moving to "small-ball" issues that are crucial to core constituencies and can be accomplished with little or no input from Congress. In doing so, the President is implementing an approach that combines elements of the Truman and Clinton playbooks, under the banner of "We Can't Wait." One example: In early January, with no prospect for comprehensive immigration reform moving through Congress, the Department of Homeland Security announced a subtle tweak to its green-card application process that will make it easier for undocumented spouses and minor children of U.S. citizens to remain at home while waiting for their permanent citizenship papers to be processed. Under prior policy, they would have had to apply for their papers from outside the United States—a wait that could last for years. Now they can do so from home, avoiding the need to travel abroad and thus to be separated from their families. Last summer, the same agency put criminals ahead of pregnant women and nursing mothers on the priority list for deportation. These may be small changes that have gone largely unnoticed by the general public, but they resonated among Hispanics, a constituency that is vital to the President's reelection bid.

The President also has moved decisively to use what he believes is his inherent constitutional authority to advance policy by appointing Richard Cordray as head of the Consumer Financial Protection Bureau and three individuals to the National Labor Relations Board, giving Democrats a majority. Faced with Republican opposition to Cordray's appointment and unwilling to compromise with Senate Republicans who had offered to approve many nominations in return for the White House committing that the President would "respect the practice and precedent of recess appointments," the President went to Ohio--a key battleground state--to place Cordray in office while the Senate was out of town over the holidays. Republicans have argued the move is unconstitutional and lawsuits already have been filed to challenge any action by the NLRB. Not surprisingly, consumer advocates and labor--two other core constituencies critical to the President's prospects in November--applauded the move.

The Bush Precedent. In 2004, the Bush-Cheney campaign team built a campaign around attacking Senator John Kerry and getting more people to the polls, irrespective of party affiliation. Through the use of sophisticated micro-targeting, the campaign was able to identify potential voters overlooked by Democrats and to get them to the polls, with Ohio being one of the most notable examples of this successful effort to go beyond the President's traditional base to find potentially receptive voters.

Given the challenging economic environment the President faces, his campaign will undoubtedly be built in part around the Bush II strategy of seeking to vilify his opponent, regardless of whom Republicans choose as their nominee. And his team in Chicago is already using far more powerful and sophisticated software than was available eight years ago to identify potentially sympathetic voters, and once identified to persuade them to support the President by going to the polls to vote for him.

Two examples of efforts to motivate core constituencies: On January 14, through a blog posting, the White House made clear that it opposed central elements of two major anti-piracy bills pending before Congress, while expressing support for a central element of Hollywood's goal of combating Internet piracy. As the posting put it, "[o]nline piracy is a real problem that harms the American economy, threatens jobs for significant numbers of middle class workers and hurts some of our nation's most creative and innovative companies and entrepreneurs." But, it added in a significant nod to Netizens and other opponents of the legislation, "[w]e will not support legislation that reduces freedom of expression, increases cybersecurity risk or undermines the dynamic, innovative global Internet."

Then, last Wednesday, the State Department rejected the Keystone XL pipeline application to move Canadian oil sands to the United States Gulf Coast region, citing the need for additional time to complete its review beyond the 60-day window provided by Congress. In its release, the Department noted that "[t]he President concurred with the Department's recommendation, which was predicated on the fact that the Department does not have sufficient time to obtain the information necessary to assess whether the project, in its current state, is in the national interest." With the prospective change of the pipeline route to avoid sensitive environmental areas in Nebraska under consideration, the Department noted that its "denial of the permit application does not preclude any subsequent permit application or applications for similar projects." In other words, it might yet approve the pipeline--after the election--once the new route has been selected.

Thus, within one week, two actions designed to appeal to two other important constituencies: Silicon Valley and environmentalists. Notably, both decisions were announced by someone other than the President--a traditional approach in an election year--creating greater flexibility for him to take a more nuanced position on the campaign trail.

The Reagan Precedent. As noted above, President Reagan faced an equally bleak economy when he gave his first and second State of the Union Addresses. But by the third one the unemployment rate had begun to fall. Factory orders had picked up. People felt more optimistic.

President Reagan captured that mood with a campaign built around it being "Morning in America." Having faced similar challenges at comparable periods in his presidency, President Obama undoubtedly will want to capture what his advisors hope will be a similar shift in the public's mood with a campaign theme built around the narrative that "Things Are Getting Better," especially for the middle class, as long as the economy continues to improve.

With the President now largely embracing a mode of governing that doesn't depend on Congress for action, what can we expect this year? And how will the separate institutional challenges facing House Speaker John Boehner and Senate Minority Leader Mitch McConnell affect the dynamic? House investigative committees are likely to be active, as they seek to challenge existing Administration programs in the run up to the elections. Speaker Boehner may reach the point at which his caucus needs to be in favor of something major that can become law before November. Leader McConnell has made it clear that defeating President Obama remains his highest priority, but recapturing control of the Senate may require a different approach. He too may see the need to support legislation that has a chance of being enacted. The House and the Senate could come together on cyber security legislation, for example, as part of the overall effort to find common ground with the President, who already has sent proposed legislation to Capitol Hill.

In the Republican response last night, Indiana Governor Mitch Daniels began framing the debate for Republicans going into the second session of the 112th Congress:

> 2012 must be the year we prove the doubters wrong. The year we strike out boldly not merely to avert national bankruptcy but to say to a new generation that America is still the world's premier land of opportunity. Republicans will speak for those who believe in the dignity and capacity of the individual citizen; who believe that government is meant to serve the people rather than supervise them; who trust Americans enough to tell them the plain truth about the fix we are in, and to lay before them a specific, credible program of change big enough to meet the emergency we are facing.
>
> We will advance our positive suggestions with confidence, because we know that Americans are still a people born to liberty. There is nothing wrong with the state of our Union that the American people, addressed as free-born, mature citizens, cannot set right. Republicans in 2012 welcome all our countrymen to a program of renewal that rebuilds the dream for all, and makes our 'city on a hill' shine once again.

As noted above, not much prior to November is likely to get to the President's desk. But some things need to get done. And other initiatives--such as preparing policy options for fundamental tax reform--will frame the debate for 2013 and 2014, irrespective of who is in the White House and which party controls the Senate and the House. And of course regulatory battles over financial services, health care, and the environment will continue unabated. We discuss below some of the issues to be addressed by Congress and the Administration.

"Must Pass" Legislation

Almost five years to the day after President George W. Bush transmitted his FAA reauthorization proposal to Congress and 22 short-term extensions later, a breakthrough deal was struck in the week leading up to the State of the Union Address, paving the way for Congress to take up and finally enact a multi-year FAA reauthorization bill. With the current extension set to expire on January 31st, one final short-term extension will be required to provide Congress time to bring up and send the compromise bill to the President.

With work on the FAA reauthorization complete, attention will quickly turn to the nation's surface transportation programs, which are set to expire after the eighth short-term extension on March 31. The President has continued to call on Congress to reauthorize the program to create jobs by rebuilding America's roads and bridges. Last night, he urged Congress to "[t]ake the money we're no longer spending at war, use half of it to pay down our debt, and use the rest to do some nation building here at home."

Both the House and Senate are poised to make a strong push to enact a multi-year reauthorization, eager at both the leadership and much of the rank-and-file level to hold out the transportation bill as a signature job-creating accomplishment. The House Transportation and Infrastructure Committee will likely mark up its version of the bill in early February as part of a swift march to the floor. In the Senate, the Banking Committee is poised to release and mark-up the mass transit title shortly, with the Senate Environment and Public Works Committee having already marked up the highway title and the Senate Commerce Committee having reported its freight and motor carrier safety provisions.

However, notwithstanding the President's suggestion that Congress use one half of the war savings, the fundamental questions of how to pay for the legislation and what its duration should be remain unresolved, with the gas tax revenues that support the Highway Trust Fund continuing to decline as fuel efficiency continues to increase. The House is expected to move forward with a five-year reauthorization bill, known as the American Energy and Infrastructure Jobs Act, that will expand domestic energy production and use the new royalties generated to help fill the approximately $65 billion shortfall in the Highway Trust Fund over the next five years. Increasingly, however, the indications are that the House's proposed energy revenues will not on their own produce the revenue needed to make up for the shortfall in the Highway Trust Fund and maintain current spending levels. And the use of royalties from offshore oil and gas production is likely to face strong opposition from most Democrats. For its part, the Senate is moving forward with a shorter two-year bill requiring $12 to $13 billion in as-of-yet-undetermined offsets. The Senate Finance Committee has been unable to reach a bipartisan accord on offsets for a two-year bill, although pressure to do so will increase once the Banking Committee marks up its bill and the revenue title is all that stands in the way of merging the titles and moving a bill to the floor.

Ultimately, given the complexities involved, it may be difficult for Congress to reach any agreement by the March 31 deadline, requiring at least another short-term extension of surface transportation programs.

Separately, Congress must pass legislation to reauthorize the Prescription Drug User Fee Act (and the comparable act for medical devices) to enable the Food and Drug Administration to continue its current programs for the review and approval of new drugs and devices. Without reauthorization, FDA will be forced to furlough or lay off drug and device reviewers, thereby disrupting that essential process and frustrating the affected industries (whose financial well being and planning is dependent on a well-funded and functioning review process) as well as numerous patient and disease groups. Conventional wisdom suggests that the two parties will find a way to get this done before the end of the fiscal year. Given that this legislation could be the last major train leaving the station prior to the November elections, it could become a legislative vehicle to carry many unrelated items.

Tax Policy

"The tax code is 10 times the size of the Bible, with none of the good news."

--House Ways and Means Committee Chairman Dave Camp (R-MI)

In his State of the Union Address last year, President Obama recognized the need for the first fundamental rewrite of our nation's tax laws since 1986. Over the course of the year, the House and Senate leadership and the tax writing committees began to tackle comprehensive reform with the goal of reducing rates for corporations and individuals while broadening the tax base in an effort to create a pro-growth tax code. Last night, Governor Daniels endorsed this effort, calling for a "dramatically simpler tax system with fewer loopholes and lower taxes."

Notwithstanding the long-term importance of getting the code right, Congress faces more immediate concerns. Congress must deal head-on with a striking array of tax issues in 2012, including extension of the payroll tax cut, whether and how to extend the Bush tax rates, the Alternative Minimum Tax "patch," and business and individual tax "extenders." While this debate occurs, fundamental reform discussions will be just that--discussions--until voters have had the chance to speak in November. Importantly, these discussions--and potential competing tax plans that will emerge this year--will almost certainly establish the framework by which Congress will approach fundamental reform in 2013 and beyond.

Comprehensive Tax Reform. Despite broad concurrence that reform is necessary and desirable, major philosophical differences between the parties over tax rates, particularly for upper-income taxpayers, make it almost certain that fundamental reform will not be achieved prior to the 2012 elections. Indeed, these differences were part of the reason the "Super Committee," as well as President Obama and Speaker Boehner, were unable to reach agreement on a major deficit reduction plan last year.

The tax policy debate will proceed at an even more robust level in 2012 than it did last year as the Obama Administration attempts to seize the high ground on voter concerns over growing income inequality and existing tax rules perceived to help only the most wealthy and sophisticated taxpayers. This political dynamic was only further reinforced by recent news reports that Republican presidential candidate Mitt Romney paid a significantly lower tax rate on his investment income from his private equity firm than middle-class Americans paid on earned income.

While the Super Committee ultimately failed in 2011 to reach a deficit reduction agreement, there was significant progress in developing a bipartisan framework for combining a reduction in the current 35% corporate rate (one of the highest in the industrialized world) with targeted, revenue-raising reforms. Chairman Camp, for example, put forward a draft bill that would move the United States toward a territorial system of taxation, the approach used by most of our economic competitors, including those nations that make up the Organization of Economic Development. The Super Committee was not, however, close to agreement on reform of the code for individual taxpayers. While President Obama is not expected to include a tax reform plan within his FY 2013 budget proposal, he is expected to include many of the corporate and individual tax offsets that figured heavily in the Super Committee's deliberations, such as scaling back research credits and deductions, deferral mechanisms for overseas profits, deductions for domestic manufacturing activities, last-in/first-out accounting methods, the taxation of carried interest, and various other targeted tax expenditures, including those aimed at the oil and gas industry.

On the individual side, President Obama will certainly continue to press to end the Bush tax cuts for "upper-income" taxpayers. The President indicated last night that he wants Congress to provide incentives for manufacturing companies to bring jobs back to the United States. We fully expect that he will recommend new tax breaks for the middle-class, including increasing the Child and Dependent Care Tax Credit, requiring employers to provide automatic direct-deposit IRAs, and expanding the Saver's Credit.

Expired and Expiring Tax Provisions. Beyond the longer term corporate and individual tax reform debate, there are other pressures that will make 2012 an active year for tax policy. First, as noted above, the Obama Administration and Congress must reach agreement before the February 29 deadline on extending the payroll tax cut and long-term unemployment benefits. Disagreements persist as to whether, and how, to offset the cost of this legislation, with Congressional Republicans demanding spending cuts and Congressional Democrats preferring tax increases (or no offsets at all). Last night, the President noted that “[t]here are plenty of ways to get this done.” He urged Congress to act without raising side issues, without drama, and without delay.

Second, absent Congressional action, the 2001 and 2003 Bush tax rates will expire at the end of December 2012, raising tax rates for all individual taxpayers (including pass-through businesses), irrespective of income level. This issue is not likely to be resolved prior to the election, as President Obama has indicated he will not sign legislation that extends the Bush tax rates for upper-income taxpayers, a scenario Congressional Republicans will work to avoid at all costs as they view lower rates on business owners, a key political constituency, as critical to job creation.

Third, Congress must also “patch” the AMT for 2012 in order to ensure that roughly 20 million Americans do not fall prey to this stealth tax when they file their 2012 taxes early next year. Congress has consistently done so in the past, but the challenge will be even greater this year given the enormous “cost”--roughly $90 billion--in doing so.

Fourth, as further discussed above, Congress must deal with extending funding for the Highway Trust Fund. The plan currently pending in the Senate requires roughly $12 to $13 billion of offsets in order to fully pay for the legislation. While it is not a given Congress will ultimately include tax increases to make up this difference--Congressional Republicans would prefer spending cuts and/or other nontax revenue increases (*e.g.,* royalties from increased offshore oil and gas production)--neither can it be ruled out, particularly if Congressional Democrats push for tax offsets.

Finally, Congress must deal with the just-expired business and individual tax “extenders” including the research and development tax credit, the active financing exception, various energy tax provisions, and a host of others.

Financial Services

Wall Street Reform. President Obama spoke briefly about financial services regulation, noting that the rulemakings approved in 2011 by federal regulatory agencies assisted individuals in "getting funding to entrepreneurs with the best ideas, and getting loans to responsible families who want to buy a home, start a business, or send a kid to college." President Obama also discussed high-profile provisions in the Dodd-Frank Wall Street Reform and Consumer Protection Act, noting that these new safeguards, including requiring "living wills" for financial institutions, restrictions on banks' proprietary trading activities, and enhanced prudential standards for systemically important financial institutions, will mean that financial institutions will no longer "make risky bets" with their customers' deposits. Similarly, the President noted that, because of the creation of the Consumer Financial Protection Bureau, American consumers “finally have a watchdog in Richard Cordray," the newly appointed Director.

It is important to remember that, in contrast with the successes identified by the President, numerous proposed rulemakings drafted by federal regulatory agencies have not yet been finalized. As a result, 2012 will continue to see a push for financial reform regulation implementation, while Republicans in Congress attempt to delay finalizing these rules or repeal of some of the more contentious provisions.

Housing Finance Market. President Obama also focused on efforts related to increases in refinancing options and reductions on improper foreclosure activities in order to assist in the country's mortgage crisis recovery. He stated that the Administration will send a plan to Congress that would allow refinancing at historically low rates, saving homeowners about $3,000 per year. This plan will allow homeowners, regardless of whether their loans are owned by Fannie Mae, Freddie Mac, or private investors, to refinance. President Obama's refinancing plan is expected to cost approximately $10 billion and will need Congressional action because it will require that the Federal Housing Administration guarantee certain mortgages that exceed the property's value. The President is expected to flesh out the details of the plan and present it to Congress in the next three to six weeks, though support from Congress is unlikely in 2012. Of note, President Obama's remarks did not include a mention of the "Real-Estate Owned (REO) to Rental" program. This program is expected to be announced by the Federal Housing Finance Agency (FHFA) soon. The President's references to the current state of the housing finance market come after pressure from House Republicans to more forward in winding down the government-sponsored enterprises (GSEs), Fannie Mae and Freddie Mac, and adopting GSE reform that brings private market investment back into the U.S. housing market. Although 2012 may not see comprehensive GSE reform, this year Congress will have a chance to build the strategic framework for reform to be considered in 2013.

Oversight and New Fees. President Obama announced the creation of the Unit on Mortgage and Securitization Abuses to investigate the misconduct and illegalities that contributed to the current mortgage crisis. This new unit will "help turn the page on an era of recklessness that hurt so many Americans" and will be headed by New York Attorney General Eric Schneiderman. In this context, President Obama also announced the creation of a new Financial Crimes Unit "to crack down on large-scale fraud and protect people's investments." Further, as a means of ensuring that, as he put it, large financial institutions that were bailed out during the crisis can "repay a deficit of trust," President Obama proposed to impose on them a "small fee." This proposal, similar to the 2010 proposal for a "financial crisis responsibility fee," would ensure that the President's refinancing plan does not add to the deficit and would have to be approved by Congress before implementation. The 2010 proposal failed in a Democratic-led Congress and it is likely to fail in 2012 as well.

Budget/Appropriations

Completing work on appropriations legislation in presidential election years has consistently fallen to the lame duck session after the election--or even later--in recent history. For FY 2009 (which began October 1, 2008), for example, Congress passed the final omnibus appropriations bill well after President Obama's inauguration--in March of 2009. The same occurred in the year of President George W. Bush's reelection, as FY 2005 appropriations were enacted in December 2004. After President Bush's initial election, FY 2001 appropriations were finally approved in the December 2000 lame duck session after 21 Continuing Resolutions had been enacted to keep the government in business from one to the next.

Even absent the dynamics of the presidential election, final work on appropriations has not been completed before December 19 in any year during President Obama's presidency--with Congress passing omnibus appropriations bills in the final days before its holiday recess in both FY 2010 and FY 2012; and with the FY 2011 process dragging more than six months late into April 2011, creating the specter of a government shutdown.

The President will send his budget to Capitol Hill on February 13, one week after the statutory date set for its submission. The battle-weariness and public backlash from last year's budget standoffs--first over a threatened government shutdown and then over raising the national debt ceiling--and proximity to the election suggests that 2012 will not see further budget brinksmanship threatening continuing appropriations for FY 2013. That being said, especially in light of the President's proposal to reduce and refocus defense spending, the spending bills are certain to be an ideological football figuring prominently in election year discourse, even if this translates into little meaningful legislative action.

While these factors point towards appropriations being part of a post-election, lame duck legislative session, there are counter factors to consider as well. Most significantly, as noted above, the Budget Control Act of 2011 has set the top-line number for appropriations. That theoretically should reduce the need for a battle over the total level of domestic discretionary spending for FY 2013, and theoretically should make the job of producing and passing the appropriations bills that much easier. And, unlike past years, there also should be plenty of floor time in the Senate for appropriations this year. On the other hand, since the $1.2 trillion in sequestration resulting from the Budget Control Act (and subsequent Super Committee failure) begins to take effect in January 2013, Members may make a major effort to address this issue as part of a "mega-deal" in the post-election legislative session.

Energy Policy

In 2008, then-candidate Barack Obama made enactment of comprehensive energy/climate change legislation a core part of his campaign. With the 111th U.S. Congress having rejected President Obama's renewable energy agenda, there was little hope that the President could advance his agenda last year. We see little prospect for anything meaningful being accomplished on Capitol Hill this year either. Making energy policy a central element of his speech last night, the President renewed his call for Congress to adopt a clean energy standard "that would create a market for innovation." But echoing a central tenet of the energy agenda put forward by Republicans, he also endorsed an "all of the above" strategy as well, making the case for increased domestic energy production, with a particular emphasis on developing our nation's vast natural gas resources.

In the absence of legislation, the Administration will continue to pursue the regulatory agenda it set last year, including implementation of the President's clean energy and sustainability initiatives at the Department of Defense and the General Services Administration. Last night, for example, the President indicated that the Department of Defense would make one of the largest commitments to clean energy in history, "with the navy purchasing enough capacity to power a quarter million homes for a year." And notwithstanding Republican efforts to shut them down, the Environmental Protection Agency will continue to move forward with its climate agenda.

Notwithstanding the President having embraced central tenets of the energy policy put forward by Congressional Republicans, such as expanding offshore oil and gas production, we continue to expect a great deal of sturm and drang on Capitol Hill. Given the Administration's rejection of the Keystone XL pipeline for now, House Republicans in particular are likely to continue to pound the President for "killing jobs" and failing to advance our national security.

They are developing legislation that will move the decision making authority away from the State Department, including giving it to themselves. We understand the logic of their approach, but we cannot envision a scenario in which the legislation will be enacted.

Separately, given the situation in the Middle East and the likelihood of steadily rising gasoline prices (which would spike dramatically if Iran were to seek to close the Strait of Hormuz even for a day), Republicans will continue to push a pro-development, pro-national security agenda. They will seek, for example, to use royalties from expanded offshore drilling to support highway bill funding. But none of the stand-alone pro-development bills they produced in the first session got anywhere in the Senate, and none of the next batch is likely to do so either, not least because the President will act unilaterally to open additional offshore areas for potential production.

By contrast, Senate Democrats will likely try to keep the focus on their clean energy agenda. Majority Leader Harry Reid has already expressed his intention to move to clean energy legislation this summer, just as gasoline prices are expected to spike as people drive more at vacation time. But this is likely to be simply an exercise in forcing Republicans to take votes that can be used against them in the run up to the November elections and that Democrats can use to appeal to their environmental base. In the end, nothing is likely to get out of the Senate, let alone to the House and on to the President's desk.

Trade Policy

Two years ago, President Obama pledged to double America's exports in five years and create 2 million jobs. Last night, the President asserted that his Administration is well on track to meeting this goal one year ahead of schedule, with exports now running at about $180 billion per month, up from $140 billion per month two years ago. According to most economists, increased exports have been one of the main catalysts driving the recovery, representing roughly half of the domestic economic growth since the end of recession. The President also referred to the successful passage of the three Free-Trade Agreements that were submitted to Congress in 2011: Korea, Colombia, and Panama. The U.S.-Korea Free-Trade Agreement was the largest and most important bilateral trade agreement entered into by the United States since NAFTA.

In his remarks, the President also highlighted the Administration's vigilance in enforcing U.S. trade laws, particularly with respect to China. The announcement of a new Trade Enforcement Unit, "charged with investigating unfair trade practices in countries like China" underscored that focus. The details of the new enforcement unit have not yet been put forward.

Looking forward and building on that success, the President is now focused on the Trans-Pacific Partnership (TPP), an ambitious effort to create a multi-country regional trade agreement by the end of 2012. In addition to the nine countries involved in the TPP talks at the beginning of 2011 (United States, Australia, New Zealand, Chili, Peru, Brunei, Vietnam, Singapore and Malaysia), Japan, Mexico, and Canada all joined in the discussion during last year's Asia Pacific Economic Cooperation summit. This will greatly expand the economic significance of the agreement.

To emphasize the Administration's commitment to streamlining efficiency in government reform, the President also referenced his recent proposal to reorganize the trade agencies of the Federal Government, which would include consolidating the Office of the U.S. Trade

Representative into a larger trade department under the umbrella of the Department of Commerce. The initial congressional reaction from both Democrats and Republicans to that proposal has been cool. Nonetheless, the President will press Congress to pass legislation that will give him the authority enjoyed by every President from Herbert Hoover to Ronald Reagan (with the exception of President Gerald Ford) to reorganize the government, subject to expedited review by Congress. And he will specifically propose this reorganization, with the recommendation that Congress use an expedited process without amendments, so as to make the reorganization legislation easier for Congress to approve.

Two other items on the Administration's trade agenda are worth noting. The President's "fast-track trade negotiating" authority or "trade promotion authority" expired four years ago and must be renewed for the Administration to enter into future trade agreements, particularly the TPP. Obtaining congressional approval of TPA in an election year poses several political challenges and could set the stage for a contentious debate between Republicans and Democrats later this year. The other trade initiative that should be considered by Congress this year is extension of Permanent Normal Trading Relations (PNTR) for Russia, now that it has acceded to the World Trade Organization (WTO). As with the exercise that Congress undertook when China acceded to the WTO, the United States must repeal the application of the Jackson-Vanik amendment to Russia before the United States (and U.S. exporters) can benefit from the advantages accruing to other trading nations when Russia became a WTO member. Congressional support as well as enthusiasm from the business community has been muted up until now. As a result, a major boost from the White House will likely be needed to repeal Jackson-Vanik. The President made an oblique reference to this when he mentioned market access to Russia.

Spectrum Legislation

In his State of the Union Address last year, the President spoke of his goal of making broadband accessible to all Americans. Last night, the President lamented that the nation still has "[a]n incomplete high-speed broadband network that prevents a small business owner in rural America from selling her products all over the world." Funding for a nationwide broadband network almost came to fruition at the close of 2011 as lawmakers worked during the final hours of the session to iron out long-term payroll tax holiday legislation that would have included spectrum incentive auctions to help make way for broadband technologies. As noted above, a House-Senate conference committee must find ways to pay for a further extension of the payroll tax holiday measure and other provisions by February 29. Spectrum incentive auctions will likely be among the "pay-fors" lawmakers consider as they seek to broker a long-term agreement before the short-term fix expires.

Three of the most senior House conferees have worked to draft competing versions of spectrum bills that emerged from the Energy and Commerce Committee, one largely supported by Republicans and another largely by Democrats. By contrast, a bipartisan bill emerged from the Senate Commerce Committee, but none of the most senior Members of the committee are conferees. Assuming they have time to resolve substantive differences, there are numerous issues to be resolved before the legislation will be ready as a potential amendment in conference. For example, public safety and municipal groups have been critical of the House Republican Jumpstarting Opportunity Through Broadband Spectrum (JOBS) Act because it contains a proposal to return public safety "narrowband" spectrum that first responders now use for voice communications to the Federal Communications Commission (FCC) and because if its governance model for the broadband network. Senate conferees are more likely to favor including the bipartisan Senate spectrum bill, S. 911, as an alternative to the House bill. While the Senate spectrum bill includes approximately $11 billion for the new public safety broadband network, Republicans in both chambers worry that S. 911 would not dedicate sufficient auction proceeds to deficit reduction. Other issues also remain sticking points, including approaches to allocating spectrum for unlicensed use and protecting television broadcasters that do not relinquish their spectrum to the FCC for auction and would have to relocate their channels.

Conclusion

As a firm with deep public policy roots, we are proud of our ability to help clients exercise a right enshrined in the U.S. Constitution by petitioning their government. We have been at it since 1965, when Jim Patton encouraged a young White House aide named Tom Boggs to help him build a different kind of law firm, one that understood that all three branches of government could provide solutions to challenging problems. By combining political know-how, legislative experience, and substantive knowledge of the law, they had a vision for helping clients achieve success. Since then, we have further developed the range of our capabilities, including more recently through the use of social media and other means of cutting-edge technology to give our clients an edge in seeking to achieve their legislative and regulatory objectives. For our paying and pro bono clients alike, we look forward to helping them achieve their legislative and regulatory objectives in the run up to the November elections and inevitable “lame duck” session that will follow.