

President-elect Barack Obama and the 111th Congress

What to Expect

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Writing to Thomas Jefferson, who had been out of the country during the Constitutional Convention, James Madison explained that the Constitution's framers considered the Senate to be the great "anchor" of the government. To the framers themselves, Madison explained that the Senate would be a "necessary fence" against the "fickleness and passion" that tended to influence the attitudes of the general public and Members of the House of Representatives.

Upon his return from France, Thomas Jefferson visited George Washington. Sipping hot coffee during their conversation about why the Convention delegates had created a Senate, Jefferson poured some coffee into his saucer. "Why did you do that?" asked Washington. "To cool it," said Jefferson. "Even so," responded Washington, "we pour legislation into the senatorial saucer to cool it."

--Adapted from the History of the Senate

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Introduction

President-elect Barack Obama is the first sitting Senator elected to the White House since 1960. He will begin his Presidency with a base of power his party has not seen since the elections of 1964 and 1974-76, which resulted in sweeping changes enacted by Congress. This will provide unprecedented opportunities, but also great challenges in meeting the expectations of a Democratic coalition that has not controlled the White House, the Senate, and the House since 1993-94.

Notwithstanding having spent only four years in the Senate, President-elect Obama has more Washington experience than Bill Clinton, George W. Bush, Ronald Reagan, and Jimmy Carter, the four governors who assumed the office in the past 32 years. Unlike them, he will not bring to the White House a home-state “posse” that knows a lot about a state capital but not much about the Nation’s Capital. We expect that his Administration will have comparatively more congressional staffers and fewer campaign staffers in senior policy making positions than more recent administrations. Moreover, his running mate has spent 34 years in the Senate, during which he has led two of its more important committees. Finally, with his selection of Representative Rahm Emanuel (D-IL) as Chief of Staff and Phil Schiliro as Assistant to the President for Legislative Affairs, he will have by his side very experienced individuals with a deep understanding of the relationship between Congress and the Executive Branch. As a result, President-elect Obama may have a better opportunity to engage earlier and more effectively with the Congress and should have a much easier time smoothing relations with the federal bureaucracy. Given the likely central role of the Senate in shaping policy for the next two years, President-elect Obama’s four years observing its members, its rhythm, and its idiosyncratic ways may help him avoid the missteps that often throw off stride newly elected presidents.

As a result of the election, Democrats now enjoy increased majorities in the House and in the Senate. (Because of likely recounts and a runoff in the Georgia Senate race, we will not know final election results for many weeks.) When the 111th Congress begins work in January, House Speaker Nancy Pelosi is likely to offer a 100-*hour* legislative agenda, which we expect will include an economic stimulus bill, union organizing (“card check”) legislation, a further attack on “Big Oil,” potential health care legislation (such as SCHIP, which President Bush vetoed), and embryonic stem cell research legislation. By then, President-elect Obama is likely to have outlined his Administration’s 100-*day* agenda, which we expect will focus on energy policy, healthcare reform, and a new regulatory structure for financial institutions. Across the Capitol, Senate Majority Leader Harry Reid will be assessing the prospects for moving forward on the President’s agenda with an enhanced majority, potentially in the range of 58-60.

In this environment, Republicans face stark choices. Will they try to work cohesively as a loyal opposition? Or will they seek to find common ground with Democrats when possible? Because House rules limit minority input on bills, we expect younger Members will attempt to revitalize the GOP’s platform and message by providing a sharp contrast to the majority, in the manner pioneered by Representative Newt Gingrich in the 1980s. Across the Capitol, we expect Senate Republicans--given their depleted ranks--to forge coalitions with moderate Senate Democrats in order to get things done (or to stop bills from going through the Senate).

Transition Planning

With the help of senior, very experienced Hill and top Clinton Administration staffers, President-elect Obama’s transition team is likely to be further along in developing a 100-day agenda by inauguration day than prior transition teams. Given the restrictions he has indicated he will put in

place for individuals joining the Administration as policy makers (such as requiring them to commit not to engage in post-employment lobbying while he is in office), President-elect Obama is likely to draw a relatively larger percentage of Hill staffers, academicians, and think tank members in policy making positions. Moreover, he can draw on experienced members of the Clinton Administration, as well as one or more retiring Republican Members of Congress, such as Senator Chuck Hagel (R-NE). In fact, we understand President-elect Obama has instructed his transition team to present him with a list of Republicans who could serve in senior policy positions. He thus is more likely than many presidents to have a fully formed legislative agenda with a strong team ready to move quickly in January to pursue his 100-day agenda.

Unlike other recent presidents, the new president will not enjoy the luxury of putting together his cabinet and White House staff, drafting an inaugural speech, and preparing a governing plan for the first 100 days with little regard for work underway by the incumbent president. At a time of comparable peril to the nation, President Franklin D. Roosevelt (who was elected on November 8, 1932 but did not assume office until March 4, 1933) is best remembered for the flurry of activity he undertook in his first 100 days. Less well remembered is the cold shoulder he turned when Herbert Hoover tried to engage Roosevelt to address with him the nation's looming foreign debt repayment challenge. Roosevelt saw Hoover's focus as akin to bailing out Wall Street and bankers, rather than homeowners facing foreclosure and workers looking for jobs. At one point Roosevelt reportedly said, "It's not my baby."

Given their party's solid control over both branches of government, President-elect Obama and the Democratic leadership will find themselves where President Clinton found himself in 1992 and 1993 and in a stronger position than President Bush and the Republican Party found themselves from 2003 to 2006. In charge of the government, they will be subject to high expectations, with no excuses for failure, especially from the expectant parts of their coalition. Moreover, President-elect Obama may not have the luxury of waiting until January to address the challenges now facing the economy. The larger, increased margin in the Senate will only make matters more challenging by further raising public expectations next year. If they fail to deliver by the mid-term elections, Democrats could face a political backlash that would result in significant election losses, as suffered by Democrats in 1994 and Republicans in 2006. The new administration and the Democratic leadership thus need to use the transition period to set achievable priorities acceptable to their coalition that mesh Speaker Pelosi's 100-hour agenda with the President-elect Obama's 100-day agenda, all the while continuing to work with President Bush for the remainder of the year.

What Then?

With such a large majority, Speaker Pelosi should have little trouble moving her 100-hour agenda through the House. Similarly, such a large margin may give Senate Democrats visions of being able to pursue an aggressive agenda to make up for lost ground when they were unable to overcome Republican filibusters in the 110th Congress. But will they be able to meld their agendas? House Democrats may be sorely tempted to ram through legislation on their own terms, with no input from Republicans, and Senate Democrats could be emboldened to go it alone based on the assumption that successful minority-led filibusters are a thing of the past. If the Democratic leadership were to make that mistake, they would likely fare no better than President Clinton and Democrats did with health care reform in 1993 or President Bush and Republicans did with Social Security reform in 2005.

When the 110th Congress adjourned for the elections in early October, its approval rating in three national polls ranged between 13-15%. A week before the election, the average of all major

national polls had its disapproval rating at 74.7%. By another measurement, which no doubt correlates with its low approval ratings, Congress is more polarized now than it has been since 1905-06. Under a polarization scale that compares voting patterns developed by Professor Sean Theriault of the University of Texas at Austin, the Watergate session of Congress was 29% polarized. By 2005-06, it had reached 46%, the highest level since the 58th Congress, when it reached 48% on Theriault's scale. When the final results are in, the 110th Congress could well top them all in polarity.

In this environment, with such high expectations among the American public that the new Congress will finally put partisan wrangling behind it and will work with a new president for the good of the country, one number may be as important for the prospects for President-elect Obama's 100-day agenda as 58, 59, or 60 votes in the Senate: 16, as in months. Having been elected in part based on the expectation that he would pull all combat troops out of Iraq within 16 months, President-elect Obama faces the prospect of a fractious fight within the Democratic party if liberal, anti-war House Democrats and their supporters among MoveOn.org and liberal bloggers insist on implementing that policy as a matter of law. He can't afford to lose the flexibility all Commanders in Chief need to promote the national interest.

To be successful, the new president and the next Congress need to govern from the center of the country, not from the center of the Democratic party. Notwithstanding the absolute majority Democrats will soon enjoy in the Senate, the advancement of a broad liberal agenda on the war or any other issue seems remote. In our view, moderate Democratic Senators will be the ones setting the agenda, as they seek to establish consensus that eluded the closely divided (51-49) Senate for the past two years. A coalition comparable to the fiscal Blue Dog Democrats in the House is likely to emerge in the Senate, urged on by new moderate Senators such as Mark Warner (D-VA). Such a coalition would likely establish common ground with moderate Republicans, providing the group with the means of achieving 60 votes to advance priorities for the benefit of the middle of the country, not principally for the middle of either party. They thus offer the real prospect of legislating from the center, insisting on fiscal discipline and blocking action written in haste in the House.

Indeed, on many issues, the new-found Senate Democratic majority will be no more likely to succeed in overcoming a filibuster than in the 110th Congress if it pushes proposals that tilt towards the extreme. Very few issues (perhaps no more than 5-10%) are purely partisan, party-line issues. Most issues depend much more on state and regional interests than on party affiliation. In this environment, moving legislation will continue to require coalition building, with Senators reaching across party and geographic lines to find common ground. As a result, moderate Republicans, such as Senators Susan Collins (R-ME), Olympia Snowe (R-ME), Arlen Specter (R-PA), and George Voinovich (R-OH), are likely to enjoy new popularity.

As we look ahead, the country faces the most threatening economic environment since the Great Depression. In addition to inheriting a global economic crisis of historic proportions, a domestic fiscal system under tremendous strain, and a looming health care and fiscal crisis as Baby Boomers begin retiring, President-elect Obama will be confronted by two wars, an overstretched military, the threat of a nuclear Iran, and strained relations with Russia. Deeply fundamental challenges await the new president and the new Congress.

The Possibilities of Change

From the catharsis of November 4, real prospects for change in this challenging environment are possible. How might they affect you? In the pages that follow, we sketch out our sense of what the possibility of change means in the areas of appropriations policy (including further

earmark reform), defense and national security, employment law, energy and natural resources, environmental policy, financial services, food and drug law, health care, homeland security, Native American affairs, tax policy, technology and telecommunications policy, trade policy, and transportation and infrastructure.

We look forward to the challenges ahead. 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. For our paying and pro bono clients alike, we look forward to helping them achieve their legislative objectives as President-elect Obama puts forward his 100-day agenda, the House takes up its 100-hour agenda, and the Senate acts as the saucer in which hot liquid is poured to cool.

Appropriations and Earmark Reform

On the campaign trail, President-elect Obama promised to send numerous proposals to Congress early in his Administration to implement major initiatives, including health care reform, energy reform, tax cuts for the middle class, and increased investments in public infrastructure and public education. However, the increasing federal deficit, coupled with the \$700 billion rescue bill and other likely stimulus measures, will limit the resources available to fund ongoing initiatives, let alone new ones. As a result, President-elect Obama and appropriators in both chambers will begin the 111th Congress faced with the continued pressure of allocating increasingly scarce revenues among many competing priorities.

Given President-elect Obama's focus on changing Washington, he will likely suggest changes in the appropriations process to make it more transparent and accountable to taxpayers. In addition, the recent conviction of senior Appropriations Committee leader Senator Ted Stevens (R-AK) on corruption charges (that the jury believed stemmed in part from gifts given by a corporation seeking earmarks) sets the stage for Congressional appropriators to look for other ways to make meaningful changes to the earmark process in order to curb the potential for abuse by individual Members.

The allocation of discretionary spending will shift significantly under the leadership of President Obama, Speaker Nancy Pelosi, and Senate Majority Leader Reid. Frustrated by protracted negotiations with President Bush over spending priorities over the past two years, the Democratic Congress finally has a President in the White House who will share its general spending priorities to increase funding for various domestic programs and to slow the rate of funding increases for military programs. We can expect generous spending increases for domestic programs, including health care, education, and energy, and potential reallocation of spending for defense programs. The 111th Congress will likely let President Bush's tax cuts expire and will seek to close tax loopholes, which could create new tax revenue for more domestic spending.

Finishing the FY 2009 Agenda and Beginning on FY 2010

During the short lame-duck Congressional session that begins on November 17, Congress could complete action on the pending FY2009 domestic appropriations bills. However, it is more likely that Democrats will wait until after the Inauguration of President Obama on January 20 to complete this work. The current Continuing Resolution (CR) that funds the federal government expires on March 6th, at which time Congressional leaders and President Obama will face two alternatives. Congress can pass a year-long CR funding domestic agencies at FY 2008 levels or it can roll-over the pending FY 2009 appropriations bills into an omnibus bill for quick passage through the House and the Senate. At this time, it appears slightly more likely that Congress will choose to pass a year-long CR, blame President Bush for having to do so, and simply move on to the FY 2010 process.

The benefit of passing a year-long CR is that it would allow Congress to dispose of the FY 2009 appropriations process quickly and move on to considering other priorities, including passage of the FY 2010 bills in a timely fashion and with funding levels that reflect the priorities of an all-Democratic federal government. The downside of a year-long CR is that it would require all domestic agencies in the first year of the Obama Administration to operate at the limited funding levels imposed by the Bush Administration. This funding would also be distributed in ways that would make it difficult for the Obama Administration to achieve its immediate policy objectives.

The benefit of completing the FY 2009 appropriations process via an omnibus appropriations bill early next year is that it would allow Democrats and the Obama Administration to re-allocate funding levels for domestic programs to better reflect their own policy priorities. The downside is that rewriting the appropriations bills to reflect these priorities will consume valuable time for both Members and Congressional staff, making it much more difficult to pass the FY 2010 appropriations bills by the end of the fiscal year.

If Congress passes a CR, it would likely do so in a manner that would exclude the thousands of pending individual project earmarks. Congress did that early in 2007, the last time it passed a year-long CR instead of completing the individual appropriations bills. If Congress pursues an omnibus appropriations bill, it will likely include most project earmarks pending in the current bills. Incumbents who had projects pending in the FY 2009 bills would likely retain those earmarks. Projects in districts or states where the Representative or Senator is changing hands are less likely to be carried forward into a new omnibus appropriations bill. The primary challenge in drafting an omnibus bill is that the House and Senate Appropriations Committees have not yet marked up all of the pending bills, and therefore all of the earmarks are not yet public.

Potential for Earmark Reform

Immediately after resolving FY 2009 spending bills, Congress will need to turn its attention to drafting the FY 2010 spending bills. It is likely that the practice of earmarking will continue in the FY 2010 appropriations bills at its current level, which is down approximately 50% from three years ago in response to pressure from the Bush Administration to reduce earmarks. While President-elect Obama has made nuanced statements regarding the practice of earmarking, he is likely to allow the Democratic Congress to continue the practice, but with new rules to increase transparency and accountability. President-elect Obama did not make any earmark requests in FY 2009. However, he had been successful in securing a significant number of earmarks in his first year in the Senate, and thus we believe he appreciates the value to Senators and Members in being able to bring dollars back to their respective states and districts.

House and Senate rules governing earmarks are likely to be strengthened and expanded in the 111th Congress, though perhaps not in ways that will have any material impact on the appropriations request process. Current rules require that the sponsors of individual earmarks be listed in each appropriations bill, that Members not have a financial interest in any earmark request, and that earmarks not be “air-dropped” into appropriations bills after they have been voted on in either chamber. Given the recent conviction of a senior Senate appropriator combined with a large influx of new Senators and Representatives elected on a platform of change in Washington, we anticipate increased pressure on Congress to impose additional safeguards on the earmarking process.

Conservative Republicans in the House attempted to self-impose a moratorium on earmarks within their own Conference in the 110th Congress; they are likely to renew this attempt in the 111th Congress. This is especially likely as the ranks of House Republicans grow more conservative with the retirements and election losses of the Conference’s more moderate Members. If they are successful in imposing this moratorium, House Republicans would abstain altogether from making earmark requests, despite the fact that this self-imposed moratorium would not keep House Democrats from continuing to pursue and secure earmarks for local projects. Senators Jim DeMint (R-SC) and Tom Coburn (R-OK) are likely to continue their crusade against earmarks in the Senate by objecting to legislation that includes funding for local projects, but they lack the support of a

majority of their fellow Republicans in the Senate. Thus, we do not expect there to be a self-imposed moratorium on earmarking in that chamber either.

Finally, in the 110th Congress many Representatives and Senators chose to voluntarily abstain from submitting earmark requests or reduced the scope of what they requested in response to public opinion that the appropriations process was broken. Many of these Members called for Congress to make significant reform to the process. It appears that the political emphasis on earmarking has peaked in the short term and that, absent House Republicans voting to impose a moratorium on their Members making requests, the number of individual Members who limit or eliminate their office's pursuit of appropriations requests will actually drop in 2009 compared to 2008.

For additional insights about likely policy developments, please feel free to contact the authors of this section, Ed Newberry, at 202-457-5285 or by email at enewberry@pattonboggs.com, and Kevin O'Neill, at 202-457-6136 or by email at koneill@pattonboggs.com.

Defense and National Security

President-elect Obama will take office inheriting two wars, an overstretched military, the threat of a nuclear Iran, strained relations with Russia, and the potential threat of developing powers. So too will he inherit a global economic crisis of historic proportions, and a domestic fiscal system under tremendous strain.

President-elect Obama's foreign policy is essentially multi-lateralist, rooted in diplomacy. (To be sure, he has indicated that he will not hesitate to use force where necessary.) He indicated throughout the campaign, for example, that he favors direct talks with Iran, though he has not taken the military option off the table. President-elect Obama favors engagement with Russia on nuclear non-proliferation and supports careful additional enlargement of NATO along with additional burden sharing by the Alliance in Afghanistan and elsewhere.

Advisors to President-elect Obama have indicated that they do not foresee overall cuts in defense spending in his administration, at least in the short term, despite the faltering economy and attendant budgetary pressures. Instead, his national security team has indicated that he would reprioritize programs within existing budget levels. An Obama Administration would seek increased cost efficiencies by scrutinizing major weapons systems and modernization programs and shift the emphasis towards more immediate personnel and hardware needs. The international security environment, including the fluid situations on the ground in Iraq and Afghanistan, constitutes a significant variable that will affect future defense budgets, with Congressional politics and military resistance also constraining significant reform. As a result, the new Administration is likely to enact relatively similar, essentially flat defense budgets over the near term.

The Fiscal Context

The current economic downturn, combined with the significant scale of the government's existing and proposed fiscal responses to it, has led some defense observers to forecast an end to defense spending increases in the coming Administration. These macroeconomic and budgetary pressures come as the recently enacted FY 2009 defense budget capped a sustained and dramatic increase in defense spending during the Bush Administration and set a post WW-II spending record. (In the last fiscal year, U.S. defense spending, including supplemental funding for the wars in Afghanistan and Iraq, was more than twice what it was in FY 2000.) In addition, personnel costs

related to long-term deployments, the need to replace equipment worn or destroyed in current operations, and the renewed focus on potential conventional adversaries (*e.g.*, Russia and Iran) all contribute to the current budgetary strain.

Predictions from within DoD, and from key Members of Congress, also suggest that defense spending will flatten, forcing reprioritization within the Pentagon. Secretary of Defense Robert A. Gates, who may continue in his position for awhile in the new Administration, has stated that he expects growth to level off and that DoD will be fortunate in the years immediately ahead to stay flat with inflation. Prior to the election, Representative John Murtha (D-PA), the Chairman of the House Appropriations Committee's Defense Subcommittee, told reporters that, "No matter who wins the White House, the next president is going to be forced to decrease defense spending to respond to . . . domestic priorities. Because of this, the Defense Department is going to have to make tough budget decisions involving trade-offs between personnel, procurement, and future weapons spending."

President-elect Obama's Budget Strategy

The Obama campaign has indicated that it will not cut defense spending during the first years of a new Administration, but it also has stated that it will seek to move funds towards procuring a greater number of less expensive and more versatile weapons systems, and towards reinvesting in conventional air and sea power. Obama campaign officials have also indicated increased focus on unmanned aerial vehicles and cyber warfare.

Within a set Pentagon budget, an Obama Administration is likely to push for increased cost efficiency by buying greater numbers of less sophisticated weapons systems. In comments that parallel those of Secretary Gates, Obama's advisors are focusing on the opportunity cost of new major initiatives compared to the goal of achieving greater balance in resource allocation. The Obama Administration is likely to look at basic hardware challenges facing the Pentagon, and concentrate on weapons with wider purpose and a full range of capabilities. President-elect Obama has indicated that he will make sure that the Pentagon does not become overly fixated on counter-terrorism and counterinsurgency strategies at the expense of traditional air and sea power. Consistent with this emphasis on conventional power, he has indicated he will recapitalize naval forces and preserve global reach in the air through unmanned aerial vehicles, the C-17 Globemaster III Cargo plane (a program opposed by Senator McCain), and the KC-X refueler.

President-elect Obama also supports the Pentagon's plan to expand the size of the Army and Marines. In addition, he has called for increases in special operations forces, language training, and human intelligence for counter-insurgency and to stabilize conflict zones. Importantly, he has also called for the removal of 1-2 brigades a month from Iraq, if compatible with military command decisions. A drawdown would reduce the need for supplemental spending.

Defense Spending in the New Administration

As the United States remains embroiled in conflicts in Iraq and Afghanistan and faces the prospect of a nuclear-armed Iran and a resurgent Russia, defense spending is likely to respond to these requirements. Military spending priorities are not easily changed. The Pentagon has already drafted the components of a FY 2010 budget, and weapons acquisitions plans are generally "tightly wound" and not easily undone without significant termination costs. Finally, weapons programs generally will be fiercely defended by the military services sponsoring them; the communities in which the systems are built and developed; and their corresponding congressional delegations. With

mounting job losses, moreover, it will be politically difficult to shutter production lines in local economies.

For these reasons, instead of major program cuts, the more likely result of increasing budgetary pressure is a paring back or delay in major weapons system, modernization programs, and R&D projects that are not immediately relevant to current conflict areas, or that have experienced significant cost overruns or other concerns related to program efficiency. The current Administration has just responded to significant cost overruns in a program by cancelling the Bell Helicopter Armed Reconnaissance Helicopter. In tightening budgets, DoD is certain to be quicker to kill programs behind schedule and over budget than in the past.

In the later years of the next Administration, however, depending on the strategic international environment, there is reason to expect that an Obama Administration will be more likely to shift defense spending toward meeting domestic priorities. First, the history of cyclical growth and contraction in defense spending suggests future reductions. The relative size of the defense budget compared to other discretionary government spending can make defense cuts hard to take off the table permanently. Second, President-elect Obama has often stated that no nation can remain militarily powerful or dominant if the country does not rest on strong economic foundations; in repeating this view, including during the presidential debates, he connects to a tradition in US foreign policy that emphasizes domestic strength as a precondition for international leadership. Given this deep-set perspective, should the strategic environment allow it, we expect greater emphasis on domestic priorities later in an Obama Administration, especially given the domestic-leaning policy preferences of the Democratic Party, especially if it continues to control the Senate and the House of Representatives.

NATO: Afghanistan and Beyond

With respect to the conflict in Afghanistan, President-elect Obama has stated that he would pressure European allies to take on additional responsibility. For example, he pledged to “ask more of our European friends” in Afghanistan. The NATO commander in Afghanistan, U.S. Gen. David McKiernan, has indicated he will need 15,000 more troops next year. The issue remains politically delicate: French President Nicolas Sarkozy sent more troops to Afghanistan, but faced fierce political criticism for doing so. German troops, while in theater, remain in the safer Northern provinces.

Beyond the question of troop levels, it increasingly looks to be the case that the Obama Administration will pursue the wider political-military strategy currently being developed by General David Petraeus and his Joint Strategic Assessment Team. As head of U.S. Central Command, General Petraeus has indicated a major strategic shift to focus on government-led reconciliation of Taliban insurgents along the Afghanistan-Pakistan border area. General Petraeus’ approach also envisions coordinated diplomacy with India, Pakistan, and China in creating necessary security assurances. General Petraeus has also coordinated with the World Bank and IMF as part of this effort. President-elect Obama has indicated that he would listen carefully to General Petraeus’ advice about Iraq and Afghanistan. It is therefore likely that he will commit to this strategy, which may shift the focus of transatlantic cooperation away from the purely military sphere.

Outside of Afghanistan, President-elect Obama envisions a stronger role for NATO and supports the previous rounds of expansion of the alliance into Central and Eastern Europe. He has signaled greater deliberateness as to whether NATO should include Ukraine and Georgia in the

Alliance. His campaign materials indicate his vision to transform the alliance from a “Cold War security structure” to a “global partnership for peace and security.”

Other Areas of Interest

Confronting Iran’s Nuclear Program. During the campaign, President-elect Obama made clear that he would be willing to hold direct negotiations without “self-defeating preconditions”—e.g., requiring Iran to first suspend uranium enrichment—and would offer incentives to halt the Iranian program. If Iran were to refuse, he would push for tougher U.N. sanctions and would work with allies on unilateral measures, potentially including a ban on exports of gasoline to Iran. President-elect Obama has refused to rule out force, but says first exhausting all diplomatic options would ensure that such action would enjoy greater international support.

Russia. President-elect Obama supports NATO enlargement in principle, but has urged deliberateness with regard to Georgia and Ukraine so as to not create more tension than necessary. President-elect Obama also calls for international peacekeepers to replace Russian troops in contested regions, which he has stated precipitated the Georgia conflict. He also emphasizes US-Russian cooperation on securing loose nuclear materials, as one prong in a strategy of intensive diplomatic engagement.

Other Issues in the Transatlantic Relationship. President-elect Obama has called for transatlantic cooperation on global warming built around a cap and trade emissions control system and focused investments in alternative energy. President-elect Obama also supports EU enlargement, increased partnership with Turkey, and a political settlement in Cyprus.

For additional insights about likely policy developments, please feel free to contact the author of this section, Jack Deschauer, at 202-457-6338 or by email at jdeschauer@pattonboggs.com.

Employment Law

With an increased Democratic majority in the Senate and Barack Obama in the White House, employers need to be prepared for dramatic changes. “Card check” legislation, the aim of which is to significantly expand the number of employees that unions represent, is at the top of an ambitious list of union legislative objectives. We expect that several other pending bills may become law, including ones that would expand the scope of employment discrimination claims and increase the amount of damages that employees could recover from such claims. In addition, under the new administration we could see legislation increasing the minimum wage again, expanding the requirements for notice to employees who are being laid off due to a plant closing or mass layoff, regulating the use of independent contractors, or requiring employers to provide some amount of paid family and medical leave.

Employee Free Choice Act

The “card check” legislation, entitled the Employee Free Choice Act (“EFCA”) (S.1041, H.R. 800), is the most important bill on organized labor’s domestic legislative agenda. The bill has 233 co-sponsors in the House and 46 in the Senate, including both Senators Obama and Biden. It has passed the House, but there were not enough votes to prevent a filibuster in the Senate. As we noted in the introduction, we anticipate that this bill will be one of the principal components of

Speaker Pelosi's 100-hour agenda. If the Senate were to agree to the legislation as well, employees will lose the right to a secret ballot election to determine if they want to be represented by a union.

Currently, only 7.5 percent of private sector employees are reportedly represented by unions. Under present law, employees generally decide if they will be represented by a union through a secret ballot election supervised by the National Labor Relations Board ("NLRB"). If the union wins the election, the employer and the union will negotiate a collective bargaining agreement.

Under the EFCA, if a union presents authorization cards from over 50% of the employees, there is no secret ballot election. Instead, the NLRB would certify the union as the employees' exclusive representative. The employer would be required to begin negotiations with the union over the terms of a collective bargaining agreement. If after 90 days the union and employer do not reach an agreement, then either party can request mediation with the Federal Mediation and Conciliation Service. If 30 days after such request the parties do not reach an agreement, then an arbitration panel decides the terms of the agreement that would be binding for two years, unless the parties agree otherwise.

Ledbetter Fair Pay Act

The Fair Pay Act ("FPA") (S. 1843, H.R. 2831) is a priority for President-elect Obama--he even mentioned it in the third presidential debate. The FPA has already passed the House. The Senate held hearings on it on September 23, 2008. The FPA would reverse the Supreme Court's decision in *Ledbetter v. Goodyear Tire & Rubber Co.*, No. 05-1074 (May 29, 2007), and extend indefinitely the time limits for employees to bring claims of pay discrimination based on race, color, religion, sex, national origin, age, or disability. In the *Ledbetter* case, the Supreme Court held that the time limit for filing a pay discrimination claim was a maximum of 300 days after an alleged discriminatory pay decision was made, because that decision was the "unlawful practice."

The FPA would make each paycheck that was affected by a discriminatory decision a new "unlawful practice." Thus, for example, an employee who claimed that she was still being paid less due to a discriminatory decision made 15 years ago, could bring a discrimination claim within 300 days after receipt of her most recent paycheck, even if she had known about the alleged discriminatory decision for years. Employers would be left to attempt to defend claims long after witnesses had disappeared and memories had faded.

Paycheck Fairness Act

The Paycheck Fairness Act ("PFA") (S. 766, H.R. 1338) passed the House on July 31, 2008 and is pending in the Senate where it has 24 co-sponsors, including Senators Obama and Biden. The PFA would amend the Equal Pay Act, which prohibits paying less to an employee of one sex for performing essentially the same work as another employee of the opposite sex at the same location. The PFA would make it more difficult for employers to defend these claims. Currently employers often win Equal Pay Act cases by showing that the pay difference is based on "any factor other than sex." The PFA would restrict this defense by requiring that the employer show that (1) the pay difference was based on a "bona fide factor other than sex" and (2) that such factor was (a) not based on or derived from a sex-based differential in compensation, (b) was job related, and (c) consistent with business necessity. Moreover, if an employee were to win under the PFA, the employee could receive not just twice the amount of back pay going back 2 or 3 years, but also an unlimited amount in compensatory and punitive damages. Finally, the PFA would give employees the right to discuss or disclose his or her wages or the wages of another employee. This would mean

that employers could no longer enforce policies requiring employees to keep compensation information confidential to prevent it from being used by competitors to lure away employees.

The Civil Rights Act of 2008

President-elect Obama is one of the co-sponsors of the Civil Rights Act of 2008 (the “CRA 2008”) (S. 2554, H.R. 5129). The CRA 2008 includes broad amendments to many discrimination laws. It has not yet been passed by either the House or the Senate. Among the most significant changes that would result from passage of the legislation:

- Removing the current caps on compensatory and punitive damages for employment discrimination based on race, color, sex, national origin or religion under Title VII of the Civil Rights Act of 1964 or based on disability under the Americans with Disabilities Act. Today, the maximum amount of such damages is capped at \$300,000.
- Prohibiting employers and employees from arbitrating disputes arising under the U.S. Constitution or federal statutes, unless they agree to arbitrate after the dispute arises.
- Making it easier for employees to win disparate impact claims under the Age Discrimination in Employment Act.

RESPECT Act

Senators Obama and Biden are among the co-sponsors of the Re-Empowerment of Skilled and Professional Employees and Construction Tradesworkers (RESPECT) Act (S. 969, H.R. 1644). This proposed legislation has not yet passed the House or the Senate, but given the new composition of Congress may become law. Under the RESPECT Act, many employees who are first line supervisors and currently part of management would become employees who could be represented by a union under the National Labor Relations Act (“NLRA”). Because they are responsible for acting on behalf of the company, NLRA excludes “supervisors” from employees whose right to unionize is protected. The NLRA defines “supervisor” as employees who act in the interest of their employer using their independent judgment to: “hire, transfer, suspend, lay off, recall, promote, discharge, *assign*, reward, or discipline other employees, or *responsibly to direct them*, or adjust their grievances, or effectively to recommend such actions.” The RESPECT Act would exclude from this definition “assigning” and “responsibly directing” other employees. Moreover under the NLRB’s current interpretation, employees can be considered “supervisors” if they spend at least 10-15% of their work time performing any of the duties included in the definition of supervisor. However, to be considered a supervisor under the RESPECT Act, employees would be required to spend the majority of their work time engaged in supervisory duties. These changes would remove many first line supervisors from the ranks of management and put them among employees who could be represented by a union.

For additional insights about likely policy developments, please feel free to contact the author of this section, Sally Garr, at 202-457-6525 or by email at sgarr@pattonboggs.com.

Energy and Natural Resources

During the campaign, President-elect Obama emphasized that developing a new energy policy would be one of his highest priorities. We thus expect it to be a central element of his 100-day agenda. President-elect Obama and his advisors have spoken often of their desire to move a comprehensive energy bill and to enact his vision of a comprehensive cap-and-trade bill to address climate change. In our view, he can persuade the 111th Congress to agree to a comprehensive energy bill, but we do not believe Congress will take final action on climate change legislation until 2011 or 2012 (as further discussed in the next section of our analysis).

Through the considerable efforts of T. Boone Pickens, the American public now appreciates the cost of our reliance on foreign oil: \$700 billion a year and growing. During the campaign, both President-elect Obama and Senator McCain pointed to that growing drain on the economy as a reason for a change of direction in our approach to energy. It has become a staple of presidential politics for decades to assert the need for “energy independence.” But we of course have never achieved it. Now that they have a number attached to its cost, Congress and the American public are more likely to support measures to reduce our reliance on foreign sources of oil. They may not agree on all the elements of the PickensPlan, but we believe they now are more likely than ever to be ready to address energy policy from a new, national perspective.

We describe below how this may play out in the 111th Congress. We provide an overview of the Obama-Biden energy plan and the various elements that may make up a comprehensive energy bill, including provisions on clean-coal technology, renewable energy production, limits on tax breaks and other restrictions on the domestic oil and gas industry, and potentially expanded electricity transmission infrastructure.

The Obama-Biden “New Energy for America Plan”

The Obama-Biden “New Energy for America” plan, if enacted, would invest \$150 billion over the next ten years to create five million new “green” jobs, put one million plug-in hybrid cars on the road by 2015, develop new low-emission coal plants, create an advanced biofuels infrastructure, and develop commercial scale renewable energy projects. In addition, the plan would raise fuel economy standards by four percent per year, would ensure ten percent of electricity is produced from renewable sources by 2012 and 25 percent by 2025, and would implement many other elements of the House Democratic agenda from the 110th Congress, including levying a “windfall profits” tax on the oil and gas industry and forcing the industry to “use or lose” existing oil and gas leases. In addition, President-elect Obama would encourage Congress to implement an economy wide cap-and-trade program to reduce greenhouse gas emissions by 80 percent by 2050.

Since it was announced, some of the elements of the plan have been overtaken by world events. When the price of gasoline at the pump had passed \$4 per gallon, providing an emergency energy rebate of \$500 per individual or \$1,000 per family would have been more politically feasible than it is likely to be in January. So too would have been a crack down on “energy speculators.” And perhaps releasing light oil from the Strategic Petroleum Reserve now and replacing it later with heavier crude oil. But given the recent collapse in world oil prices and relief consumers are now seeing at the pump, we see little immediate interest in making these measures a central element of a comprehensive energy plan, especially if paying for them would force a reallocation of funds away from other spending priorities. When gasoline prices begin their inevitable rise, we expect further calls to regulate the energy commodities market. But not in the short term.

Committees of Jurisdiction

The bulk of the Obama-Biden energy plan is likely to be considered in the House Energy and Commerce Committee and the Senate Energy and Natural Resources Committee. The renewable energy tax incentives will be considered by the House Ways and Means Committee and the Senate Finance Committee. The House Natural Resources Committee also will have input with respect to energy development on federal lands.

Major leadership changes will occur in the House Energy and Commerce Committee. Representative Henry Waxman (D-CA) will take over the gavel from Representative John Dingell (D-MI), the Dean of the House. Representative Joe Barton (R-TX) will continue to serve as Ranking Member. We continue to expect that the Energy and Air Quality Subcommittee will be led by Representative Rick Boucher (D-VA), with Representative Fred Upton (R-MI) serving as Ranking Member.

Senator Jeff Bingaman (D-NM) will continue to chair the Energy and Natural Resources Committee. With the retirement of Senator Pete Domenici (R-NM), Republicans will choose a new Ranking Member, widely expected to be Senator Lisa Murkowski (R-AK). Chairman Bingaman has made it clear that he hopes to work in the new Congress on bipartisan energy legislation, as he has put it recently, with the goal of “rescuing energy from partisanship.”

Attack on “Big Oil”

Throughout the 110th Congress, the Democratic majority in the House was able to ram through legislative proposals aimed at the domestic oil and gas industry. As part of the Speaker’s 100-hour agenda, for example, the House passed a bill that would have required oil companies holding leases in the deep waters of the U.S. Gulf of Mexico issued in 1998 and 1999 to “voluntarily renegotiate” them to include price thresholds that would trigger royalty payments or face the prospect of not being able to bid on new leases in the future. In addition, the House would have authorized antitrust lawsuits against OPEC, would have subjected the industry to price gouging penalties, and would have forced lease holders to give up leases not then in production (even those leases the industry could not develop because they were the subject of litigation brought by environmentalists intent on blocking further oil development). None of these proposals became law, in part because of Republican and oil-state Democratic opposition in the Senate.

We have little doubt that the House Democratic leadership can move those same bills through the House again in the first 100 hours or as part of a larger, more comprehensive energy bill. But they will not become law unless moderate Democrats in the Senate agree.

Coal

President-elect Obama voted for the Energy Policy Act of 2005 in part because it encouraged greater use of clean coal technology. His energy plan would provide incentives to accelerate private-sector investment in commercial scale zero-carbon coal facilities. He envisions building five “first of a kind” commercial scale coal-fired plants that implement carbon capture and sequestration (CCS).

To advance the development of CCS technology, Representative Rick Boucher, an early supporter of President-elect Obama, introduced H.R. 6258 in the 110th Congress. Over a ten-year period, the bill would encourage \$10 billion in research to bring CCS technology to market. We

expect comparable legislation to be introduced in the 111th Congress and for it to be part of any comprehensive energy legislation adopted by the House.

Electric Transmission Grid

During the debate over the Energy Policy Act of 2005, one of the most contentious issues involved the construction of new electric transmission lines. In the end, Congress agreed to give the Federal Energy Regulatory Commission (FERC) “backstop” siting authority to permit the construction or modification of electric transmission lines in “national interest electric transmission corridors” if stalled or blocked by state regulatory authorities. The Department of Energy subsequently identified only two corridors as meeting the threshold set in the law (one in the mid-Atlantic region and one in the Southwest part of the country). Because its backstop authority was limited to these specially designated corridors, FERC does not have authority to ensure construction of the nationwide grid the country will soon need.

Given the growing demand for the use of renewable energy and the emphasis the Pickens Plan put on wind as a source of electric generation capacity, the debate over expanding the grid is likely to intensify in the 111th Congress. The Obama-Biden plan calls for an investment in a smart grid, but not a wholesale expansion in its size. As the plan recognizes, “[a]chieving . . . aggressive energy efficiency goals will require significant innovation in the way we transmit electricity and monitor its use.” President-elect Obama proposes to pursue major investments in the grid using smart metering, distributed storage, and other advanced technologies.

As the country seeks to increase the use of renewable energy, whether geothermal, hydro, wind, or solar, it must confront a basic fact that can no longer be avoided: to get renewable electric energy from where it is to where it is needed, we must build new transmission capacity. This will require moving beyond the prevailing nationwide NIMBY philosophy (not in my back yard) and the emerging BANANA mentality (build absolutely nothing anywhere near anyone) in order to achieve greater energy independence through greater reliance on renewable energy. In the end, we expect Congress to approach the problem from a national energy security perspective, which should lead to enactment of measures that will lead to the construction of a much larger, smarter grid. As Chairman Bingaman recently put it, “[w]ithout a major focus on putting in place a 21st-century energy infrastructure, we will not be able to make progress on either our energy security goals or our climate security goals.”

Renewable Energy

The Energy Policy Act of 2005 also mandated substantially increased ethanol production. The Obama-Biden plan would further that legislation by developing next-generation biofuels and an infrastructure to get them to market. It is unclear how the plan would do this and whether doing so would require changes to the recently adopted federal Renewable Fuels Standard, which mandates production of 36 billion gallons of renewable fuels by 2022. In addition, as noted above, the Obama-Biden plan also would invest \$150 billion over ten years to accelerate the development of plug-in hybrid vehicles and to develop commercial scale renewable energy projects. Given his past support, we anticipate President-elect Obama will support legislation next year to extend energy tax incentives, such as the production tax credit and the Clean Renewable Energy Bonds program.

The plan also calls for an aggressive renewable energy portfolio standard (RPS), an issue dropped from the energy bill in 2005 because of broad opposition in the House. The Obama-Biden plan would require that ten percent of electricity be produced from “clean, sustainable energy

sources” by 2012 and 25 percent by 2025. With many states already putting in place their own RPS standards, we anticipate that the next Congress will adopt an RPS standard as part of a comprehensive energy bill, with adjustments for areas of the country (*e.g.*, the Southeast) where the challenge of meeting a numerical threshold will be greater.

President-elect Obama has indicated that he wants to keep nuclear power as an option, but says no more reactors should be built until the nation finds a safe way of disposing of commercial nuclear waste. He opposes storing the waste at Nevada’s Yucca Mountain. Chairman Bingaman has indicated that his proposed legislation will help the country develop and deploy a new generation of clean, low-carbon energy technologies, including nuclear power.

OCS Drilling

Following an oil spill off the coast of Santa Barbara, California, in 1969, Congress adopted a one-year moratorium on the awarding of new leases in the Outer Continental Shelf, which begins three miles off shore. This “temporary” moratorium has since been kept in place pursuant to an Executive Order and a rider that accompanied the annual appropriations legislation that funded the Department of the Interior. In July, President Bush lifted the Executive Order. Out of concern that Republicans could successfully block the annual spending bill for FY 2009 had it extended the moratorium for another year, the Democratic leadership decided to let the moratorium and to revisit the issue next year.

Prior to adjourning and to give Democratic Members a “drilling bill” they could support, the Democratic leadership included an OCS drilling measure in a comprehensive energy bill that then died in the Senate. Under the bill approved by the House, oil and gas exploration would have been authorized between 100-200 miles offshore or starting 50 miles offshore for those states that “opted in” to the program. Unlike the regime that applies in the U.S. Gulf of Mexico today, none of the revenues generated by any revenue-generating leases would be shared with the states. In addition, the legislation permanently withdrew national monuments and marine sanctuaries from oil and gas leasing, kept in place restrictions on leasing in the Eastern Gulf of Mexico until 2022, and exempted the Georges Bank off the New England Coast.

We expect comparable legislation to be introduced in the House next year, to pass the House, and to again be rejected by the Senate as too limited in scope. The Senate “Gang of 10” proposal, for example, would have allowed Virginia, North and South Carolina, and Georgia to opt in to leasing more than 50 miles off shore, but with revenue sharing included as an inducement for them to do so. In addition, the Gang of 10 proposal would have created a commission to make recommendations to Congress on future areas that should be opened to leasing. Because President-elect Obama has expressed willingness to support limited OCS drilling (while continuing to oppose drilling in the Arctic National Wildlife Refuge), we anticipate his Administration will find common ground with Senate moderates on legislation that ultimately will be acceptable to the House as part of a larger energy bill.

Further Increase in CAFE Standards

The Obama-Biden energy plan calls for fuel economy standards to increase by four percent per year, while giving motor vehicle manufacturers flexibility to meet the new targets. The plan is projected to save a half trillion gallons of gasoline and six billion metric tons of greenhouse gas emissions. (The plan also calls for \$4 billion in retooling tax credits and loan guarantees for domestic

manufacturers and parts suppliers.) But as Dana Carvey appearing as President George H. W. Bush on Saturday Night Live would put it: “Not gonna happen.”

As part of the Energy Independence and Security Act signed into law in December 2007, Congress has already substantially raised fuel economy standards on cars and trucks. By model year 2020, the industry must achieve a combined fuel economy target of 35 miles per gallon. The Bush Administration will soon issue final regulations that would implement the new law. Under the Notice of Proposed Rulemaking published by the National Highway Traffic Safety Administration in May, the industry would face enormous challenges in bringing more fuel efficient cars and trucks to market under current law.

In the current economic environment, in which domestic sales of cars and trucks have fallen to the lowest level in over two decades, with hundreds of dealerships closing and mass layoffs being announced on a regular basis, it is inconceivable to us that the Obama Administration will aggressively push this part of the plan in the next two years. Much more likely will be further efforts by the new administration to partner with the domestic industry, through loans and loan guarantees, to help the industry regain its footing. Thus, for example, if the Bush Administration fails to do so, we expect the Obama Administration to aggressively push the release of up to \$25 billion in loans to help domestic manufacturers and parts suppliers bring advanced technology vehicles and components to market.

Other Energy Bill Components

Chairman Bingaman and his staff already are developing a comprehensive energy bill, one that may look much different than traditional energy bills. We expect close coordination with the new administration as they ready the bill for introduction next year. In describing his anticipated legislative agenda, Chairman Bingaman has indicated he will look beyond infrastructure and renewables to find ways to use energy more efficiently, including in manufacturing, buildings, commercial equipment, and appliances. He also hopes to expand funding for energy science and engineering, as well as on training a new generation of energy researchers, engineers, and technicians. Finally, he wants to find a way to improve the functioning of federal agencies and programs, and to encourage entrepreneurs to join the government.

With the Senate likely to take up a comprehensive energy bill next year, industry should have the opportunity to address outstanding issues that have already or could limit further energy production, such as section 526 of last year’s energy bill (potentially limiting the development of Canadian oil sands). In addition, the industry should expect a further battle over a moratorium on shale oil production in the West and the use of water for hydraulic fracturing.

If we as a nation are going to reduce our dependence on the Middle East for oil, we will need to address our failure to encourage greater oil and gas production in North America and to build the necessary infrastructure to get it to market. In the end, the Senate could produce bipartisan legislation that not only would encourage enhanced use of renewable resources, but also would take advantage of abundant sources of energy located in Alaska, the Lower 48, the OCS, and Canada.

For additional insights about likely policy developments, please feel free to contact the author of this section, Jeff Turner, at 202-457-6434 or by email at jturner@pattonboggs.com.

Environmental Policy

Without question one of the most important issues that President-elect Obama and the new Congress will attempt to address is global climate change. The challenge is great. The impact on both the economy and ecology of the United States will be tremendous. The consequences will be felt for decades to come. They thus need to get it right.

President-elect Obama often spoke of combating global climate change as a moral imperative and as essential to addressing the nation's energy challenges. In a web address to the Bipartisan Governors Global Climate Summit held in California, he recently reiterated his view that the United States must demonstrate leadership on addressing climate change in order to strengthen the nation's energy security and to assist in creating millions of new "green jobs" In his address, he pledged that his Administration will actively support the adoption of a federal cap and trade system with "strong annual targets that set us on a course to reduce emissions to their 1990 levels by 2020 and reduce them an additional 80% by 2050." Moreover, he said that "any governor who's willing to promote clean energy will have a partner in the White House." He further challenged industry to participate in meeting this challenge and made clear his commitment to international partners by stating, "any company that's willing to invest in clean energy will have an ally in Washington. And any nation that's willing to join the cause of combating climate change will have an ally in the United States of America."

While we anticipate intense legislative action in the 111th Congress, the road ahead contains many potential pitfalls. Although the recent elevation of long-time environmental activist and energy industry antagonist Representative Henry Waxman (D-CA) to the chairmanship of the powerful Energy and Commerce Committee (more on this below) may give the proponents of enacting climate legislation some additional "wind at their backs," we do not believe final action on climate change legislation is likely until at least 2011 at the earliest given the overall health of the nation's economy, lingering questions about low-carbon technological capabilities and the adequacy of research and development efforts to date, uncertainty in the international community about emission reduction targets ahead of the next round of negotiations of the Kyoto treaty in Copenhagen next winter, and unresolved empirical questions about the underpinnings, assumptions, and regulatory infrastructure of a national and international "carbon market."

We set forth below an overview of the Obama-Biden environmental plan, which has two bookends. One is enactment of an economy-wide cap-and-trade program to reduce greenhouse gas emissions and create millions of new "green jobs". The other is rolling back Bush Administration environmental regulations. We also offer our thoughts on additional environmental policy initiatives that have a nexus to greenhouse gas emissions.

Climate Change Cap-and-Trade Program to Reduce GHG Emissions

Last April, the U.S. Supreme Court in *Massachusetts v. EPA* ruled that the Clean Air Act authorizes regulation of greenhouse gases (GHGs) because they meet the definition of an "air pollutant" under the Act. In response to this ruling, President Bush signed an Executive Order that tasked four federal agencies to work together to craft an administrative rule that would comport with the Court's decision. On July 31, the Environmental Protection Agency issued an Advanced Notice of Proposed Rulemaking to regulate GHGs under the Clean Air Act. In doing so, as further discussed below, the EPA made it clear that it would not take final action and instead was leaving resolution of the issue to the next administration.

The Supreme Court's decision also had the effect of reinvigorating congressional efforts to enact climate change legislation, which had begun four years earlier when Senators Joe Lieberman and John McCain introduced the first comprehensive cap-and-trade program legislation to address climate change. While climate change was an issue that many Democrats successfully ran on when they took control of the Congress in 2006, it was not until the Supreme Court's decision that a congressional effort began in earnest to craft legislation to cap GHG emissions.

President-elect Obama supports a program that would cap GHG emissions at 80 percent below 1990 levels by 2050 as noted above. (Senator McCain's plan would have capped emissions at 66 percent below 1990 levels by 2050.) As part of this program, President-elect Obama would require all emissions permits (also referred to as "allowances" when issued for free to covered entities) to be auctioned by the federal government and would distribute the proceeds to various "funds" to support, among other things, clean technology research and development, consumer rebates, deficit reduction, and lost states and local government revenues. While President-elect Obama claims that a 100 percent auction system would "ensure" that all industries pay for every ton of carbon they release, this position is at odds with many moderate Democrats, who advocate a free allocation distribution model for at least the first fifteen years of a cap-and-trade program so as to avoid consumer and energy price shocks to the economy.

The Obama-Biden plan would reassert the United States as a global leader on GHG reduction efforts and would encourage the development of multilateral agreements on low-carbon technology and products for export. Critics often point to the current Administration's less aggressive approach to addressing global climate change as a lost opportunity. President-elect Obama has pledged that he will utilize the diplomatic expertise of Vice President-elect Biden to engage all the major emitting nations as a means of demonstrating to the world that the United States is committed to cutting its GHG emissions and to addressing global energy and environmental issues.

Environmental Regulatory "Roll-backs" and Pro-active Regulation

Like many Democrats in Congress, President-elect Obama would like to "roll-back" certain Bush Administration regulatory actions and would like to implement pro-environmental court decisions under the Clean Air Act, the National Environmental Policy Act, the Endangered Species Act, and the Clean Water Act. While there may be jubilation among some in the greater environmental and land conservation movements at the prospect of their own "pay back" to industry, we anticipate that the regulatory "roll backs" and other proactive regulatory action will be more deliberate and not as sweeping as many anticipate. Rather, President-elect Obama and the Democratic majority in the 111th Congress may find themselves confronted with politically challenging decisions on environmental policy. Thus, for example, they need to address how to put in place a new and robust low-carbon energy infrastructure in a timely way to (i) deter catastrophic climate change; (ii) meet domestic energy demands; (iii) promote economic growth, job creation, and export markets; and (iv) protect consumers and the economy from energy price shocks or supply disruptions if there is business uncertainty related to overly stringent and duplicative environmental regulation that may act as a deterrent to achieving a 21st century low-carbon economy.

Committees of Jurisdiction

In the House, the primary committees of jurisdiction are the Energy and Commerce Committee, the Natural Resources Committee, and the Transportation and Infrastructure Committee. Given the importance of climate change, other committees may attempt to assert their

jurisdiction, such as the Ways and Means Committee (revenues, trade policies, tax credits), the Budget Committee (auctioning of emissions permits that would generate federal revenue), the Appropriations Committee (allocation of auction revenue and other climate related agency expenditures), the Agriculture Committee (carbon commodity trading), and the Financial Services Committee (carbon markets and financial regulation of “carbon instruments” and the financial disclosure of “carbon footprints” of regulated companies).

The elevation of Representative Waxman to the chairmanship of the Energy and Commerce Committee represents an unexpected shift in the balance of power on the committee from the strapped industrial states of the mid-west, like auto manufacturing dependent Michigan, to more heavily regulated environmentally conscious states such as California. The shift in leadership will also give the President-elect a key ally in moving his environmental agenda forward. We still expect Joe Barton (R-TX) to continue to serve as Ranking Member. For the time being, we anticipate that the Energy and Air Quality Subcommittee will continue to be led by Representative Rick Boucher (D-VA), with Representative Fred Upton (R-MI) serving as Ranking Member. On the Natural Resources Committee we expect Representative Nick Rahall (D-WV) to retain his chairmanship and Representative Don Young (R-AK) to continue to serve as Ranking Member. Finally, we anticipate that Representative James Oberstar (D-MN) and Representative John Mica (R-FL) will continue to serve as Chairman and Ranking Member, respectively, of the Transportation and Infrastructure Committee.

In the Senate, Senator Jeff Bingaman (D-NM) will continue to chair the Energy and Natural Resources Committee. With the retirement of Senator Pete Domenici (R-NM), Republicans will choose a new Ranking Member, widely expected to be Senator Lisa Murkowski (R-AK). On the Environment and Public Works Committee, we anticipate that Senator Barbara Boxer (D-CA) will continue as Chairman and Senator James Inhofe (R-OK) as Ranking Member, respectively. As in the House, other committees may attempt to assert their interests over climate change legislation, most notably the Finance, Banking, Commerce, Appropriations, and Agriculture Committees.

We anticipate a potential realignment of the balance of power in the climate debate in the Senate. The Environment and Public Works panel, which has exclusive jurisdiction over the Clean Air Act, is unlikely to dominate the debate as it did this year. Moreover, the changing composition of the Senate will give more power to moderate Democrats, especially from heavy industry manufacturing and coal producing states. The risk of “getting it wrong” will place a check on any overreaching in the Senate.

Lieberman-Warner--America's Climate Security Act of 2007

Last December, the Senate Environment and Public Works Committee (EPW) favorably reported legislation that would cap GHG emissions from covered sources, which represents approximately 80 percent of the economy. Better known as the “Lieberman-Warner” bill, the legislation would have established a comprehensive “cap-and-trade” program administered by the EPA. The bill was approved with a 10-9 margin, with Senator John Warner providing the sole Republican vote. Chairman Boxer also forged a consensus on the Democratic side of the committee by working with moderates such as Max Baucus (MT) and Tom Carper (DE) and more liberal members Bernie Sanders (I-VT) and Frank Lautenberg (NJ) with the goal of reporting a “good bill” out of the committee and to the Senate floor.

Prior to its consideration in the full Senate, the bill was amended to ostensibly satisfy some lingering concerns of Democratic EPW committee members as well as other Democrats regarding

the overall costs of the bill. The amended form of the bill (S. 3026) still set a declining cap on U.S. emissions of greenhouse gases: Starting from 2005 levels, the bill would cut covered sources' emissions of carbon dioxide and four other global warming pollutants by 71 percent in 2050. Emissions of heat-trapping hydrofluorocarbons (HFCs) would be cut more rapidly, declining from 2012 levels by at least 15 percent in 2020 to 70 percent by 2040.

Regarding costs, the bill would issue emission permits or allowances (one allowance = one metric ton equivalent of CO₂) for free to covered entities initially and then would slowly phase out the free emission allowances with a corresponding increase in permit auctioning, reaching 100 percent auctioning by 2031. The bill would also allow covered entities to comply with their annual emission reduction obligations with "carbon offsets" in lieu of allowances or permits. Covered entities would also be allowed to bank and borrow emissions allowances, but borrowed emissions allowances would be limited to five years and would have to be repaid with interest by making deeper reductions in the out years of the program. The bill would create a new independent "carbon market efficiency board," similar to the Federal Reserve Board, that would oversee this process and have the authority to change borrowing and offset limits and payback periods. To address potentially high costs, the bill would allow covered entities to purchase a limited number of emissions allowances borrowed from the program's later years ("cost containment auction") if allowance prices rise above certain prescribed levels.

Finally, the bill would authorize the EPA to work with other agencies, including the Federal Energy Regulatory Commission, the Federal Trade Commission, the Commodities Futures Trading Commission, and the Securities and Exchange Commission, to develop a regulatory and administrative framework to regulate the purchase, sale, transfer, and reporting of allowances, offsets, and the overall financial market related to carbon emission reductions.

The Obama-Biden cap-and-trade program does not differ in too many material respects from the Lieberman-Warner approach, which does not bode well for its prospects in the Senate. The Lieberman-Warner bill was soundly defeated on the Senate floor on a procedural vote. While many blamed Republicans and "scare tactics" by the business community, ten Democratic Senators penned a letter to Chairman Boxer indicating their continued concerns with the Lieberman-Warner bill. They further went on to state that if the vote in the Senate had been a vote for final passage all would have voted "no."

There is one critically important area in which the Obama-Biden approach differs from Lieberman-Warner--a 100 percent auctioning of emission permits vs. the free allocation approach. Senators Obama and Biden were both original cosponsors of the Lieberman-Warner legislation and by implication would appear to have endorsed the free allocation model established in that bill. One can ascribe certain political motivations during a campaign for supporting a 100 percent auction system (such as ensuring that all "polluters pay" for the right to emit greenhouse gases). But it won't fly on Capitol Hill. We thus fully anticipate that President-elect Obama will soften his 100 percent auction position.

Dingell-Boucher Discussion Draft

House Energy and Commerce Chairman John Dingell and Energy and Air Quality Subcommittee Chairman Rick Boucher recently released a Discussion Draft ("Draft") of a bill that would establish an economy-wide national cap-and-trade program to cap GHG emissions over a fifty-year period. They held dozens of hearings and issued several "white papers" on a variety of important elements of any comprehensive legislation. If the production of the Draft was not enough

to draw attention to their commitment to legislating next year, they said in a letter accompanying the release of the Draft: “*We believe that elected and accountable representatives in the Congress, not the Executive Branch, should properly design that regulatory program.*” While this statement was also a response to the Supreme Court’s ruling in *Massachusetts v. EPA*, it made clear that addressing climate change will be the prerogative of the Congress.

Overall, the Draft calls for emissions reductions of 80 percent from 2005 levels by 2050, which is similar in scope to Lieberman-Warner and the Obama-Biden plan, and it would establish a similar overall cap on emissions. Like Lieberman-Warner, the Draft excludes the transportation sector and it provides for the ability to bank and borrow emission allowances. (The Obama-Biden plan is silent on these questions, but we expect from President-elect Obama’s past support for Lieberman-Warner that he will endorse the thrust of these provisions.) However, these areas may be where current similarities end. For example, in contrast to the Lieberman-Warner target of 19% reductions in GHG emissions by 2020, the Draft calls for GHG reduction reductions of only 6% below 2005 levels by 2020. This has the functional effect of pushing a large amount of emissions reduction to 2020 and beyond, which would certainly assist covered entities in the early years of the program make the transition to low-carbon technology and renewable alternatives. It also is a way of protecting energy consumers (both commercial and residential) from volatile energy prices.

Regarding costs, the Draft remains neutral on its emission allocation distribution. The Draft contains four allocation options (Options A-D) most of which issue permits for free to covered entities, and represents different approaches for reducing overall emissions. One of the allocation options (D) would not only provide consumers with tax breaks and direct rebates, but would also provide for large investments in new technology deployment (*e.g.*, renewables, carbon sequestration, and advanced technology vehicles) and would dedicate a third of allocations to deficit reduction. Auctioning of permits is reserved for the out years of the program (2026 and beyond). In another sharp contrast to Lieberman-Warner, the Draft would allow covered entities to use carbon offsets to meet annual compliance obligations, starting with 5% for the first five years of the program and then steadily rising up to a 35% cap in 2024 and beyond.

The Draft contains provisions likely to generate stiff opposition from President-elect Obama’s Administration as well as fellow Democrats in the Congress (especially Members from California). The Draft would have the effect of overturning the Supreme Court’s ruling confirming that the EPA can regulate carbon dioxide if it finds it is a “hazardous pollutant” by removing GHGs from the Clean Air Act’s National Ambient Air Quality Standards regulations. In addition, the Draft provides a broad range of options for dealing with motor vehicle emissions standards, ranging from preempting the right of California and other states to regulate tailpipe emissions to allowing the EPA and the states to implement such protections. Finally, the Draft also contemplates the preemption of state-level regulation of GHG emissions, such as the Regional Greenhouse Gas Initiative, California’s A.B. 32 legislation, and the Western Climate Initiative.

The Safe Climate Act - Waxman Bill

In contrast to the Dingell-Boucher Draft, Representative Waxman’s proposed legislation (the Safe Climate Act, H.R. 1590) is modeled after the State of California’s GHG reduction program. That program grants broad discretion to regulatory agencies with jurisdiction over energy and air policies--under federal law the Department of Energy and the EPA--to develop an economy-wide cap-and-trade system and other measures to reduce GHG emissions. While the bill contains specific recommendations on what the structure of the emission reduction program should look like, the bill is largely silent on details. Congress would have the opportunity to ratify any program the

agencies propose. The bill is similar to the Obama-Biden plan in its target of reducing greenhouse gas emissions by 80% below 1990 levels by 2050 as well as an interim goal of reducing emissions by 15 to 20 percent below current levels by 2020. It would require the auctioning of all emission permits, with very limited exceptions, and use the revenue to fund a Climate Reinvestment Fund, which could be used to assist with, among other things, consumer costs, regional transition assistance, and low-carbon technology research and development.

The Safe Climate Act also contains a provision that raises complex political questions that heretofore have not been addressed with sufficient forthrightness: federal preemption of state and regional cap-and-trade programs and other state environmental regulations. The Dingell-Boucher Draft would expressly preempt state and regional programs, whereas Lieberman-Warner remained silent on the issue. The Safe Climate Act in contrast would preserve a state's authority to maintain or enact stricter environmental regulations, including a stricter cap on GHG emissions.

While it is still too early to assess what approach the new chairman will take on climate legislation, we anticipate a robust and intense debate that will cut across not only ideological lines, but regional lines as well. Ultimately, it may take the President-elect to bridge the political divide for any cap-and-trade program to be enacted into law.

Regulating Greenhouse Gas Emissions Under the Clean Air Act

As noted above, the EPA issued an ANPR regarding the regulation of GHGs under the Clean Air Act in response to *Massachusetts v. EPA*. In issuing the ANPR, the EPA clearly stated that the ANPR does not represent Administrative policy. Among other things, the notice “*reviews the various Clean Air Act provisions that may be applicable to regulate GHGs, examines the issues that regulating GHGs under those provisions may raise, provides information regarding potential regulatory approaches and technologies for reducing GHG emissions, and raised issues relevant to possible legislation and the potential for overlap between legislation and Clean Air Act regulation.*” While the notice is broad and sweeping in its scope and addresses many issues that will be critical in controlling GHG emissions, it does not present nor make an “endangerment finding” related to CO₂ cited by the Supreme Court as the necessary trigger under the Clean Air Act to regulate GHG emissions as an air pollutant. We fully anticipate that the new EPA Administrator will issue an endangerment finding and set the EPA on a regulatory course to address GHG emissions, particularly if Congress appears unlikely to move climate change legislation within a reasonable period of time. Before then, we expect that President-elect Obama will use that threat as a proverbial “stick” to encourage all private and public stakeholders to find consensus on a legislative approach to global climate change.

We also anticipate that President-elect Obama will be under pressure to have his EPA Administrator issue a “waiver” for the state of California to move ahead with stricter motor-vehicle emission standards under Section 219 of the Clean Air Act. However, given the current condition of the automotive industry as well as President-elect Obama's desire to achieve a significant legislative victory on energy and GHG legislation, we believe that he may reserve or even defer a decision on that waiver for a set period of time to gain commitments from stakeholders to work toward a common goal of enacting a national policy on GHG emissions.

Greenhouse Gas Registry

In perhaps an overlooked section of the FY 2008 consolidated omnibus appropriations bill, the EPA was given until September 26, 2008, to issue a rule that would establish a federal greenhouse gas registry. A well-constructed and transparent registry will be critically important for the efficacy of any federal GHG emission program or regulation. The EPA has sent a draft registry

rule to the Office of Management Budget. While the timing of OMB's review and final issuance of a proposed rule is uncertain, we expect President-elect Obama to support swift issuance of the proposed rule should it not be promulgated prior to January 19, 2009. A final rule is due in June 2009.

Biofuels--Renewable Fuels Standard

As part of the Energy Independence and Security Act of 2007 (EISA), Congress mandated a sharp increase in the production and use of biofuels under the federal Renewable Fuels Standard (RFS). The legislation increased the targets for biofuels production to 36 billion gallons by 2022 with a cap on corn-based ethanol of 15 billion gallons by 2015 or whichever comes first. By the end of the year, the EPA had planned to issue a proposed rule implementing the EISA provisions, including one that requires the EPA to consider indirect GHG emissions from land-use changes stemming from the production of biofuels. The law requires that next-generation biofuels have at least 50 percent lower lifecycle GHG emissions than conventional petroleum fuels. However, developers of next-generation biofuels, such as cellulosic ethanol and biodiesel fuels, are pressing the EPA to delay portions of the rule because of questions raised regarding the science used by the EPA in determining what "indirect land use" means and how it is measured. While this particular issue was not specifically addressed in the Obama-Biden environmental policy agenda, it will be an early political test for President-elect Obama and the Democratic Congress. As an outspoken proponent of renewable fuels and innovation in low-carbon technology and the expanded use of renewable fuels as means to lessen the nation's dependence on foreign supplies of oil, President-elect Obama may find that "consensus" and "common ground" may not be achievable on certain issues. Executive decisions must be made to give business and regulatory certainty to allow innovation and investment to continue in the clean-technology sector.

New Source Review

In early 2001, the EPA indicated that it would reconsider the New Source Review (NSR) provisions of the Clean Air Act. As enacted, NSR requires power plants and other industrial facilities, such as refineries, to install modern pollution controls whenever they make plant upgrades or undertake plant expansions. Since 2005, EPA has been locked in a fierce battle with opponents, including the Congress, in trying to amend the NSR provisions. At the heart of the NSR debate has been the dueling efforts of the industrial sector to increase energy and materials production and the states' obligations under the Clean Air Act to maintain air quality standards. The EPA has been attempting to change the NSR's review triggering language from annual emissions to maximum hourly emissions. Opponents have argued that this causes problems because repairs to older power plants and refineries might leave the maximum hourly emissions unchanged but increase total operating hours, meaning annual emissions could rise. Notwithstanding these concerns, the EPA is preparing to issue a final rule that would implement this new triggering language. Assuming the new final rule is issued soon, we expect President-elect Obama will work with the Democrats in the Congress to ensure that it is either rescinded administratively, which may trigger prolonged litigation, or abrogated with legislation.

CAIR (Clean Air Interstate Rule)

On July 11, the U.S. Court of Appeals for the D.C. Circuit struck down the Clean Air Interstate Rule (CAIR). CAIR sought to reduce the amount of contaminants, such as sulfur dioxide (SO₂) and nitrogen oxide (NO₂), from power plants by 70 percent and 60 percent, respectively. CAIR covered the District of Columbia and 28 states in the Midwest and the East and set region-wide "caps" on emissions from power plants. CAIR was also used as a pretext for the need to issue

the new NSR rule discussed above. The court's ruling was not only a blow to the Administration, but also to the power sector and environmental community as well. Many utilities moved forward with capital expenditures to comply with CAIR. The environmental community was supportive of the intent and scope of CAIR as it would have improved air quality for millions of people. In addition, the opinion has been closely analyzed by many stakeholders and policy makers who are working on crafting GHG legislation and regulatory programs as the trading program authorized in CAIR was found to be unlawful by the court. The decision sent a clear signal to policy makers and the advisers of President-elect Obama, and reinforced the belief, that the Congress should be the body that authorizes any cap-and-trade program for GHGs, not the Executive Branch. We expect a "CAIR fix" to be a top priority of the new Congress and President-elect Obama's Administration.

Clean Water Act

In response to the Supreme Court's decision in *Solid Waste Agency of Northern Cook County v. United States Army Corps of Engineers* and the Court's plurality opinion in *Rapanos v. United States*, legislation has been introduced in both the House and the Senate to address the question of what "navigable waters" means under the Clean Water Act (CWA). In these decisions, the Court held that the CWA did not apply to traditional "navigable waters" and other adjacent waters with a "significant nexus" to navigable waters. The Court did not, however, provide a test for what "navigable" means under CWA. In the interim, there have been differing court interpretations and a number of states have passed laws in an attempt to "close the gap." Having legal certainty on this issue is important not only to federal regulators and state and local governments, but to industrial businesses that either have facilities or are planning expansions or additions near bodies of water such as isolated ponds, wetlands, or bogs. Senator Russ Feingold (D-WI) and House Transportation and Infrastructure Committee Chairman Jim Oberstar (D-MN) have offered legislation (S. 1870, H.R. 2421, The Clean Water Restoration Act) that would address the question left unresolved by the courts. The legislation would reaffirm the intent of Congress and scope of the Act by replacing the term "navigable waters" with the term "waters of the United States," and defining that term to mean all waters subject to the ebb and flow of the tide, the territorial seas, and all interstate and intrastate waters and their tributaries, including lakes, rivers, streams (including intermittent streams), mudflats, sandflats, wetlands, sloughs, prairie potholes, wet meadows, playa lakes, natural ponds, and all impoundments. We fully anticipate that the new Congress will attempt to pass this legislation early in the 111th Congress and that President-elect Obama will sign the legislation into law.

Endangered Species Act

Over the last two years, the Department of the Interior has been working on a regulatory overhaul of the Endangered Species Act (ESA). Recently, it indicated that it would allow federal agencies to decide on their own whether protected species would be put at risk by projects. Today, agencies across the government must consult with the Fish and Wildlife Service or the National Marine Fisheries Service. Administration officials believe the proposed change will allow government biologists to focus on the most critical conservation efforts and that consultations between agencies will continue in most cases. Environmental groups say the proposed change would put more species at risk. On October 16, the Administration closed the comment period on this proposed change to the ESA and is expediting its review of over 200,000 comments that have been received with the goal of issuing a final rule by the end of the year. Before President Bush leaves office, the Administration may decide whether the greater sage grouse should be listed as an endangered species. A decision by the U.S. Fish and Wildlife Service to list the bird--whose range stretches 258,000 square miles from Idaho through Montana, Utah, New Mexico, and Colorado to Wyoming--could have far-reaching impacts on energy development in the West. Should these

rulemakings become final, we fully anticipate that the new Congress and President-elect Obama may work with the Democratic Congress to reverse them.

In perhaps the most closely watched decision of the year, the Department of the Interior accepted the recommendation of the U.S. Fish and Wildlife Service to list the polar bear as a threatened species under the ESA. The listing was based on the grounds that the loss of sea ice threatens and will likely continue to threaten polar bear habitat. The Department went out of its way to affirm current Administration policy that the ESA was never intended to regulate global climate change and that the listing should not open the door to use of the ESA to regulate greenhouse gas emissions from automobiles, power plants, and other sources. In fact, shortly after the announcement by the Interior Department, and long before the nation became familiar with Alaska Governor Sarah Palin--and perhaps Tina Fey as well--the Governor announced that Alaska would sue the U.S. government, arguing the designation would slow energy development in the state. She was also the first public official to argue publicly that the listing would open the door to using the ESA as another tool to regulate GHGs (notwithstanding the Administration's pronouncements). While one can argue the merits of the Governor's logic, an open question remains--what's to stop the designation of other species in other habitats (*e.g.*, deserts, mountains, forests) from being listed under the ESA under the polar bear precedent that global warming is threatening their habitat? How would such listings affect solar, wind, biomass, and geothermal energy production, which are at the heart of President-elect Obama's energy plan? While we fully expect that President-elect Obama and the Democrats in Congress will work to ensure that the ESA is not "weakened" in any meaningful way, we foresee a robust policy debate in the near future over the scope and breadth of the ESA especially if the polar bear listing stands.

National Environmental Policy Act

The other major environmental statute that has received a tremendous amount of attention is the National Environmental Policy Act (NEPA). The landmark statute has been the subject of much debate regarding its relationship to the nation's energy, natural resource, materials, and infrastructure development for decades. Not surprisingly, in the waning days of the current Administration, the Interior Department has launched a bevy of rulemaking activity related to NEPA's scope and reach as it relates to energy development on federal lands: (i) Issuance of a new Bureau of Land Management (BLM) handbook on implementing NEPA, which has the effect of exempting some drilling, logging and mining activities from environmental review; (ii) revisions of the BLM's manual on threatened and endangered species that would remove state-designated species from protection on BLM land; (iii) New National Forest Management Act regulations that would remove protecting species on national forest land as a management goal and loosen controls on logging; and (iv) BLM oil-shale-leasing rules in Colorado. Lastly and perhaps most watched will be how many additional "categorical exemptions" or CXs will be issued by the BLM prior to January 19, 2009. CXs, which were authorized under EPAct 2005, allow oil and gas operations to be exempted from NEPA's environmental assessment requirements in areas where a drilling operation disturbs less than 5 acres, is on a site where drilling has occurred in the past five years, or is in a field that has had an environmental impact study in the past five years. From August 2005 to September 2007, a total of 1,632 exclusions were issued in Colorado, Wyoming, Montana, New Mexico, and Utah. In response, legislation was introduced in the House of Representatives (H.R. 7231) to repeal CX exemptions under the Safe Water Drinking Act for hydraulic fracturing, which would require additional environmental permitting and adversely affect oil, gas, and geothermal energy development. President-elect Obama and the Democratic Congress might reverse these NEPA related rulemakings, but also may give considerable reconsideration to repealing all the CX exemptions of EPAct 2005.

For additional insights about likely policy developments, please feel free to contact the author of this section, Joshua C. Greene, at 202-457-5204 or by email at jgreene@pattonboggs.com.

Financial Services

Reform and oversight initiatives will dominate the financial services agenda in the 111th Congress. The confluence of recent events, including the collapse of the housing market, the tightening of the credit markets, and the volatility of the equity markets, have led to unprecedented federal government intervention into our capital markets. The Senate Committee Banking, Housing and Urban Affairs (Banking Committee) and the House Committee on Financial Services (Financial Services) are certain to expand the inquiries begun in the 110th Congress to determine, among other things, how we restructure our markets to prevent similar episodes in the future and to determine who was responsible for the debilitating erosion of the capital markets. These efforts will likely result in legislation and potentially criminal referrals. This would have been true regardless of the election results. With the increased Democratic majorities in both chambers, the Banking and Financial Services agendas will also aggressively address consumer protection issues such as mortgage origination practices and credit card practices reform that they started in the 110th Congress.

Committees of Jurisdiction

Senator Christopher Dodd (D-CT) currently serves as Chairman and Senator Richard Shelby (R-AL) serves as the Ranking Member of the Banking Committee. Chairman Dodd also is the second most senior Democrat on the Senate Foreign Relations Committee. With Senator Joe Biden's ascension to the Vice Presidency, Senator Dodd will have the choice of shifting his chairmanship from Banking to Foreign Relations. We expect Senator Dodd will remain Chairman of the Senate Banking Committee in large part because of the importance of the issues currently before it and because of Connecticut's very heavy constituency of financial services oriented companies (UBS, RBS, Travelers, Hartford Financial Group, GE Capital, and a number of major hedge funds) and many people who live in the state, but work on Wall Street. Senator Dodd is up for reelection in 2010. Assuming he remains chairman, Senator Dodd will continue to focus the Banking Committee's legislative and oversight efforts on market structure and modernization issues with a bent towards consumer protection and preservation of public assets such as pension funds.

Representative Barney Frank (D-MA) is the Chairman and Representative Spencer Bachus (R-AL) serves as the Ranking Member of the House Financial Services Committee. The leadership of this committee is expected to remain the same.

Because the impact of the financial crisis has affected so many sectors, there is a distinct possibility that Congress may create a special, joint, or select committee to consider what legislative measures may be appropriate to address, among other things, systemic risks. On the House side, such a committee would likely include representation from the Financial Services, Agriculture and Ways and Means Committees. On the Senate side, the Banking, Finance and Agriculture Committees would be involved.

The Economic Crisis of 2008

The Emergency Economic Stabilization Act of 2008 (EESA)--Execution. President-elect Obama will take office in the midst of the economic crisis and implementation of EESA, which Congress enacted in early October. The immediate agenda for the Congress will focus on

ensuring that all is being done to help mitigate the problems in the economy and the capital markets and providing oversight of the implementation of EESA by the Treasury Department and other federal agencies.

During the transition period, Congress will be exploring whether the actions being undertaken are appropriate and sufficient to ease the crisis. One area that is surely to get early attention revolves around the home mortgage market and whether there is more that can be done to avoid the historic levels of foreclosures that currently plague the market. Both Chairmen Dodd and Frank have called for more action by the federal government, banks, other lenders, servicers, and investors to stem the tide of foreclosures. Also, the FDIC is working on an aggressive plan to pursue modifications. Finally, several financial institutions that are participating in the EESA program have announced their intention to modify more mortgages and avoid foreclosures where they can. Nonetheless, Congress is expected to watch this very carefully.

We also expect the Obama Administration and Congress quickly to determine whether anything more or different needs to be done to address the financial market crisis. This could include specific actions in certain industries particularly hard hit by the crisis, including the auto industry, the student loan market, and possibly others. While the Treasury arguably already has discretionary authority to address such issues, the new Administration and the Congress may believe that new authority is necessary to accelerate the recovery.

The Emergency Economic Stabilization Act of 2008 (EESA)--Oversight. Congress has begun oversight, with hearings already planned with respect to implementation of EESA. With a new Congress, you can expect aggressive oversight into the actions of the Treasury Department and other federal agencies over the last few months. The oversight will focus on not only how effectively the Department and other agencies were implementing the program, but how they managed the outsourcing process, conflicts of interest, executive compensation issues, and generally how and why decisions were made.

Congress has significant oversight responsibility for the implementation of this landmark legislation, which empowers the Secretary of the Treasury to, among other things, use up to \$700 billion to purchase, manage, and sell troubled assets of various types from financial institutions doing business in the United States, as well as to make investments in financial institutions. Pursuant to EESA, the Secretary will implement this authority through the troubled asset relief program (TARP) and he or she must provide Congress with regular reports regarding, among other things, the value of assets under management. Also, the Secretary must seek Congressional authorization prior to accessing additional tranches of the \$700 billion beyond the first \$250 billion made available already. Given the high level of apprehension about implementation of this legislation on both sides of the isle, Congress will undoubtedly monitor the program very closely, particularly the outsourcing process and the executive compensation provisions. For example, the EESA requires a congressionally appointed oversight panel to submit, by January 20, 2009, a report containing recommendations on how to improve TARP and any analysis of the current state of the regulatory system.

Secretary Paulson was sworn into office on July 10, 2006. Tradition would hold that the new President will nominate a new Secretary by the time of the inauguration. All Presidential appointees and Secretary-appointed individuals will also have to leave their positions or be reappointed in the new Administration. This would include the entire team of Assistant Secretaries and the Under Secretary for Domestic Finance, the group responsible for implementing the TARP program. The current Treasury Department is currently trying to build an infrastructure of professional career staff

to lead various functional areas of the TARP program to ensure continuity during and after the transition process.

The Emergency Economic Stabilization Act of 2008 (EESA)--Regulatory Reform.

Congress has made clear that it will take a thorough and exhaustive look at the current financial market infrastructure to determine where systemic risks lie and what Congress needs to do to address them. An important starting point of this review will likely be the Treasury Department's Blueprint for a Modernized Regulatory Structure that Secretary Henry Paulson released in March 2008. This evaluation will include an evaluation of all of the financial regulators--the Securities and Exchange Commission (SEC), the Federal Reserve Board (Fed), the Commodities Futures Trading Commission (CFTC), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS). Congress will review the existing regulatory regime to determine where there is unnecessary duplication of efforts as well as gaps in the regulation of the capital markets. For example, in the wake of the perceived (if not acknowledged) lack of oversight of credit default swaps, there will be renewed calls to combine the SEC and the CFTC. In late October, SEC Chairman Chris Cox expressed open-mindedness to such an idea. Additionally, Congress will continue to evaluate the appropriate level of oversight and regulation for investment banks, credit rating agencies, and bond insurers; all entities that have been identified as playing a role (accurately or inaccurately) in the financial meltdown.

Secretary Paulson presented the Blueprint as a starting point for the discussion about financial services regulatory modernization and reform. In the months following the financial markets continue to spiral downward with the escalating credit crisis. Although the next Administration and the new Congress are sure to put their own imprint on this reform process, the Blueprint provides as starting point for this discussion. For more information on the Blueprint, see <http://www.treas.gov/press/releases/hp896.htm>.

Systemic oversight of market participants, institutional reform, and market and product developments will likely be the lasting legacy of this financial crisis. Even if much of the Blueprint is not adopted, the key notion that there will be on regulator to oversee systemic risk and market stability will likely be carried forward. The linchpin of regulatory reform will likely encompass the creation of a market stability regulator (or assigning that responsibility to an existing regulator (*e.g.*, the Federal Reserve)) that is not limited to traditional banking institutions. This regulator would focus on capital adequacy, risk assessment, and market mechanisms to identify and prevent the trading difficulties we have seen recently. The new regulator may also revisit institutional regulatory structures to reassess their ability to effectively and systemically regulate markets. Particular attention may be focused on the large market players, given the role they played in the recent financial markets collapse.

The United States historically has been the dominant financial center and power in the world. With the growth of sophisticated markets in Europe, Asia, and the Middle East and the effects of the current financial market meltdown, such domination, however, is not likely to survive the upcoming financial market reform debate. The U.S. government will have to engage in dialogue with its international counterparts to coordinate a global economic response that would among other things, address the issue of regulatory forum shopping for the least transparent and burdensome system.

Hedge Funds and Derivatives

The new Congress and the new Administration will continue to pursue actions to better understand the role that hedge funds play in the financial market in order to determine what systemic risks they pose in the economy and what regulatory options may be appropriate. A federal court invalidated an SEC rule requiring most hedge fund managers to register with the SEC under the Investment Advisers Act of 1940. Since the rule was held invalid, the SEC has been considering how to achieve the desired goal of monitoring hedge fund activities without running afoul of the courts.

Both chambers of Congress have been studying the role of hedge funds in the U.S. economy, as has the Treasury Department, which has undertaken a study of the systemic risks that they pose. During 2007 and 2008 the President's Working Group on Financial Markets began a review of hedge fund regulation. The Obama Administration can be expected to be even more aggressive than the outgoing one in its review of hedge funds. Chairman Frank requested that the Government Accountability Office undertake a broad review of hedge funds; it has released two reports to date. The first report issued in January 2008 found that while regulators and market participants have taken steps to improve market discipline and transparency of operations, continued attention to these issues is needed. The second report, issued in August 2008, found that defined benefit pension plans need better guidance concerning the risks associated with having hedge funds and private equity funds in their portfolios. Because many hedge funds engage in off-exchange derivative contracts, Congress will continue to look closely at how the lack of regulation in this area affects pension and retirement accounts.

The Commodity Futures Modernization Act of 2000 (Pub. L. No. 106-554), which governs trading in energy and agriculture futures, generally left credit default swaps unregulated. However, due to the downturn in financial markets, there will be great pressure to impose some form of regulatory oversight or monitoring. We expect several regulatory agencies will seek to exercise some level of regulatory authority over the derivatives markets. SEC Chairman Cox and CFTC Commissioner Bart Chilton have expressed interest in regulating these investments. Chairman Frank has indicated that his committee should write the rules for credit default swaps and other derivatives, while the Agriculture committees that oversee the CFTC also wishes to pen legislation. Senator Tom Harkin (D-IA) has introduced legislation to give authority to the CFTC to regulate credit default swaps. Moreover, it has been suggested that credit default swaps be regulated by state insurance supervisors. Finally, the Federal Reserve has been most involved in issues surrounding the clearance and settlement of derivatives transactions.

Short Selling

Short selling is the practice of borrowing shares of securities that the seller does not own in order to sell them with the intention of later purchasing the same shares at a lower price to replace the borrowed shares. When used properly, this trading strategy is viewed by many as an important tool in maintaining orderly markets and an important risk management and hedging tool. Naked short selling, however, is an illegal strategy where, at the time of the transaction, the short seller has not borrowed the security or does not know where he can obtain the necessary shares to replace the borrowed shares or he never intends to replace the borrowed shares. This results in failures to deliver the shares at the appropriate time. The House Financial Services Committee held hearings to determine the impact of these practices on the capital markets and the SEC has in the last several months imposed restrictions and outright temporary bans on shorting securities to stabilize the markets. Congress will continue to monitor the SEC's role in regulating this practice and may introduce legislation if the leaders of the committees with oversight conclude that the SEC is not taking sufficient steps to prevent abuses.

Accounting Rules

Congress will continue to evaluate accounting rules in the context of their accuracy in evolving markets and their impact on the global competitiveness of U.S. markets. In the aftermath of the Enron debacle, both the Congress and the accounting rule makers began a general review of accounting rules to determine their efficacy and relevance. Congress has tended to defer to the accounting rule makers, such as the independent Financial Accounting Standards Board, on these matters but concerns regarding the role that practices such as mark to market (fair value) accounting may have had in the recent market downturn have spurred policy makers to take action. Furthermore, the International Accounting Standards Board has been much more aggressive in its pursuits of a global accounting standard in this area. A provision of EESA calls upon the SEC to conduct a study of the mark to market accounting rule. Once the study has been completed, the committees of jurisdiction will likely hold hearings to evaluate the findings and recommendations made in the report. Chairman Frank has indicated that there is consensus on a reform process for mark to market accounting and that this will be a part of his committee's agenda in 2009.

Bankruptcy Reform

Senator Dodd has publicly stated that he is interested in pursuing broad reform of the Federal Bankruptcy Code. There were several unsuccessful efforts at bankruptcy reform in the 110th Congress. Similar efforts are expected in 2009, particularly since the level of support for such changes may increase due to the state of the economy and the financial plight that many American families will continue to confront. Of particular note is a bankruptcy provision commonly referred to as the "cram down" provision that Senator Richard Durbin (D-IL) introduced. This provision would permit Bankruptcy Judges to reduce mortgage loan principal to the home's current market value for homeowners who have filed for bankruptcy. Senator Durbin initially attempted to include this controversial provision in the first housing rescue bill but it failed to garner enough support. More recently, he unsuccessfully attempted to include it in EESA. Foreclosures will continue to rise next year. As policy makers continue to seek ways of minimizing the numbers, they are likely to revisit the cram down provision as part of bankruptcy reform or other legislation, including any consumer protection, economic stimulus, or bankruptcy reform legislation introduced.

Oversight of Fannie Mae, Freddie Mac and the Federal Home Loan Banks

The importance of a healthy Fannie Mae and Freddie Mac (formerly known as government sponsored enterprises) to the larger U.S. economy as well as the housing market became acutely appreciated as the housing market and economy slipped to unprecedented low levels. A key subtitle of the Housing and Economic Recovery Act of 2008 codifies long-sought reform of their operations. Both chambers will hold hearings in 2009 to evaluate the effectiveness of the new and more powerful regulator as well as the operations of Fannie, Freddie and the Federal Home Loan Banks. Since the federal government took the major action in October to place Fannie and Freddie in conservatorship, Congress will be monitoring closely the actions of the new regulator, the Federal Housing Finance Administration. Congressional hearings will also explore how well the regulated entities are adhering to new guidelines that, among other things, restrict the types of instruments that they can hold in their portfolios and requires them to seek authorization prior to marketing new financial products.

Enforcement Measures

With the events in the financial markets in 2008, financial regulatory agencies at both the federal and state levels are poised to take a more aggressive approach to regulation and enforcement. Under an Obama Administration such efforts can be expected to intensify. Conduct that was once defensible or was at least arguably permissible in the past will now be viewed as unacceptable and inappropriate. We also expect to see the government aggressively pursue investigations in response to demands for accountability of financial services firms and executives. In this regard, we are only now starting to see what likely will be a surge in private litigation against various members of the financial services industry. EESA requires all federal and state financial regulatory agencies to cooperate with the FBI and other enforcement agencies investigating “fraud, misrepresentation, and malfeasance with respect to development, advertising, and sale of financial products.”

The SEC will remain one of the principal enforcement agencies in at least the near term. It consists of five presidentially-appointed Commissioners, with staggered five-year terms. One of the Commissioners is designated by the President as Chairman of the Commission--the agency's chief executive. By law, no more than three of the Commissioners may belong to the same political party in an effort to ensure non-partisanship. Commissioners may continue to serve beyond the expiration of their terms, until reappointed or replaced. The term of Chairman Cox expires in June 2009. Presumably, President Obama will appoint a Democrat to serve as the chairman within the first few months.

The SEC will likely adopt policies or regulations that will increase their regulatory oversight to help stabilize the markets. Specifically, the SEC may extend the restrictions on short selling. Enforcement will likely be stepped up due to public sentiment against the federal government's handling of this crisis. As stated above, the SEC might be granted oversight over credit default swaps, which would require legislation. Overall, the SEC, under an Obama Administration and supported by a more aggressive Congress, will take a much more activist role in fashioning and enforcing regulations.

Consumer Protection, Data Protection and Privacy

Many consumer protection and data security bills were introduced in both chambers during the last Congress, but they did not advance for several reasons, including ongoing jurisdictional battles between committees and a lack of clear consensus among members that legislation was necessary. The dramatic downturn in our economy has served to increase the sensitivity to and interest in initiatives related to, for example, credit cards, payday loans, and data security that a more Democratic Congress is likely to champion. One area in particular that is likely to receive renewed attention is credit card interest rate limits. Several members in both the House and the Senate introduced legislation in the 110th Congress that would limit the allowable interest rate charge to a figure in the 35 percent range. With larger Democratic majorities in the Congress next year, we expect more focus on these issues.

The data protection issues remain on the agenda of the Financial Services and Banking Committees, but were put on the backburner in the midst of the financial crisis and foreclosure problems. In 2008, multiple committees approved data security bills and legislation was pending when the House and Senate adjourned. A key issue remains whether any new federal standards should preempt laws that have been enacted in more than 35 states and whether state Attorneys General should be given authority to enforce new federal standards. In addition, there will be renewed consideration of questions such as determining what level of data breach will trigger mandatory notice to consumers. If there are additional major data security breaches next year, pressure for federal legislation could continue to grow.

For additional insights about like policy developments, please feel free to contact the principal author of this section, Micah Green, at 202-457-5258 or by email at mgreen@pattonboggs.com.

Food and Drug Law

The Food and Drug Administration (FDA) has been the subject of widespread criticism in recent years, particularly from senior Members of Congress who allege that the agency has not been enforcing existing laws and has not been adequately protecting public health. Criticism has been directed against virtually all classes of products regulated by FDA, including prescription drugs (innovator and generic), biologics, over-the-counter (OTC) drugs, medical devices, dietary supplements, conventional foods, and cosmetics.

Regardless of whether such criticism has been justified, within the past two years FDA has been criticized for a wide range of perceived lapses, including (1) failing to inspect foreign drug facilities and protect against drug contamination; (2) failing to ensure the safety of OTC cough/cold drug products; (3) wrongly concluding that low-dose exposure to bisphenol-A is safe; (4) failing to protect the food supply from unintentional contamination and intentional adulteration (*e.g.*, melamine); (5) wrongly approving an antibiotic despite data integrity concerns; (6) permitting generic drugs suspected of being manufactured in gross violation of good manufacturing practices (GMPs) to be sold in the United States; (7) failing to timely identify the source of a nationwide salmonella outbreak; and (8) failing to protect U.S. consumers from tainted food produced in China.

We anticipate that the new Secretary of Health and Human Services will desire to be responsive to Congressional concerns, and improve some of the perceived flaws within the agency. In addition, regardless of when a new FDA Commissioner is nominated by the President, a more activist, enforcement-minded FDA is likely to emerge, particularly if the agency is appropriated additional funds by Congress (as seems likely). Some have argued that FDA has suffered from excessive control and intervention by political appointees, and that decisions have been based more on political considerations and less on the law and science. It will be a challenge for new leadership to rebalance the decision-making equation and interesting to observe how much leeway Congressional critics such as current House Energy and Commerce Committee Chairman John Dingell are willing to give FDA.

The changes within FDA, however, may pale in comparison to the legislative changes imposed upon FDA and FDA-regulated industry by Congress during the next two years. Congress may introduce legislation that would:

- Establish an accelerated regulatory pathway for the licensing of follow-on versions of biological therapies;
- Prohibit or otherwise discourage the marketing of authorized generics;
- Loosen restrictions on the importation or re-importation of prescription drugs;
- Establish stringent drug pedigree requirements;

- Expand the market for generic drugs, and restrict the ability of innovator companies to block or delay generic market entry;
- Restrict direct-to-consumer (DTC) advertising and other promotional and marketing practices for medical products;
- Alter the regulation of OTC drug products marketed pursuant to the OTC Drug Review;
- Limit the extent to which compliance with certain FDA requirements may be deemed to preempt a drug or medical device manufacturer's liability in actions brought in State courts;
- Restructure the 510(k) clearance process for medical devices (based upon a pending GAO report);
- Impose substantial new responsibilities on the food industry to ensure the safety of their products, especially those products and ingredients that are imported; and enhance the authority of FDA to inspect food facilities, including records, and to impose sanctions for violations;
- Establish tighter restrictions on dietary supplements;
- Grant FDA jurisdiction over tobacco products; and
- Impose expansive new requirements to promote the safety of food, dietary supplements, drugs, medical devices, and cosmetics via passage of the FDA Globalization Act.

In short, we expect a very active Congress, and it will therefore be critically important for FDA-regulated industry, and all interested parties, to share their views and insights with Congress as early in the session as possible. We expect fast movement on many of the above issues, and delayed involvement may prove detrimental for advancing reasonable, science-based policy initiatives.

For additional insights about likely FDA policy developments, please feel free to contact the principal authors of this section, Paul D. Rubin, at 202-457-5646 or by email at prubin@pattonboggs.com, or Stuart M. Pape, at 202-457-5240 or by email at spape@pattonboggs.com.

Foreign Investment in the United States

Six months ago, with the U.S. dollar in freefall and large amounts of foreign capital looking for long-term investments, all the talk was of a fire sale on U.S. companies and infrastructure. The global economic meltdown has slowed inward investment, but will that be temporary or sustained? The answer will depend in large part on the policy choices of the new Administration and the new President's ability and willingness to direct the political debate. Traditionally, recessions strengthen underlying protectionist sentiment. Signs suggest it is already growing.

President-elect Obama appealed to the Democratic base during the primaries by talking about the need to protect U.S. jobs and to reopen NAFTA and other trade agreements. In the general election, he toned down that rhetoric somewhat, but a Congress heavily weighted in favor of the Democrats will put tremendous pressure on the next Administration's approach to foreign investment in the United States. While some view foreign investment as creating jobs, organized labor often views it as a first step toward outsourcing and will be looking for its reward for delivering a key part of the Democratic base in the election. The visceral labor opposition to the now-cancelled award of a multi-billion dollar Air Force tanker deal to the European EADS consortium may be a harbinger of things to come. President-elect Obama can expect to face Congressional demands to condition significant foreign acquisitions of U.S. assets with long-term job guarantees and greater restrictions on the export of skills and technology.

Some senior Democratic congressional staff suggest that there may be renewed interest in further reform of the Committee on Foreign Investment in the United States (CFIUS) to expand its authority beyond national and homeland security issues. The idea would be to allow CFIUS to look at whether a particular investment is in America's interests. Proponents point to Canada's foreign investment act under which the Canadian government reviews foreign investments to determine if they will have a "net benefit" for Canada. Similar standards are employed or being considered in several European economies. As the recession worsens, the call for introducing such a review standard in the United States could grow.

The Democratic leadership in Congress, particularly Chairman Barney Frank of the House Financial Services Committee, resisted calls to politicize CFIUS reviews during last year's debate on the Foreign Investment and National Security Act (FINSA). Now, however, the combination of a larger Democratic majority and significant freshman class of Members with a new President whose views on the subject appear not yet settled raise concerns that FINSA could be reexamined next year with all the uncertainty that will entail.

As we point out in the section below on the new President's approach to trade policy, his overall approach to trade in goods and services is likely to be similar to that of President Clinton. The general view seems to be that President-elect Obama is a student of history who will strongly resist any protectionist measures reminiscent of those imposed in the 1930s that deepened the 1929 recession into the Great Depression. Whether he can convince the Congress to see it his way to preserve inward foreign investment may well be an early test of his leadership.

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Health Care

While the economy and financial rescue legislation have continued to dominate the headlines, recent polls show health care continues to be an important priority for voters. The continued prominence of health care concerns reflects in part the following realities:

- 45 million Americans, including almost nine million children, are currently uninsured;

- The uninsured are expected to spend \$30 billion out-of-pocket on medical care this year;
- Health care costs are estimated to increase by 5.7 percent next year for both workers and their employers; and
- Rising Medicare and Medicaid expenditures present serious fiscal sustainability problems for federal and state budgets, which will become increasingly critical as the Baby Boomers retire.

Health Care Agenda Outlook

Republicans and Democrats agree that these problems must be addressed. In general terms, Republicans have focused on market-based solutions, increasing consumer responsibility, and providing greater transparency to drive improvements and reduce costs in the health care industry. Republicans have also promoted private insurance options and health savings accounts (HSAs). In contrast, Democrats have sought to address health care reform through federal subsidies, expansions of public sector coverage, and a larger role for the government in regulating health care delivery. Both parties have gravitated toward adopting health information technology (health IT) and quality improvement (*e.g.*, pay-for-performance and value-based purchasing).

Senate Democratic staff on the Finance Committee and the Health, Education, Labor and Pensions (HELP) Committee have already begun working proactively to lay the groundwork for comprehensive health reform through public hearings and private discussions with a range of stakeholders. Likewise, the House Ways and Means Committee and the Energy and Commerce Committee have held a series of hearings on issues including access and coverage, quality and costs of care, the role of Medicare and Medicaid, and systemic reforms.

Despite an ambitious agenda, the \$700 billion financial rescue package and burgeoning federal deficit may force Democratic leaders to reconsider broad-based health care reform in favor of more incremental measures. Nonetheless, reauthorization of the State Children's Health Insurance Program (SCHIP) and legislation to avoid a looming cut in Medicare physician payments are viewed as "must do" items and could serve as vehicles for other reforms.

Given the record \$438 billion deficit estimated by the Congressional Budget Office (CBO) for FY 2008, proposals to save the health care system money and increase its efficiency may ultimately have the greatest chance of enactment. CBO is scheduled to release a two-volume report in December 2008, which will identify proposals for savings that may be used to offset the costs of financing coverage expansions. Additionally, CBO has begun considering "dynamic scoring" to credit savings for prevention initiatives.

Under current "pay-as-you-go" budget rules, CBO's estimates will have a significant impact on the viability of any health care legislation, and the areas it identifies for potential savings will be ripe targets for policy-makers. For example, CBO's estimated savings from expansion of comparative effectiveness research have totaled hundreds of billions of dollars and could help drive passage of related legislation.

Congressional Priorities

Before the financial crisis, Congress was poised to tackle comprehensive health care reform next year. As noted above, budgetary realities may instead produce more piecemeal legislation. Congressional Democrats are nonetheless anxious to consider SCHIP reauthorization legislation that would expand the program to families with higher income levels. The next Congress is also apt to seek a long-term solution to the Medicare physician payment fee schedule and to address a range of priorities that generally enjoy bipartisan support.

Senate Finance Committee Chairman Max Baucus (D-MT) and Ranking Member Charles Grassley (R-IA) have a history of working closely together. Despite this year's dramatic partisan split over the passage of the "Medicare Improvements for Patients and Providers Act" (Pub. L. No. 110-275), they will likely work together to move legislation. Senator Baucus continues to stress his commitment to health care reform despite the financial crisis. In 2008, the Senate Finance Committee held eight hearings on health care reform. The topics included reviewing health insurance markets, creating incentives for delivery system reform, improving health care quality, and reforming the health benefits in the tax code.

Chairman Baucus has also held a number of meetings with individual Members of the Finance and HELP Committees. Earlier this year, he sponsored, "Prepare for Launch," a health care reform summit attended by Finance Committee members and other Senators who have demonstrated leadership in this area. Further, Senator Baucus has jointly introduced legislation with Senate Budget Chairman Kent Conrad (D-ND) to expand comparative effectiveness research as a tool to improve quality and reduce costs, and the bill is a priority for consideration by the Committee. During the anticipated "lame duck" session of Congress after the elections, Senator Baucus also intends to hold a hearing and release a white paper on health care reform priorities. The white paper will likely pitch health care as a vital priority for the federal government to address before it becomes a national crisis similar to the financial sector.

Whether Chairman Edward Kennedy (D-MA) returns to work in early January to again lead the HELP Committee remains to be seen. While he has been recovering from a brain tumor, his staff has focused intensely on health care reform. He intends to play a pivotal role in the health reform debate on issues involving employer-provided health coverage and has directed his staff to hold regular stakeholder meetings to formulate ideas and strategies for reforming the Employee Retirement Income Security Act (ERISA). Senator Kennedy recently held a videoconference with Democratic Committee members to begin formalizing a health care reform plan for the next Congress. Ranking Member Mike Enzi (R-WY) will likely take a different approach and is expected to advocate his own health reform proposal, "10 Steps to Health Care Reform." His bill eliminates the employee health benefit, presents working families with a standard tax deduction to purchase health insurance, offers tax subsidies, and provides market-based pooling to reduce growing health care costs and increase access.

Although the leadership of the House Ways and Means Committee will not likely be in play, the House Ethics Committee announced a formal investigation into allegations made against Representative Charles Rangel (D-NY). While Representative Rangel is expected to remain Chair, Representative Stark will play a critically important role in any health reform effort. He has focused considerable interest on Medicare managed care plans, rising health costs, the private insurance market, Medicare's physician payment system, and health information technology. Full Committee Ranking Member Jim McCrery (R-LA) is retiring, and Representative Dave Camp (R-MI), currently Ranking Member of the Health Subcommittee, is favored to succeed him. Representative Camp has been a leader on health information technology issues and will continue his efforts to preserve Medicare Advantage and Health Savings Accounts (HSAs) from an expected Democratic effort to

amend these options. Due to the untimely death of Representative Stephanie Tubbs Jones, a seat on the Committee has opened up and is likely to be filled by Delegate Donna M. Christensen (D-VI).

House Energy and Commerce Committee Chairman Dingell has already announced his plans to advance major Food and Drug Administration (FDA) reform legislation in the next Congress, with a focus on food and drug safety. Health Subcommittee Chairman Frank Pallone (D-NJ) has shifted his attention to health reform more recently with hearings addressing the rising costs in the face of poor health outcomes, the problem of the uninsured and the underinsured, and the inability of U.S. companies to compete with global firms in countries that offer universal care. Representative Pallone has led efforts in the House to assist states with increased Medicaid costs and will be heavily involved in SCHIP reauthorization in the next Congress. Committee Republicans, led by Ranking Member Joe Barton (R-TX) and Health Subcommittee Ranking Member Nathan Deal (R-GA), are likely to continue their strong opposition to expansion of SCHIP coverage to higher income children and families during reauthorization of the program next year. Given the increased Democratic Majority, Republicans are likely to lose seats on the Energy and Commerce Committee.

The Obama-Biden Plan

President-elect Obama proposes to expand access to high quality, affordable health care for all Americans. The federal government would play a significant oversight and investment role in the three-part plan, which builds upon the current U.S. health care system. According to its authors, the plan would save a typical American family up to \$2,500 every year on medical expenditures by:

- Providing affordable, comprehensive and portable health coverage for every American;
- Modernizing the U.S. health care system to contain spiraling health care costs and improve the quality of patient care; and
- Promoting prevention and strengthening public health to prevent disease and protect against natural and man-made disasters.

President-elect Obama intends to create the National Health Insurance Exchange Program, similar to the Massachusetts model, through which individuals could purchase either a public plan or a qualified private insurance plan. Participating insurers would be required to offer coverage on a guaranteed issue basis, to charge a fair and stable premium that is not rated on the basis of health status, and to meet certain standards for quality and efficiency.

The plan would impose a “play or pay” mandate to require employers either to offer health insurance to their employees or pay a tax to help fund the public plan. Small businesses could enter into the National Health Insurance Exchange to purchase a public or private plan for their employees, or if eligible, qualify for subsidies. President-elect Obama’s plan would also reimburse small business health plans for a portion of catastrophic costs incurred above a threshold if they guarantee such savings are used to reduce the cost of worker’s premiums.

President-elect Obama has rejected the broader mandate for individuals to obtain health coverage advocated by Senator Hillary Clinton (D-NY) during the primaries in favor of a requirement for coverage of all children. The plan calls for expansion of eligibility under Medicaid

and the State Children's Health Insurance Program (SCHIP). It would allow states to maintain existing health reform initiatives if they meet the minimum standards of the national plan.

The campaign has estimated the President-elect Obama's plan would cost between \$50 billion and \$65 billion, which would be paid by expiring tax cuts enacted in 2001 and 2003 for families that make more than \$250,000 a year. Other cost savings are projected through increased investment in health IT as well as prevention and chronic disease management programs. The plan calls for policies that promote generic drugs, allow prescription drug reimportation, and repeal the ban on direct drug price negotiation by the Secretary of Health and Human Services (HHS) under Medicare Part D. President-elect Obama's plan also would reduce Medicare Advantage (MA) plan payments to fee-for-service levels.

To improve quality within the health care system, President-elect Obama supports an independent institute to guide comparative effectiveness reviews and requires reporting on preventable errors. Through the National Health Insurance Exchange and other public programs, providers would be rewarded for their performance. The plan would also address health disparities and require quality and price transparency from providers and health plans. On a recent campaign stop, President-elect Obama added that he would prevent Medicare and Medicaid waste and abuse by allowing the HHS Inspector General to implement anti-fraud measures in contracting arrangements by CMS.

Legislative Health Care Priorities in the Next Congress

SCHIP Reauthorization. The current authorization for the SCHIP program will expire on March 31, 2009. Congress temporarily extended the program's funding in 2007 when the House was unable to sustain a veto-proof majority to pass the Children's Health and Medicare Protection (CHAMP) Act, which would have expanded eligibility and benefits under the program. The next Congress will likely build upon the CHAMP Act's provisions, and President-elect Obama's plan similarly calls for expanded Medicaid and SCHIP eligibility, so these programs could continue to serve their critical safety net functions.

Medicare Physician Payment "Fix". The next Congress must adopt changes to the Medicare Sustainable Growth Rate formula before January 1, 2010, to avoid a scheduled 20-percent cut in physician payments. After several years of consecutive short-term patches, lawmakers have signaled they are ready to take on the difficult task of fundamentally overhauling Medicare's physician payment system, reflecting serious concerns that physicians will no longer take Medicare beneficiaries as new patients.

Medicaid Reform. In the first actuarial analysis issued by CMS, the agency declared Medicaid spending is unsustainable and will rise to \$674 billion by 2017. Rising entitlement pressure on the budget is a concern for both political parties, and the recent CMS analysis could prompt introduction of new proposals to reform Medicaid in the next Congress. However, significant cut-backs in Medicaid spending are unlikely to advance in the face of opposition from key Democrats in the House and Senate. By contrast, Democratic leaders have indicated they will seek to overturn Bush Administration regulations restricting Medicaid coverage, to authorize the expansion of coverage to uninsured adults, and potentially, to increase Medicaid drug rebates.

Increased Coverage. Members of both parties agree that the problem of the uninsured must be addressed, but their approaches differ substantially. Democrats will likely seek to expand eligibility for federal health care programs or create a federally operated and administered national

health insurance risk pool for small businesses. With increased Democratic majorities in the House and Senate, support for Republican-backed health savings accounts and consumer-driven health care approaches will substantially wane. Given budgetary constraints, however, changes in the tax treatment of employer-sponsored health insurance could garner consideration on a bipartisan basis.

Improved Quality. A range of quality improvement initiatives seek to achieve health outcomes by paying more for reaching certain results rather than paying more simply for performing more procedures. Congress most recently established a quality initiative within the End-Stage Renal Disease Medicare Program that would link quality improvement and attainment to provider payments. Congress may adopt additional measures as a tool to increase the quality of care and to reduce the over-utilization of services and procedures that many lawmakers feel the current payment system encourages.

Health IT. Committee leaders in both the House and Senate have advanced several different versions of health IT legislation, but privacy and funding concerns have derailed attempts to date to enact a bill. Health IT remains a bipartisan priority, however, and renewed legislative action is expected in the next Congress.

Medical Homes. By providing comprehensive primary care that is readily accessible, the medical home concept aims to improve the quality of primary and preventive care, ensure effective care coordination, and reduce more severe illnesses and resulting utilization of higher cost services. President-elect Obama encourages adoption of this model, which has also been endorsed by the Medicare Payment Advisory Commission. It has also garnered bipartisan support in Congress with increased funding for medical home demonstration projects. A recent solicitation by the Commonwealth Fund for medical home demonstrations in partnership with community health centers may provide evidence regarding the effectiveness of the model and could influence future funding decisions by Congress and the Administration.

Health Disparities. The issue of health disparities resonates across the aisle and is high priority for Democrats, especially for Members of the Congressional Black, Hispanic, and Asian-Pacific Islander Caucuses. Disparities legislation stalled in the 110th Congress, but Democrats are likely to reintroduce proposals next year to reduce disparities, increase health literacy and cultural competency, and expand safety net coverage under health care programs.

Comparative Effectiveness. As noted previously, comparative effectiveness research (CER) has gained considerable interest among policy-makers for its potential to control rising costs while improving the quality of care. One of the most contentious issues is whether the findings issued by a CER entity should be used to shape coverage and payment policy. Although supporters of CER in Congress have crafted bills that explicitly de-link research findings from coverage and payment considerations, the potential savings are strong incentives to promote broader use of CER. Early action is expected next year on legislation jointly introduced by Senators Baucus and Conrad.

Medicare Part D. As monthly premiums under Medicare's Part D prescription drug program continue to rise, Democrats remain concerned about closing the gap in coverage for the 3.4 million beneficiaries who fall into the "doughnut hole." Further, rising plan premiums under Part D have drawn the ire of Representative Henry Waxman (D-CA), Chairman of the Committee on Oversight and Government Reform. Along with other Democratic leaders, Representative Waxman has called for the payment of rebates by pharmaceutical manufacturers for drugs dispensed to low-income, dual eligible beneficiaries, who previously received their medications under Medicaid.

NIH Funding. Congressional appropriators, particularly Senate Appropriations Labor, Health and Human Services, and Education Subcommittee Chairman Tom Harkin (D-IA) and Ranking Member Arlen Specter (R-PA), will continue to push for increased funding for the National Institutes of Health (NIH) despite the bleak financial state the next Administration will inherit.

HHS Regulatory Agenda

Implementation of MIPPA. The new Administration will oversee continued implementation of the “Medicare Improvements for Patients and Providers Act” (MIPPA) enacted earlier this year. Among its provisions, MIPAA provided an 18-month increase in physician payments through reductions in Medicare Advantage plan payments, authorized the HHS Secretary to cover new preventive services recommended by the U.S. Preventive Services Task Force, required physicians to adopt e-prescribing systems by 2011, delayed the durable medical equipment competitive bidding program for 18 months, and reduced co-payments for mental health services.

Quality and Health IT. The new Administration is expected to continue ongoing efforts within HHS to speed the adoption of health IT, promote the development of quality standards, and increase the information available to health care consumers. The new CMS Administrator will likely seek to build upon established quality programs such as the Physician Quality Reporting Initiative, the Hospital Quality Initiative, and the Nursing Home Quality Initiative.

HIPAA and Privacy Issues. HHS has been criticized for its performance in investigating complaints of HIPAA noncompliance and Democratic leaders will likely push the new HHS Secretary to step up enforcement efforts in this area, including the new statutory requirements established in the Genetic Information Nondiscrimination Act of 2008. It is also likely that the push for health IT will lead to a renewed interest in strengthening regulatory privacy protections.

Hospital-Acquired Conditions (HACs). CMS reduced payment for hospital-acquired infections in its Inpatient Prospective Payment System FY 2009 Final Rule. In addition, CMS has encouraged State Medicaid Agencies to deny payment for select HACs. CMS also has initiated three National Coverage Determination proceedings for a category of “never events.” Beyond the hospital sector, the Agency may seek to extend all of these policies to a broad range of providers.

Recovery Audit Contractors. In early October, CMS announced the nationwide expansion of a permanent Recovery Audit Contractor (RAC) program and the selection of four new contractors. Key Members of Congress, including Representatives John Dingell, Charles Rangel, Pete Stark, and Frank Pallone, have called for the Government Accountability Office to examine the changes made in the permanent program, reflecting in part their concerns about the payment incentives for contractors.

Election Impact on Key Committees

The additional Democrats in the House, of course, will result in increased Democratic ratios on key committees. Nowhere is the change likely to be more dramatic than on the House Ways and Means Committee. A significant number of Republicans lost by either retirement or electoral defeat--Representatives McCreery, Ramstad, English, Weller, Hulshof, Ron Lewis, Tom Reynolds, and John Porter. Democrats will have three seat changes--Representatives Rahm Emanuel, who will depart the committee for the Chief of Staff position in the Obama White House, Representative

McNulty's retirement, and Stephanie Tubbs-Jones, whose seat was not filled, which produces a total potential change of ten current Members. Depending on how the ratios are restructured, potentially the size of the Committee may shrink. We could have as many as fourteen new Members of the Ways and Means Committee, which would represent a dramatic change for a committee where new seats rarely open up. We anticipate that Congressman-Elect Dan Maffei, who is taking the seat previously held by Representative Walsh, will be selected to serve on the Ways and Means Committee where he previously served as staff, and given Representative McNulty's retirement.

On the Health Subcommittee (which reorganizes itself by full committee seniority) departing Members include Representatives Emanuel, Tubbs-Jones, Ramstad, English, and Hulshof, resulting in a dramatically new Health Subcommittee. We perceive the changes in the House as further strengthening the position of Speaker Nancy Pelosi and her leadership team. Interestingly, it looks like the number of Blue Dog Democrats actually declined somewhat from the last Congress. We label the House of Representatives not as liberal, but as pro-Obama, giving the new administration, relatively broad ability to direct health care policy in the House. We expect Representative Stark to retain the Chairmanship of the Health Subcommittee. He will have a stronger position because he will have a relatively new Subcommittee roster with more Democrats, fewer Republicans, and the ability to back-channel quite easily with the new White House Chief of Staff.

While the membership of the Energy and Commerce Committee will not change as dramatically, the leadership of the Committee appears to be in dispute. Representative Henry Waxman, the second most senior Democrat on the Committee, is reportedly challenging Chairman John Dingell, the longest-serving Democrat in the House, for the position. In his current role as Chairman of the Oversight and Government Reform Committee, Representative Waxman has led major investigations of pharmaceutical manufacturers and Medicare managed care plans, among others. If Representative Waxman were to replace Chairman Dingell, the committee's agenda would likely shift to the left politically on many issues, which could complicate efforts for the Obama Administration to govern from the middle.

As of this writing, three Senate seats remain in doubt; so an in-depth analysis must await the final outcomes. Clearly, however, Democrats did not reach their stated goal of 60 seats but they have put a comfortable cushion on what had been previously narrow Democratic margin. Not only are several seats undecided but a number of Senators will be appointed for interim terms as a result of the election. We believe that Representative Jan Schakowsky of Illinois has the inside track to take the seat of President-Elect Obama. We believe current Lt. Governor John C. Carney of Delaware has the inside track to replace Vice President-elect Joe Biden.

Given the uncertainty of three Senate elections, it is hard to be specific on committee ratios, but the range of additional seats particularly on Finance is narrow, with perhaps two possible additional Democratic seats. Senator Pat Roberts is most likely to lose his seat on the Finance Committee. Changes at the staff level are likely to be more dramatic than changes at the Member level.

Health, Education, Labor and Pensions (HELP) Committee Democrats have discussed the formation of a new Health Subcommittee, possibly chaired by Senator Hillary Clinton (D-NY). Senators Judd Gregg (R-NH) or Richard Burr (R-NC) both may be considered to serve as Ranking Member. Organization of the Committee will become clearer during the November 17 lame duck session, but at least two seats became vacant due to President-elect Obama and retiring Senator Wayne Allard (R-CO).

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Homeland Security

Issues related to Homeland Security will continue to be front and center in the 111th Congress under President-elect Obama. The Department of Homeland Security (DHS), like the Department of Defense, is one of the few agencies that continues to see high profile Member interest and budget increases. The leaders of the existing committees of jurisdiction have shown a commitment to working together to craft policy, with differences driven more by demographic and regional issues (urban vs. rural states, big cities vs. small cities) than by party affiliation. We anticipate continued bipartisan cooperation in a host of areas, though gains by the Democrats in the House and Senate and the large Democratic majority in the Senate will reduce Republican influence in the process.

We expect the Democratic majority in the Congress to give the new Secretary of DHS a “honeymoon” of about six months to make assessments and potential changes in how the agency is run. Both Democrats and Republicans in Congress are concerned about the pace of implementation on a host of congressional mandates from the 9/11 bill to various post Hurricanes Katrina and Rita issues. Many of the ongoing and planned initiatives and programs proposed by Secretary Chertoff will be completely reexamined with the Democrats solidly in control of Congress, particularly now. President-elect Obama has placed an emphasis on preventing nuclear terrorism, strengthening bioterrorism capabilities and protecting cyber security issues, all priorities that would likely be taken up by the Committee under his administration.

The potential candidates for DHS Secretary abound at this point. History has provided two examples, one with political experience on the national stage and another without. Pundits argue whether the Secretary needs to be someone from a law enforcement background like Los Angeles Police Chief William Bratton or even the head of the U.S. Coast Guard Thad Allen. Some have said someone like Arizona Governor Janet Napolitano, who understands the challenges of border security, would be a possibility as well. There are a host of Democratic Members of Congress who might be interested, including House Homeland Security Chairman Bennie Thompson (D-MS), who has been a vocal critic of Secretary Chertoff for some time, or Homeland Security Subcommittee Chairman Henry Cuellar, whose focus is on emergency communications, preparedness and response. One other member, Homeland Security Subcommittee Chairman Rep. Jane Harman (D-CA), is also rumored to be considered for the role based on her long standing expertise on intelligence issues. Finally, former Representative Tim Roemer and active member of the 9/11 Commission is another possibility. He has continued to focus on the need for major reforms and streamlining of roles at DHS, which continues to be an area of interest for Democrats.

We expect Congress to increase its scrutiny of departmental agencies, including the Transportation Security Administration (TSA), Customs and Border Protection (CBP), and the Federal Emergency Management Disaster Agency (FEMA), on the effectiveness of their programs like aviation and port security, and on natural disaster preparedness and their levels of funding. Congress will work with the White House to increase oversight of the agency and review Bush-era policies. Key agencies, like FEMA, will also be re-evaluated in the 111th Congress. Democrats in Congress have argued that the role and mission of FEMA has been completely subsumed in DHS, causing a lack of adequate funding and preparedness capabilities for assisting state and local governments in disaster preparedness, as evidenced by FEMA’s response to Hurricanes Katrina and Rita.

The primary focus of DHS remains on preparedness for incidents that pose the greatest potential consequences to human life and the functioning of our society and economy. Other important, but lesser, priorities include better security at ports of entry and along the borders; further integration of counter-terrorism databases; enhanced visa issuance processes; biometric entry requirements; ensuring access to passenger name record information; monitoring the progress of the Western Hemisphere Travel Initiative; resolving differences with state governments over implementation of the drivers' license requirements of the Real ID Act; and full enforcement of immigration laws.

House Homeland Security Committee

In the 111th Congress, Representative Bennie Thompson (D-MS) will remain as Chairman of the Committee and Representative Peter King (R-NY) will remain as Ranking Member. In the 110th Congress, Speaker Pelosi and Chairman Thompson came through on their promise to enact the remaining 9/11 Commission recommendations within 100 hours of taking control of the House. Democrats will turn to cleaning up unfinished business from their “Homeland Security 100 day agenda” and push DHS to complete implementation of the bill and focus on a comprehensive DHS Reauthorization bill which will review and potentially change a variety of mission critical areas. Expect continued widespread oversight of all of the Bush Administration policies as well as on large homeland security contracts. Other items include:

- *Cargo and Port Security.* The 9/11 Commission Recommendations Act included the mandate to screen all U.S.-bound cargo containers at the port of shipment. Cargo and port security will remain key issues, as DHS and CBP work for increased inspection of containers abroad, the ongoing need for more customs inspectors, and regulations to implement the new port security laws. Democrats will continue to push DHS hard to implement the 9/11 law that requires DHS to screen 100% of all cargo by 2012. Secretary Chertoff and others have informed Congress that this deadline is not feasible and have met severe Democratic Congressional pushback.

- *Aviation Security.* The 9/11 Commission Recommendations Act Bill also focused on the ongoing need to secure air cargo security, which continues to be a contentious issue, as well as the need to better screen airport employees as well. Expect Democrats to focus on problems surrounding the decreasing lifespan on the Explosives Detection Systems machines at airports, the need for “smarter” technology and ongoing implementation of TSA rulemakings.

- *Chemical, Biological, Radiological, and Nuclear Threats (CBRNE)* refers to terrorist threats emanating from chemical, biological, radiological, nuclear and explosive sources, a continued problem area for DHS. The agency has issued standards for radiological equipment; however, the radiological equipment does not currently meet the standards. Chemical detection is further along than biological detection, but improved systems and wider deployment is a priority. Improved explosive detection capabilities are also still needed and will continue to be a high-demand technology. Democrats will emphasize the need for additional measures to enhance prevention of nuclear terrorism and strengthen bio-protection and chemical security.

- *Emergency Communications and Interoperability of Communication Equipment.* This was a critical component of the 9/11 bill and still remains a sticking point with Democrats. Expect a focus on the need for DHS and the FCC to work better together with first responders to implement a real system that works.

- *Medical Surge and Mass Prophylaxis.* The national priority is to establish “emergency-ready”

public health and healthcare entities across the Nation working with HHS, NIH, and CDC. Medical surge and mass prophylaxis is the concept of mass dispensation of medicine and vaccines to fight terrorist-released disease strains, such as small pox, etc., or natural occurring strains such as avian flu. Expect Democrats to focus on the the current inability of state and local hospitals and health systems to absorb huge amounts of casualties and the need to better integrate them into emergency response and preparedness planning.

- *Border Security.* Democrats on the committee have been very critical of DHS' implementation of the "Secure Border Initiative," and will hone in on the agencies inability to secure the southern border. The search for a balance between traditional physical security measures like the 700-mile fence and increased Border Patrol manpower and new technology and tactical infrastructure will be a critical part of the debate. .

- *International Borders and Biometrics.* DHS continues to focus on improved screening capabilities at our international ports of entry to prevent terrorists and criminals from successfully entering our borders. DHS has integrated counter-terror databases and along with the State Department, has enhanced visa issuance processes. DHS has implemented US-VISIT biometric entry capabilities at 117 airports, 16 seaports, and 153 land ports of entry. Democrats are concerned about privacy issues, lack of sufficient consultation with the private sector and whether or not they believe the agency really has secured our borders. Expect additional oversight on these programs on an ongoing basis.

- *Credentialing and Secure Travel Documents.* DHS continues to work on programs to create secure travel and identification documents. This includes developing standard, secure credentials that give a high degree of confidence that an individual is not using false or stolen documents to enter the U.S. or to access our transportation systems or sensitive critical infrastructure. The Western Hemisphere Travel Initiative has been implemented, and Congress will be monitoring the success of the program. The REAL ID Act, which focuses on working with states to develop standards for secure driver's licenses, has not been successfully implemented and majority of states have rebelled against the program, forcing DHS to extend deadlines. Some states have even passed anti-Real ID legislation, prohibiting state employees or state funds being used to support the program. Democrats will need to step in and identify real solutions to these problems.

- *FEMA/Emergency Preparedness, Readiness and Response.* Evacuations and damage resulting from Hurricanes Gustav and Ike have provided the opportunity to assess the evolution of FEMA's abilities since Hurricane Katrina. Although FEMA's abilities have improved, Gustav and Ike demonstrate the need for continued improvement at all levels of government across the country to improve emergency operations plans for catastrophic events such as a major terrorist attack or natural disaster, and the need to fund such requirements. Democrats on the committee may again revisit whether or not FEMA should be in DHS or pulled out as a stand-alone agency like it was pre-9/11.

- *Critical Infrastructure Protection.* Critical infrastructure protection that includes ports, transit, chemical, nuclear and power plants, and iconic buildings remains a high priority. Democrats are skeptical that the technology currently employed by DHS will protect infrastructure. They will likely push for additional regulations to mandate change in this area. Chemical plants continue to be a concern. Although DHS issued the Chemical Facility Anti-Terrorism Standards (CFATS) in April, many House and Senate Members believe CFATS does not go far enough, and plan to introduce legislation that would crack down even harder on companies. As a Senator, President-elect Obama supported making CFATS permanent. Both he and Senator Biden cosponsored legislation in the 109th Congress that would

have mandated a conversion to “inherently safe technologies” when feasible at chemical plants, would have provided for stricter state requirements, and would have ensured a role for EPA in overseeing certain facilities. Senator Biden also sought to expand CFATS jurisdiction to high-risk water facilities (particularly those using gaseous chlorine). The debate over protection of critical infrastructure and how to fund the requirement will continue.

- *Cyber security.* President-elect Obama has featured cyber security as a key element of his homeland security plans. The DHS National Cyber security Division may receive additional attention and funding for its missions of building and maintaining an effective national cyberspace response system and implementing a cyber-risk management program for protection of critical infrastructure.

- *Homeland Security Management Reform.* Democrats will likely hold high-profile hearings and investigations regarding management/re-structuring of DHS. The creation of a single, principal point of oversight and review for homeland security remains unfinished business from the 9/11 Commission recommendations.

House Judiciary Committee

Representative John Conyers (D-MI) will remain at the helm of the committee. Representative Bobby Scott (D-VA) will retain the chair of the Crime, Terrorism, and Homeland Security Subcommittee. As with the Senate Homeland Security Committee, the main focus for the Democrats will be enhanced oversight.

With the Democrats solidly in control of both the House and Senate, they will likely reexamine the balance between the need for security and surveillance and the need to increase protections for civil liberties. With President-elect Obama in the White House, House Democrats will engage in oversight and investigation of the former Bush Administration programs and actions, such as the status of detainees.

Senate Homeland Security and Governmental Affairs Committee

Both Democrats and Republicans have similar agendas, and have been vocal critics of the Bush Administration. Key issues will remain focused on infrastructure security and border security, with an emphasis on transit (airline and rail) security, supply chain security as well as cyber security and potentially increased scrutiny and regulations around chemical plant security.

It is uncertain whether Senator Lieberman will be able to retain his role as Chairman or if he will be relegated to a subcommittee chair as a result of his active support for Senator McCain’s presidential bid. Vocal critics of Senator Lieberman, including Senators Levin (D-MI) and Lautenberg (D-NJ) (who resigned from the committee in protest two years ago), would be possible candidates to replace him. Senator Susan Collins (R-ME) is expected to continue to serve as the Ranking Member.

All areas under the committee’s jurisdiction, including potential investigations of agencies within its jurisdiction, will be a major theme. Continued efforts to increase funding for the Transportation Security Administration will also be a focus. Regulations aimed at infrastructure security are generally expected to remain on the agenda, with explosive-detection and aviation security specifically standing out as issues that will remain a priority focus. This committee will also focus on the same issues raised by the House Homeland Security Committee as listed above.

The leadership of the Senate Judiciary Committee is not expected to change. Senator Pat Leahy (D-VT) is expected to remain Chairman and Senator Arlen Specter (R-PA) is expected to serve as the Ranking Member.

With a solid Democratic majority in the House and Senate, a comprehensive immigration reform bill will again be on the table. Like its predecessor bills, new legislation would be a compromise between legalization of illegal immigrants and increased border enforcement. The increased Democratic majority would also result in a considerable amount of time dedicated to oversight hearings and investigations.

House and Senate Appropriations Committee (Subcommittee on Homeland Security)

While the political climate in the 110th Congress did not allow the Homeland Security Appropriations bill to be passed as a stand-alone bill, it was one of only two appropriations bills to pass before the Congress recessed. With the leadership of the committee remaining in place and a solid majority in both chambers, the Democrats will probably work to expedite the fiscal year 2010 budget process and to clean up any unfinished business from fiscal year 2009. In the full committee, debate will focus on how to wind down spending for the Iraq war effort, and how to shift the focus of the Global War on Terrorism to Afghanistan and Pakistan. The homeland security subcommittees will also like undertake an assessment of the nations ability to respond to potential natural disasters, examining the evolution of DHS and FEMA's abilities from Hurricane Katrina in 2005 and this year's Hurricane Ike. Senator Byrd (D-WV) serves as both the Chair of the full Appropriations Committee as well as the Homeland Security Subcommittee. Members are concerned about his overall health and it is unclear how this will be handled in the 111th Congress.

For additional insights about likely policy developments, please contact the Co-Chairs of Homeland Security, Defense and Technology Practice Groups: Norma M. Krayem, at 202-457-5206 or by email at nkrayem@pattonboggs.com or Stephen J. McHale at 202-457-6344 or by email at smchale@pattonboggs.com.

Native American Policy

In his campaign materials, President-elect Obama included only general policy statements on Native American issues. They were not specific enough to offer real insight into how he will modify or extend current Indian policy. Because the issues faced by Native governments are so directly affected by decisions made by the Executive Branch (particularly the Department of the Interior), President-elect Obama's choice of policy makers will have a significant impact on Native governments and their interests. Moreover, because many Native governments still rely on federal appropriations to fund basic governmental services, the ways in which the new President seeks to address the economy through the Administration's budget requests also will have a significant impact on Indian Country.

For the same reason, the way in which the 111th Congress addresses the federal budget deficit likely will affect the ability of Native governments to obtain the federal funding needed to address fundamental needs in Indian Country. Furthermore, the new makeup of Congress could have a significant impact on a wide-range of Indian-related legislation that stalled in the current Congress, including legislation relating to Indian health care, Indian water rights settlements, Indian land claim settlements, and federal recognition bills. Also unfinished this year were legislative efforts to reauthorize the small and disadvantaged business (8(a)) programs, including contracting programs that have been beneficial for Native-owned businesses.

Notwithstanding the substantial increase in the majority of Democrats in the House and the Senate, the widening of the gap between the number of Democrats and Republicans will not by itself likely make a significant difference on the way Indian issues are managed on the Hill. While the Democrats' enhanced majority in the Senate may help move some important legislation, the ability of one Senator to place a hold on a bill could continue to impede some key Indian Country initiatives. Generally, however, the Administration and the Congress are likely to be more in step on Indian issues and on the Administration's Native-related political nominees.

President-elect Obama's transition team for the Department of the Interior includes several people who are very familiar with the range of Native issues that are of particular concern to tribal governments. Based on their previous experience with these issues, the Obama Administration's Interior Department is likely to be more focused on assisting Native Americans and more comfortable with the federal government's role as trustee. As a result, we believe there will be a greater emphasis on the settlement of Indian land and water rights claims, a greater focus on finding a substantive solution to the backlog of federal recognition requests, and genuine efforts to address the dire consequences that a long history of chronic under-funding has wrecked on tribal detention facilities and tribal education. Presumably the Indian Health Service and HUD's Indian Housing programs will benefit from increased attention as well. However, given the nation's economic condition and budgetary constraints, the Administration and Congress may well increase their attention on tribal economic development (by including more tribal provisions in tax, economic development, and small business legislation) as a way to help reduce the need for additional appropriated funds. Indeed, we caution that the needs are so great, the backlogs so severe, and the expectations so high, that tribal governments may come to feel that the Obama Administration cannot address needs fast enough.

For additional insights about likely policy developments, please feel free to contact the author of this section, Heather Sibbison, at 202-457-6148 or by email at hsibbison@pattonboggs.com.

Tax Policy

When he takes office in January, President-elect Obama will enjoy increased and now commanding majorities of Democrats in both the House of Representatives and the Senate. As a result, ratios on the Congressional tax committees may well shift markedly in favor of the Democrats, thus paving the way for a comparatively more accelerated tax legislative process than has been possible in prior years, particularly in the Senate where the Democrats will in 2009 enjoy an enhanced majority.

The centerpiece of candidate Obama's tax program was a tax cut for American families earning less than \$250,000 per year, presumably to be provided through a tax rebate intended to

offset payroll taxes. The proposal would be paid for by increasing taxes on the incomes of families earning more than \$250,000 per year. This would result in an increase in the top individual tax rate from 35 to 39.6 percent and increase in the 15 percent tax rate on capital gains and dividends to 20 percent. Candidate Obama argued that this would be achieved not by “raising taxes,” but by simply allowing portions of the Bush tax cuts enacted in 2001 and 2003 to expire.

Campaigns are one thing, but governing is quite another. When they formally take office in January 2009, President Obama and the new Congress will face the most daunting tax policy challenges in at least a generation and perhaps longer. Revenues will be at low levels as the economy wallows in a deep recession. Budget deficits will continue to soar as new spending is authorized to combat the recession and deal with the aftermath of the meltdown of 2008. The scheduled expiration of the Bush tax cuts at year-end 2010 will threaten to trigger the largest de facto tax increase in American history at the very time when fiscal stimulus may still be needed. Demands for revenues to “fix” the alternative minimum tax, address the growing crisis in entitlements and implement the domestic social agenda on which the Democrats were elected will be unceasing.

Committees of Jurisdiction

Representative Charles Rangel (D-NY) will remain Chairman of the House Ways and Means Committee, and retiring Ranking Minority Member Jim McCrery (R-LA) will likely be replaced by David Camp (R-MI) or Wally Herger (R-CA). While the roster of Majority Members of the Ways and Means Committee will remain relatively unchanged in the 111th Congress, the retirement of six Republican Members of the Committee will alter the composition of the Minority roster. With the Democratic pick up, it can be expected that the number of Democrats on the Committee will increase to closer to 2-1, thereby strengthening Chairman Rangel’s ability to move legislation through his committee.

On the other side of the Capitol, the membership of the Senate Finance Committee will remain relatively unchanged in the 111th Congress. Given the large gains by the Democrats in the Senate, the ratios on the Committee could change, resulting in an additional Democratic member. Senator Max Baucus (D-MT) will remain Chairman and Senator Chuck Grassley (R-IA) will remain Ranking Minority Member. While Senators Grassley and Baucus have a history of working closely together on issues that attract bipartisan support, Senator Baucus will likely face increased pressure from Senate Democratic leadership to pursue a more liberal tax policy agenda.

Fulfilling the Basic Campaign Promise to Middle Income Americans

Democrats may decide to provide the promised tax cuts for middle and low income Americans immediately, but not to seek early repeal of the Bush tax cuts before they expire automatically on December 31, 2010, both for fear of stalling the hoped for economic recovery and in an attempt to avoid cries of “tax and spend” from the beleaguered Republican minority. Instead, the Bush tax cuts that apply to Americans with annual incomes above \$250,000 could be allowed to expire in 2010. The estate tax could be reinstated at that time with a larger exemption for smaller and medium-sized estates and possibly a somewhat lower rate of tax. Advocates for complete repeal of what Republicans have labeled the “death tax” may have to wait for more than a decade, and perhaps longer, to have another chance for success.

Increasing Tax Revenues to Pay for Other Tax Initiatives

Congress may also face pressures to enact new economic stimulus measures, extend and perhaps expand tax incentives for alternative energy and environmental technologies, and provide other tax relief. These pressures will necessitate a search for additional tax revenues within the existing tax system, particularly from Wall Street, wealthy investors and the business community.

--Wall Street, but not Main Street, may face new taxes in response to the meltdown of 2008 and the perception that wealthy investment fund managers and other executives continued to receive excessive compensation during the meltdown. For example, hedge fund, private equity, and real estate fund managers who now have an opportunity for tax-preferred capital gains on their so-called "carried interests" in the funds they manage may find much of that income re-characterized as income from personal services that will be taxed at the reinstated higher rates for ordinary income. New limitations could be imposed on the ability of companies to deduct executive compensation, including amounts that executives now frequently elect to defer to future years, and new limitations could be imposed on "golden parachute" arrangements.

--Wealthy investors may likewise see increased tax bills. In addition to increased tax rates on capital gains and dividends, they may find that some investment vehicles and products carry new tax costs. For example, financial instruments such as credit default and equity swaps, as well as commodity funds, could be subjected to new tax regimes, not only to raise revenues but to deter their excessive use as part of a broader effort by Congress and the new Administration to impose tax penalties on speculation and other financial practices, including the use of excessive leverage, which many policymakers believe contributed to the meltdown of 2008.

--Corporate taxes will likewise come in for a strict review. Republicans have over the past several years sought reductions in the basic corporate income tax rate by contending that the U.S. has become a comparatively "high tax" country. While some Democrats, including House Ways and Means Committee Chairman Rangel, have supported lowering the corporate tax rate, Congressional Democrats can be expected to continue to insist, and the Obama Administration may do likewise, that any such reductions be offset by measures intended to tighten the corporate income tax, such as repealing the deduction now provided for domestic production activities (at least in the case of major oil companies) and modifying complex accounting and allocation rules that many believe enable corporations, including those with multinational operations, to reduce or at least defer U.S. taxes.

-- U.S. corporations with international operations will also come in for scrutiny, most notably those that can be characterized, correctly or incorrectly, as "exporting U.S. jobs." Consistent with his campaign position, President-elect Obama may propose legislation intended to deter such practices by limiting the ability of U.S. corporations to defer U.S. taxes on the earnings of their foreign corporate subsidiaries.

-- Congress will also continue to take a look at the use of tax havens by wealthy Americans to shelter their assets from U.S. taxes and on the use of tax haven intermediaries by foreign investors as vehicles for investing in the United States, including hedge funds and private equity funds.

VAT as a New Revenue Source

As a practical matter, the existing federal income tax system will not produce sufficient revenues in the long term to return the budget deficit to its pre-2000 levels in the foreseeable future even if federal spending remains constant. In fact, however, domestic spending may continue to increase in response to the aging population and pressure for new spending programs. In these circumstances, President-elect Obama and the Congress may be forced to consider alternative sources of revenue outside the income tax. One possibility is a value-added tax (VAT). Historically, a VAT has been opposed by many Democrats who consider consumption taxes inherently regressive and by many Republicans who have characterized it as a hidden tax that could fuel an explosion in domestic social spending. While a VAT may have to be considered, it remains difficult to envision a near-term consensus to move forward on what has been a most contentious issue.

Farewell to the Flat Tax and the National Sales Tax

Structural tax reform, either within the income tax system such as a flat tax or replacing the income tax with a national sales tax, seems likely to be “off the agenda” for the next four years. Both the flat tax and the national retail sales tax have been opposed by Democrats as regressive and Republicans will, at least for the next two years, lack sufficient numbers to be able to force these proposals onto the tax policy agenda even if Congress moves to consider “tax reform.” If there is a reform movement, it is most likely to be a replay of 1986, when Republicans traded base broadening revenue increases for a lower tax rate. Such a trade may or may not be feasible in the political climate of 2009-10.

Other Tax Policy Issues

Although a broad based flat tax may not have viability, an issue that is likely to get attention is Social Security. During the campaign, President-elect Obama indicated that while he does not support uncapping the current income limitation on the application of the Social Security tax (currently \$102,000), his Administration will consider plans that would ask those making over \$250,000 to pay in the range of 2 to 4 percent more in total taxes (above the combined employer and employee 12.4 percent rate in effect today).

The U.S. tax system remains inordinately complex and, as a result, one can expect that there will be many other issues that will confront both Congress and the tax regulators. Some of these issues will reflect current economic conditions. For example, how should foreign investment in the U.S. (both private investment and foreign sovereign investment) be taxed, particularly in times when increased liquidity is urgently needed throughout the U.S. economy? Likewise, should there be increased tax subsidies for home ownership and should Americans be permitted to make tax-free withdrawals from their retirement plans to use for current expenses and if so what kind of expenses? Other issues will reflect continuing and long-standing concerns, but many of these may be crowded out during the next two years by more pressing issues tied to prevailing economic conditions.

For additional insights about likely policy developments, please feel free to contact the principal author of this section, Don Moorehead, at 202-457-5212 or by email at dmoorehead@pattonboggs.com.

Technology and Communications Policy

“Let us be the generation that reshapes our economy to compete in the digital age. Let's set high standards for our schools and give them the resources they need to succeed . . . let's invest in scientific research, and let's lay down broadband lines through the heart of inner cities and rural towns all across America.”

--President-elect Obama's Presidential Announcement Speech in Springfield, IL

Conventional wisdom might suggest that addressing advanced communications and technology issues is not central to stimulating an ailing economy and should not be a priority for the 111th Congress. But President-elect Barack Obama views technology development and improvements to the nation's communications infrastructure as two important and long-term drivers of economic growth. The high-tech sector is responsible for creating millions of jobs. Development of advanced information technologies by the high-tech sector also is critical to future growth in other sectors, notably health care and energy. President-elect Obama plans to double federal funding for technology research (including information technology, nanotechnology, and biotech) and believes that encouraging technology research, innovation and investment will ensure that U.S. technology companies are competitive and so that 21st century jobs grow in America.

President-elect Obama also believes that working to become a global broadband and Internet access leader (we are presently ranked 15th in the world), and advancing nationwide broadband as both a strategy and a priority, will result in billions of investment dollars flowing to the technology and communications sector. His goal is to make high-speed Internet access available to all Americans, specifically focusing on rural and unserved areas, schools, libraries, government, low-income households, hospitals, and the disabled. Reform of the Universal Service Fund will be a key enabler of President-elect Obama's national broadband policy. In his view, the Universal Service Fund should support not just universal service for voice, but also universal access to affordable broadband.

We expect the President-elect's vision for technology and broadband development to be supported by the enhanced Democratic majority in Congress and at the Federal Communications Commission (FCC). Technology and communications policy, and related business opportunities, should be transformed over the next four years.

Communications Leadership

In the early days of his administration, President-elect Obama will nominate individuals to Chair the FCC, to become the nation's first Chief Technology Officer (a new cabinet position focused on ensuring that our government has the right communications infrastructure, that our nation's IT network is safe and secure, and that our first responders have a wireless interoperable network), and to serve as the Assistant Secretary of Communications and Information at the National Telecommunications and Information Administration (NTIA), the person who will be the President's principal advisor on telecommunications and information policy. Among these organizations, the FCC likely has the greatest ability to effectuate the President's communications goals.

A New FCC

We expect the new Chair of the FCC to share the views of the President-elect's top advisors on communications policy (Former FCC Chairmen Reed Hundt and Bill Kennard)--investment and

modernization of the nation's technology and communications infrastructure will enhance our economy and our global competitiveness. The lineup of potential FCC Chairs include Blair Levin, former Chief of Staff to Chairman Hundt; Julius Genachowski, former Chief Counsel to Chairman Hundt and Special Counsel to Chairman Kennard; and Larry Strickling, currently working with the Obama Campaign, who held several positions at the FCC, ultimately serving as Deputy Chief of the Wireline Competition Bureau. Either of the current Democratic FCC Commissioners (Michael Cops or Jonathan Adelstein) also could be tapped.

Although the five-member Commission will likely change by just one member (the Chairman), the current Republican majority will switch to a Democratic majority. Commissioner Cops will stay until his term expires on June 30, 2010. We believe Commissioner Adelstein, whose term expired June 30, 2008, will be easily reconfirmed by the Senate. On the Republican side, Chairman Kevin Martin's term does not expire until July 1, 2011. He could choose to stay on as a Commissioner, but his plans are unclear. Republican Commissioner Robert McDowell will stay on, with a term expiring on June 30, 2009. The last FCC Commissioner, Republican Deborah Taylor Tate, is serving under an expired term and is expected to leave the Commission when Congress adjourns this year.

A New Congress

We do not expect business as usual in the major Senate and House committees with jurisdiction over technology and communications issues. We expect senior openings and leadership changes, as well as membership changes and expanded Democratic membership ratios given the outcome of the election.

Senate Commerce Committee

Commerce Committee Chairman Daniel Inouye (D-HI) will lead the Appropriations Committee. Senator Jay Rockefeller (D-WV) is likely to succeed him. With Senator Stevens having lost his bid for re-election, Republicans will be selecting a new Ranking Member.

Senate Judiciary Committee

Senator Patrick Leahy (D-VT) is expected to continue to serve as Chairman and Arlen Specter (R-PA) will continue to serve as Ranking Member. Intellectual Property issues will continue to be handled at the full committee level, while technology issues will vary. Some technology issues will be handled by the Terrorism, Technology and Homeland Security Subcommittee, which should be chaired by Senator Dianne Feinstein (D-CA) if she chooses not to pursue an opening on another major subcommittee. The subcommittee minority side will be led by Senator Jon Kyl (R-AZ).

House Energy and Commerce Committee

Chair of the House Energy and Commerce Committee, John Dingell (D-MI), will retain his post, as will Ranking Member Joe Barton (R-TX). We expect Representative Ed Markey (D-MA) to continue to chair the House Telecommunications and Internet Subcommittee, though it is possible he could leave Congress for the Administration or a Senate run. In that event, Representative Rick Boucher (D-VA), an early supporter of President-elect Obama, would likely succeed him. The committee's membership also will shift, in the wake of retirements for Representatives Barbara

Cubin (R-WY), Vito Fossella (R-NY), Chip Pickering (R-MS), Mike Ferguson (R-NJ), and Heather Wilson (R-NM).

House Judiciary Committee

Representative Howard Berman (D-CA), Chair of the Judiciary Subcommittee on the Courts, the Internet and Intellectual Property, will give up the gavel to chair the House Foreign Affairs Committee. Representative Berman was a champion of the content industry. Chairman Conyers recently announced his intent to abolish the subcommittee next year so that IP issues can be addressed at full committee, as in the Senate Judiciary Committee.

Major Legislative Issues

National Broadband Strategy

In President-elect Obama's view, a national broadband strategy is good not only for our economy but also for our democracy. By connecting all Americans to each other, our government and the world, he believes we can enhance democratic discourse, competition and economic growth. To bring broadband to every community, President-elect Obama believes we need a combination of Universal Service reforms, wireless spectrum reforms, promotion of next-generation facilities, technologies and applications, and new tax and loan incentives. President-elect Obama also believes we need to meaningfully redefine "broadband" for the 21st century. Today, the FCC defines "broadband" as just 200 kbps, a standard so low that it stymies federal policy efforts to enhance broadband access.

Congress will almost certainly engage in a debate over a national broadband strategy in 2009. Countless congressional hours were spent in 2008 working on more than a dozen broadband measures seeking to encourage broadband deployment, preserve the ability of local governments to offer broadband, and allow tax payers to earn tax credits for broadband installations and connections. A bill by Senators Rockefeller and Obama sought to deploy a nationwide next-generation broadband network by 2010 with the capability of transmitting data at 10 Mbps in each direction by 2015. Representative Anna Eshoo (D-CA) introduced a companion bill in the House.

Of note, Congress passed the Broadband Data Improvement Act in late 2008, which President Bush has since signed into law. The law provides for Commerce Department grants for designated state entities to identify and track the availability and adoption of broadband services. In addition, the law directs the FCC to issue an order within 120 days of the law's enactment that would revise or update, if necessary, the existing definitions of advanced telecommunications capability, or broadband; and establish a new definition of second generation broadband to reflect a data rate that is not less than the data rate required to reliably transmit full-motion, high-definition video.

Universal Service Reform

Nearly a dozen measures addressing Universal Service reform were introduced in the last Congress. In view of the national broadband goals of President-elect Obama, Universal Service reform is certain to garner attention this year from Congress, the FCC, and the Administration. The President-elect favors a plan to change the Universal Service Fund from a program that supports voice communications to one that supports affordable broadband, with an emphasis on reaching unserved communities.

President-elect Obama's vision for Universal Service reform is mirrored in legislation proposed by Representatives Boucher and Terry (R-NE) that would modify USF to broaden the base of contributions, assist with broadband rollouts and cap growth of the high-cost fund. Notably, the members' Universal Service Reform Act of 2007, H.R. 2054, would require USF recipients to deploy broadband with a download speed of 1 Mbps or greater within five years of enactment.

The FCC also will address Universal Service reform this year, including the management and the administration of the Universal Service Fund by the Universal Service Administrative Company (USAC). USAC has come under Congressional scrutiny for how it processes funding requests and awards, numerous audits and reviews of USF recipients, and inconsistent policies that often result in funding delays and nonpayment of USF recipients. The FCC just recently tried to advance changes to the Universal Service Fund to shift contributions from a system based on usage and interstate revenues to a flat-rate system focused on the number of phone numbers served. The item is still circulating at the FCC.

Net Neutrality

President-elect Obama believes the Internet has been successful because it is "the most open network in history." He supports the principle of net neutrality and preserving open competition. With strong Democratic majorities in Congress, look for Congress to continue to push to codify net neutrality principles, originally advanced by the FCC in 2005 as an expression that consumers are entitled to access lawful content and run any applications and services they wish on the Internet.

We expect Representative Markey to press ahead with the Internet Freedom Preservation Act of 2007, H.R. 5353, introduced last year. The measure calls for a national broadband policy that establishes "open" broadband networks and safeguards against unreasonable discriminatory favoritism for, or degradation of, content by network operators based upon source, ownership, or destination. Markey's bill will need a new Republican advocate, since his co-sponsor, Representative Pickering, retired.

A companion bill (S. 215) in the Senate offered by Senators Dorgan and Olympia Snowe (R-ME) also is likely to resurface. The legislation would enact enforcement mechanisms against service providers that block Internet access or content, including an expedited 90-day review before the FCC of complaints. The bill has the support of 11 influential co-sponsors, including Senator Obama and Judiciary Chairman Leahy.

We also expect that the FCC will step up action against violators of net neutrality principles in 2009. Last year, the FCC ruled that Comcast impermissibly blocked customer Internet traffic and ordered the company to change how it manages its network and how it discloses network management practices to customers.

Patent Reform

In order to be globally competitive, President-elect Obama has supported patent laws that protect legitimate patent rights but don't stifle innovation and collaboration. Congress has been struggling with overhauling the nation's patent system for some time. Efforts to enact patent reform legislation in the 110th Congress stalled over important provisions regarding how courts may calculate infringement damages. Patent reform may take a new turn in the 111th Congress with

Representative Berman chairing the House Foreign Affairs Committee instead of the IP Subcommittee. In any event, we expect patent reform to surface early in 2009. Legislation in both chambers would establish a federal system akin to those in Europe and Asia that award patents on a first-to-file basis, rather than the existing system that awards patents to the first person to make a showing that she is the inventor. Opposition to the legislation rests primarily with patent holders; patent users support the legislation.

On the issue of damages, different approaches have emerged. One proposal backed by Representative Berman would permit plaintiffs to recover damages based on the value of the patent's contribution to the infringing product. An alternative proposal supported by Senators Leahy and Specter would allow courts to award damages on the entire market value of the product if the infringing invention's specific contribution is the predominant basis for the product's market demand.

In addition, the House and Senate bills differ on how to challenge patents after they are granted, abuses by so-called "patent trolls," and forum shopping. Certain jurisdictions--especially the Eastern District of Texas--have become havens for plaintiffs in patent cases. While the House and Senate versions differ slightly, both require that patent litigation occur in a location where either the plaintiff or the defendant has a significant presence.

Orphan Works

Leading Members will revive legislation to address so-called "orphan works"--works protected by copyright, but whose owners cannot be found. Potential users of orphan works often fail to use them out of concern that they may be found liable for statutory damages. Senate legislation introduced last year by Senators Leahy and Orrin Hatch (R-UT) would enable users to use orphan works if, after a thorough, documented search, the copyright owners are unable to be located. A companion bill was introduced in the House by Representatives Berman and Lamar Smith (R-TX). This is one of the few areas in which there is a broad consensus between content owners and traditional fair use advocates, such as libraries and universities. All of them need access to orphan works for creating new works without fear of liability. Given the effort invested on the issue so far over the past two Congresses, we expect legislation on orphan works will be enacted in the 111th Congress.

Health Information Technology ("Health IT")

Committee leaders in both the House and Senate have advanced several different versions of Health IT legislation, but privacy and funding concerns have derailed attempts to enact a bill. Health IT remains a bipartisan priority, however, and renewed legislative action is expected in the next Congress.

President-elect Obama also supports Health IT. He has pledged \$10 billion a year for five years to fund adoption of electronic healthcare records and other standards-based electronic healthcare information to move our healthcare systems from paper, which is expensive and makes it difficult to coordinate care, to electronic form. President-elect Obama views information technology as critical to improving healthcare and reducing costs. He would task the Department of Health and Human Services with adoption and implementation of standards.

Health IT could be subsumed in a larger debate about overhauling the nation's healthcare system, another priority of the new administration. During its last session, Congress devoted

considerable energy to passing legislation that would permit electronic medical records to travel with a patient from provider to provider, including a framework for developing a minimum set of interoperability standards for securing exchange and use of electronic health information. A Senate bill, S. 1693, did not advance beyond committee approval, largely because of concerns that its privacy protections were too weak. A House bill, H.R. 6357, was reported favorably out of committee, but stalled when Ways and Means Health Subcommittee Chairman Pete Stark (D-CA) voiced concern about the absence of an enforcement mechanism.

Broad adoption of an interoperable, standards-based health information network will depend on financial incentives for providers who implement and use Health IT, as well as on technology providers that build the network architecture to transmit health data. A bill introduced by Representative Eshoo would authorize grants for the purchase of qualified Health IT systems.

Consumer Privacy and Data Protection

Privacy law and policy involves balancing individual rights against government and business uses of information. During the Bush administration, and after September 11th, the pendulum swung sharply in favor of making personal information accessible for the benefit of government and commercial interests. Now, with Democrats regaining critical government leadership, expect the pendulum to swing back toward heightened concerns over individual privacy. President-elect Obama has expressed concern that our open information platforms can leave citizens vulnerable to violations of their privacy and that government and businesses must be held accountable when privacy is compromised.

“Deep packet inspection,” used to target advertising, and data mining, are likely to re-emerge as issues in the next Congress. Lawmakers devoted significant time to such matters late last year. In the Senate, the Commerce Committee held two hearings to explore the privacy implications of online advertising. Senator Dorgan presided over the second hearing and noted that consumers are concerned that their online behavior is being tracked and that a lack of robust competition in the broadband market makes it necessary to ensure that consumer privacy is protected. Executives from leading telecommunications carriers told the committee that their companies did not engage in such practices and that the industry should be allowed to police itself.

The House Energy and Commerce Committee also expressed concern over data mining, and sent letters to more than 30 telecommunications and Internet companies to determine whether they target online advertising based upon consumer search queries and web surfing habits. The responses to those letters may serve as the basis for oversight hearings in early 2009.

Public Safety

The President-elect is committed to improving the communications capabilities of our nation’s public safety agencies and first responders who are saddled with outdated technology. One of the priorities of the nation’s first CTO will be to ensure that public safety, first responders and government agencies use best-in-class technologies and the right infrastructure in order to enhance our safety, their effectiveness and government service. The FCC, the Department of Homeland Security, the NTIA and Congress all have grappled with how to improve the communications capabilities of our nation’s first responders and public safety agencies; we expect these issues to continue.

In 2009, we expect the FCC to complete examination of how best to authorize wireless spectrum for public-safety and homeland security needs. Despite significant efforts by Chairman Martin in 2008, the FCC was not successful in assigning 20 megahertz of 700-MHz spectrum (the “D-Block”) intended for first responders. It also has not completed authorizing spectrum set aside at 4.9 GHz for homeland security. Earlier in 2008, the Commission failed to secure a minimum bid for the sale of the 700 MHz D-Block spectrum, due largely to its controversial mandate that the spectrum must be shared by commercial and public safety interests. Commissioners must now decide how to re-auction that spectrum and a rulemaking is pending.

Satellite Home Viewer Act

The makeup of the House and Senate Judiciary Committees also will affect reauthorization of the Satellite Home Viewer Act, which sunsets in December 2009. It provides the legal framework through which cable systems distribute broadcast television signals. The reauthorization debate is certain to be contentious, pitting program owners receiving royalty payments against users.

The advent of digital television and the rapid growth of the Internet as a major video programming distribution outlet both call into question the current statutory licensing systems. In 2008, the Copyright Office recommended that Congress abandon the cable compulsory license that permits cable operators to retransmit both local and distant radio and television signals to subscribers and another license that permits satellite carriers to retransmit distant television (but not radio) signals to subscribers. The Copyright office suggests that Congress should adopt a new statutory licensing system built around digital television technology and other distribution mechanisms.

Digital Television

The digital television transition is certain to receive early attention from Congress as television stations are required to cease broadcasting analog video on February 17, 2009. The shut-off has Congress uneasy as they prepare for a backlash from constituents who have not planned for the digital conversion and may lose their analog television signal. FCC Commissioner Robert McDowell acknowledged that congressional action would be necessary to permit television stations to broadcast analog advisories beyond the February deadline.

Representative Lois Capps (D-CA) introduced in late 2008 a bill that would allow a brief extension through March 3, 2009 of analog broadcasting authority to permit broadcasting emergency information. Her Short-term Analog Flash and Emergency Readiness Act, H.R. 7013, also would allow broadcast of English and Spanish information about the DTV transition and steps viewers can take to convert digital television service, including a phone number and Internet address to obtain more details.

Communications Taxes

With economic issues front and center in 2009, we expect lawmakers to reintroduce various measures from the 110th Congress seeking to reverse discriminatory taxes on the communications industry. The Cell Tax Fairness Act introduced by Representative Zoe Lofgren (D-CA), for example, would restrict states or local governments from imposing any new discriminatory tax on mobile services, mobile service providers, or mobile service property for five years. Taxes imposed on mobile services, providers, or property that is not generally imposed on other types of services or property would be banned. Other tax measures of note would curtail the business activities tax on

telephone and other communications devices, and would result in a state streamlined sales tax, simplifying state sales and use taxes by creating uniform definitions within tax bases and simplifying audit and administrative procedures. Thirty-nine states currently support the proposal.

Return of the Fairness Doctrine and Other Issues of Note

There has been some speculation that a Democratically controlled White House and Congress may hasten the return of the Fairness Doctrine. The original Fairness Doctrine, phased out in the 1980s, required television and radio stations to provide balanced airtime to opposing viewpoints or risk fines or license revocation. Conservative talk shows dominate radio broadcasting and if the Fairness Doctrine is adopted, that influence will be diminished.

Additional communications and technology issues that may percolate in the new Congress include a national framework for how states regulate wireless terms and conditions, measures to extend the Federal Trade Commission's reach to mobile authority, spectrum management issues, shield laws for the press, and improvements for telecommunications capabilities for the disabled. Finally, consolidation of the communications industry may slow under heightened scrutiny by antitrust officials in the wake of a series of high-profile mergers last year that included the merger of XM and Sirius, Verizon Wireless' purchase of Alltel, and Sprint's merger with Clearwire.

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Trade Policy

Despite the populist anti-trade and anti-globalization rhetoric during the Presidential primaries and to a lesser extent during the general election debate, the Obama Administration's trade policy will likely be comparable to that of the Clinton Administration, which could be characterized as moderately free trade. President Clinton, for example, supported the negotiation of "side agreements" to the North American Free Trade Agreement (NAFTA), extension of Permanent Normal Trading Relations to China, and other trade liberalizing measures. To be sure, we expect the Obama Administration to place increased importance on labor and environmental aspects of any future trade agreements, and possibly to seek retroactive modification of these subjects in already-completed negotiations. Moreover, there will be an effort to renew the President's Trade Promotion Authority (TPA), previously referred to as "fast track authority," which may prove to be a contentious issue between the Obama Administration and the more trade-adverse Democratic Congress. Trade enforcement of existing agreements will also be a high priority. However, given the urgency of financial stability and reform, as well as higher priority issues such as health care and climate change, trade issues generally will not be in the forefront of either the Obama Administration or the Congressional work agenda in the first half of 2009.

The Obama Campaign's emphasis on an inclusive foreign policy that reaches out to our allies will translate into a renewed effort to work with our major trading partners to resuscitate the multilateral Doha Development Agenda talks in the World Trade Organization (WTO). We trust that, notwithstanding the current the financial crisis, neither the Executive Branch nor Congress will adopt a stridently protectionist approach, thereby dooming any meaningful progress in the Doha Round. Simultaneously, the new Administration will initiate a tougher enforcement attitude relative to countries perceived as ignoring their WTO commitments, such as China and India. With that background, the following specific issues will be important to the trade policy agenda of the 111th Congress and the Obama Administration.

Signed, But Not Implemented, Pending Free Trade Agreements (FTAs). With the inability of the 110th Congress to pass FTAs that already have been negotiated and signed with Colombia, Korea, and Panama, the Obama Administration can be expected to revisit the text of each agreement, particularly in the areas of labor and environment. (This would be similar to the Clinton Administration's handling of NAFTA.) We continue to hope that the Colombian FTA will be approved in the lame duck session of the 110th Congress, possibly as part of a larger deal involving an economic stimulus measure.

If Congress fails to act on the Colombia FTA, the Obama Administration may determine that it is in its political interest not to alienate this strong Latin American ally by re-opening the FTA negotiations. To avoid this, the new Administration may consider preserving fast track protections by resubmitting to Congress the identical legislation that President Bush sent to Congress in 2008.

Trade Adjustment Assistance (TAA). The recent decision of the 110th Congress to extend the current TAA program was intended in part to give Democrats next year the leverage to legislate a reformed version of the program. Senator Max Baucus (D-MT), Chairman of the Senate Committee on Finance, will once again lead this effort. However, it is unclear at this point if he will take the position he took during the 110th Congress, and make passage of the Colombia FTA (or perhaps other bilateral or multilateral trade legislation) conditioned upon first passing a reformed TAA bill. A more robust TAA program is likely to be embraced enthusiastically by both the Obama Administration and the Congress as a measure to help alleviate some of the results of the financial meltdown.

Extension of ATPDEA and GSP. Similarly, the 110th Congress extended both the Andean Trade Preference and Drug Eradication Act (ATPDEA) and the Generalized System of Preferences (GSP) for only a short period of time, *i.e.*, until the end of 2009. This will force another renewal effort sometime during the 111th Congress in order to continue these programs. However, should the Peru and Colombia FTAs be implemented during 2009, there will be far less pressure to renew ATPDEA, particularly if the other two countries under the program--Bolivia and Ecuador--continue to strengthen their ties to the Latin America's leftist movement.

Renewal of Trade Promotion Authority (TPA). Like every recent President before him, President-elect Obama will seek extension of his trade negotiating authority (formerly referred to as "fast track authority") in order to negotiate additional agreements. These include completion of the Doha Development Agenda in the WTO as well as bilateral FTAs. With a stronger Democratic majority on Capitol Hill, we anticipate the Administration and Congress will work together to improve TPA procedures while guaranteeing the basic fundamentals of fast track protection. It should be expected, however, that some in Congress may attempt to weaken the President's authority under TPA by amending the law to include greater Congressional involvement in the passage and implementation of trade agreements. There could be an "agreement in principle"

similar to the May 10, 2007 agreement reached by the 110th Congress and the Bush Administration, which spelled out guidelines for the upcoming FTAs.

China-Specific Legislation. The Obama Administration will take a tough position on trade with China, particularly with respect to enforcement efforts to ensure that China meets its WTO commitments in a number of important areas, including intellectual property, subsidies, and market access commitments. For example, an Obama Administration can be expected to employ U.S. trade remedy laws and the WTO's dispute settlement mechanism far more frequently than the Bush Administration. Central to his economic engagement with China will be President Obama's policy to "use all diplomatic avenues available to seek a change in China's currency practices." Congress, however, may force the President's hand on this particular issue. After several failed attempts, there may finally be enough support in the new Congress to pass legislation addressing China's currency practices. There may also be more China-specific dispute settlement cases brought by the US in the WTO.

Russia-Specific Legislation. At this point it is too early to tell whether or not there will be continued pressure to impose economic sanctions against Russia in response to its clash with Georgia in the fall of 2008. However, we anticipate an Obama Administration will take a tough stance on Russia's admission to the WTO and the completion of the U.S.-Russia Civil Nuclear Cooperation Agreement. There may be an effort to begin negotiations of a Free Trade Agreement with Georgia.

Revival of the Doha Development Agenda in the WTO. The new Administration certainly will make a good faith effort to resuscitate the stalled Doha Development Agenda talks in the WTO, although the outcome of this effort is by no means clear. Look for USTR to announce a "new approach" to the WTO negotiations in an effort to forge a consensus view with the European Union and Japan. There is still a possibility of a breakthrough on Doha before the end of 2008, particularly an agreement on "negotiating modalities" and the special safeguard mechanism in agriculture. Whether progress on Doha becomes linked to broader, global financial reform remains to be seen. Recent statements by the leaders of the G8 indicate their interest in intensifying efforts to complete the Doha Round.

Import/Food Safety Issues. There is likely to be continued emphasis on food safety issues for products entering the U.S. market from countries like China and India, as well as China's actions in restricting access to its market as retaliation (*e.g.*, poultry and pork). These efforts will be included in the increased trade enforcement strategy of the Obama Administration and are likely to continue through 2009.

Continuation of the Strategic Economic Dialogue (SED) with China. The Obama Administration is likely to continue the Bush Administration's SED and the Joint Committee on Commerce and Trade, although the modalities and strategic objectives of both dialogues may change. The new Administration is likely to maintain this structure as a way of encouraging ongoing discussion with the Chinese on a wide variety of trade issues.

Bilateral Investment Treaty (BIT) with India. The lagging BIT negotiations with India have the potential to gain momentum given the passage on October 1 of the United States-India Nuclear Cooperation Approval and Nonproliferation Enhancement Act. The passage of this landmark legislation was driven in large part by U.S. business which is interested in greater two-way trade with India, beyond just the civil nuclear sector. Capitalizing on the passage of this agreement, we expect U.S. business will again lead the charge to seek the removal of other barriers to trade with this increasingly important U.S. ally.

Extractive Industries Transparency Disclosure Act (EITDA). Over the years, there has been a growing movement to address the lack of transparency in extractive industries. Introduced during the 110th Congress, the EITDA proposes to amend the Securities Exchange Act of 1934 to require the disclosure of payments to foreign governments for the extraction of natural resources. If enacted, the EITDA would essentially legislate the disclosure principles of the voluntary initiative known as “Publish What You Pay.” This initiative was sponsored by Revenue Watch, an affiliate of George Soros’ Open Society Institute, officials of which have testified in support of the EITDA. The EITDA will not pass the 110th Congress, but we expect it will be reintroduced during the 111th Congress.

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Transportation and Infrastructure

The 111th Congress and the new Administration will have a full transportation and infrastructure agenda. They will have to grapple with unresolved issues of system financing that stalled aviation legislation in the 110th Congress. In surface transportation, they will have the opportunity to set the nation in a new direction to address the mobility needs of the 21st century.

Aviation

Authority for most Federal Aviation Administration (FAA) programs, including the Air Traffic Control System, the Airport Improvement Program (AIP), the Research and Development Program, and the Facilities and Equipment Program, will expire March 31, 2009. The programs originally were set to expire September 30, 2007. While the House passed H.R. 2881 in late September 2007, the Senate failed to pass a bill. Congress extended the authorization several times, for a few months at a time, most recently this past September.

The FAA reauthorization legislation must be reintroduced in the 111th Congress. The House Committee on Transportation and Infrastructure is expected to reintroduce the House-passed bill early in the Session, perhaps in early March. The full Committee or Aviation Subcommittee may hold a few hearings in advance of a markup. The most prominent features of H.R. 2881 are expected to remain the same: funding and authorizing the satellite-based Next Generation Air Traffic Control System (NextGen), increasing fuel taxes but keeping the current structure of taxes and fees paid into the Airport and Airway Trust Fund to finance the system, and raising the maximum allowed Passenger Facility Charge (PFC) at airports from \$4.50 to \$7.00.

Prospects for a reauthorization bill in the Senate are also good. The Senate Commerce Committee wants to move a bill, but the question remains whether past will be prologue. In the 110th Congress, FAA reauthorization foundered in the Senate on the fee structure issue. Currently, taxes and charges on airlines provide the bulk of Trust Fund receipts, including the domestic passenger ticket tax (7.5% of the ticket price), a domestic flight segment fee (\$3.30), an international arrival and departure tax (\$14.50), and a commercial fuel tax (\$0.043 per gallon). Business and general aviation pay a fuel tax (\$0.193 per gallon avgas; \$0.218 per gallon jet fuel). The Bush Administration, with strong airline support, proposed a new fee structure that would have charged business aviation for its proportionate use of the air traffic control system. The House bill ignored the Administration’s proposal, but the Senate Commerce Committee included a \$25 per flight surcharge and an increase in the fuel tax in its bill. The Senate Finance Committee resisted the surcharge, considering other changes to the system of fees and charges. The impasse between the

two committees lasted for the better part of a year, broken only by an agreement in late summer 2008 to drop the surcharge. The airlines again will push for additional charges on business aviation and the business groups will likely push back as successfully as they did in the 110th Congress.

President-elect Obama has spoken about the need to modernize the Air Traffic Control System, but has not provided any details on whether he supports the shift of the tax burden from the airlines to business aviation. He would likely defer to whatever deal the House and Senate ultimately craft.

Another difference between the House-passed and Senate Committee bills was the absence of a general increase in the PFC in the Senate bill. Instead, the Senate bill would have allowed six airports to charge a PFC without limitation, except that any increase in the PFC over the current \$4.50 would be required to be collected by the airport from the passenger directly at kiosks or via the Internet, with no air carrier involvement. While airport trade associations strongly support an across-the-board increase in the PFC, some airports are also attracted to the Senate provision.

Both the House-passed and the Senate Committee bills included provisions to promote development of intermodal facilities, although they were narrowly drawn. These provisions did not get much attention, but this could change if there is an effort to broaden the eligibility of intermodal projects for AIP or PFC funding.

Two labor provisions in H.R. 2881 might have prompted a veto by President Bush had a reauthorization bill been sent to him. One would reopen the FAA's contract with the National Air Traffic Controllers Association. President-elect Obama co-sponsored a bill to force the FAA to reinitiate discussions with controllers. An Obama Administration might well agree to a new contract with controllers. The other provision would place FedEx Express employees other than pilots and aircraft mechanics under the jurisdiction of the National Labor Relations Act, which would allow labor to organize on a station-by-station basis.

It is quite possible that the House Committee will add provisions regarding FAA oversight and supervision of air carriers to the bill, such as those in H.R. 6493, the Aviation Safety Enhancement Act, passed by the House in July 2008. H.R. 6493 would establish an independent whistleblower office and prohibit an FAA inspector from going to work for an air carrier for two years if the inspector had responsibility for inspecting that carrier. Supervisory inspectors would be prohibited from working for any air carrier for two years after leaving the government.

The House Committee may also include the provisions in H.R. 6355, the Air Service Improvements Act of 2008, introduced by House Transportation and Infrastructure Committee Chairman James Oberstar (D-MN) and House Aviation Subcommittee Chairman Jerry Costello (D-IL) in June. This "passenger bill of rights" would provide additional protection for passengers for delayed or canceled flights--requiring both airlines and airports to develop plans subject to DOT approval--and includes a provision requiring binding arbitration should the FAA and its employee unions fail to reach an agreement.

Other provisions that might be added include: a ban on passenger use of cell phones on commercial flights, a ban or limit on the Department of Transportation's (DOT) use of market mechanisms to address airport congestion and delays (such as auctions and peak-period pricing), revisions to the Railway Labor Act to change National Mediation Board guidelines on recognition of craft unions, and provisions to increase oversight of foreign repair stations.

The Democratic majority, with a Democratic President, may push some or all of these issues. The Obama Administration may be willing to tackle some of these issues through regulations and policy initiatives.

The airline industry remains in financial distress. One response that was expected last year—consolidation—has been quite modest to date. The Delta-Northwest merger was the only domestic airline merger pending, and now has been cleared by the Justice Department. But the continuing credit crisis may pinch some air carriers to the point of reconsidering consolidation. Frontier Airlines declared bankruptcy largely because of a change in the reserve requirements of credit card companies. Should other carriers feel a similar credit squeeze, the airline industry could seek relief from Congress to avoid a rash of new Chapter 11 filings.

U.S. air carriers may also look to tap into foreign capital, but current law significantly limits foreign investment in U.S. airlines. Under current law U.S. citizens must own at least 75% of the voting stock of a U.S. air carrier and “actually control” the carrier. Under current DOT policy, non-U.S. citizens may not hold more than 49% of the equity of a U.S. air carrier. Further, U.S. law considers a limited partnership with one or more non-U.S. citizen limited partners to be a foreign partnership. DOT treats a limited liability company that is structured like a partnership as subject to this strict partnership limitation. Without a change in this law, air carriers will be limited in the extent they can receive funding from hedge funds and other potential partnership investors. Should the financial distress of the airline industry become more acute, Congress may be asked to open up investment opportunities to keep some U.S. airlines in business. However, based on the strong resistance in recent years in both the House and the Senate to any relaxation of the ownership and control provisions, neither is likely to be receptive to any airline industry effort to expand foreign investment.

Ownership and control provisions are also front and center in the recently begun Second Stage U.S.-EU negotiations. Under the terms of the open skies Air Transport Agreement between and among the U.S., the EU, and EU Member States, effective March 2008, Member States may pull out if the parties have not reached a Second Stage Agreement by the end of 2010. EU officials continue to insist on a relaxation of foreign ownership restrictions and a grant of cabotage rights (allowing an EU carrier to operate service between two U.S. cities). U.S. negotiators have no authority to agree to these changes without a change in the Federal Aviation Act. To date Congress has shown no interest in making any changes to the ownership and control provisions. Without movement in Congress, the next Administration will be hard pressed to deliver a Second Stage Agreement attractive to the EU. This may well prompt one or more EU Member States to pull out of the Air Transport Agreement, thereby denying U.S. air carriers certain rights and opportunities.

President-elect Obama has pledged to maintain the status quo on foreign ownership and control provisions in U.S. It thus may be difficult for the Obama Administration to offer the EU anything attractive in the Second Stage negotiations.

Two other international aviation issues will receive attention in 2009. The EU wants to include all aviation operations to, from, and inside the EU by 2012 within its Emissions Trading System (ETS) intended to reduce greenhouse gas emissions. The Bush Administration, along with the International Air Transport Association (IATA), has attempted to move the issue to the International Civil Aviation Organization (ICAO) in an effort to reach a global consensus. However, the European Commission last month formally adopted this measure, prompting a protest from the IATA and from FAA, which argues that applying the ETS to U.S. carriers violates international aviation agreements. The Obama Administration’s position may depend in part on the

impact these fees might have on U.S. air carriers. On the other side, foreign carriers continue to bridle at certain security requirements imposed on any commercial aircraft operation to or from the U.S. by the Transportation Security Administration and U.S. Customs and Border Protection.

Surface Transportation

The 111th Congress will grapple with the most significant reauthorization of the nation's surface transportation programs and financing since the Interstate System and the Highway Trust Fund were created over fifty years ago. The current law, the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU) expires on September 30, 2009. It must be reauthorized or extended before then.

The nation's surface transportation system is at a critical juncture. Existing infrastructure is deteriorating and becoming increasingly congested. New infrastructure needs to be built to serve changing demographics and trade patterns. Revenues--primarily federal gas taxes paid into the Highway Trust Fund--are declining and there is a general sense that the federal program has lost its mission. The National Surface Transportation Policy and Revenue Study Commission, one of two national commissions created by SAFETEA-LU to examine the federal role, financing, program and structure, issued its report in December 2007 and recommended that new financing must be coupled with major structural reform. The House and Senate authorizing committees held hearings from January to September on the Commission's findings and recommendations. A number of themes have emerged from the Commission report and the hearings.

There is a view that federal resources should be focused on programs and projects of federal interest, with discussion of a national strategic plan and a corresponding decision making structure as well as federal standards, performance measures and accountability. There is likely to be program consolidation with a focus on creating broad programs to implement federal priorities. Program reform will likely be combined with streamlining of requirements and approval processes while incorporating energy savings, air quality and sustainability measures.

There appears to be a consensus that the Interstate System and freight corridors are of clear federal interest. There have been several proposals to fund Freight Corridors through a Freight Trust Fund financed by container fees, Customs fees, levies on bills of lading and other freight related user fees. A freight corridor program could focus on the most cost beneficial approach to freight movement in a corridor, recognizing rail, as well as highway capacity needs and intermodal connections.

Metropolitan mobility and congestion relief has also emerged as a major theme. A restructured program could result in more direct funding to metropolitan regions, additional funding for transit, greater local flexibility in using funds for either highways and transit and increased use of congestion pricing mechanisms, such as high occupancy toll (HOT) lanes.

In the short term, the major source of financing will continue to be the gas tax. The committees are discussing a gas tax increase, although not of the magnitude recommended by the Commission, and increased funding. They are also examining other financing mechanisms to supplement the gas tax, i.e. freight user fees and bonding. There is recognition that public private partnership financing is appropriate for some projects, as well as discussion of how to protect the public interest. There is interest in easing the restrictions on tolling and increased use of innovative financing mechanisms. The committees are also examining various national infrastructure bank proposals and changes in federal budgeting to provide more positive treatment of capital

investments. For the long term, discussion is focused on a vehicle-miles-traveled (VMT) tax, although technology and privacy issues need to be addressed first. There is consideration of testing a VMT tax on commercial motor vehicles, in combination with changes in truck size and weight requirements.

After reviewing the Commission's findings and holding nine months of hearings, the congressional committees will draft legislation. The House Transportation and Infrastructure Committee plans to produce a detailed outline of its proposal by February 2009 with the intent of marking-up a bill in the spring and passing it in the House by Memorial Day. The Senate Environment and Public Works Committee plans to adhere to a similar schedule. This timetable is necessary if these and the other committees of jurisdiction, including the House Ways and Means Committee, the Senate Banking, Housing and Urban Affairs Committee, and the Commerce, Science and Transportation and Finance Committees, are to have a conference report passed by Congress and signed by the President before the expiration of SAFETEA-LU. Historically, Congress has not met the deadline and a new reauthorization has passed only after several extensions of current law.

If the authorizing committees adhere to their stated schedules, it will be difficult for the new Administration to play a significant role in the detailed development of the reauthorization, as the legislative process will be well underway by the time the Secretary of Transportation submits the Department's proposal to Congress. A lag in developing legislation by either the Senate or House committees will provide a greater opportunity for the Administration to become involved. Some committees may change their schedules to give the Administration the opportunity to submit a proposal. On the back end, the longer Congress takes to enact SAFETEA-LU reauthorization, the greater the opportunity for interaction with the new Administration.

Traditionally, the authorizing committees ultimately take a bipartisan approach to surface transportation issues. The major differences tend to be between the House and Senate, not between Democrats and Republicans. Many of President-elect Obama's positions mirror those emerging in the authorizing committees--a strong federal role and increased investment in infrastructure, greater emphasis on transit and more focus on smart growth and energy conservation. His favored approach of a national infrastructure reinvestment bank is one of several financing mechanisms being considering. However, there are also key differences. While the President-elect opposes a gas tax increase and earmarking, the committees may well take the opposite view. Regardless of their differences, it is likely that President-elect Obama will work with Congress on a bill that is acceptable to all parties and sign it into law.

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