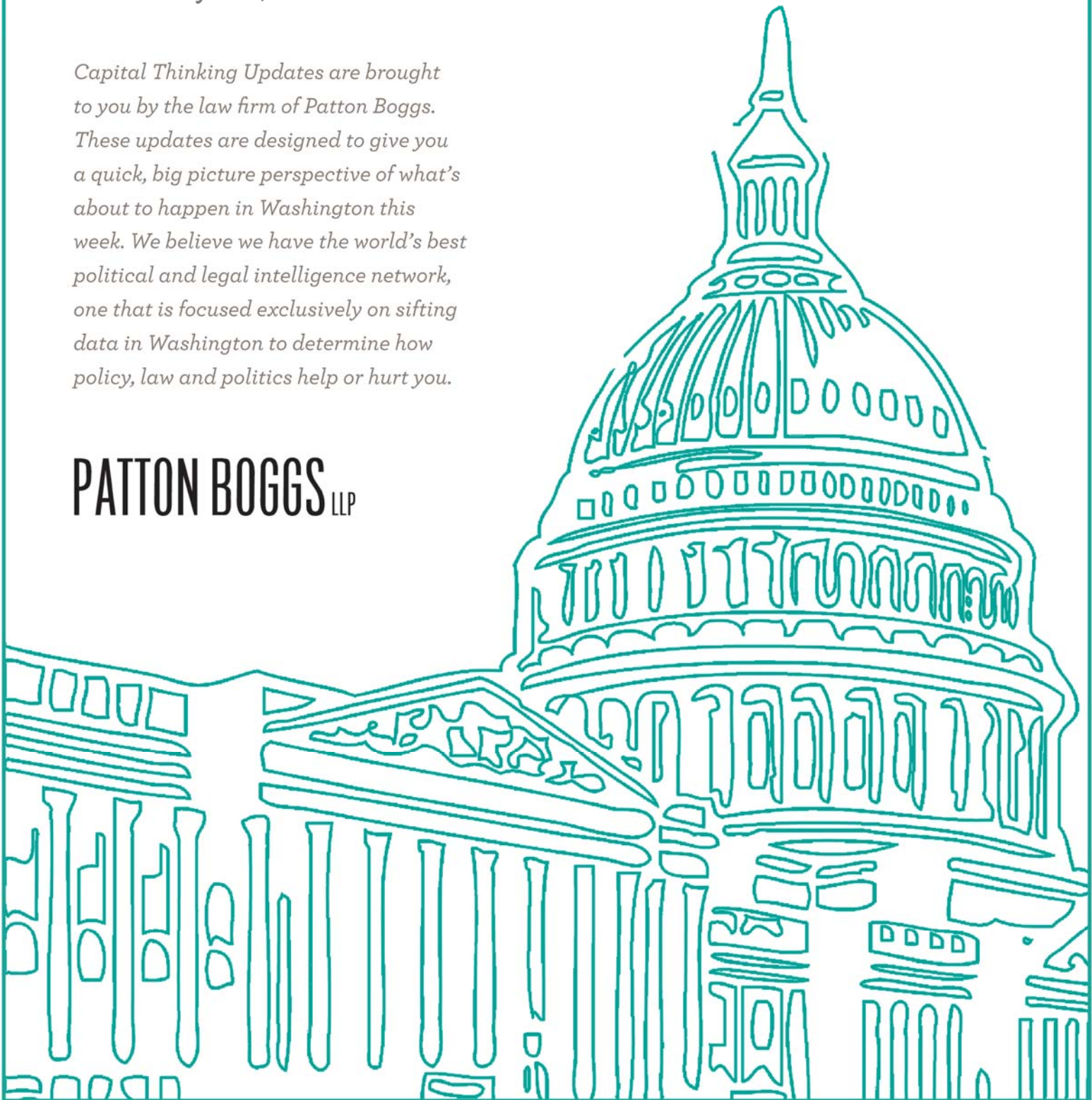


CAPITAL **thinking** UPDATES

February 27, 2012

Capital Thinking Updates are brought to you by the law firm of Patton Boggs. These updates are designed to give you a quick, big picture perspective of what's about to happen in Washington this week. We believe we have the world's best political and legal intelligence network, one that is focused exclusively on sifting data in Washington to determine how policy, law and politics help or hurt you.

PATTON BOGGS LLP



General Legislative

On Monday, February 27, 2012, the House will meet at 2:00 p.m. for legislative business. The following matters will be considered under suspension of the rules: H.R. 1433, the Private Property Rights Protection Act of 2012; and a motion to concur in the Senate Amendment to H.R. 347, the Federal Restricted Buildings and Grounds Improvement Act of 2011. The Senate will convene at 2:00 p.m. and proceed to the reading of Washington's Farewell Address before a period of morning business. Thereafter, the Senate will proceed to executive session to consider the nomination of Margo Kitsy Brodie to be United States District Judge for the Eastern District of New York.

Budget, Appropriations

LEGISLATIVE ACTIVITY

- **Efforts to Avoid Sequestration.** On Thursday, February 16, Representative Chuck Fleischmann (R-TN) introduced the latest piece of legislation aimed to avoid the sequestration process scheduled for January 2013. His bill (H.R. 4060) proposes to implement annual discretionary spending caps at \$949 billion for FY 2013 through FY 2021. The Budget Control Act of 2011 (P.L. 112-25) established a discretionary spending cap of \$1.047 trillion for FY 2013 and capped overall growth for years going forward through FY 2021 at 2 percent.
- **Congressional Budget and Appropriations Committee Hearings.** Following the release of the President's Budget Proposal on Monday, February 13 (detailed below), the Budget and Appropriations Committees in each chamber began individual agency hearings on the FY 2013 Budget Request. These hearings will continue this week:
 - Senate Appropriations Subcommittees will hold hearings on the FY 2013 Budget Request for the Department of State and Foreign Operations (Tuesday, February 28); the Department of Interior (Wednesday, February 29); the Department of Defense (Wednesday, February 29); the Department of Housing and Urban Development (Thursday, March 1); and areas of jurisdiction under the Legislative Branch Subcommittee (Thursday, March 1).
 - The Senate Budget Committee will hold a hearing on the FY 2013 Budget Request for the Department of Defense (Tuesday, February 28) and Health Care Spending (Wednesday, February 29).
 - House Appropriations Subcommittees will hold a number of hearing on the FY 2013 Budget Request: Department of Justice (Tuesday, February 28); Indian Health Service (Tuesday, February 28); Department of Agriculture (Tuesday, February 28); Transportation Security Administration (Tuesday, February 28); Bureau of Indian Affairs (Tuesday, February 28); Department of Energy (Tuesday, February 28); Department of State (Wednesday, February 29); Food and Drug Administration (Wednesday, February 29); Department of Commerce and NOAA (February 29); National Nuclear Security Administration (Wednesday, February 29); Customs and Border Protection (Wednesday, February 29); EPA (Wednesday, February 29); Department of Agriculture (Wednesday, February 29); Office of Science and Technology

(Wednesday, February 29); National Protection and Programs Directorate, DHS (Thursday, March 1); Fish and Wildlife Service (Thursday, March 1); US Patent and Trademark Office (Thursday, March 1); Military Construction (Thursday, March 1); Department of Agriculture (March 1); and U.S. Navy / Marine Corps (Thursday, March 1).

- The House Budget Committee will hold hearings on Health and Retirement Security (Tuesday, February 28) and the FY 2013 Budget Request for the Department of Defense (Wednesday, February 29).

OTHER BUDGET, APPROPRIATIONS NEWS

- **FY 2013 Budget Proposal.** On Monday, February 13, President Obama presented his FY 2013 Budget Proposal to Congress. The President's \$3.8 trillion plan highlights deficit reduction of \$4 trillion over 10 years, a figure which brought prompt criticism from Congressional Republicans in both House and Senate Budget Committee hearings. Republicans countered that the proposal would achieve only \$400 million in deficit reduction while growing the national debt by \$11.2 trillion. The President's Budget Proposal is much more political than legislative, and serves primarily as the focal point for hearings on agency funding levels and operations that will lead to the final funding and policy decisions determined by Congress and included in the FY 2013 appropriations bills.

The President's FY 2013 Budget incorporates many of the components of various jobs and budget-related proposals he has introduced in recent months. The President adheres to the discretionary spending cap of \$1.047 trillion established in the Budget Control Act of 2011 (P.L. 112-25) and proposes deficit reduction measures designed to prevent the sequestration process mandated in the Budget Control Act.

Overall, the President's Budget includes \$3.8 trillion in spending, a slight increase from the \$3.79 trillion in FY 2012. Of that amount, 67 percent is mandatory entitlement spending (e.g. Medicare, Medicaid, Social Security) or interest on the national debt, and less than 15 percent is domestic non-defense spending. On the spending side, it calls for \$350 billion in investments to maintain lower payroll taxes, to strengthen incentives for domestic manufacturing while rewarding companies that have scaled back overseas operations, to hire first responders and teachers, to retrain workers, to invest in civilian scientific research and green energy, and to invest in infrastructure and school modernization. The budget adds two major new initiatives: \$12 billion for Pathways Back to Work, an initiative that would support summer youth and year round jobs for low-income youth, and \$8 billion for Community College Partnerships to improve access to job training across the nation. It must be remembered, however, that all new spending initiatives or tax changes are subject to PAYGO rules (in order not to add to the federal deficit) which require offsets with savings derived from existing funds.

The Budget also projects about \$3.6 trillion in deficit reduction over 10 years, including major entitlement reforms saving about \$600 billion and increased tax revenues of \$1.6 trillion. It proposes raising taxes over the next decade on corporations and the wealthy in part by letting the Bush era tax cuts expire on household income over \$250,000 a year. It encourages Congress to reform the tax code by eliminating the alternative minimum tax and places a budget cap on certain tax exclusions, including interest on municipal bonds issued by state and local governments.

The forecasts in the FY 2013 Budget also assume strong overall economic growth that many analysts challenge, including the Congressional Budget Office. The Budget proposes new revenue sources that are either not realistic for passage or not identified, such as the source of \$50 billion for upfront transportation spending.

The defense budget, which impacts most localities directly through military presence and indirectly through procurement or research spending, faces reductions in nearly all spending categories, totaling \$9 billion in FY 2013 and \$487 billion over 10 years. Beyond reductions in military personnel and individual procurements, a central point of debate will be the proposal for two new rounds of the Base Realignment and Closure (BRAC) process for in 2013 and 2015.

Education

LEGISLATIVE ACTIVITY

- **House Reauthorization of the Elementary and Secondary Education Act (ESEA).** As part of Republican efforts to rewrite the law, Education and the Workforce Committee Chairman John Kline (R-MN) held a hearing Thursday, February 16 on two newly introduced bills (the “Student Success Act” (H.R. 3989) and the “Encouraging Innovation and Effective Teachers Act” (H.R. 3990)) aimed at significantly reducing the federal government’s role in overseeing K-12 policy. The legislation would remove the adequate yearly progress provision at the center of the law, allowing states to craft their own accountability systems, but it has as yet to garner Democratic support. A committee markup related to these bills is scheduled for Tuesday, February 28.
- **Military Education Benefits.** A report released February 23 by Senate HELP Committee staff revealed that for-profit colleges receive nearly 50 percent of military Tuition Assistance (TA) dollars, raising concerns about oversight practices at the Department of Defense (DOD). The report called for stronger DOD oversight and enforcement of the TA program to “ensure that students’ time and benefits, and taxpayer dollars, are not wasted on schools with dubious practices and poor outcomes.”
- **Repeal of Higher Education Regulations.** The House Rules Committee is set to review H.R. 2117, the Protecting Academic Freedom in Higher Education Act, on Monday, February 27, setting up a likely floor vote later in the week. The regulations targeted seek to set the definition of a credit hour and expand state oversight of institutions of higher education through authorization requirements. While the measure is expected to pass the House easily, it is unlikely to make progress in the Democrat-controlled Senate.

REGULATORY ACTIVITY

- **College Admissions.** On Tuesday, February 21, the U.S. Supreme Court granted certiorari in *Fisher v. University of Texas at Austin* (No. 11-345), a case challenging the University of Texas’s undergraduate use of affirmative action in its admissions process. The case will be heard in the October 2012 term, and the Supreme Court’s decision could have implications for federal guidance issued December 2, 2011, by the Departments of Education and Justice for K-12 schools and postsecondary institutions, which outlines both race-neutral and race-conscious practices that may be used to advance racial diversity and avoid racial isolation.
- **College Graduation Rates.** On January 30, 2012, the Secretary of Education published a notice inviting submissions by the higher education community for ideas related to “improved rates of postsecondary success, transfer, and graduation,” with a focus on “strategies that emphasize the quality of what students learn and timely or accelerated attainment of postsecondary degrees.” The Department intends to use the information provided during consideration of improvements to the Higher Education Act of 1965 and other legislative proposals submitted to Congress. Comments are due by April 30, 2012.

- **Draft Cohort Default Rates.** The Department of Education has delayed its release of the draft two-year and draft three-year cohort default rates until Monday, February 27 and March 5, respectively. The Department had originally scheduled the release dates for Monday, February 13 and Monday, February 20, respectively.

In September 2012, the Department will publish the final cohort default rates. This is the first year the Department will issue three-year cohort default rates as directed under the Higher Education Opportunity Act (HEOA) enacted in August 2008.

- **No Child Left Behind (NCLB) Waiver Requests.** On Wednesday, February 15, the Department of Education announced it approved New Mexico's waiver request. In total, the Department has approved 11 waiver requests of states: Colorado, Florida, Georgia, Indiana, Kentucky, Massachusetts, Minnesota, New Jersey, Oklahoma, and Tennessee. These states are now required to set new performance targets for student achievement and establish accountability systems to reward high-performing schools and address the needs of the lowest-performing schools.

Since the President's announcement in September 2011 to allow states flexibility in meeting the 2014 targets set by NCLB, 39 states, Washington D.C., and Puerto Rico have signaled their intent to request waivers.

- **Teacher Preparation Rules.** The second session of negotiations regarding the Department's rule making process for teacher preparation programs will be held Monday, February 27 through Wednesday, February 29. The regulation would require states to report data on employment outcomes for newly graduated teachers and student learning outcomes for those teachers' students.

Energy

LEGISLATIVE ACTIVITY

- **CES.** Senate Energy and Natural Resources Committee Chairman Jeff Bingaman (D-NM) is soon expected to propose long-awaited legislation that would create a national Clean Energy Standard. It follows President Obama's call last year and again this year in his State of the Union Address for Congressional action, an effort with Ranking Member Lisa Murkowski (R-AK) to solicit stakeholder comments on a "White Paper" on what a CES could look like, and independent modeling analysis requested from the Energy Information Administration. The proposal faces long odds towards Senate passage and enactment in an election year.
- **Renewable PTC.** President Obama's "Framework for Business Tax Reform" proposes to make permanent the energy production tax credit, and address programmatic inefficiencies by making the credit refundable.
- **Congressional Hearings.** On Monday, a House Natural Resources subcommittee will hold a field hearing in Steubenville, Ohio on how natural gas production can create jobs, energy, and community growth. On Tuesday, the Senate Energy and Natural Resources Committee will hold a hearing on the independent Department of Energy (DOE) Loan Guarantee Program audit report; Energy Secretary Steven Chu will testify before a House Appropriations subcommittee on DOE's FY 2013 budget request; a House Energy and Commerce subcommittee will hold a hearing to assess "smart grid" security; and a House Natural Resources subcommittee will hold an oversight hearing on the Bureau of Land Management's FY 2013 budget request.

REGULATORY ACTIVITY

- **Transmission.** The DOE will issue a formal Request for Information on questions related to the permitting of transmission lines, such as how to make development times for generation and transmission more commensurate with one another. Comments will be due by the end of March.
- **Ultra-Deepwater Advisory Committee.** The DOE will host an open meeting on March 8.
- **Hydraulic Fracturing.** The Bureau of Land Management submitted its proposed rule to the Office of Management and Budget (OMB) for Executive Order 12866 regulatory review on Wednesday, February 15. It would require disclosure of components used in hydraulic fracturing fluids and self-certification that fluids comply with applicable laws and regulations, and include certain wellbore integrity rules at various stages of operation. OMB typically has 45-90 calendar days to complete its review of proposed regulatory actions before an agency can begin the formal public comment process as part of a proposed rulemaking.

Environment

LEGISLATIVE ACTIVITY

- **U.S. Department of Interior Budget.** On Tuesday, February 28, the Senate Committee on Energy and Natural Resources will hold a full committee oversight hearing on the U.S. Department of Interior's budget for FY 2013. Secretary Ken Salazar will testify.
- **National Park Service and Bureau of Land Management.** On Tuesday, February 28, the House Committee on Natural Resources, Subcommittee on National Parks, Forests And Public Lands will hold an oversight hearing on the FY 2013 budget requests from the National Park Service and the Bureau of Land Management.

REGULATORY ACTIVITY

- **EPA Nominations.** The U.S. Environmental Protection Agency (EPA) is inviting nominations from qualified candidates to be considered for appointment to its Local Government Advisory Committee (LGAC). The LGAC was chartered to provide advice to the EPA Administrator on a broad range of environmental issues affecting local governments. The EPA is soliciting nominations to fill 23 vacancies through August 2014. Nominees will be selected to represent: large cities; moderate-sized cities; small communities and townships (under 10,000); county elected officials from urban, suburban and rural areas; city elected and appointed officials (city council members, city managers); state elected and appointed officials (state representatives, state environmental commissioners); and tribal elected and appointed officials (chair, president, natural resources directors). Vacancies are anticipated to be filled by September 2012. Nominations should be submitted no later than March 26.
- **Ozone.** The EPA is taking final action on additional revisions to the Transport Rule (Federal Implementation Plans: Interstate Transport of Fine Particulate Matter and Ozone and Correction of SIP Approvals published August 8, 2011). Based on comments received, EPA is finalizing adjustments that result in revisions to 2012 and 2014 state budgets in Arkansas, Georgia, Indiana, Kansas, Louisiana, Mississippi, Missouri, New York, Nebraska, Ohio, Oklahoma, South Carolina and Texas, and revisions to new unit set-asides in Arkansas,

Louisiana and Missouri. This rule is effective on May 21, 2012, unless EPA receives significant adverse comments by March 22.

- **Nitrogen Dioxide (NO₂).** The EPA has issued a final rule for Nitrogen Dioxide (NO₂). This rule establishes air quality designations for all areas in the United States for the 2010 Primary Nitrogen Dioxide (NO₂) National Ambient Air Quality Standards (NAAQS). Based on air quality monitoring data, the EPA is issuing this rule to designate all areas of the country as “unclassifiable/attainment” for the 2010 NO₂ NAAQS. The EPA is designating areas as “unclassifiable/ attainment” to mean that available information does not indicate that the air quality in these areas exceeds the 2010 NO₂ NAAQS. The effective date of this rule is Wednesday, February 29, 2012. The EPA and state agencies are currently working to establish an expanded network of NO₂ monitors, expected to be deployed in 2013. Once three years of air quality data have been collected from the expanded network, the EPA will be able to evaluate NO₂ air quality in specific locations.

Financial Services

LEGISLATIVE ACTIVITY

- **STOCK Act Awaiting Senate Action.** On February 2, the Senate overwhelmingly passed legislation that would ban insider trading by Members of Congress and senior aides. A week later, the House passed a revised version of the Senate bill, eliminating various provisions such as the restoration of criminal penalties in some public corruption cases and the imposition of new disclosure requirements for political intelligence consultants. The revised bill now awaits Senate consideration. The Senate can choose to approve or reject the revised bill, or it can choose to send the legislation to a Conference Committee to negotiate a compromise between the two bills. A Conference Committee is likely to prolong ultimate passage of the legislation. A detailed comparison of the House and Senate bills can be found in the *Patton Boggs Client Alert*, [“TAKING STOCK: House Passes Amended Insider-Trading Bill.”](#)
- **Congress to Discuss Housing Market; Government Involvement.** On Tuesday, February 28, the House Financial Services Subcommittee on Insurance, Housing, and Community Opportunity will hold a hearing to discuss the Department of Housing and Urban Development (HUD). In the afternoon, the Senate Banking Committee will hear from HUD Secretary Shaun Donovan, Federal Reserve Governor Elizabeth Duke and Federal Housing Finance Agency (FHFA) Acting Director Ed DeMarco on the state of the housing market.
- **House Agriculture Committee to Review CFTC Agenda.** On Wednesday, February 29, the House Agriculture Committee will hold a hearing to discuss the Commodity Futures Trading Commission’s (CFTC) 2012 agenda.
- **Bernanke to Appear Before Congress.** On Wednesday, February 29, the House Financial Services Committee will hold a hearing titled, “Monetary Policy and the State of the Economy.” On Thursday, March 1, the Senate Banking Committee will hold a hearing titled, “The Semiannual Monetary Policy Report to the Congress.” Ben Bernanke, Chairman, Board of Governors of the Federal Reserve System, will testify at both hearings.

REGULATORY ACTIVITY

- **FHFA Sends Congress Strategic Plan for Fannie Mae and Freddie Mac Conservatorships.** On Tuesday, February 21, the FHFA sent Congress a strategic plan for the next phase of the conservatorships of Fannie

Mae and Freddie Mac. The plan sets forth objectives and steps FHFA is taking or will take to meet FHFA's obligations as conservator, including (i) building a new infrastructure for the secondary mortgage market; (ii) gradually contracting the GSEs dominant presence in the marketplace while simplifying and shrinking their operations; and (iii) maintaining foreclosure prevention activities and credit availability for new and refinanced mortgages.

- **CFTC to Review Collateral Protection for Customers.** On Wednesday, February 28 and Thursday, February 29, the CFTC will host a two-day public roundtable to discuss additional customer collateral protection. Discussions will focus on issues related to the advisability and practicality of implementing the legal segregation with operational commingling (LSOC) model as the segregation model for collateral posted by futures customers and the protection of customer funds deposited with futures commission merchants for trading on foreign futures markets.

Health Care

LEGISLATIVE ACTIVITY

- **House Budget Hearing.** The House Committee on the Budget will hold a hearing on Tuesday, February 28 on "Strengthening Health and Retirement Security." Witnesses include Richard Foster, Chief Actuary, Center for Medicare and Medicaid Services (CMS) and Stephen Goss, Chief Actuary, Social Security Administration (SSA).
- **House Ways and Means Hearing.** The House Committee on Ways and Means will hold a hearing on Tuesday, February 28 on the President's FY 2013 Budget Proposal with U.S. Department of Health and Human Services (HHS) Secretary Kathleen Sebelius.
- **House Judiciary Hearing.** The House Committee on the Judiciary has scheduled a hearing on Tuesday, February 28 on "Executive Overreach: The HHS Mandate Versus Religious Liberty." Witnesses have yet to be announced.
- **Senate Budget Hearing.** On Wednesday, February 29, the Senate Budget Committee will hold a hearing entitled "Putting Health Care Spending on a Sustainable Path." Three expert witnesses are scheduled to testify, including Dr. David Cutler, Professor of Economics, Harvard University; Dr. Len Nichols, Professor of Health Policy and Director of the Center for Health Policy Research and Ethics, George Mason University; and James Capretta with the Ethics and Public Policy Center.
- **Senate HELP Hearing.** The Senate Committee on Health, Education, Labor and Pensions has scheduled a hearing for Wednesday, February 29 on "Dental Crisis in America: The Need to Expand Access." Witnesses will include: Burton Edelstein, DDS, MPH, Professor of Dentistry and Health Policy & Management at Columbia University, New York, New York; Shelly Gehshan, MPP, Director of the Pew Children's Dental Campaign, Pew Center on the States, Washington, DC; Grant Whitmer, MBA, CEO at Community Health Center of Rutland County, Rutland, Vermont; Gregory Folse, DDS, President of Outreach Dentistry, Lafayette, Louisiana; Christy Jo Fogarty, RDH, MSOHP, Licensed Dental Hygienist and Licensed Dental Therapist at Children's Dental Services, Farmington, Minnesota.

- **Energy and Commerce Hearing.** On Thursday, March 1, the House Energy and Commerce Committee will hold a hearing on the FY 2013 HHS Budget. HHS Secretary Kathleen Sebelius will testify.
- **Energy and Commerce Hearing.** The Committee on Energy and Commerce Subcommittee on Commerce, Manufacturing and Trade has scheduled a hearing on Thursday, March 1, titled “Prescription Drug Diversion: Combating the Scourge.” Witnesses will be announced in the coming days.

REGULATORY ACTIVITY

- **FDA Releases Draft Guidance on Drug Shortages.** The Food and Drug Administration (FDA) released a “Notification to FDA of Issues that May Result in a Prescription Drug or Biological Product Shortage.” The draft guidance relates to the Federal Food, Drug, and Cosmetic Act (FD&C) which requires sole manufacturers to notify the FDA of a discontinuance of certain drug products and to the President’s Executive Order of October 31, 2011 directing the FDA to use all available administrative tools to expand the Agency’s efforts to combat the problem of drug shortages. The Agency is requesting comments from interested stakeholders on the specific questions posed in the Federal Register within 90 days.
- **CMS Releases Stage Two Meaningful Use Proposed Rule.** The Centers for Medicare and Medicaid Services (CMS) released the proposed rule that would specify the Stage 2 criteria that eligible professionals (EPs), eligible hospitals, and critical access hospitals (CAHs) must meet in order to qualify for Medicare and/or Medicaid electronic health record (EHR) incentive payments. In addition, it would specify payment adjustments under Medicare for covered professional services and hospital services provided by EPs, eligible hospitals, and CAHs failing to demonstrate meaningful use of certified EHR technology and other program participation requirements. This proposed rule revises certain Stage 1 criteria, as well as criteria that apply regardless of Stage, as finalized in the final rule titled “Medicare and Medicaid Programs; Electronic Health Record Incentive Program,” published on July 28, 2010 in the Federal Register. The provisions included in the Medicaid section of the proposed rule (which relate to calculations of patient volume and hospital eligibility) would take effect shortly after finalization of this rule, not subject to the proposed one-year delay for Stage 2 of meaningful use of certified EHR technology. The proposed rule delays the onset of Stage 2 criteria until 2014. Comments on the proposed rule must be received by May 6, 2012.
- **HHS Releases Final Regulations on the Medicaid Waiver Process.** The Department of Health and Human Services released two final rules related to the Medicaid program. The first details the review and application process for Section 1115 Demonstration waivers that allow states to design their own health reform programs, and the second outlines transparency requirements for the Medicaid demonstration waiver review and approval process. The innovation waiver rule purportedly only makes a small number of changes to the application process. Additionally, the Administration has come out in favor a plan from Senator Ron Wyden (D-OR) and Senator Scott Brown (R-MA) to move up the innovation waivers from 2017 to 2014, but Congress is unlikely to take up legislation to support that change.

OTHER HEALTH NEWS

- **MedPAC Meeting.** The Medicare Payment Advisory Commission (MedPAC) has scheduled its next public meeting on Wednesday and Thursday March 8 -9, 2012. An agenda will be released when available.

- **IOM Meeting.** The Institute of Medicine's Best Practices Innovation Collaborative will meet on Tuesday, February 28, 2012. The Collaborative members will review principles and expectations developed for team-based care to serve as common reference points guiding collaboration to improve care, improve health, and reduce costs; identify opportunities for collaboration among participants in implementation and spread of the team-based care principles; and consider other potential applications of team-based care principles, including the intersection with research, health informatics, policy and payment.

International, Defense, Homeland Security

Syria Developments. As multilateral diplomatic efforts intensify to forge both a ceasefire and a longer-term transition in Syria, the Obama Administration is moving closer to supporting the arming of the Free Syrian Army opposition movement. Several Arab states, likely including several Sunni-led members of the Gulf Cooperation Council, reportedly already have begun to supply the resistance fighters. Secretary of State Hillary Clinton signaled the Administration's evolution toward tacit approval with her comments on Thursday that the Syrian rebels "will find somewhere, somehow the means to defend themselves, as well as begin offensive measures..." However, the Administration has not indicated its intent to supply such arms directly, and most senior Administration officials remain skeptical of closer security cooperation with the ideologically disparate, militarily-disorganized, and largely diaspora-led opposition. However, Washington has supported nascent United Nations planning for a joint UN-Arab League peacekeeping force that a hypothetical post-Assad Syrian government would invite into the country.

Iran Developments. The Administration continues to counsel patience toward the Israeli government and hawks in Congress regarding a potential attack on Iran's nuclear program, also signaling an underlying belief that the Iranian regime is a more rational actor on "life-or-death" matters than often assumed. Chairman of the Joint Chiefs of Staff Martin Dempsey has intimated that U.S. intelligence suggests that Iran has not yet decided to assemble and weaponize a nuclear device and delivery system, despite Tehran's clear pursuit of the technology necessary to do so. The Pentagon also continues to remind Israel that the U.S.'s superior "bunker busting" capability allows for greater flexibility on timing for any future targeted or sustained bombing campaign, compared to the Israelis' own options. In other words, Washington is emphasizing, or arguably creating, decision points from which Iran can strike a deal and back away relatively gracefully. Still, many variables must play out before that scenario could emerge.

National Security Budget Hearings. Several of the Administration top's national security officials will testify on Capitol Hill this week on their FY 2013 budget requests and related policy issues, defending proposed targeted cuts while arguing for continued support for Administration priorities. Secretary Clinton will defend the Administration's proposed cuts to the FY 2013 international affairs budget before the Senate Foreign Relations Committee on Tuesday, February 28 and the House Foreign Affairs Committee on Wednesday, February 29. In the Senate Armed Services Committee, the Commanders of the U.S. European Command (EUCOM), African Command (AFRICOM), Pacific Command (PACOM), and the Transportation Command also will testify in support of their FY 2013 budget requests this week. Admiral James Stavridis, NATO's Supreme Allied Commander, and General Carter Ham also will defend the FY 2013 EUCOM and AFRICOM budgets, respectively, in front of the House Armed Services Committee (HASC) on Wednesday, February 29. Admiral Robert Willard, PACOM Commander, will follow suit for his area of responsibility on Thursday, March 1. Secretary of the Air Force Michael Donley will appear before the HASC in a budget hearing on Tuesday,

February 28. The House Homeland Security Committee's Emergency Preparedness Subcommittee will examine the Federal Emergency Management Agency's FY 2013 budget request on Wednesday, February 29.

Tax

LEGISLATIVE ACTIVITY

- **Administration Unveils Corporate Tax Reform Proposal.** On Wednesday, February 22, President Obama through the White House and the Treasury Department released a corporate tax reform proposal: "The President's Framework for Business Tax Reform" (Proposal). The Proposal focuses on corporate rather than individual income tax, and in general, seeks to lower rates while broadening the tax base, but does not eliminate the current worldwide system of taxation. The Proposal adds an important voice to the ongoing discussions on Capitol Hill surrounding the need to fundamentally reform the Internal Revenue Code.

It proposes reducing the top corporate rate from 35 to 28 percent while providing manufacturers with additional tax preferences that would effectively lower their tax rate to 25 percent, with even lower rates for firms engaged in "advanced manufacturing." To help pay for the cost associated with this rate cut, the Proposal includes previous Administration tax increases such as eliminating the last in first out (LIFO) method of accounting, taxing carried interest at ordinary rates, and eliminating a variety of oil and gas tax incentives.

Several of the Proposal's significant revenue raising ideas, while not new to those following the corporate tax reform debate, have not before been included in prior budget and/or deficit reduction proposals. These ideas, all of which are in broad outline form with significant details yet to be filled in, include changes to depreciation schedules, the tax treatment of debt versus equity financing, and increased taxes on some pass-through entities.

On international taxation, the Administration flatly rejects any proposal that would move to a "pure territorial system." Instead, the Proposal moves in the opposite direction by seeking to establish a minimum tax on U.S.-based multinational corporations' foreign earnings, eroding the use of "deferral" of foreign-source income. Thus, the Proposal strikes a clear contrast from Representative Dave Camp's (R-MI), Chairman of the House Ways and Means Committee, October 2011 draft legislation which would create a participation exemption system of taxation similar to a territorial system, with base erosion protections.

For a full analysis of the President's Business Tax Reform Proposal please see Patton Boggs' summary [here](#).

- **Payroll Tax/Unemployment Insurance/Doc Fix Signed.** On Wednesday, February 22, President Obama signed into law the Middle Class Tax Relief and Job Creation Act (H.R. 3630), which extends the payroll tax cut originally enacted for 2011 through 2012. The bill also extends enhanced unemployment insurance (UI) benefits and forestalls a scheduled 27 percent cut in doctors' Medicare reimbursements known as the "doc fix," through 2012. The total cost to the package is approximately \$150 billion, and lawmakers agreed that the \$93.2 billion cost of the payroll tax holiday extension would not be offset.

To offset the remaining cost of the package, the agreement requires future federal workers and Members of Congress to contribute more toward their defined benefit pension plans, raising approximately \$15 billion. The

other offsets include: (1) roughly \$15 billion from the auction of a portion of the wireless spectrum; (2) about \$11 billion that hospitals will lose in government payments for bad debt, incurred when Medicare recipients fail to make their co-payments or pay deductibles; (3) a 2 percent Medicare payment cut to clinical laboratories in 2013; and (4) shaving \$5 billion over a decade from a \$2 billion-a-year fund created by the Affordable Care Act to support community preventative and public health care programs. While a part of the discussion, the bill did not ultimately include tax “extenders” that lapsed at the end of 2011 such as the R&D credit, active financing exception, and various incentives for alternative energy, nor did it include 100 percent bonus depreciation for capital expenditures incurred by businesses in 2012.

- **Tax Hearings Next Week.** The following hearings are scheduled next week in the House Ways and Means and Senate Finance Committees:
 - Tuesday, February 28: House Ways and Means Committee hearing on the “President's Fiscal Year 2013 Budget Proposal” with U.S. Department of Health and Human Services Secretary Kathleen Sebelius
 - Wednesday, February 29: House Ways and Means Committee hearing on “President Obama’s Trade Policy Agenda” with U.S. Trade Representative Ron Kirk and Second Panel on the Future of U.S. Trade Negotiations
 - Thursday, March 1: Senate Budget Committee hearing on “Tax Reform to Encourage Growth, Reduce the Deficit, and Promote Fairness”

TechComm

- **Privacy.** The White House unveiled its Consumer Privacy Bill of Rights on Thursday, February 23 as part of a comprehensive report “Consumer Data Privacy in a Networked World: A Framework for Protecting Privacy and Promoting Innovation in the Global Digital Economy.” The Consumer Privacy Bill of Rights provides a baseline of protections for consumers and greater certainty for businesses. The rights are individual control, transparency, security, access and accuracy, focused collection, and accountability.

The Bill of Rights is one of four key elements of the report, which also includes a stakeholder-driven process to specify how these rights apply in particular business contexts; strong enforcement by the Federal Trade Commission (FTC); and greater interoperability between the United States’ privacy framework and those of international partners. In the coming weeks, the Commerce Department’s National Telecommunications and Information Administration (NTIA) will convene stakeholders – including companies, privacy and consumer advocates, technical experts, international partners, and academics – to establish practices or codes of conduct that implement the general principles in the Consumer Privacy Bill of Rights.

Representatives Joe Barton (R-TX) and Ed Markey (D-MA) intend to move forward with privacy legislation to protect children even as Internet companies renew their commitments to privacy. Google, Microsoft, Yahoo and other members of the Digital Advertising Alliance said they would collaborate with Web browsers to create a “Do Not Track” button that would allow consumers to opt out of tracking by Internet advertisers with a single click. The companies’ commitment came in the wake of the White House’s announcement of the Consumer Privacy Bill of Rights— a set of principles for how companies should handle user information. The Administration plans to work with companies and privacy advocates to turn the set of principles into an

industry code of conduct. Barton and Markey said voluntary commitments are insufficient to protect consumer privacy, with Barton noting that the White House's new guidelines will not be enforceable. The lawmakers' "Do Not Track Kids Act" would restrict online marketing to children and create an "Eraser Button" for parents to delete information that companies gather about their children. Meanwhile, House Commerce, Manufacturing and Trade Subcommittee Chair Mary Bono Mack (R-CA) said she plans to hold a hearing sometime in March as part of a series of hearings to determine whether legislation on consumer online privacy is necessary.

- **Spectrum.** The President on Wednesday, February 22 signed The Middle Class Tax Relief and Job Creation Act (the Act), which would be paid for in part by the auction of television broadcast spectrum, with at least \$20.4 billion of auction proceeds set aside to offset the federal deficit.

The spectrum provisions in the Act are largely the same as those in H.R. 3630 as passed by the House in December 2011 with two exceptions: (1) the provisions relating to unlicensed spectrum and (2) the provisions relating to FCC auction authority. With respect to unlicensed spectrum, the law gives the FCC the authority to preserve existing TV white spaces; and it gives the FCC the authority to use part of the spectrum relinquished by TV broadcasters in the incentive auction to create nationwide guard bands that can be used for unlicensed use, including in high-value markets that currently have little or no white spaces today. With respect to auction authority, H.R. 3630 would have restricted the FCC's future ability to limit participation in spectrum auctions, regardless of the size or market dominance of potential bidders. The Act modifies this prohibition by expressly preserving the FCC's ability to ensure competition through spectrum aggregation limits and other rules. The legislation also drops a provision in the House-passed bill that would have limited the FCC's authority to set license conditions, such as open-Internet requirements, on auctioned spectrum.

Proceeds from voluntary spectrum auctions would be used to establish a Public Safety Trust Fund in the Treasury available until 2022. It would provide up to \$2 billion to reimburse funds NTIA borrowed for First Responder Network Authority; \$100 million for the State and Local Implementation Fund; \$7 billion in NTIA grants for build out of the First Responder Network Authority; \$20.4 billion for deficit reduction; and \$250 million for Next Generation 9-1-1. Any remaining funds would be used for deficit reduction.

The Act provides first responders with access to the so-called D block spectrum and advanced wireless broadband communications they need to protect the public and to communicate with each other across the country. The Act provides for the construction of a nationwide public safety broadband network, as envisioned in S. 911, with an "opt-out" option for states that demonstrate the capacity to build their own networks and connect them to the national network.

The Act creates a First Responder Network Authority (FirstNet) within the NTIA and provides FirstNet with \$7 billion and a license to use the D block and adjacent public safety spectrum to build the nationwide public safety network. To ensure national interoperability, the legislation also creates a technical advisory board at the FCC to develop interoperability standards. States that want to construct their own portion of the national public safety network have the option to apply for NTIA grants to build and operate the radio access network in the state if they can demonstrate to the FCC that the network will meet the interoperability standards and to NTIA that they have the resources and capability to provide comparable coverage and security, and maintain ongoing interoperability.

Unlike the House-passed bill, the Act does not require public safety officials to return the 700 MHz "narrowband" spectrum to the FCC for auction. Instead, the legislation requires the return of less efficient

spectrum known as the “T-band” of spectrum located between 470 MHz and 512 MHz in 13 major cities and surrounding counties. This transition occurs 11 years from the date of enactment, and public safety relocation costs will be reimbursed from any auction proceeds.

The Act provides \$1.75 billion for the relocation of broadcast television channels that do not participate in the voluntary spectrum auction and must be relocated to clear spectrum for auction by the FCC. The Act also would allow for the modification of an existing wireless tower or base station that does not substantially change the physical dimensions of the tower or base station. Historic preservation and environmental requirements will still have to be met.

Transportation

LEGISLATIVE ACTIVITY

- **SAFETEA-LU Reauthorization.** Late breaking reports on Thursday, February 24 indicated that the House would be moving forward with a shorter-term bill that preserves dedicated gas tax funding for mass transit. The transit funding issue had been a core obstacle to getting enough votes to pass the bill, and the House also had increasing trouble with coming up with sufficient revenue for the original, five-year bill. In that it addresses the major obstacles to passage, this development would appear to represent a deal that will allow the bill to move to the floor and pass the House. However, reports indicate that the House leadership is weighing the idea of a shorter term bill but no decision has been made. A shorter-term bill, if that is indeed the path forward, would not be a “clean” extension but would be the substance of H.R. 7 just with a shorter duration and corresponding changes in funding. While action in the Senate had been delayed over how to handle non-germane amendments in particular and the amendment process more generally, the Senate is expected to turn to its two-year reauthorization bill, MAP-21 (S. 1813) when it returns from recess next week. The Senate is ultimately expected to pass its reauthorization bill, although the floor process and amount of time the bill will be on the floor remains uncertain. More detail on the Senate floor process should emerge next week when Members return to Washington.