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Washington Update

March 3, 2014

Congress dealt with several high profile issues in February. Lawmakers sustained their recent trend of bipartisanship by passing the Farm Bill and increasing the statutory debt limit, which helped to stave off a potential federal default and financial crisis. Despite that notable progress, Congress continues to find itself at an impasse on other major issues. Legislators have yet to agree on a way forward on key tax issues and the implementation (or in some cases, postponement) of key provisions of the Affordable Care Act (ACA) continues to define daily debate in the halls of the Capitol. There are some signs, however, that lawmakers will be able to find common ground on issues such as Medicare reimbursement (the Sustainable Growth Rate formula) and the forthcoming transportation reauthorization bill. Debate over the extension of unemployment insurance and raising the minimum wage are expected to dominate the headlines in the weeks ahead.

ISSUE—FUNDING THE FEDERAL GOVERNMENT

In mid-January, Congress passed an omnibus spending bill to fund the federal government through September 30, which is the end of Fiscal Year 2014 (FY14). The omnibus spending bill followed a topline funding level for FY14 of $1.012 billion, which was established by the December bipartisan budget agreement and was $45 billion over the sequester cap, thanks to some sequester relief included in the budget deal.

The December budget deal also established the topline number for the FY15 appropriations bills at $1.014 trillion, allowing appropriators to begin the preliminary work of crafting the annual appropriations bills to allocate funding for federal programs and agencies. Appropriators will work through the summer and most likely into the fall to pass these measures, though election year dynamics may make the process more difficult. In a change from recent years, the Appropriations Committee may even bring its first bill (the Military Construction and Veterans Affairs bill) to the floor as early as April.

The White House announced that it will submit a budget for FY15 by March 4, which is after the congressionally mandated deadline, but sooner than the Administration has delivered it in the past. While the budget is unlikely to contain many surprises, Congress is expected to stick with the agreed-upon topline number of $1.014 trillion for FY15 regardless of the President's proposal. The President's budget proposal has no force of law, but does serve as an outline of the President's spending and policy priorities and contains his recommendations for allocating taxpayer dollars to federal agencies.

ISSUE—DEBT CEILING

Congress successfully passed a debt ceiling increase in February. The Treasury Department had warned that a debt limit breach would occur toward the end of February and urged Congress to move quickly. Debt ceiling politics have been tense in recent years, and Republicans spent much of January and parts of February deciding what they would demand as a concession to increase the debt limit. Initial discussions among Republican leaders included the possibility of abandoning previous calls for cuts in spending and instead pursue reforms to the ACA in return for raising the debt ceiling.

In the end, Republicans leaders settled on trying to move a package that would increase the debt limit until the first quarter of 2015 while also reversing a provision in the December budget agreement that effectively reduced pension benefits for working-age military retirees. Republican leaders hoped that the package would garner support from rank-and-file Republican members while also putting House Democrats in a tough position by forcing them to take a vote on military pensions. However, internal Republican resistance to the legislation was too much to overcome, and Republican leaders pulled the bill before it was considered on the floor. Ultimately, the House was forced to pass a "clean" debt limit increase, and move the military piece as a separate measure. The debt limit bill passed by a vote of 221-201. Only 28 House Republicans voted for the measure.

In the Senate, the bill faced additional opposition from Republicans. Senator Ted Cruz (R-TX) demanded that the vote to end debate and proceed to a final vote on the measure face a 60-vote threshold, effectively requiring at least five Republicans to vote with all of the Senate Democrats to allow the debt ceiling package to move forward. In the end, Senate Minority Leader Mitch McConnell (R-KY) and Whip John Cornyn (R-TX) led a small group of Republicans in casting votes to get the bill over the 60-vote threshold, though no Republicans voted for final passage of the debt ceiling bill which occurred on a party line vote of 55-44. The President signed the bill into law on February 15, which both raised the debt ceiling until March 2015 and took the issue off the table as a major mid-term election issue. A handful of Republicans criticized the Senate GOP leadership for allowing the debt ceiling bill to come to a vote while other Republicans applauded the GOP leadership for taking the final moment of fiscal brinksmanship off the table for 2014 and allowing the public debate to focus on the Affordable Care Act and the economy for the remainder of the election year.

ISSUE—TAXES

Tax policy issues were pushed to the forefront in February as Senator Ron Wyden (D-OR) assumed chairmanship of the Senate Finance Committee and long-stalled tax reform efforts were given renewed attention in the House.

Tax Reform

The proposed rewrite of the federal tax code has been in limbo for several months as attitudes toward tax reform soured despite the public and private lobbying of Senate Finance Committee Chairman Max Baucus (D-MT) and House Ways and Means Chairman Dave Camp (R-MI). Tax reform's prospects darkened further when Chairman Baucus was approved by the Senate to be the new U.S. Ambassador to China. With Ambassador Baucus leaving the Senate, tax reform lost one of its greatest advocates. Baucus' successor, Senator Wyden, has shown interest in tax reform efforts in the past, but has publicly stated in recent weeks that his priority will be moving a tax extenders bill first.

Chairman Camp, who is expected to give up leadership of his committee next year due to term limits, sought to refocus attention on his efforts and help frame future debate on the issue by releasing his long-awaited tax reform proposal. On February 26, Chairman Camp unveiled his comprehensive tax reform proposal. The measure addresses both the individual and corporate tax code and would:

Individual

- Consolidate seven tax brackets to effectively three brackets at 10%, 25%, and then a third bracket for joint income above $450,000 and individual income over $400,000 that be subject to a 10% surtax;
- Cap home mortgage interest deduction at $500,000, down from $1 million;
- Eliminate the state and local tax deduction;
- Eliminate the Alternative Minimum Tax; and
- Tax capital gains and qualified dividends at ordinary income tax rates with a 40 % exclusion.

Corporate

- Eliminate the modified accelerated cost recovery system;
- Extend lives for depreciation of property by requiring amortization instead of expensing for R&D and advertising expenses;
- Institute a territorial tax system with a 95% exemption of dividends received by U.S. corporations from foreign subsidiaries;

- Tax intangible income from foreign markets at 15%; and
- Allow for a one time transition tax on all previously untaxed foreign earnings and profits of foreign subsidiaries of U.S. corporations.

Reaction to the plan was mixed. Republican leaders have long worried that a GOP tax reform bill could be used as a political weapon by Democrats, which would be particularly problematic in an election year. House Republican leadership had previously convinced Chairman Camp to delay the release of his plan, fearing that the proposal would put incumbents in an uncomfortable position while also distracting from their core message on the beleaguered ACA. Upon the release of the proposal, Republican lawmakers began distancing themselves from the plan by lauding Camp's hard work but suggesting that it only provides a starting point for the discussion.

While the proposal includes many ideas originated by President Obama and congressional Democrats, most Democrats pounced on the plan, attacking it as a handout to the wealthy and assailing Chairman Camp for going after popular tax deductions, like the mortgage interest and state and local sales tax deductions. Democrats are likely to campaign on the proposal, casting it in a negative light and attempting to tie vulnerable Republican members to it.

The business community was also mostly displeased. By eliminating tax provisions such as accelerated depreciation, the LIFO accounting method, and scores of industry-related tax deductions, the plan calls for ending many of the provisions that companies hold sacred.

The future of the proposal is unclear. Chairman Camp will likely hold hearings on the proposal and may even mark up the bill in Committee. If the measure becomes politically toxic, however, Republican leadership will intervene and move the House away from the controversial effort. Regardless of what is to come, the proposal will have a major impact on the tax reform debate going forward, even after Chairman Camp relinquishes his gavel next year.

Tax Extenders

Congress made no progress this month on replacing the expired package of short-term tax provisions known as extenders. The nearly 60 provisions expired on December 31, 2013, following a last minute and mainly political attempt by Senate Majority Leader Harry Reid (D-NV) to quickly pass an extension through the upper chamber. Newly-minted Chairman Wyden has announced his commitment to passing a new extenders package. Chairman Wyden has said that he prefers to deal with extenders before moving on to tax reform in order to provide certainty for the business community. This position is at odds with Chairman Camp's position that tax reform would eliminate the need for extenders altogether.

The timeline for extenders legislation remains unclear. Though Wyden is likely to take up tax extenders soon, Camp will likely not turn to extenders before his tax reform package gets a thorough vetting. There are also lingering questions on what should be included in the next extenders package. Some tax provisions are unpopular with legislators and the American public, and the $50 billion per year price tag raises questions over how Congress will pay for the measure. Lawmakers may look to narrow the number of provisions in an extenders bill, which is likely to set off a battle among key industry groups.

Since the tax provisions would apply to income earned in 2014, Congress can technically approve a new extenders package any time this year that would be effective retroactively. However, the closer to 2015 the nation gets, the more pressure industry is likely to put on Congress to provide a solution that allows the business community to plan appropriately.

ISSUE—HEALTHCARE

Healthcare issues saw quite a bit of action this month as Republicans continued to focus on the ACA's shortcomings and Democrats, led by the White House, attempted to sell the benefits of the law to a still-skeptical public.

ACA – Delay of Employer Mandate for Smaller Employers

Controversy continued to swirl around the ACA this month as several new developments emboldened opponents' criticism of the law. On February 10, the Obama Administration announced that it would again delay implementation of key aspects of the employer mandate, which required companies with 50 or more full-time workers to provide employee health coverage. Originally slated to be enacted in 2014, the Administration had delayed the mandate until 2015, allowing businesses an extra year to prepare to cover their employees' health plans.

The Administration's February announcement will allow mid-size businesses—those with 50 to 99 employees—to be exempt from the mandate until 2016. Larger businesses will still be required to provide coverage next year, but the Administration will only obligate these corporations to cover up to 70% of their employees in 2015. By the start of 2016, that figure will rise to 95%.

Just as in the case with the original delay of the employer mandate, the Administration said they were simply reacting to business community concerns that companies would not be adequately prepared to provide full coverage to all employees by 2015. Republicans harshly criticized the decision and held it up as supporting evidence to their argument that the law is inherently flawed. The announcement also renewed Republican calls to also delay the individual mandate to give individuals the same relief afforded to businesses

ACA – Impact on Employment

The Administration's delay announcement also reignited a debate over how the federal government should define a "full-time" employee. Under the ACA, a worker is deemed a full-time employee if he or she works on average 30 hours or more per week. Businesses have said that 30 hours is too low a threshold for full-time work and have cautioned that the requirement may force them to cut jobs and hours. Consequently, several members have introduced bills to redefine full-time work at the traditional 40 hours. A bill introduced by Rep. Todd Young (R-IN) recently cleared the House Ways and Means Committee and awaits a vote on the floor, which House Majority Leader Eric Cantor (R-VA) has promised. The bill has over 200 co-sponsors, including a handful of Democrats. In the Senate, Senator Susan Collins (R-ME) introduced similar legislation, but Democratic control of that chamber has dimmed the bill's prospects. The Administration's delay of the employer mandate is likely to continue the debate over the definition of a full-time employee and may give the House version of the bill extra momentum when it is brought up for a final vote.

Healthcare policy was further rocked by the release of a Congressional Budget Office (CBO) report that provided some troubling projections for the ACA. The CBO revised its projected ACA enrollment figures from seven million to six million in the first year of operation for the state and federal exchanges. The CBO also estimated that the ACA would lead to a total reduction in full-time employment by the equivalent of 2 million jobs as employers eliminate jobs or reduce hours. Controversy erupted over the latter point. Republicans argued that the report confirmed their suspicions that the ACA will lead to massive job loss. Democrats countered by pointing out that many of the jobs factored into CBO's calculations will come from those who no longer need to work thanks to new health insurance coverage through the ACA and subsidies to make premiums more affordable. However, Republicans are likely to wrap the CBO report into their ACA narrative and election strategy.

Yet another report created problems for the ACA's defenders this month. The Center for Medicare and Medicaid Services (CMS) estimated that around 11 million small business employees will see an increase in their health insurance premiums. The ACA's supporters attempted to soften the report's blow by insisting that the figures were to be expected as the ACA was creating a fairer marketplace. Republicans latched onto the report and attacked the Administration for not keeping its promise of lowering Americans' premiums.

ACA – Medical Device Tax

Another ACA provision gave rise to concerns in February that the law may be having an impact on jobs. AdvaMed, a medical device makers' trade group, estimated that the ACA's 2.3% medical device tax has already cost the industry 33,000 jobs. Industry leaders and legislators have warned for years that it could have a chilling effect on innovation and access to necessary medical equipment. While there is growing support for repealing the provision, Congress has yet to come up with a way to "pay for" the $29 million in the revenue that the provision is estimated to generate over the next decade. As an aside, Chairman Camp's tax reform proposal included a provision to repeal the medical device tax as part of a comprehensive overhaul of the tax code.

ACA – Risk Adjustment for Insurance Companies or a Bailout?

Republicans also spent the month calling attention to provisions in the ACA that they believe amount to a bailout of the insurance industry. The law included three mechanisms for helping insurance companies manage the potential losses of offering plans in the exchanges, effectively encouraging insurance companies to do so at more affordable rates. These provisions to spread risk are known as temporary reinsurance, temporary risk corridors, and permanent risk adjustment (A breakdown of each program can be found here.) Each has a mechanism that will transfer funds to insurance companies that have incurred higher than expected costs by participating in the exchanges and covering high-risk patients. The programs were criticized in a House Oversight Committee hearing on February 5, where Senator Marco Rubio (R-FL) testified about his bill to end these mechanisms. Rep. Tim Griffin (R-AR) introduced an identical bill in the House.

Democrats countered these attacks by pointing to a CBO analysis that states that the risk mitigation programs will actually save the country $8 billion over the long term. The report states that while insurance companies will receive funds to cover losses, they are expected to pay the federal government if their costs are lower than anticipated.

ACA – Enrollment at Four Million

Despite all of these negative stories, the ACA received some good news this month when the Administration announced that around four million people have enrolled using the state and federal insurance exchanges. While the figure still falls short of the seven million the Administration hopes to enroll by the end of March, it is closer to the revised CBO projected total enrollment of six million.

Sustainable Growth Rate ("Doc Fix")

Members in both chambers have spent the past several months negotiating a compromise on a bill to replace the flawed Sustainable Growth Rate (SGR) formula, the method used to calculate the Medicare reimbursement rates for physician services. On February 4, negotiators announced they had reached a deal on the policy components. A day later, Rep. Michael Burgess (R-TX) introduced the compromise legislation. As reported by the House Ways and Means Committee, the bill would:

- Repeal the SGR and institute a 0.5 percent payment update for five years;
- Improve the fee-for-service system by streamlining Medicare's existing web of quality programs into one value-based performance program;
- Incentivize movement to alternative payment models to encourage doctors and providers to focus more on coordination and prevention to improve quality and reduce costs; and

- Make Medicare more transparent by giving patients more access to information and supplying doctors with data they can use to improve care.

While negotiators may have agreed on the policy aspects of the bill, its greatest hurdle remains. Legislators will need to agree on a "pay-for" for the legislation before it will advance.

ISSUE—TRANSPORTATION

There were several transportation-related developments this month. Congress continued its work on surface transportation reauthorization, with the Senate Environment and Public Works (EPW) Committee holding a February 12 hearing to begin work on a reauthorization bill. EPW Chairman Barbara Boxer (D-CA) and Ranking Member David Vitter (R-LA) both hope to have legislation before the Committee by April. However, during the hearing, Chairman Boxer hinted that the EPW Committee may focus their attention on regulations and guidelines for surface transportation programs and leave the question of how to pay for the bill to the Senate Finance Committee.

President Obama waded into the reauthorization debate in February by releasing details for his own transportation proposal. In the four-year measure, the President calls for $302 billion to be authorized for transportation projects. Though the specific details will be included in his FY15 budget proposal on March 4, the White House said it will include $206 billion for highways, $72 billion for transit, and $19 billion for rail.

The President's plan would also make changes to the funding of the Highway Trust Fund (HTF). Due to dwindling revenue from fuel taxes, analysts had warned previously that the HTF would run out of funds before the end of 2014. In late February, the Department of Transportation shortened that deadline, estimating that HTF's funds will be completely exhausted by the third week of August. To help stave off this funding shortage, the President's transportation plan proposes that HTF receive $150 billion in new one-time transition revenue through tax reform, but no further details were given. The President's proposal also calls for the merger of rail funding into the HTF, renaming it the Transportation Trust Fund. The HTF funding shortage is also addressed in Chairman Camp's new tax reform plan. His proposal would allocate $126 billion of the new revenue generated to the HTF. Neither proposal provided a solution to the HTF's long-term solvency issues.

The eagerness of legislators and the White House to move forward with finding a solution to the HTF's funding woes is a positive sign. However, Congress still has a long way to go to reach a consensus on how to deal with the HTF funding shortfall that will occur late this summer and how to fund the larger reauthorization bill.

Outside of the HTF, the President's proposal calls for additional funding for other transportation programs. The plan calls on Congress to make the stimulus-era Transportation Investment Generating Economic Recovery (TIGER) grant program permanent, allocating $5 billion to it over four years. The White House also proposes to authorize $1 billion in annual funding to the Transportation Infrastructure Finance and Innovation Act (TIFIA) program.

RECENT POLLING

Job Approval: President Obama

Poll	Date	Results
Rasmussen Reports	March 3	Approve 47, Disapprove 52
Gallup	March 1	Approve 40, Disapprove 56
Economist/YouGov	February 24	Approve 43 Disapprove 55

Job Approval: Congress

Poll	Date	Results
Economist/YouGov	February 24	Approve 10, Disapprove 74
CBS News/NY Times	February 23	Approve 13, Disapprove 80
Fox News	February 11	Approve 14, Disapprove 81

Generic Congressional Ballot

Poll	Date	Results
CBS News/NY Times	February 23	Democrats 39, Republicans 42
Rasmussen Reports	February 23	Democrats 41, Republicans 37
McClatchy/Marist	February 9	Democrats 46, Republicans 44

Direction of the Country

	Date	Results
The Economist/ YouGov	February 24	Right Direction 29, Wrong Direction 59
CBS News/NY Times	February 23	Right Direction 32, Wrong Direction 63
Rasmussen Reports	February 23	Right Direction 32, Wrong Direction 61