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The State of the Union:

What to Expect Next From President Trump and the 115th Congress

January 31, 2018

Introduction

In his first official State of the Union Address last night, President Trump made the case for his first year in office as one of extraordinary legislative and regulatory accomplishments as part of his Administration's efforts to build a "Safe, Strong, and Proud America." In his remarks before a joint session of Congress 11 months ago, the President had called on Congress to "repeal and replace" the Affordable Care Act (Obamacare), to enact a trillion-dollar infrastructure bill, to adopt comprehensive immigration reform legislation and to adopt tax reform legislation that would make American companies more competitive and would provide "massive tax relief for the middle class."

Legislatively speaking, 2017 was not a year of major legislative accomplishments . . . until it was, as the year ended on a particularly high note, when Congress approved and President Trump signed into law the first major overhaul of the tax code since 1986.

A year ago, we suggested that year one of the Trump presidency might end up looking a lot like the Trump presidential campaign: chaotic, disorganized, controversial and divisive, but nonetheless, somewhat effective, in spite of itself. We argued that moving an infrastructure bill would be a way to accomplish something important with bipartisan support. We also previewed a path for tax reform, especially given the decade of preparatory work by Speaker Paul Ryan (R-WI). That Republicans would overcome deep philosophical differences to work together in rare harmony in what was arguably the most discordant legislative year in modern history is not something we saw coming. But the way in which they won that victory will likely have significant ramifications for the year ahead.

As the President emphasized last night, the economic state of the union appears to be quite strong. Unfortunately, as the Democratic response confirmed, the state of affairs on Capitol Hill is anything but.

The second session of the 115th Congress will be no more predictable than the roller-coaster ride that was the first session. With the added dynamic of 2018 being a mid-term election year, the second session could be even more divisive and tumultuous. But we would caution against making the assumption that nothing of consequence will happen. To date, the American experience with Donald Trump in government and politics alike has been that when it comes to results, he tends to end up exceeding conventional wisdom and expectations – often, it would seem, in spite of himself.

The President's Speech and the Democratic Response

Last night, the President talked at length about the broadly distributed benefits of the tax reform bill and the strength of the economy, shared his vision for a trade policy that would be "free, fair and reciprocal," called for increased military spending and warned about continuing threats from North Korea. In a plea for bipartisan support, he specifically called on Congress to adopt a comprehensive immigration reform bill and an infrastructure bill that would generate at least $1.5 trillion in new spending.

In the Democratic response from the auto shop of a technical training school in his blue collar district, Rep. Joseph P. Kennedy III (D-MA), a grandson of Robert F. Kennedy, argued that the President's first year in office had been anything but the one he had described earlier in the evening. He said that the President's policy agenda had presented Americans with "one false choice after another" and was driving people further apart rather than bringing them together. He largely avoided a discussion of legislative or regulatory policy options, but did signal support for infrastructure spending and suggested Democratic alignment with the President on trade policy, calling for "trade pacts that are fair [and] roads and bridges that won't rust away. . ." But beyond that there was little in common with what the President offered in his address.

As was evident in the fundamentally different priorities they advanced and the vision they articulated, the President and congressional Democrats appear to have little in common. But they share the need to resolve some major issues, which must be addressed soon for the sake of the country.

In the following pages, we outline what needs to be done in the next month or so, when a host of issues must be resolved, including funding the government beyond February 8 and raising the debt ceiling (or suspending enforcement of it) so that the full faith and credit of the United States is not put at risk. In addition, we take a deeper dive with our assessment of what Congress is likely to do now that the President has called on Congress to join him in producing a bipartisan infrastructure bill. But before turning to those subjects, we think it useful to review how and why the President and Republican leadership were able to come together to accomplish something that had eluded President Barack Obama and every other President since Ronald Reagan was in the White House.

Tax Reform: A One-Off Legislative Victory?

In previewing the potential for fundamental tax reform last year, we noted that, "[w]ith Republicans in control of Congress and the White House, the GOP is poised to move forward alone with comprehensive tax reform (i.e., legislation that restructures both the individual and business income tax provisions of the tax code). The Republican leadership has indicated it is prepared to use a Fiscal Year 2018 budget resolution with reconciliation instructions in order to move a bill through the Senate on a straight party-line vote if necessary. But given the limits of reconciliation, including likely application of the Byrd rule, the Senate may not be able to make permanent changes to the tax code that would increase the deficit beyond the 10-year budget window."

President Trump and the Republican Congress were successful in pursuing this approach because virtually every Republican agreed it had to be done. The effort was propelled in part by the high-profile failures that had preceded it. Prior to the launch of the tax reform process in September, Republicans had been largely unsuccessful in parlaying their majorities in the House and Senate and control of the White House into the passage of major new legislation. They achieved some significant victories: approving the nomination of Judge Neil M. Gorsuch to serve as a Justice on the Supreme Court, using the Congressional Review Act to overturn 15 final rules issued in the waning days of the Obama Administration, and overseeing robust economic growth and a steady increase in the stock market.

But notwithstanding their majorities, Republicans in Washington DC had been unable to achieve consensus about how to repeal and replace Obamacare, burning up months of precious legislative time that might otherwise have been used to advance other major priorities of the President and his party, including infrastructure spending.

Coming out of the August recess, the GOP was confronted with the prospect of going into the 2018 midterm-election year without a signature legislative accomplishment that would motivate its base of voters to show up at the polls and help preserve their current 23-seat House majority in a likely very challenging electoral environment. (According to a recent Bloomberg article, when the President's popularity is below 50%, his party has lost an average of 33 House seats in mid-term elections since 1970.) Faced with this political imperative – indeed, existential threat – they found a way to come together on a budget resolution that allowed them to use reconciliation to achieve tax reform. As they headed into the fall, Republicans had agreed on two fundamental points: (1) they needed to do something big by the end of the year and (2) tax reform would be that thing. The consensus held firm throughout the fall, allowing Republican leaders to move tax legislation steadily through the legislative process in both chambers and ultimately to craft a final bill that could clear the Senate without any Democratic support and that would be signed into law by President Trump shortly before the end of the year.

The successful tax overhaul effort has given President Trump and congressional Republicans an important legislative achievement as they enter the new year. The win has been bolstered by a steady drumbeat of announcements by US companies that they are giving bonuses to their workers as a result of the changes set in motion by the new law, and given the president and his party the ability to claim they have taken action to allow American families to keep more of what they earn and, importantly, to bring jobs home to the US. Politically, the accomplishment has also helped kill what just months ago had threatened to become an overwhelming narrative about the inability of the GOP-controlled Washington DC to pass important legislation.

But the tax reform victory may have been the high-water mark for the 115th Congress. The political imperative that enabled the GOP to unify around tax reform last fall has given way to a familiar intraparty debate about what the party's next priority should be. Meanwhile, Congress continues to struggle with the breakdown of the budget process, divisions over immigration and spending, the need to pass a massive disaster relief bill in the wake of last year's devastating hurricanes, rising deficits and debt, and the need to raise the nation's debt ceiling in March. These struggles, coupled with uncertainty over where President Trump really stands on these issues, will severely test GOP unity in the coming months, potentially making it difficult for the party to enact significant legislation, such as the infrastructure initiative the President has vowed to make a priority. Moreover, the President could find himself at continuing odds with congressional Republicans on a host of trade issues, including NAFTA, Trade Promotion Authority (which expires July 1 if not renewed by April 1) and multiple ongoing section 232 investigations (steel, aluminum and uranium).

Democratic leaders, for their part, will be under constant pressure from their progressive base to deny President Trump and the GOP votes for anything that might assist them in governing. They may struggle, as they did in the recent government shutdown, to balance this pressure against the desires of Democrats in competitive states and districts who need to be seen as willing to work in a bipartisan fashion. Which brings us to a month of looming deadlines.

Funding the Government, Dealing With the Debt Ceiling, Providing Hurricane-Recovery Relief, and Addressing DACA and the Wall

Congress enters the month of February struggling to reach agreement on two matters that have vexed the legislature since last fall: immigration and spending levels for a fiscal year that began four months ago.

On immigration, President Trump is asking Congress to provide billions in new spending for border security, including the construction of a wall on the US-Mexico border, and to adopt other limitations on immigration (including so-called "chain migration"); while Democrats are demanding legislation to extend and authorize the Deferred Action for Childhood Arrivals (DACA) program and to guarantee other rights to undocumented immigrants.

On spending, the two parties have been attempting since last fall to strike an agreement to lift the budget caps imposed by the 2011 Budget Control Act on defense and non-defense spending. Once agreement is reached on these caps, appropriators will be able to write an omnibus spending bill to the newly established spending levels that will fund the federal government for the remainder of the fiscal year.

An additional "must-pass" spending matter from 2017 lingers as well, in the form of a disaster relief package to assist our fellow citizens in the US Virgin Islands and Puerto Rico and individuals in Florida and Texas who lost so much in last year's hurricanes. The House passed an $81 billion supplemental appropriations bill shortly before Christmas, but the Senate has not yet taken the bill up, in large part because congressional Democrats have insisted that hurricane relief be part of a "global" deal that includes solutions on immigration and appropriations.

By early March, yet another major challenge will likely be added to the mix of "must-pass" items when the Trump Administration notifies Congress that the debt ceiling has been reached and must again be raised to prevent a default on the nation's debt payments. In testimony this week, the Secretary of the Treasury indicated that that day is fast approaching, but without specifying precisely when it will arrive.

In order to clear the Senate, bipartisan agreements are needed to address all these matters, which require 60 votes, since Democrats have enough votes to block action on any of them. Hence, the ongoing discussions about a potential global agreement to resolve everything.

POLITICO reports that congressional negotiators are discussing a budget deal that would not just lift the current spending caps on defense and non-defense spending, but obliterate them. "Congress' caps-busting spending deal could easily cost more than $400 billion over just two years, according to the gurus at the Committee for a Responsible Federal Budget. The biggest piece of that compromise, of course, involves lifting limits for defense and nondefense programs. The GOP's latest offer to Democrats would exceed $250 billion over two years – far more than the $175 billion estimate of the party's initial proposal."

If a budget caps deal is reached soon, Congress will then need three to four weeks to produce an omnibus spending bill written to the newly set spending levels dictated by the agreement. This omnibus legislation would likely go to the floor in mid- to late-March, and could carry the debt limit increase, as well as the final version of the disaster relief bill, if not taken up sooner as a stand-alone measure or moved along with the continuing resolution (CR) that will be needed to keep the federal government operating past February 8, when appropriations are next set to lapse.

The DACA program, established by executive order by President Obama, will expire in March. With the program now being litigated in the courts, the program's fate may not need to be determined by then. But with the President continuing to press Congress for a solution, as well as funding for his border wall and other border security measures, immigration will remain critical to the ongoing negotiations over government spending.

Resolving this tangle of thorny, vital issues will undoubtedly require tough choices and deft navigation by GOP leaders. It was not long ago that conservative legislators in Congress were threatening to mutiny against the Republican congressional leadership out of fear that the leadership might agree to a bipartisan immigration deal that included a path to citizenship for undocumented immigrations, or an increase in the debt ceiling without massive spending cuts, or large increases in deficit spending. Congress is about to be asked by President Trump to deliver on all these things.

To date, conservatives in the House Freedom Caucus and elsewhere have been willing to give President Trump much more running room on issues such as the deficit, the debt ceiling and immigration than they gave President Obama or GOP leaders in the 113th or 114th Congresses. But the weeks ahead will likely force them to choose between their allegiance to President Trump and their previously stated principles like never before. Our expectation is that congressional conservatives will balk at any deals that emerge on these issues, forcing Republican leaders to depend on Democrats to help pass in both chambers of Congress. A key question, for House Speaker Paul Ryan, in particular, will be whether these agreements can muster enough support to pass the House with a "majority of the majority" voting in favor (the so-called "Hastert Rule") or whether we will see the emergence of the "Trump Rule" (if the President wants something, enough Republicans will be rallied to support it).

As in the successful effort to move tax reform, we expect Speaker Ryan and Senate Majority Leader Mitch McConnell (R-KY) to find a way to get things done. But they are going to need President Trump's help and they are going to need to craft a bill or bills that Senate Minority Leader Chuck Schumer (D-NY) will support.

The Year an Infrastructure Spending Bill Finally Gets Signed Into Law?

Last year, we noted that the $1 trillion infrastructure proposal the President touted during the campaign could provide significant and long-awaited opportunities for private investment in major, high-cost, revenue-supported projects. But the White House never addressed how to fund the routine capital improvements needed to maintain and upgrade our transportation and infrastructure systems, nor did it advance a sustainable, long-term source of funding to augment or replace declining Highway Trust Fund revenues. Will this be the year of action?

In the run up to the President's address last night, Senate Minority Leader Chuck Schumer made the case again for Democrats to work with the President and congressional Republicans, but in doing so, emphasized the need for direct federal spending rather than relying on "capital from private companies or states and localities in lieu of real investment." As he put it, "Democrats want to work with President Trump to rebuild America's infrastructure . . . But we shouldn't ask the middle class to pay $1 trillion in new tolls and local tax increases to get there."

Now that the President has spoken, the challenge of revitalizing and updating the nation's transportation and infrastructure will be a focus for the Trump Administration and Congress in the coming months. In his State of the Union address last night, President Trump called on Congress to produce a bill "that generates at least $1.5 trillion for the new infrastructure investment our country so desperately needs." It is important to note that the President did not pledge $1.5 trillion in federal funding, but instead called for legislation that generates a $1.5 trillion investment. The President said every federal dollar "should be leveraged by partnering with state and local governments and, where appropriate, tapping into private sector investment."

The White House is expected to release additional details about its infrastructure proposal in the coming weeks, which will provide a starting point for Congress to begin developing infrastructure legislation. Last week, a six-page memorandum outlining the Trump Administration's infrastructure proposal was obtained by the press. The White House has not confirmed the authenticity of the document, but it reflects the broad policy positions and main program proposals that the Administration has been publicly discussing for months.

Recently, a senior White House advisor on infrastructure, DJ Gribbin, said the President's infrastructure proposal will not include new funding, but instead will provide $200 billion derived from redirecting funds away from existing programs, in line with the President's FY 2018 budget proposal. Mr. Gribbin also noted that transportation formula programs would remain unchanged. In his budget, the President proposed significant reductions to the transit Capital Investment Grant program, Amtrak, and the multi-modal Transportation Infrastructure Generating Economic Recovery (TIGER) grant program, among other cuts. Many transportation stakeholders have stated that this approach would create a situation in which stakeholders would be fighting over existing limited transportation funds and would not directly address the nation's need for increased infrastructure investment. Democrats have opposed this approach, and Senate Minority Leader Chuck Schumer (D-NY) recently said that only direct federal investment "can properly address the scale of the challenge we face." The spending cuts proposed in President Trump's budget were rejected by congressional appropriators in their FY 2018 Transportation, Housing and Urban Development (THUD) appropriations bills.

The memorandum outlines three new federal infrastructure funding programs: (1) Infrastructure Incentives Initiative; (2) Transformative Projects Program; and (3) Rural Infrastructure Program. A wide variety of infrastructure projects would be eligible for funding under the proposal, including projects relating to surface transportation, airports, passenger rail, commercial space, maritime and inland waterway ports, flood control, water supply, hydropower, water resources, drinking water facilities, storm water facilities, Brownfield or Superfund sites, and telecommunications and broadband infrastructure.

To incentivize state and local governments to raise their own revenues – or attract private revenues – the Infrastructure Incentives Initiative would provide federal discretionary grants for projects with significant contributions of non-federal funds from public and private project sources. Where federal highway and transit formula programs now fund up to 80% of project costs, federal grants under this new incentive initiative would be limited to 20% of project costs. However, states and local governments would earn some credit for non-federal revenues raised in the previous three years. A White House fact sheet released last night indicates that half of the new federal infrastructure funds would go toward this initiative.

To fund higher-risk projects that may be unable to secure financing through the private sector, the Transformative Projects Program would provide discretionary grants focused on innovative and transformative infrastructure projects that have more risk but also offer larger potential benefits. Understanding that many rural infrastructure projects are not able to attract private financing, the Rural Infrastructure Program would provide federal funding directly to states through block grants. Notably, these grants would not be subject to federal infrastructure requirements. According to the White House fact sheet, a quarter of the federal funds would be dedicated to the rural program.

Additionally, the proposal would significantly increase funding for several existing federal credit assistance programs, including the Transportation Infrastructure Finance and Innovation Act (TIFIA), Railroad Rehabilitation and Improvement Financing (RRIF) and Water Infrastructure Finance and Innovation Act (WIFIA) programs. The proposal would also broaden TIFIA eligibility to include airports and ports.

To enable greater non-federal infrastructure funding, the proposal would allow states greater flexibility to toll interstates and require value-capture financing for large transit projects under the Capital Investment Grant program. Value-capture financing, such as a local property tax, enables transit project sponsors to more directly share in the benefits they bring to the communities they serve. The proposal would remove the application of federal requirements for projects with a *de minimis* federal share and raise the cost threshold for major project requirements to $1 billion.

President Trump's infrastructure proposal also seeks to advance infrastructure projects more quickly and lower project costs by streamlining federal project delivery requirements. During his speech, the President said any infrastructure legislation "must also streamline the permitting and approval process, getting it down to no more than two years, and perhaps even one." The White House fact sheet cites a 2014 Government Accountability Office report noting that the median time to complete an environmental review process for complex highway projects is at least seven years.

The key question that remains unanswered is how to pay for an infrastructure package. Late last year, President Trump's chief economic advisor, Gary Cohn, told a bipartisan group of House lawmakers that they would have an opportunity to consider increasing the federal fuel tax to pay for an infrastructure package. At the time, House Transportation and Infrastructure (T&I) Committee Chairman Bill Shuster (R-PA) said there were not enough votes in the House to support a fuel tax increase. However, this month, Chairman Shuster indicated support for raising the gas tax, while Senate Environment and Public Works (EPW) Committee Chairman John Barrasso (R-WY) voiced his opposition. Senate Commerce, Science and Transportation (Commerce) Committee Chairman John Thune (R-SD) said he is open to raising the gas tax, but that it would take leadership from the White House. Recently, stakeholder groups such as the Chamber of Commerce have advocated for a significant increase in the federal gas tax, potentially providing political cover for Congress to raise the gas tax to fund infrastructure investment.

Infrastructure investment may provide an opportunity for bipartisan legislation in an increasingly divided Congress; however, Republicans and Democrats appear to be far from consensus on what infrastructure legislation should include. Several Democrats have called for increased direct federal investment, stating that simply leveraging private sector funding or incentivizing increased state and local spending will not be enough to solve our infrastructure needs. Additionally, Democrats will likely oppose rolling back environmental protections in the name of project streamlining.

The main congressional committees with jurisdiction over infrastructure have held hearings over the past year examining the nation's infrastructure needs in anticipation of considering infrastructure legislation. This year, Congress is expected consider a Water Resources Development Act (WRDA) reauthorization. Additionally, while the FAST Act does not need to be reauthorized until 2020, infrastructure legislation would provide an opportunity for an early FAST Act reauthorization. Perhaps Congress will combine these reauthorizations with a broad infrastructure package this year.

The House Rules Committee has also recently held hearings to examine whether the House should eliminate its ban on earmarks. In particular, Members of both parties in Congress have called for allowing earmarks in infrastructure legislation. The President also recently suggested that Congress should consider eliminating the ban on earmarks with "better controls" to increase support for bipartisan legislation. Reestablishing earmarks would likely facilitate building broad bipartisan support for infrastructure legislation; however, additional revenue would be needed to fund those earmarks.

The current short-term extension of FAA programs expires March 31, 2018, and Congress will have to pass either a long-term reauthorization or another extension. Congress could also include FAA reauthorization in any infrastructure legislation. The current Senate and House proposals are vastly different, with the Senate's FAA Reauthorization Act of 2017 (S. 1405) generally maintaining the status quo with various policy changes and the House's 21st Century Aviation Innovation, Reform, and Reauthorization Act (21st Century AIRR Act) (H.R. 2997) providing comprehensive reform to the air traffic control (ATC) system.

The 21st Century AIRR Act would substantially reform FAA, removing the ATC system from FAA and creating an independent, not-for-profit corporation, while FAA would retain responsibility for safety regulation. The ATC reform proposal has faced significant opposition from Democrats and House and Senate appropriators. The House T&I Committee approved the 21st Century AIRR Act in June 2017 on a largely party-line vote. However, the House has not considered the bill on the floor, as Chairman Shuster continues to build support for the legislation.

The Senate FAA Reauthorization Act is less controversial, but includes a provision to relax co-pilot training hour requirements that Senate Commerce Committee Ranking Member Bill Nelson (D-FL) has said that Democrats will not support. Recently, Chairman Thune has indicated that he is open to removing the provision so the bill can be considered on the Floor before the current extension expires in March.

While there is significant bipartisan support for infrastructure investment, it is unclear whether Republicans and Democrats can agree on how to pay for an infrastructure package. Without additional funding, it will be difficult to gain the support of Democrats or use earmarks to increase bipartisan support.

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