In light of the recent election, we thought it might be helpful to provide you with some observations on the national elections, the outlook for legislation on Capitol Hill in the post-election session of Congress and efforts to avoid the so-called “Fiscal Cliff.”

Election Overview
It is clear that the elections which determined the fate of President Obama and the Democratic majority in the U.S. Senate came down to the wire and were too close to call. The Presidential election was determined in Ohio, Virginia and a handful of other states. While the playing field seemed to favor the Republicans when it came to Senate races across the country, the Democrats made a strong move in the months before the election to keep control of the body (even if by just one vote). It seemed probable that the House Republicans would retain their majority, if by a smaller margin than enjoyed in this Congress. Needless to say, the results of these various elections, particularly for President, determined the next steps in a post-election “lame duck” session of Congress. We continue to hold out some hope that Congressional leaders and President Obama can reach the compromises necessary to keep the country from jumping off the “fiscal cliff” while augmenting the fairly poor legislative record of accomplishment to date by this Congress.

Productivity of the 112th Congress
This has been an exceptional two years here in the Nation’s capital, at least when it comes to the overall legislative record of the 112th Congress. It has been a common theme of many political commentators to describe the lack of productivity on the part of this Congress, which opened for business on January 5, 2011 and will close down sometime before the end of the year. To date, 195 bills and joint resolutions have been enacted into law during the 112th Congress. To provide some insight into what measures have made it through both the House and Senate to be signed into law by the President, consider the following: 30 of these bills named postal facilities across the country; another 8 designated the names of U.S. Courthouses; 20 bills dealt with public lands issues; and, another 20 simply extended current laws by a short period of time.

By comparison, the next least productive Congress dating back to the 96th (1979-1980, which, as an aside, enacted 735 measures into law) was the 104th (1995-1996, when the House Republicans first came to power under Speaker Newt Gingrich) which enacted 337 measures that were signed into law. The numbers for each Congress since 2000 are as follows: 107th – 384; 108th – 528; 109th – 483; 110th – 460; 111th – 385. The infamous “Do Nothing” 80th Congress which President Harry Truman ran against in 1948 enacted 908 laws.

Unfortunately, this lack of cooperation between the parties and the House and Senate have basically stalled important reforms across broad sections of the U.S. economy, blocked extension or creation of important tax policies, limited directives to and oversight over various federal
agencies and programs, and essentially limited the number of potential funding opportunities available for our clients. The list of unfinished business facing this Congress in the “lame duck” session, set to begin November 13th, is large and diverse. It covers everything from the defense authorization bill, the expired five year farm bill, and cyber security legislation to online sales taxes and reauthorization of the Water Resources Development Act. Most importantly, this breakdown in political comity has threatened attempts to overturn the previously scheduled budget sequestration cuts.

**A Sequestration Primer**

The Budget Control Act of 2011, signed into law as a result of last year’s debt crisis, mandated $2.1 trillion in reductions in federal spending over a ten year period. An initial $900 billion was built into the FY13-22 budget caps and the remaining $1.2 trillion was left to Congress to decide how to implement. The Act created a Joint Select Committee on Deficit Reduction to come up with the proposed reductions and afforded the Committee’s bill expedited consideration by the House and Senate (the bill could not be filibustered in the Senate). The Committee failed to produce a bill, which has triggered a sequester enforcement mechanism. The initial sequester will become effective on January 2, 2013 without further action by Congress and the President.

Beginning on January 2, the sequester is scheduled to reduce federal expenditures for nine consecutive fiscal years such that the cuts, including associated debt service savings, total $1.2 trillion. Of that amount, $216 billion will come from debt service savings. The remaining $984 billion will come from cuts divided evenly among the nine relevant years, meaning that $109 billion will be sequestered each year. The annual cuts are, in turn, split evenly between defense and non-defense spending – an approximate cut of $55 billion to each.

<table>
<thead>
<tr>
<th>Calculation</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Joint Committee savings target</td>
<td>$1,200 B</td>
</tr>
<tr>
<td>Deduct debt service savings (18%)</td>
<td>-$216 B</td>
</tr>
<tr>
<td>Net programmatic reductions</td>
<td>$984 B</td>
</tr>
<tr>
<td>Divide by 9 to calculate annual reduction</td>
<td>$109.333 B</td>
</tr>
<tr>
<td>Split 50/50 between defense and nondefense functions</td>
<td>$54.667 B annual reduction</td>
</tr>
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The President has said that he will exercise his authority granted in the Act to shield military personnel pay from the reduction, which will result in a 9.4% reduction in defense discretionary funding and an 8.2% reduction in non-exempt nondefense discretionary funding. The sequestration would also impose cuts of 2.0% to Medicare, 7.6% to other non-exempt nondefense mandatory programs, and 10.0% to non-exempt defense mandatory programs.

While some areas of the budget are exempt from sequestration, such as war funding and the Children’s Health Insurance Program, these cuts are potentially devastating for other areas of the federal budget, such as the technology research and development accounts at the Department of Defense and the Department of Energy. For example, the Navy’s Fiscal Year 2013 RDT&E account is $18.899 billion, which would be reduced by 9.4% ($1.777 billion). The Navy RDT&E reduction would likely be applied across the board on all program accounts.
“The Fiscal Cliff”
Unfortunately, the sequestration budget cuts are only one portion of the so-called “fiscal cliff.” We also face a significant number of tax, budget and entitlement issues which must be addressed before the end of the year. Congress must deal with expiration of the Bush-era tax cuts on individual tax rates, capital gains and dividends. Also on tap is a hodgepodge of expired or expiring business tax breaks, such as the renewable energy production tax credit, and the likelihood that the U.S. will once again hit its debt ceiling, provoking a major fight over the conditions to increase the federal borrowing limit. The Congressional Budget Office has said the American economy would likely contract in the first half of 2013 if across-the-board spending cuts under sequester go forward while all the tax cuts due to expire are allowed to fall. In recent weeks, we have seen Members discussing proposals to avoid a legislative logjam at the end of the year. However, given the history of this Congress and its leadership to date, we should expect a significant amount of brinksmanship on a host of matters before this Congress comes to an eventual conclusion sometime in late December.

Current Status of the Fiscal Year 2013 Appropriations Measures
Another challenge this year has been the lack of action on the FY 2013 Appropriations measures. On September 28th, the President signed into law a continuing resolution (CR) to fund the federal government through March 27th, 2013. This stopgap measure avoided a government shutdown on October 1st (the first day of Fiscal Year 2013) and laid out a budget plan for the first half of FY 2013. The measure will increase the federal budget of FY 2012 by approximately 0.6 percent for FY 2013, resulting in a total discretionary budget of approximately $1.047 trillion. Unfortunately, no new start initiatives are permitted under the CR, although federal agencies have some discretion under a CR to make these determinations (something this Administration has not been shy to do). If the President is reelected, Congress is likely to try to pass a separate FY 2013 defense appropriations bill in the “lame duck” session. If Governor Romney wins, Congress will likely wait until returning in January or February to deal with the FY 2013 appropriations.

Government agencies are facing difficult decisions on how to allocate their funding. Do they take the gamble that new legislation will be passed and spend at the levels laid out in the continuing resolution, or do they rein in spending in order to prepare for the possibility of sequestration?

Conclusion
While we have aggressively worked to maneuver various funding and policy proposals through the least productive Congress for at least 40 years, there is still time before the end of the year for positive action on a host of issues. The elections will play an important role in determining the potential legislative accomplishments of the upcoming “lame duck” session of Congress. We maintain some hope that Congressional leaders and President Obama (whether he is reelected or not) will determine it is in the country’s best interest, along with their own political interests, to reach some resolution on dealing with the “fiscal cliff” and a host of other policy and tax matters before the end of the year. At this point it seems likely that the Fiscal Year 2013 Appropriations bills will not be finally enacted until a month or two into the new Congress early next year (or we could end up with a full year Continuing Resolution – not a desired outcome).

We will be back in touch with you in mid-November with a post-election update. Hopefully we will be able to provide additional clarity with regard to the various items discussed in this report.