

ARNOLD & PORTER LLP

ADVISORY

November 2010

Republican Gains and a Return to Divided Government

The Election

Riding a wave of voter discontent with the lagging economy, high unemployment, the Obama Administration, and congressional leadership, Republicans made historic gains in the US House of Representatives and nearly retook control of the US Senate. Fueled by an insurgent Tea Party political movement that made significant inroads with disaffected independent voters across the country, the GOP won a net gain of over 60 seats in the House, providing well over the 39 seats they needed to wrest control of the chamber from Democrats. Republicans came within four seats of taking control of the Senate, winning the seats of six Democrats that were either defeated or retired this cycle.

Republicans' biggest gains in the House came from districts in the South and Midwest where voters supported Republican Presidential nominee John McCain in 2008 but elected a Democratic representative attributed mainly to the momentum created by Obama's Presidential campaign. Gains for Republicans also came in suburban districts and rural districts across the country proving that the wave of discontent ran deeper than many, including Republicans, had anticipated. The majority of Republican gains came from the group of 55 Democrats first elected within the last four years claiming 14 seats from the Democratic freshman class of 2006 and 21 in races against Democrats first elected in 2008. Republicans also defeated veteran Democratic lawmakers including Budget Chair John Spratt of South Carolina, Armed Services Chair Ike Skelton of Missouri, Transportation and Infrastructure Chair Jim Oberstar of Minnesota, and Communications and Technology Subcommittee Chair Rick Boucher of Virginia. The fiscally conservative Democratic Blue Dog Coalition was particularly hard hit, losing over half of its 54 members.

In the Senate, Democrats retained seats in competitive races including California, Colorado, Connecticut, Nevada, and West Virginia to prevent Republicans from sweeping both chambers. Democrats were able to win one of the most closely watched races in the country, returning Harry Reid to his position as Majority Leader of the Senate, but lost seats previously held by Democrats in Arkansas, Indiana, North Dakota, Pennsylvania, Wisconsin, and President Obama's home state of Illinois.

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Exit polls indicated that the majority of voters were overwhelmingly concerned with the direction of the economy. Most voters disapproved of President Obama's performance and, to an even higher degree, of the agenda enacted by Congress. Majorities of voters had unfavorable opinions of both Democrats and Republicans.

Most Important Issue to Voters

2010 Election Cycle¹

- Economic Conditions
- Health Care
- The Size and Power of the Federal Government
- The Situation in Afghanistan
- Illegal Immigration

2008 Election Cycle²

- The Economy
- The Federal Budget Deficit
- Terrorism
- Energy (including gas prices)
- The Situation in Iraq
- Health Care

Voter Opinion on the Direction of the Nation³

	Nov-10	Jun-10	Mar-10	Oct-08	Oct-06	Oct-04
Right Track	31%	29%	33%	12%	31%	39%
Wrong Track	60%	62%	59%	78%	54%	49%

Voters Likely to Vote Democrat/Republican Echoes 1994⁴

	Nov-10	Jun-10	Nov-06	Nov-02	Nov-98	Nov-94
Democrat	45%	44%	51%	50%	49%	45%
Republican	49%	48%	45%	49%	46%	48%

1. Gallup, Oct. 21-24, 2010: <http://www.gallup.com/poll/144029/economy-top-issue-voters-size-gov-may-pivotal.aspx>.

2. Gallup, Oct. 23-26, 2008: <http://www.gallup.com/poll/111586/Economy-Reigns-Supreme-Voters.aspx>.

3. http://msnbcmedia.msn.com/i/MSNBC/Sections/NEWS/A_Politics/___Politics_Today_Stories_Teases/101686Late-OctNBC-WSJFilledin.pdf.

4. http://www.washingtonpost.com/wp-srv/politics/polls/postpoll_10302010.html.

Along with returning incumbent Republicans Jim DeMint (SC), and Tom Coburn (OK), who won their races handily, the loosely affiliated Tea Party movement will count at least six new members in the Senate: Rand Paul (KY), Ron Johnson (WI), Pat Toomey (PA), Marco Rubio (FL), Kelly Ayotte (NH) and Mike Lee (UT). In a move to keep these new senators coalesced around the Tea Party agenda of fiscal responsibility, smaller government and less government control, Sen. DeMint sent out a letter warning Tea Party Senators not to be swayed by attempts to recruit them into the more mainstream Republican fold.

In an ironic twist, despite the energy and victories the Tea Party brought to the Republican party and its candidates, weak Tea Party Senate candidates in Delaware, Nevada, and Colorado lost races that would have forced the Senate into a 50-50 split between the parties. Regardless, this new class of Tea Party members will have considerable influence in the Senate and House and has immediately empowered members such as Senators Jim DeMint (SC) and Tom Coburn (OK) and Representative Michele Bachmann (MN), who is running for House Conference Chair. Additionally, Tea Party wins in 2010 will likely embolden primary challenges, particularly if their agenda is not considered or approved. Republican Senate leaders like Mitch McConnell (KY) and Orrin Hatch (UT), may find themselves running in primary challenges in the states where Tea Party candidates won handily in the primary and general elections.

Additionally, Senate Democratic members will be facing more reelection bids than the Republicans in 2012 and many could easily support an agenda that angles away from the White House and their progressive colleagues. Senate Democrats like Ben Nelson of Nebraska, a moderate, may regularly vote against the Democratic agenda and stay away from the White House if he sees little that positively impacts his electorate.

Change in Leadership

The Republican takeover of the House returns the power and agenda to the GOP where they will assume control of the speakership, legislative committees, have subpoena power, the ability to call hearings, and set the floor agenda for votes and amendments. Representative John Boehner (OH) is set to become Speaker of the House, with Eric Cantor (VA) likely to assume the second-in-command majority leader position for Republicans.

The change in leadership will see new chairs for each of the House's committees. Expected chairs include:

- Fred Upton (MI), Energy and Commerce
- Dave Camp (MI), Ways and Means
- Paul Ryan (WI), Budget
- Buck McKeon (CA), Armed Services
- John Mica (FL), Transportation & Infrastructure
- John Kline (MN), Education and Labor
- Darrell Issa (CA), Oversight and Government Reform
- Lamar Smith (TX), Judiciary
- Ilena Ros-Lehtinen (FL), Foreign Affairs
- Peter King (NY), Homeland Security
- Frank Lucas (OK), Agriculture
- David Drier (CA), Rules

A battle between Hal Rogers (KY) and Jerry Lewis (CA) has emerged for Chair of the Appropriations Committee, and Spencer Bachus (AL) and Ed Royce (CA) are running for Chair of the Financial Services Committee.

In the Senate, retiring Senator Chris Dodd left open the Chair of the Financial Services Committee, which will be assumed by Senator Tim Johnson (SD). The loss of Senator Blanche Lincoln (AR) creates an opening for the Chair of the Agriculture committee, which Senator Stabenow (MI) is slated to fill although, with a tough reelection expected, Senate leadership could give this chairmanship to Senator Ben Nelson. With the win in Nevada, Democrats in the Senate are not likely to change majority leadership from Senator Reid.

On November 5, 2010, Speaker Pelosi announced her plans to run for Minority Leader in 112th Congress. She may receive a challenge from Blue Dog coalition members or others from the more moderate wing of the party. For example, Representative Jim Matheson (UT) recently called for Pelosi to step aside and Representative Heath Schuler (NC) indicated before the election his intention to challenge Pelosi if she decides to run.

Legislative Activity

With Republican control of the House and Democratic control of the Senate and the Presidential veto, consensus, compromise, and gridlock will define the legislative session, with the latter likely the most dominant force. Republicans in the House will have a significant opportunity to set the legislative agenda for the next two years and the Obama Administration will likely significantly pare back its expectations for legislative accomplishments in the next Congress.

Legislative activity is expected in the following areas:

Tax Policy. Both parties are likely to address the tax cuts set to expire at the end of 2010 with Republicans seeking a full extension of all of the tax cuts and Democrats seeking to extend the tax cuts to only those making less than US\$250,000 per year. Both sides have signaled they are willing to compromise and the election results are likely to buoy Republican efforts to extend all tax cuts for at least a short period of time.

Health Care Reform. Republicans have promised immediate votes on a full repeal of the Health Care Reform law but

Democrats in the Senate are likely to block any wholesale repeal. And, even if a law passed, the President's veto would likely not be overturned. Rather, Republicans are likely to target specific provisions of the law, such as the individual and employer mandates for repeal or modification. They may use the appropriations process as a vehicle for certain cuts. However, the Republicans will likely proceed cautiously with any attempts to undermine the many popular programs within Health Care Reform—fully understanding that they did not win the majority due to Health Care but to concerns with the economy. Taking up significant time on numerous attempts to repeal Health Care Reform could signal a message to constituents that they were not listening to voter discontent.

Energy and Climate Change. President Obama has already signaled that a comprehensive cap and trade bill will not be successful, but there may be consensus on an energy bill that includes natural gas exploration, nuclear energy development and renewable energy provisions. In addition, the US Environmental Protection Agency will continue its efforts to regulate carbon emissions, which may prompt legislative action to curtail their authority to do so.

Deficit Reduction. The report of the National Commission on Fiscal Responsibility is due in December 2010 and will likely include recommendations on entitlement reform, discretionary spending and tax policy. Republicans ran on a campaign message of fiscal discipline and have pledged to cut spending immediately.

Financial Services. Republicans do not appear likely to seek a full repeal of the financial regulatory reform legislation but will closely monitor the formation of the newly established Bureau of Consumer Financial Protection and possibly seek to move funding for the agency into the appropriations process instead of through existing revenue from the Federal Reserve (not subject to congressional approval). President Obama is expected to present a proposal for overhaul of Fannie Mae and Freddie Mac to Congress in the early part of 2011.

Investigations

Given the difficulties both parties will have in passing legislation over the next two years, the change in the gavels on House committees will drive much of the activity in Congress. Republicans will have power to hold hearings and issue subpoenas for testimony and documents. Prospective committee chairs have already given some indication of their oversight priorities.

Darrell Issa, incoming Chairman of the House Oversight and Government Reform Committee, has indicated he will focus investigations on stimulus spending, federal emergency response capabilities, the independence of Inspector Generals, the Securities and Exchange Commission, Countrywide Financial Corporation, food safety regulations, Fannie Mae and Freddie Mac, oversight of the Minerals Management Service, and healthcare fraud. Oversight investigations will generally focus on the executive branch but may involve companies in the financial, healthcare, and energy sectors, among others.

Fred Upton, the likely chair of the Energy and Commerce Committee will focus investigations on Health Care Reform implementation. Dave Camp, presumptive chair of the Ways and Means Committee will also launch investigations of the Center for Medicare and Medicaid Services.

The Administration—Moving Forward

In the face of almost inevitable legislative gridlock, we will likely see an emboldened Republican party moving further to the right in response to Tea Party primary successes. And with aggressive congressional investigations, the Obama Administration will be faced with a choice between compromise and collaboration or advancing an agenda that will appeal to the Democratic base and independent voters but that has little chance of success.

Recognizing the significant ground lost with independent voters, the Obama Administration is likely to focus on issues that matter to independents frustrated with Washington, primarily the economy. The first sign of this was announced immediately following the election when the Federal

Reserve announced the intent to purchase US\$600 billion in US Department of the Treasury securities in the form of bonds to assist in lowering interest rates and boosting the housing market. Additionally, the Administration is likely to work with Congress to push forward the Surface Transportation Authorization Act (STAA), which will infuse significant funding into surface transportation projects and create 48,000 new jobs per every US\$1 billion spent.

The Administration will also likely focus on transparency and reform and find areas of consensus with the new Republican majority in the House and be active on matters that do not require congressional approval, including rulemaking and implementation of the Health Care Reform and financial regulatory reform legislation passed last Congress.

Voters sent a message to the Obama Administration to focus on the economy and the deficit. The President's ability to effectively address those issues without the help of a Democratic controlled House and a slim majority in the Senate will be difficult but paramount to his chances of reelection in 2012. While Senator McConnell and the Republican party will be doing everything they can to stop any momentum the White House creates, they will ultimately need to work with the Administration on the economy or risk continuing to be labeled as the party of "no" and obstructionism.

We hope that you have found this advisory useful. If you have any questions, please contact your Arnold & Porter attorney or:

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