Alert

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COZEN O'CONNOR

Cozen Currents: Democrats May Be Down But Are Not Out

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The Cozen Lens

- In politics, you're only as good as your last poll. But politicians polling poorly have a remarkable track record of getting meaningful policy accomplished (just ask the poorest polling senator, Mitch McConnell). Despite the dread of Democrats and glee of Republicans over President Biden's polling slump, the policy agenda is full of potential this summer.
- Climbing prices at the gas pump is not the only energy crisis President Biden is likely to face this summer and, unfortunately, he is left with few, if any, viable policy options to address any of them, at least in the short term.
- A new bill from Senators Cynthia Lummis (R-WY) and Kirsten Gillibrand (D-NY) has returned discussions of a federal legislative framework for digital assets to the forefront. While the bill is not expected to pass in the current Congress, it provides a starting point for future legislative discussions around digital assets.

Joe's Hot Summer

Democrats Freak Out About Biden: The stories are flying from DC of a Democratic Party searching for an elusive alternative to President Joe Biden as he struggles.

- Biden has reached his polling nadir, below 40 percent, adding fuel to the fire of all the hesitancies about him. He's too old, he's not inspiring, voters (even Democrats) don't want him to run for reelection.
- 2022 is not 2024. There was plenty of chatter among the political class of President Trump not running for reelection. Even some were saying President Obama shouldn't go for a second term. Just as common as the president's party facing a midterm "shellacking" is the fears of an election shellacking two years later. But Obama won reelection and Trump almost won his reelection – in the middle of a pandemic.
- There's no clear alternative to Biden. Vice President Harris is the frontrunner if Biden doesn't run, but she has almost as low favorability ratings as Biden. Many of the other names being floated include 2020 also-rans like Transportation Secretary Pete Buttigieg and Senators Amy Klobuchar (D-MN) and Elizabeth Warren (D-MA). But they didn't win in 2020 for a reason.

The Biden Legislative Summer: From the partisan to the bipartisan, there's no signs of a summer slump in legislative action.

- The rigmarole of reconciliation continues, with a chance of a deal reached by the August recess. Senate Majority Leader Chuck Schumer (D-NY) and most other Democrats see even a pared-back reconciliation bill as a shot in the arm for the campaign season and an important legacy milestone. But neither Senator Joe Manchin (D-WV) nor Kyrsten Sinema (D-AZ) has an election this year and are more concerned about a deal that works for them.
- The conference of the Bipartisan Innovation Act continues, with a chance of a deal reached by the August recess. Leadership is seeking a conclusion to negotiations of the China competitiveness package by the July 4th recess. But several issues remain outstanding, with Republicans looking to drive a hard bargain or wait until they could have a majority in the next Congress to draft a better deal.
- There are several other irons in the legislative fire. Senate negotiators reached a deal on gun control legislation. Bipartisan behavioral health and retirement security legislation is working its way through Congress. While not necessarily likely to pass this year, bipartisan data privacy and antitrust legislation are garnering attention too.
- Getting some items done may downgrade a red tsunami to a red wave as it gives

Democrats something to tout on the campaign trail. It also pads Biden's CV for 2024.

The Biden Regulatory and Executive Summer: While still respecting the institutions of power, the Biden administration is not afraid to push the envelope for near and long-term regulatory and executive victories.

- The Biden administration is looking to balance the competing Democratic coalitions to take action for the here and now. Executive action on partially forgiving student loan debt is expected in July or August. It's an attempt to boost Democratic enthusiasm in the run-up to the midterms but not go too far to cause a political or inflation backlash.
- Additionally, the administration is balancing labor and domestic production with clean energy and inflation. The White House announced a two-year pause on any new solar tariffs and is considering removing some tariffs on Chinese goods to help ease inflation pressures.
- The Biden administration isn't shying away from embarking on long-term regulatory overhauls. In the past week, Securities and Exchange Commission (SEC) Chair Gary Gensler announced plans for the biggest change to how equities are traded in nearly two decades. The Food and Drug Administration (FDA) is reportedly planning to soon introduce a proposed rule that would lower the level of nicotine in cigarettes to non-addictive levels, the biggest anti-smoking action since the 1990s. Successful implementation by the SEC and FDA face a long road ahead, but the administration is gearing up for a fight.

Biden's Expanding Energy Crises

The Leader of the Free World’s Limitations: President Biden is bearing the political burden of being in office during multiple energy crises with few tools at his disposal to address them.

- Biden is staring down the November midterms and hoping that his stagnant approval rating that recently dipped below 40 percent will rise in the intervening 146 days. This would likely necessitate the ticking down of another metric: the cost of gas. If Biden could wave away the record high cost of fuel – gas reached $5 nationally last week – to save his political skin, he would do so. The same goes for the forecasted increase in power shortages across swaths of the West, Midwest, and in Texas, the record price of natural gas, and the diesel shortage on the East Coast. The trouble is that Biden has no viable short-term solutions before the midterms and will be blamed for these shortcomings that are the result of long-entrenched problems.
- Republicans have already begun to pounce on the anticipated pain of possible blackouts this summer, and Republican House Energy and Commerce Committee members sent letters last week to Energy Secretary Jennifer Granholm and to the chair of the Federal Energy Regulatory Commission demanding that the Biden administration provide specific plans for how it will prevent potential electricity emergencies in the coming months. These Republicans view today’s circumstances as a result of pushing a clean energy transition at the expense of reliability, while Democrats counter that the green transition is needed to save the planet.
- Americans have traditionally expected the federal government to provide fixes and aid in ensuring a basic quality of life. Though this trust in Washington to “do what is right” is rapidly eroding – it has fallen from 73 percent in 1958 to 20 percent today – Biden campaigned on a return to normalcy. Soaring energy costs, extreme weather events, and major power system failures were not a part of this vision. But the reality is that a confluence of long-term trends and geopolitical events have converged to result in the present situation.
- Disinvestment over time has allowed the average age of power plants in the US to grow to over 30 years old and the average age of power transformers to over 40 years old. Plants are up against conditions they were not designed to withstand including a more extreme range of temperatures — like the heat wave that knocked six Texas power plants offline last month and the heat that is to come with the National Oceanic and Atmospheric Administration forecasting above average temperatures for every county in the country — and an increase in extreme weather events that can also damage infrastructure, like the mega drought in the western US. Lack of water poses its own challenges and threatens hydropower and nuclear power generation.

The Current Crisis: The price of gas has received the most political and public attention so far among the energy crises.

- US gas prices have surged 52 percent in the past year and reached record national highs that are also driving up overall inflation. At first, the president's team tried to paint the elevated gas price as "Putin's price hike," but this messaging did not take. A Quinnipiac Poll earlier this spring found that 41 percent of those who responded say the Biden administration's economic policies are to blame for increased gas prices, with 39 percent of independents agreeing. And just 24 percent of those polled say the high prices are due to the war in Ukraine and sanctions against Russia.
- These dire numbers show how much is at stake if and when other types of energy crises strike this summer and why the Biden administration has poured so much time into lowering the cost of gas. The problem now for Biden is that he has already played his biggest hand when it comes to gas prices by releasing an unprecedented up to one million barrels of oil per day from the US Strategic Petroleum Reserve (SPR) over six months, which is set to conclude in October – just before the midterm elections. The move was talked up by the White House as a record release but it so far only reduced prices minimally before seeing those reductions reversed. Biden has had the same lack of success in urging oil and gas companies to boost their own drilling. There are few viable options left.
- Congress has not come up with any better ideas. Democratic leadership considered suspending the federal gas tax, but this angered transportation groups who rely on already meager gas tax revenue. Similarly, Biden considered waiving certain smog rules through the summer to lower costs but has apparently scrapped it over health and environmental opposition. Opposition though was still not enough to halt Biden from lifting the usual summer ban on the use of E-15 ethanol fuel, which did not significantly lower gas prices and angered climate groups.
- This lack of options is what is driving Biden to consider his political possibilities with a number of problematic petrochemical states. The fact that Biden is planning to travel to Saudi Arabia is emblematic on its own of the political desperation to lower gas prices. Another unpalatable possibility is further engaging with Venezuela, which the administration has already initiated. The Treasury Department in May allowed Chevron to resume talks with the country over restarting oil production but the outcome of these efforts remains to be seen. There is also the unknown of the outcome of Russia's war in Ukraine and whether if it ends and a status quo is reached, Biden would ultimately support relaxing sanctions on Russia while Putin is still in power.

The Looming Crises: Biden is trying to avoid appearing to be caught flat-footed and unprepared for energy crises as he has with other threats including the baby formula shortage, so-called "transitory" inflation, and the Omicron wave of Covid, but the policy levers here are different.

- The price of natural gas in the US has nearly tripled in the last year and has hit its highest prices in over a decade despite the US producing record amounts. These prices are less readily apparent to most Americans than gas prices but the costs of natural gas are still contributing to overall inflation. Here, Biden has fewer options than with gas: climate groups vigorously oppose constructing new fossil fuel infrastructure and even if Biden were to alienate their views in favor of building pipelines, any relief from such pipelines would take years. Another option would be to ban exports of liquefied natural gas (LNG) but this is also unlikely because Biden has sought to increase the US's LNG export capacity to send to Europe.
- Blackouts and power interruptions may become increasingly common this summer. The North American Electric Reliability Corporation's May reliability assessment cites the possibilities of extreme weather wreaking havoc on power systems that are already facing their own reliability challenges as they reduce fossil fuel resources and increase intermittent clean energy resources and contend with an aging system. It highlighted states served by the Midcontinent Independent System Operator in the Midwest as being particularly at risk because of "a capacity shortfall in its North and Central areas, resulting in high risk of energy emergencies during peak summer conditions." Other areas of concern are California, where demand is expected to outstrip supply, and Texas.
- The political challenges here are familiar. The decentralized nature of power and transmission systems makes it challenging to enact large-scale change. Biden has tried to support sectors of the power industry such as nuclear through legislation and the bipartisan Infrastructure Investment and Jobs Act (IIJA) provided $6 million in support for struggling nuclear power plants that are critical in some regions to keeping enough supply on the grid.

This support was meant to keep Entergy Corporation's 0.8 GW Palisades nuclear reactor open in Michigan but it is not known why its operators chose to shut it down instead of applying for the available aid. Governor Gavin Newsom (D-CA) is looking for federal help to delay the planned retirement of the Diablo Canyon nuclear plant's two generators in 2024 and 2025 to help with reliability.

- Biden also attempted to address this in the IIJA, which includes a provision that gave the Federal Energy Regulatory Commission additional authority in siting transmission lines. But there are debates over how consequential this will be given the complex nature of siting and permitting transmission projects. And larger incentives for building out high-voltage transmission lines with a new investment tax credit is still caught up in budget reconciliation negotiations.
- Finally, the Northeast is facing a diesel shortage and prices are up 63 percent from the start of this year. This is fueling inflation woes among the trucking industry and in part stems from the same infrastructure and market forces that fall outside the traditional realm of the federal government. The number of diesel refineries on the East Coast has halved to seven over the past 15 years, meaning more fuel must be shuttled in via the Colonial Pipeline at a time and cost disadvantage. The war in Ukraine has exacerbated this as Europe, a net importer of diesel, looks for replacements from its Russian supply.

A Crypto Bill At Last

Every Journey Starts Somewhere. Introduction of a comprehensive crypto legislative framework by a pair of bipartisan senators is the first step in the next chapter of Congress' effort to regulate digital assets.

- Senators Cynthia Lummis (R-WY) and Kirsten Gillibrand (D-NY) introduced the Responsible Financial Innovation Act last week, the first attempt to create a comprehensive legislative digital assets framework. The bill is a sprawling attempt to provide clarity on many different issues ranging from consumer protection to banking. While the bill is not expected to pass in the current Congress, it provides a starting point for future legislative discussions.
- One of the most important areas that the legislation addresses is whether most tokens are commodities or securities. The bill creates a new asset class called "ancillary assets," which most tokens would fall under and would be regulated as commodities under the Commodity Futures Trading Commission (CFTC). The Securities and Exchange Commission (SEC) would still be involved as firms would be required to disclose certain basic business information to the agency on a semi-annual basis. This would include details like the background of the board of directors and personnel changes, legal proceedings, and risk factors.
- Also covered by the bill are several issues related to taxation. One provision in the proposal would resolve an issue created by the expanded definition of a broker included in the Infrastructure Investment and Jobs Act by clarifying that miners, node operators, and other crypto-transaction participants will be exempt. The bill would also seek to make use of cryptocurrency more viable for day-to-day transactions by excluding those under $200 from tax obligations.

Stabilizing Stablecoins. Stablecoins have become one of the top focuses for legislators and regulators, so it comes as no surprise that Gillibrand and Lummis set out to address them in their bill too.

- In Gillibrand and Lummis' bill, they create a new asset class called a "payment stablecoin." Such an asset would have to be "denominated or pegged" to the dollar or a foreign currency or "[derive] value from or is backed by 1 or more underlying financial assets (except other digital assets)." These assets would have to be 100 percent backed by "high-quality liquid assets," which includes cash, balances at a Federal Reserve bank, foreign withdrawable reserves, consistent with the legal tender in which the payment stablecoin is denominated or pegged, short-term Treasury securities, and "any other high-quality, liquid asset determined to be consistent with safe and sound banking practices." Public disclosure of the assets, and their value, backing the token would be required as part of the legislation too. Under this bill, issuers would also not just be limited to registered financial depository institutions.
- What the legislation does not include is algorithmic stablecoins as part of its framework. This has been a common trend in discussions around regulating stablecoins with the focus

falling disproportionately on fiat-backed stablecoins, despite the risk that algorithmic ones present, as highlighted by Terra's recent collapse. Lawmakers and regulators acknowledge they are different assets, and the dangers associated with the latter, but to date no clear plan has been put forward from any official.

- Stablecoins have been one of the more popular legislative subjects with several other members creating their own draft proposals. A common thread among them is having the assets be 100 percent backed by liquid assets, similar to the language in Gillibrand and Lummis' bill. Where these proposals have tended to differ is who can issue stablecoins and with what regulatory agency those issuers have to register. What this signals is that despite the agreement on the need to improve oversight of stablecoins, legislation may stall out due to partisan bickering and instead regulators will be left to do what they can with their existing authorities.

Digital Assets Beyond Washington. As much focus as Washington gets for its regulation of digital assets, state officials are working to advance their own rules in the absence of federal actions.

- At the end of its legislative session, the New York state legislature passed a narrow proof-of-work mining moratorium. The bill is a first-of-its-kind effort that narrowly targets facilities using behind-the-meter electricity from fossil fuel plants. Governor Kathy Hochul (D) has yet to signal whether she will sign it into law or not and does not have to make a decision until December 31.
- Last month, California Governor Gavin Newsom (D) issued an executive order laying out a roadmap for regulation and consumer protection in the state. In many respects, the order seeks to align California's approach to the industry with that laid out in President Biden's executive order earlier this year. State agencies are now working to craft reports and issue recommendations for the next steps. Taking this step was seen as a key signal that the state will try to foster a welcoming environment for cryptocurrency businesses.
- State securities agencies have been particularly active in cracking down on companies offering interest-bearing crypto accounts as they view these to be unregistered securities. This led to a $100 million settlement between the SEC, 32 states, and BlockFi in what remains the largest crypto-related penalty handed out by the SEC to date. Voyager Digital is the latest to come under the microscope with at least seven states reportedly looking at its "Earn Program." The SEC has not been reported to be involved, but the state scrutiny may prove to be a canary in the coal mine as the case against BlockFi began with investigations at the state level.