# INTERNAL REVENUE PUBLIC HEARING

SUBJECT: PROPOSED AND TEMPORARY REGULATIONS (REG-115471--03, T.D. 9116) ON NEW MARKETS TAX CREDIT

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LOCATION: INTERNAL REVENUE SERVICE, WASHINGTON, D.C.

WITNESSES:
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MS. REAMAN: Good morning and welcome to the public hearing for the proposed and revised temporary regulation for new markets tax credit. My name is Susan Reaman. I am the branch chief in the Office of Chief Counsel, Passthroughs and Special Industries, and I will be the moderator today. Let me introduce our panel. To my solid left is Matt Josephs, who is the program manager for the new markets tax credit at the CDFI fund. And right next to me, to my left, is Steve Watson, associate tax legislative counsel at the Department of Treasury. And to my right is Paul Handleman, attorney-adviser in the Office of Chief Counsel, Passthroughs and Special Industries.

The proposed and temporary regulations were published in the Federal Register on March 11 of this year. We received four comments. We have two speakers today, and each speaker will speak for around 10 minutes. And after their presentation, if there are any comments that the panel has we can address those at that time.

Our first speaker is Mr. Michael Novogradac with Novogradac and Company.

MR. NOVOGRADAC: Thank you. I am Mike Novogradac with Novogradac and Company. We are an accounting and consulting firm that works in affordable housing and community development area. I want to just start by commending the Treasury Department on the original regs, as well as the amendment to the regs that were released in March. I think they've done a very good job of making the program more workable, and then after the initial draft and the subsequent amendments have allowed a lot of transactions before that, a lot would have been inhibited. And I'd especially like to thank Paul Handleman for all of us hard work with respect to the regs, as well as Lauren Taylor (sp).

There are seven points I wanted to cover in terms of comments on the amended regulations. Writing additional guidance is necessary to make the program more effective and more efficient. And I wanted to start -- I'll name the seven and then kind of walk through each one of them. One is the definition of "redemption." Two is the impact of the profit motive. Three is recapture and right to cure for implementation of direct tracing. Fifth is the substantially all measurement test. Sixth, investment in not-for-profit. And then, lastly, the allocation of the new market tax credit within a partnership.

First, dealing with redemption, as we all know the new market tax credit has a very severe penalty for recapture. As a consequence, investors are very sensitive to anything that could potentially cause recapture. One area that does cause recapture is if an interest, your equity interest is a CDE is redeemed. The problem is there is no clear guidance as to what redemption is, particularly when the CDE is a limited liability company that's choosing to tax as a partnership. It's sense is unclear as to what types of cash distributions from a CDE to its investors. If it's a partnership, many investors are adopting a rule that will limit cash distributions from the CDE to the taxable income of the CDE. The problem with this rule is you will end up accumulating cash inside the CDE as a result of this, because the cash income generated by a CDE will generally be less than the actual taxable income of the CDE. And that's largely driven by the way the tax cut works.

Just to go through a quick example -- I'm an accountant, so I have to throw some numbers out there at some point -- if a CDE were to received $10 million of investment, and it was to use that $10 million, take that $10 million and invest 95 percent of it in making loans, that CDE would then have $9.5 million of loans. And if you assume for a moment that that $500,000 difference between $10 million and $9.5 million is used for loan origination, start-up, any other costs to get the CDE up and started and funding all the loans. That's $500,000 ends up being deducted over some period of time. That $9.5 million goes out, and at a 5 percent interest rate regenerates $275,000 interest income every year. However, the taxable income would be less than that $475,000. And in the extreme, over that seven-year period the CDE under the taxable income limitation would generate $500,000 cash that cannot be distributed -- cash from interest income cannot be distributed to investors. This ends up creating negative arbitrage within the CDE, and ultimately makes less resources available to the actual businesses. You could buy down the interest rate at a greater rate if you didn't have to accumulate this cash inside the CDE. So I think that the regulation should develop a safe harbor calculation. Given the sheer complexity of actually further defining redemption as a concept to develop a safe harbor wherein distributions within the safe harbor would be not deemed to be a redemption, and the key aspects toward

calculation of a safe harbor would be to start with the overall investment income of the CDE and back out the cash operating expenses of the CDE, and not adjust this test by depreciation, amortization or other costs paid for out of the equity of the CDE.

And I'm working on a memorandum with Herb Stevens -- he's a tax attorney with the firm Nixon Peabody -- and I expect in the next week or so to have a draft of that available. That will go into some more details of a couple of ways you could actually further define the test. So I would sort of encourage that the redemption issue and the safe harbor be adopted.

Secondly, the second item on the profit motive, here I will make it brief. As a practical matter, profit motive test is often viewed as a Code Section 183 test. This subsection 183 only applies to individual net corporations -- and we published some articles in our newsletter, New Market Tax Credit Newsletter, to that effect. However, there's still a concern of tax attorneys out there that there is some judicial doctrine of profit motive that applies to a CDE. The impact of that is in some circumstances you actually have to give the investors more of a return than they are otherwise mandating. As a way to help mitigate the impact of this, I'd encourage the Treasury Department to adopt a regulation that exempts the amount of tax credits from Section 183. The technical matter only applies to individuals and S corporations. Investors have -- corporate investors in the cash credit area have gained comfort from that exemption within 183. I think they would similarly gain comfort in the new market tax credit area.

Thirdly, recapture and right to cure. The regulations do have a CDE the ability to request a waiver of a particular rule or potential of a deadline to avoid recapture, if it doesn't frustrate the purposes of Section 45D. However, investors are so sensitive to recapture that going to them and saying that there is some inadvertent noncompliance event, we have to apply it to the IRS via ruling, does cause some concern, and we recommend that there be a six-month right to cure just within the regulation there's a right to cure, a recapture event within six months. And if an additional six months is needed, because the error can't be corrected within six months, and reasonable efforts have been made during that six months to cure it, that that be extended to 12 months.

Moving on to direct tracing -- and this is one that -- number four -- it's one that you become more and more aware of as you start to pull a transaction together, and we've had discussions -- I've had discussions with Treasury before on this point, about how you trace cash when you commingle funds. And just to give an example, if a CDE raises all five equity investments, QEIs, from their investors and puts them into a bank account and put multiple QEIs into the same bank account, and then out of that bank account they draw funds to make investments, the question becomes: How do you directly trace the funds from the QEI into that ultimate investment? One solution is to go to CDEs and say, create multiple bank accounts -- which is what the solution is and asking for the guidance -- and draw each QEI into a separate bank account and don't do anything else with that money but fund directly the loan. And then as a consequence CDEs can have multiple bank accounts and do that direct funding. It's an administrative burden, but at that point it's somewhat manageable.

What gets to be more problematic is when you look at those accounts and of interest income generated, when you pull one out of the account what's it attributable to -- interest income of the

equity. And then if you look at the other end of the transaction, and you look at once you've made your loans and then the borrowers are returning, paying interest and principal, that money then goes into an account, and you have to reinvest some of that principal. How do you trace the principal between the interest and the principal payments?

As a consequence, right now, many CDEs are creating an elaborate number of very lengthy number of bank accounts, and having very specific rules as to how to tie all the cash through, and even in that circumstance there are areas where it's next to impossible to conceptually directly trace the cash.

So in the context of a commingled bank account, I would encourage the Treasury Department to create a presumption where if an allocation is being used that's reasonable, consistently applied, and most significantly documented contemporaneously, and not under audit or some later day -- documented contemporaneous with the investments or the use of the funds, that that be accepted.

For other purposes of accounting, the Treasury has developed very elaborate tracing rules on bank accounts, where you have last in, first out, your first instance out. And I wouldn't encourage you to develop a lengthy set of rules as to how to deal with cash that's commingled -- rather have an approach like this which is -- and there are similar types of approaches for taxes and bonds. So that's the direct tracing issue.

Moving on once again to another administrative matter, number five is substantially-all test. The substantially-all test has to be measured on six-month increments relative to when the original investment is made. The situation here is that if you have a CDE that is drawing multiple -- drawing equity from its investors on multiple dates, and most are drawing the equity as they need the money to make the investment. You end up with a CDE that makes 50 loans, having 50 quality equity investments. So you end up with 50 different dates where you have to measure at six-month increments, or you have 100 measuring dates potentially in a given year.

It gets even more problematic if the CDE is making construction loans. If the CDE has five construction loans where they're drawing down money once a month, then they will go to their investors who are investing in the five different construction loans, and if it's a 12-month process, they'll have 60 draws out of 60 substantially-all measurement dates every six months, or 120 in a year.

Indeed, a solution would be to allow CDEs with multiple QEIs in a quarter to apply the substantially-all test at the end of every quarter. The real estate investment trust have a quarterly measurement period, and trying to roll all this into a quarterly measurement period would definitely ease the burden on the CDE in terms of documenting compliance with this test.

Six, I have investments in nonprofits. The Section 45D clearly contemplates a not-for-profit being able to qualify as an active low-income community business, QALICB. The area that causes some concern among tax attorneys and tax accountants like myself is whether -- is how you determine if a nonprofit has a qualified active low-income community business? Most notably, how do you determine if that business of the not-for-profit is an active business? Does there need to be a profit motive? Does there need to be an expectation of generating a profit from

that business? It's causing some concern in terms of the ability of not-for-profits to participate in the program as QALICBs, as active businesses, and I would simply suggest that there be some type of rule that with respect to the active business test, a taxable entity would meet that test so long as they were engaging in activities that were consistent with its charitable purpose.

And then, lastly, a little bit of a broken record at this point dealing with partnership allocations -- and I know it's a different part of Treasury that is in charge of the actual allocation rules, but I'd still like to encourage Treasury to develop regulations that govern how the new market tax credit is allocated among partners in a partnership. A partnership invests in a CDE, and it has multiple partners. It's unclear as to how that tax credit would be allocated among those partners. As a consequences, transactions are being structured where all of the partners have similar interests. And if there's an investor that is not able to use the tax credit, they have to come in as a lender. They can't come in as an equity investor for fear that they would be allocated tax credit they couldn't use.

And where this issue probably rears its head the most is in real estate transactions, where you have a taxable entity that cannot use tax credits. They would like to be investing equity into the fund that is investing in the CDE, but they can't come in as an equity investor for fear that they will now get credits. As a consequence, they have to come in as a lender. However, if they come in as a lender and it's real estate development, the generating taxable income from the interest pooled and such, and they don't want that taxable income, so they end up choosing not to invest. And the ultimate effect is the cost of capital to the CDE ends up being hire.

And so in sort of closing there, the sooner we could have regulations that provide guidance on how the new market tax credit is allocated among investors in a partnership, the sooner we'd have more flexibility to buy down the cost of capital within a CDE.

So, with that, those are the seven points I wanted to comment on, and any follow-up questions.

MS. REAMAN: Thank you, Mr. Novogradac. Are there any comments from the panel?

MR. HANDLEMAN: Yeah, I guess, I have a question, Mike. On the issue for nonprofits, when we issued the amendments for temporary regs in March, and we added the new special rule for the active conduct of a trader business, for start-ups and nonprofits, we thought that that rule would take care of the issue for QALICBs that are nonprofit corporations. You don't think that's correct, or is there some aspect of that rule in the amended temporary regulations that doesn't reach a result you think appropriate?

MR. NOVOGRADAC: Let me -- I'll have to go back and recheck that part of the rule and see what -- fine-tune what the asterisk of that rule is.

MR. WATSON: I have a couple other questions, Mike. Do you have any sort of examples of reasonable allocation methods that you might suggest? Assuming we wanted to -- would it make sense for us to consider listing -- maybe not going into great detail, but maybe listing certain types of reasonable allocation methods that might make sense, like the (five-four ?) or something like that?

MR. NOVOGRADAC: You know, I probably prefer to stay away from the LIFO or FIFO, something of that aspect and emphasize more then contemporaneous nature if there's some document at the time the money is coming out of the account that documents what sources that money is coming from. And there's an ongoing schedule that tracks to ensure that more money is not coming out than coming in. That would be fairly general, you know, much like on the tax and bonds where you have the ability to essentially document how the tax and bond proceeds are coming out, you know, sort of contemporaneous with bonds themselves. And making the FIFO and LIFO, you raise the level of work that the investor or that the CDE needs to do to track those approaches.

MR. WATSON: Actually one other question relating to what you labeled a substantially-all issue in terms of testing dates, and you're suggesting quarterly testing dates. I take it you're reading the regulations to require basically two testing dates per QEI, as opposed to two testing dates per CDE. Is it --

MR. NOVOGRADAC: That's correct.

MR. WATSON: Is there something in the regulations that --

MR. NOVOGRADAC: Well, I look at the QEI as being the equity coming in, and that the CDE then has six months after that QEI to measure the substantially-all test, and then six months after that to measure the substantially-all test. So it's twice based upon the QEI. And if you have multiple QEIs, you end up with multiple six-month measurements.

MR. WATSON: This is an issue that may need some clarification on the regulations because I don't think they specifically say that you test on the six-month anniversary of the issuance of the QEI. I think it's spread a little broadly than that, so you need to take a look at that.

MR. NOVOGRADAC: Okay. I can tell you that in the tax world out there that's being interpreted as six months from each QEI. And if that's an incorrect interpretation, certainly some guidance as to what date you're supposed to peg and when your first measuring period is, that would be very helpful.

MS. REAMAN: Other comments? Well, thank you very much.

Our next speaker is Mr. Robert Rapoza, who is representing the New Markets Tax Credit Coalition.

MR. RAPOZA: Thank you very much. I'm Bob Rapoza, and I represent the New Markets Tax Credit Coalition, which is a national membership organization of local, state and regional CDEs and investors that came together to support the establishment of a tax credit for community development, and has worked with the IRS tax policy and the CDFI Fund to implement the new markets. We are glad to have the opportunity to testify today. We appreciate very much the good work of the department and its staff in getting the tax credit up and going.

Let me take a second to talk about some of the items that were included in the revised temporary rule, and then talk about some of the recommendations we have for the final rule, which I gather will be coming at us at the end of this year. And finally talk a second about the first two rounds of tax credits.

There were several items in the revised temporary rule which the coalition had supported, and we hope they will find their way into the final rule. And these include a revision on the definition of control as it relates to the reasonable expectation test from 32 percent to more than 50 percent; and a cure period for CDEs that springs into control one year; a provision that permits a business without any employees to qualify as a qualified low-income community business if it has a higher rate of its tangible assets in the qualified areas.

We also support the rule to facilitate the participation of new start-up businesses. We support the provisions which permit the multiple loan sales between CDEs and permit CDEs to finance lower-tier CDEs. And finally we are pleased that the look-back period has been institutionalized in the revised rule.

With regard to further modifications to the rule and the final rule, there is some concern on the part of investors that new markets might become ensnared in some of the concern over the use of tax shelters. We think the Congress when it set up the tax credit contemplated a social good coming from the credit, which was investing in poor communities. And it was with that the expectation on some of these that the investments might not yield the kind of return that might be gotten elsewhere. For this reason, we believe that the credit ought to be exempted from the provisions of Section 183 the in the same fashion as low-income tax credits.

In addition, Congress is debating the economic substance rule to S. 16237, and has once again taken a broader look at tax shelters. We believe once again, as I said, that Congress did contemplate a different standard for new markets. And we have for the record a colloquy between Senators Baucus and Rockefeller on this particular issue, and we believe if this becomes law, and the department is charged with writing a rule with regard to economic substance, that the credit would be exempted from those requirements.

With regard to redemption, the rule does not offer guidance on the redemption, what constitutes redemption of a qualified equity investment investors recapture. This is certainly an important issue for CDEs those with allocation, both those using the leverage and the non-leverage model that need to pass on returns, cash distributions to investors before the end of the seven-year term. These investors need to be assured that the cash distributions will not be treated as redemption of the principal.

We recommend that the IRS provide additional guidance on this issue, and to clarify that as long as a CDE does not repurchase ownership interest from an investor, and continues to satisfy the substantially-all test, that it be permitted to pass through cash distributions to its investors as it sees fit, rather than the seven-year term.

With regard to cure period, we have long supported a cure period for CDE allocatees. The revised temporary rule provides a cure period for certain CDEs with regard to control, and we

thought that was an important first step, and we hope not the last step. There are certain instances in which a CDE could fall out of compliance, such as a case in which a CDE might lose its certification because the member of the advisory board of the CDE that represents low-income areas resigns from the board, in which case the CDE would lose its certification, and therefore the investors would be subject to a recapture. Also the other instance is in which an investor would own -- or the CDE would own more than 50 percent of a business, and therefore not have the option of the reasonable expectation test, and therefore in the case of noncompliance would need time to bring that deal back into compliance, or substitute a deal.

While at the moment the temporary rule provides the option to waive recapture or to provide a cure period for recapture, it does not set a time period, and we continue to support the idea of a time period, a defined time period of one year for the cure period.

We recommend also that the definition of "non-qualified financial property" be modified as it applies to start-up businesses, so that such businesses can accumulate capital for a sinking fund related to a loan financed through the credit. It's come to our attention that some CDEs are providing seven-year or five-year interest-only loans to start-up businesses. These businesses have one or two -- set up a sinking fund into which they would deposit principal repayments. The difficulties they face is if the value of that sinking fund exceeds five percent of the unadjusted basis of the business, they would run afoul of the definition of a qualified business as contained in 45D(d)(4)(i)(e) and therefore be ruled out of the credit. And therefore we think seeing the fund as the service has taken an important step with regard to some of the other requirements for start-ups, this would be sort of an important step to take.

Regarding qualified census tracks, there has been some confusion on the part of CDEs as to which government Web site which contains data on the census can be used to verify eligibility for a community. And it would be important for the department to work with the Census Bureau and with others to resolve this issue.

We have also heard from a number of CDEs on the issue of census tracks with a realm of populations very often adjacent to low-income areas that are at the moment not considered to be eligible for the credit. And that would be a good thing to consider and modify.

Let me just take a second with regard to the first and second round allocations. At this point the CDFI Fund has done a great job in providing $6 billion in new markets allocations. Thus far it is clear in both round one and round two that real estate appears to be the dominant activity. And while there's nothing in the statute or the allocation that would necessarily drive the program in that direction, there are regulatory and administrative issues that are contributing to this trend.

Chief on that list or first on that list was the recapture provisions which certainly encourage the investment in real estate because as somebody said to me once, Dirt doesn't move. And this is an important area of concern to us, because we believe Congress intended a program that would not just do real estate but would do small business lending and venture capital. And we understand from investors and CDEs with the new program the comfort level on real estate is much higher than some of the other activities.

I would just note further that we are concerned about the low participation of rural areas thus far. In the first round, roughly 20 percent of the allocation went to rural areas. In the second round that dropped to 14 percent. While there might have been a definitional issue here, we nonetheless think that rural areas ought to be doing better than they have been, and that is something that we hope to work with the fund and the department on.

Finally, the second round required those allocatees in the first round as the basis for their participation in the second round to have at least 60 percent of their quality equity investments by a date certain, I believe March 7th -- March 5th. We believe that standard was hard to make, though several CDEs did it. And we are concerned that it would drive some decision-making in terms of the kind of deals that CDEs had to do to meet the thresholds. Certainly the more difficult deals take more time in lots of cases. And for many CDEs they can sign their allocations late in the fall, which only gave them a few months to meet the March 5th deadline. For the coming round, we recommend that while the 50 percent benchmark be maintained, we suggest that only have of that be in cash, and the other half be in binding commitments to provide a bit more flexibility for the CDEs.

I just wanted to say once again thank you to the department and its staff for its work. Demand for the credit far exceeds the expectations any of us have in the two rounds, $55 billion in the requests is really quite something, and shows the need for this sort of aid and the value of the credit.

Thank you very much. I'd be happy to answer any questions you might have.

MS. REAMAN: Any questions?

MR. WATSON: I have a question. On your comment concerning non-qualified financial property, you make the point that people may -- QALICBs may want to set up sinking funds or back-pay loans to CDEs. And I'm just wondering if there are business reasons why they would want to structure the debt repayments as sinking funds rather than just serial bonds that amortize principal?

MR. RAPOZA: I don't know that. But wouldn't that still be a financial asset of the CDE? Would that affect their basis?

MR. WATSON: Well, I think it's the -- I think the concern is you've got a QALICB whose as I understand a comity of a QALICB setting up sinking funds for repaid debt to the CDE, and it has --

MR. RAPOZA: Right.

MR. WATSON: This sinking fund money is on the books of the QALICB, and it could be considered non-qualified financial property, which would put them over the five percent limit.

MR. RAPOZA: Right, right.

MR. WATSON: But you could structure the same transaction I would think -- or actually this is the question that I'm asking: Are there business reasons why you'd want to use a sinking fund structure rather than just simply amortizing the principal so that the --

MR. RAPOZA: To pay it back or to --

MR. WATSON: The loan gets paid if they're a CDE.

MR. RAPOZA: Well, the reason for -- I think I understand the question -- the reason that some of CDEs have structured their loans like this is so they don't have to get into the redeployment issue of maintaining the substantially-all test.

MR. WATSON: Okay, that makes sense.

I guess one other point -- perhaps more an observation than a question. One of your suggestions is that we adopt a cure period for noncompliance.

MR. RAPOZA: That's been a long-standing tradition of ours.

MR. WATSON: And obviously one of the biggest challenges in these regulations is to make sure the rules that we write result in a program that's workable to investors, but also ensures that the investments in the program benefit low-income communities --

MR. RAPOZA: Right, right.

MR. WATSON: In furtherance of powers of intent. I think whenever you start talking about cure periods at least one policy issue that raises is whether you still have enough incentives at the CDE level to ensure ongoing compliance.

MR. RAPOZA: Right.

MR. WATSON: And I guess one observation I would have from these comments is that if that issue is particularly raised if the cure event is notification by the Treasury Department that you're out of compliance, and so you might ask whether that would mean enough incentive at the CDE level to comply if they've always got some period, say a year, to get back into compliance after they've been notified.

MR. RAPOZA: Right. But on the other hand you could say how if you were a CDE and your board representative that represents the loan takes a job elsewhere, that automatically triggers noncompliance and recapture. So they would need some way -- I mean, even if they are in compliance with regard to their qualified investments and so on, this fact of life might draw them out of compliance and therefore they would need some time period to find a representative, get them on the board, get the CDFI Fund to recertify or to reinstate their certification. And that's -- I mean, that's not something where they are not obligated to fund, where just for a reason at some level beyond their control they have that problem.

MR. HANDLEMAN: Could I say for that example it seems to me that may be more an issue for the CDFI Fund, because that is the one recapture event that really is determined -- has been delegated to the CDFI Fund in terms of CDE status. So perhaps the CDFI Fund could have some long-tier period if there's a problem with the governance of the CDE, because all the IRS would want is the notification that the CDE has lost its status. And that would be up to the fund to determine when that occurs.

MR. JOSEPHS: I was about to raise the same point, is the fund would determine when someone has lost their CDE designation. So that particular example is one that we may in fact while we are working on now discussing what the appropriate cure period would be if someone falls off the board, we would entertain the idea that we'd give some reasonable amount of time to allow them to replace that before we were to deem them not in compliance with CDE certification.

MR. RAPOZA: But there are cases also, as I said before, where a CDE has more than 50 percent in a deal, has control, and for whatever reason the deal falls out of compliance, and a defined cure period to bring them back into compliance will be very helpful. I mean, at the moment the regulation does have the option for the cure period -- we're just wanting to define that further.

MS. REAMAN: Could I ask one last question? We do have in our regulations currently a practice that you can come into the IRS and seek a waiver.

MR. RAPOZA: Right.

MS. REAMAN: A certain deadline that you might have missed. How effective do you think that practice is? Do you think it does give some level of comfort to investors?

MR. RAPOZA: I think it does. Though what I hear is that they want more -- they would like a defined period. Now, there's concern that the response time might take time for them until you do other stuff beyond this program. And therefore it's in that case if the time period goes by when they don't hear what is the status of the -- what is the -- are they in compliance, out of compliance?

MS. REAMAN: Well, my only comment is that that process generally would take into account the multiple facts and circumstances that might arise with each individual transaction, and drafting rules it is very difficult to capture all the situations in which a CDE may run afoul of our rules. So I would just comment that perhaps maybe by clarifying some of the practices within that waiver process that might take care of the different situations that might arise that we may not contemplate when we are drafting specific cure periods.

MR. JOSEPHS: Let me ask -- I do want to ask one question for Bob. This is in response to your observations. I think you mentioned that you noticed -- you have some trends -- that money is going primarily to real estate, maybe at the expense of business funds, that there used to be more money going to urban areas as opposed to rural. Are you hearing feedback that there's something in our application or selection process that is leading those results to happen, or is coming from outside of our own internal review processes?

MR. RAPOZA: Well, I mean I think a couple things. As I said before, the recapture provision drives to safer sorts of deals in the sense of compliance issues. I think that the previous definition of control with regard to the reasonable expectations that has had a chilling effect with regard to venture capital -- I'll be interested to see even -- (inaudible) -- venture capital moved up.

I think with regard to rural, I think part of the problem is that in general there is not the volume of deals in the rural areas that there are in big cities, and that it is hard for a CDE to accumulate a deal flow, and to have the connections to investors to compete in a way that would make sense. I mean, I think that -- when talking to the allocatees, because of the high cost for lawyers and accountants and so on, several CDEs have a strategy of wanting to build a bigger program to spread those costs. And I think it's harder for rural organizations, particularly the community-based organizations that we work with, to put together a package that would make sense in terms of the volume that you do to cover those funds. And I think part of it is there's an issue with regard to whether they can find the investors and get the commitments from those investors to compete effectively in worthy allocations.

I don't know whether the percentage of the CDEs or those CDEs that want to serve in rural areas, whether they did as well as a group as the urban CDEs, and I think that would something important to find out. But I think those issues are some of these that were to mitigate rural participation.

I was surprised the rural number, the rural share went down in the second round, because I had the impression that some of the organizations that sat out the first round decided to participate in the second round.

MR. JOSEPHS: Right. And one of the things you alluded to -- I think you referred to it as a definitional issue -- was what you were referring to is this year we had asked groups to identify whether they were serving rural whether a minor urban area versus a major urban area. And I do believe that people last year were only given the choice of rural versus urban -- might have counted some of these minor urban areas in their rural, because I think minor urban areas is like a town with less than 18,000 or something like that. So it can be in many cases be rural areas. But we normally view those as rurals.

MS. REAMAN: Any other comments? Thank you.

MR. RAPOZA: Thank you very much.

MS. REAMAN: Any other comments from the audience at this time?

I would just like to thank our speakers, Mediterranean and Mr. Rapoza, for participating in this public hearing today, and for providing us with such thoughtful comments. This concludes our hearing. Thank you.