

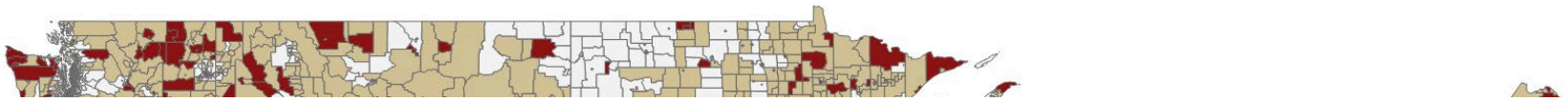
What Determines Where Opportunity Knocks? Political Affiliation in the Selection and Early Effects of Opportunity Zones

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Brookings Opportunity Zones Conference
Hutchins Center on Fiscal and Monetary Policy
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Research Question

What factors influenced the selection of Opportunity Zones?



List of > 42,000 eligible Census tracts published by U.S. Treasury in early 2018

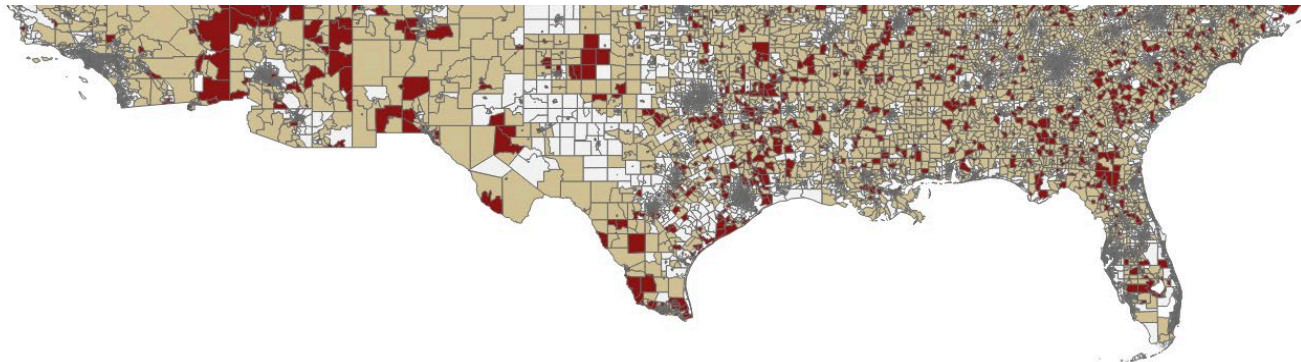
Tracts are neighborhoods with ~2,500-8,000 people

Eligible if:

- Median income no greater than 80% of area's median family income OR
- Tract had poverty rate over 20%

Each governor selected up to 25% of eligible tracts as Opportunity Zones

Final list reviewed and announced by Treasury in May-June 2018



How did politics affect the OZ selection process?

1. To what extent did governors select politically aligned zones?
 - Due to superior information via political networks, or
 - Way to reward constituencies
2. Did the type of information used by states alter the influence of political affiliation?
 - Examine selection processes used
3. Do any of the early outcomes of the policy vary based on political affiliation?

Critiques of OZ selection

A Trump Tax Break To Help The Poor To a Rich GOP Donor's Superyacht

Wealthy donors Wayne Huizenga Jr. and Jeff Vinik lobbied then-Gov. Rick Scott for the lucrative tax break — and won it. Poorer communities lost out.

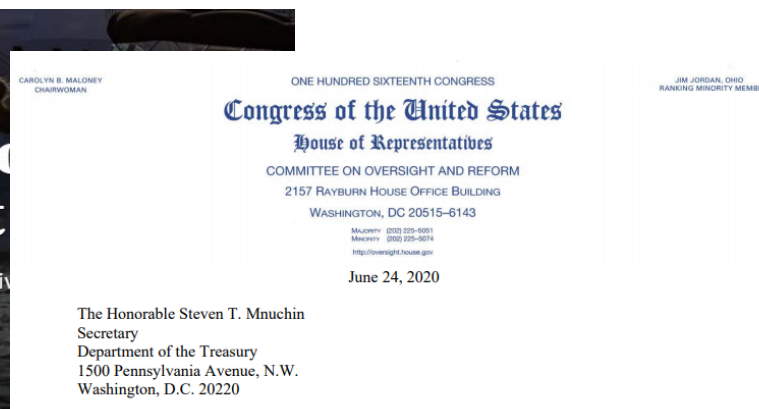
by Justin Elliott, Jeff Ernsthausen and Kyle Edwards, Nov. 14, 5 a.m. EST

After Nevada GOP push, Treasury benefiting one county

Bloomberg

Technology

Amazon May Get a Tax Break With a Project in American County



Dear Secretary Mnuchin:

The Subcommittee on Economic and Consumer Policy requests documents and information on the Department of the Treasury's administration of the Opportunity Zone program established by the Tax Cuts and Jobs Act.¹ In particular, we are concerned about possible abuses in the Department's designation of certain census tracts as "qualified opportunity zones" (QOZ) in Detroit, Los Angeles, and Oklahoma City.

As the Department has stated, Opportunity Zones "are designed to spur economic development and job creation in distressed communities."² The statute targeted distressed communities by making census tracts eligible as QOZs if they have high rates of poverty or sufficiently low average incomes. Only a limited number of tracts in each state may be designated as QOZs, and the Department's role is to certify lists of eligible tracts selected and nominated by the states.³ Designation as a QOZ provides an incentive for community development projects by reducing or eliminating capital gains taxes for investments in QOZs.⁴

It appears that the Department designated tracts in Detroit, Los Angeles, and Oklahoma City as "low-income communities" even though they do not appear to meet the statutory income qualifications for low-income communities.⁵ Erroneous designation of higher-income tracts as low-income communities undermines the purpose of the Opportunity Zone program since it gives valuable tax breaks to developers that do not benefit the distressed communities the law was designed to help. It would be especially concerning if investors that obtained tax breaks for

¹ Pub. L. 115-97, § 13823 (codified at Internal Revenue Code § 1400Z-1 to 2).

² Internal Revenue Service, *Opportunity Zones Frequently Asked Questions* (updated Oct. 22, 2019) (online at www.irs.gov/newsroom/opportunity-zones-frequently-asked-questions) (accessed on Feb. 12, 2020).

³ Internal Revenue Code § 1400z-1.

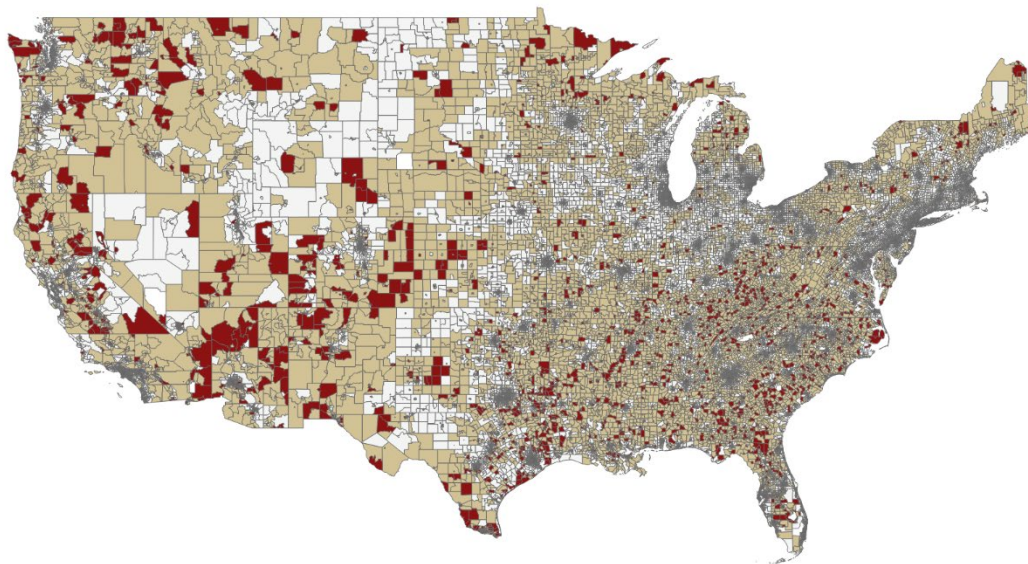
⁴ Internal Revenue Code § 1400z-2.

⁵ Internal Revenue Code § 45D(e).

Research Design & Sample of Census Tracts

Sample:

- All Eligible Census Tracts in U.S. States with data (n=40,620 (98.8%))
- Selected Census Tracts (**Opportunity Zones**) vs. **Eligible-but-not-selected** Tracts



- Political affiliation
 - Construct: whether local constituents are of the same party as the governor
 - Measure: whether local state representative is of the same party as the governor

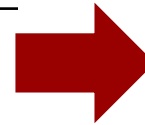
$$\textit{Selected as OZ} = \alpha + \beta_1 \textit{Same Party} + \beta_2 \textit{Poverty Rate} + \beta_3 \textit{Median HH Income} + \beta_4 \textit{Census Tract Characteristics} + \textit{State FE} + \varepsilon$$

Demographics, Political Connections, & OZ Selection

Dependent Var: Indicator = 1 if OZ	(1)		One p. point increase results in
Poverty Rate	0.005*** (0.000)	➔	0.5 p.p. higher likelihood of selection (~ 2.0% inc.)
Median HH Income	-0.004*** (0.000)	➔	0.4 p.p. lower likelihood of selection (~ 1.6% dec.)
Tract Population	0.005*** (0.001)	➔	0.6 p.p. higher likelihood of selection (~2.0% inc.)
% White	-0.000*** (0.000)		
Urban Level	-0.011*** (0.001)		
% Educated	-0.000 (0.000)		
Employment Rate	-0.005*** (0.001)		
Socioeconomic Change	0.087*** (0.019)	➔	9.8 p.p. lower likelihood of selection (~39.2% inc.)
Investment Score	0.008*** (0.001)		
Observations	40,620		
State Fixed Effects?	Yes		
R-squared	0.113		

Demographics, Political Connections, & OZ Selection

<i>Dependent Var: Indicator = 1 if OZ</i>	(1)	(2)
<i>Same Party</i>		0.019*** (0.005)
<i>Poverty Rate</i>	0.005*** (0.000)	0.005*** (0.000)
<i>Median HH Income</i>	-0.004*** (0.000)	-0.004*** (0.000)
<i>Tract Population</i>	0.005*** (0.001)	0.005*** (0.001)
<i>% White</i>	-0.000*** (0.000)	-0.000*** (0.000)
<i>Urban Level</i>	-0.011*** (0.001)	-0.010*** (0.001)
<i>% Educated</i>	-0.000 (0.000)	-0.000 (0.000)
<i>Employment Rate</i>	-0.005*** (0.001)	-0.006*** (0.001)
<i>Socioeconomic Change</i>	0.087*** (0.019)	0.087*** (0.019)
<i>Investment Score</i>	0.008*** (0.001)	0.008*** (0.001)
Observations	40,620	40,620
State Fixed Effects?	Yes	Yes
R-squared	0.113	0.113



If the local area is of the same party,
1.9 p.p higher likelihood of selection
(~ 7.6% increase)

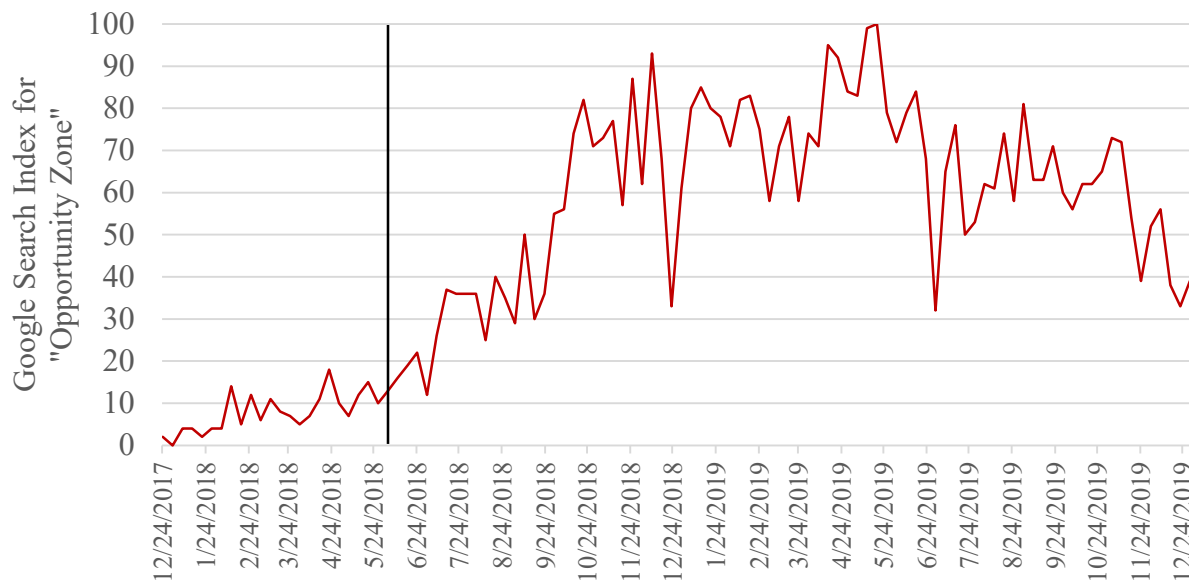
Summary of Results for RQ#1

On average, governors chose OZ tracts that were:

- Poorer, more populous
- Already-improving (“gentrifying”)
- Of the same political party

Very little public information about Opportunity Zones present during the selection period

Google Searches for "Opportunity Zone"
December 2017 – December 2019



RQ2: Did information channels alter the influence of political affiliation?

- Augment specification to include interaction terms that span all processes
- Professional engagement, public comment, application

<i>Dep. Var = 1 if OZ</i>	(1)
<i>Same Party</i>	0.064*** (0.018)
<i>Same Party x Prof. Engagement</i>	-0.065*** (0.019)
<i>Same Party x Public Comment & Prof. Eng.</i>	-0.061*** (0.020)
<i>Same Party x Application & Prof. Eng.</i>	-0.023 (0.021)
<i>Same Party x All Three Processes</i>	0.010 (0.027)
Controls?	Yes
Observations	40,620
State Fixed Effects?	Yes
R-squared	0.114



In states with **no formal process**, likelihood of picking same party area is 25.6%



Professional engagement completely offsets the role of political connections

RQ3: Is any economic response affected by political affiliation?

Does political affiliation signal better information or rewarding of politically aligned constituencies?

We study the industry most likely to respond:

- Commercial real estate transactions (2016- Q1 2019)
- New construction building permits (2016-2019)
- Construction employment (2016-2019)

Greater investment in Same Party areas → More optimal selections

Less investment in Same Party areas → Less optimal selections

Assumptions in studying economic outcomes:

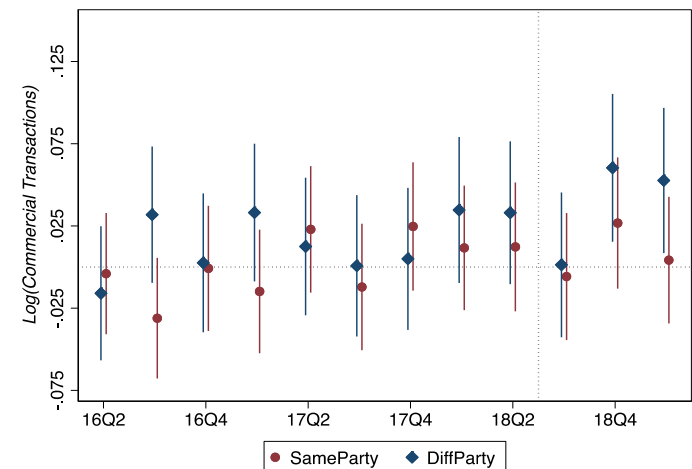
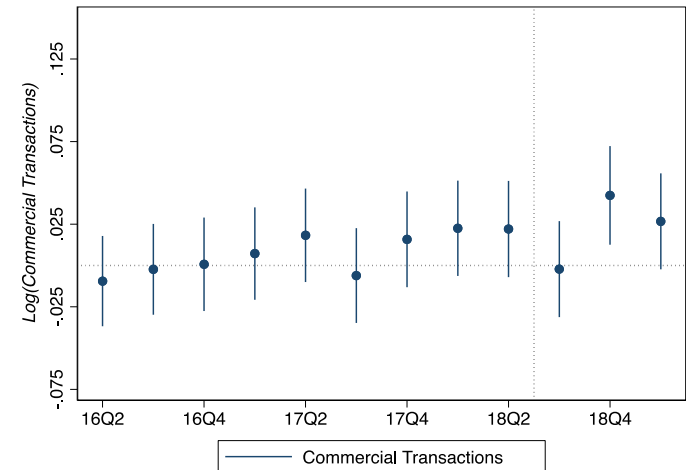
1. Real estate investment is representative of all OZ investment
2. Real estate investment is aligned with policy intent

Is any economic response affected by this political affiliation?

$\ln(\# \text{ Commerical Real Estate Transactions})$

$$= \beta_1 \text{Selected} \times \text{Post} + \beta_2 \text{Selected} \times \text{Post} \times \text{Same Party} + \text{Controls} \\ + \text{Tract FE} + \text{YearQuarterFE} + \varepsilon$$

	All Areas
$\ln(\# \text{ Commerical Real Estate Transactions})$	
<i>Selected as OZ * Post</i>	0.025*** (0.011)
<i>Selected as OZ * Post * Same Party</i>	-0.018 (0.015)
$\ln(\# \text{ New Building Permits})$	
<i>Selected as OZ * Post</i>	0.037*** (0.017)
<i>Selected as OZ * Post * Same Party</i>	-0.013 (0.026)
$\ln(\# \text{ Construction Employees})$	
<i>Selected as OZ * Post</i>	0.030** (0.013)
<i>Selected as OZ * Post * Same Party</i>	-0.017 (0.017)



What decides where opportunity knocks?

- Demographic and political affiliation
- The type of information used appears to play a critical role in selection.
- Early outcomes do not seem to vary based on political affiliation

Evidence important for:

- Future empirical evaluation of policy
- Potential future changes in selected Opportunity Zones based on recent census

Thank you