BookReview

License to Bill

LICENSING OCCUPATIONS: ENSURING QUALITY OR RESTRICTING COMPETITION?
BY MORRIS M. KLEINER
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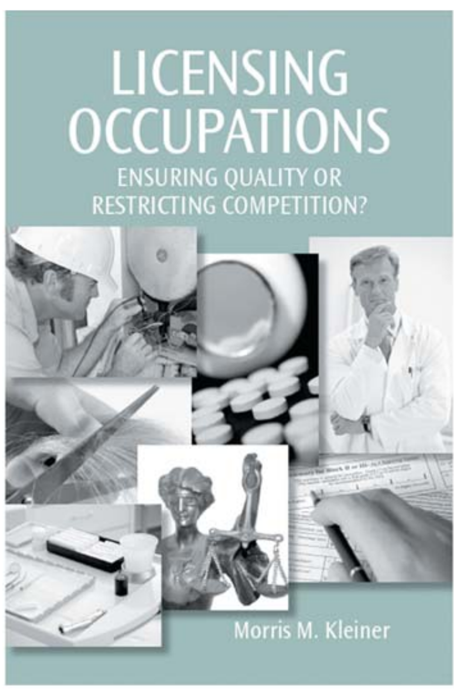
Who knew some states require a license to raise frogs? Boxers, auctioneers, and hair braiders along with doctors, lawyers, and dentists, of course, all need licenses. So do wrestlers. California licenses 178 occupations, while Kansas regulates only 47. Most Fifth District states fall somewhere in between: from South Carolina, which licenses 55 occupations, to Maryland, which licenses 89.

Morris M. Kleiner, a labor economist at the University of Minnesota, has spent much of his career studying licensing. In his new book *Licensing Occupations: Ensuring Quality or Restricting Competition?*, he covers a lot of ground, from the earliest codified laws, the Babylonian Code of Hammurabi, to present trends.

Today, licensing is one of the fastest-growing labor market institutions in the United States. It hasn't exactly resulted in what consumers might expect. Economists have found that occupational licensing increases prices in most regulated services by driving up wages from 4 percent to 12 percent. Meanwhile, it's unclear whether quality improves enough so that consumers are better off.

In an effort to provide a full account of licensing's costs and benefits, Kleiner has gathered history and research, adding new analysis, tables, and figures that document and update licensing issues. He discusses at length the economic theory that underpins licensing and includes state trends as well as how employment rules abroad affect the labor market and wages in the European Union. The ultimate question is whether the public is better off when occupations are regulated or whether consumers just end up paying more without much benefit.



More Licensing but Less Research

Although the number of people in licensed occupations has grown to about 20 percent of the work force from some 4.5 percent in the 1950s, studies of licensing lately have been few and far between. How come?

On the recent dearth of research, Kleiner has this to say: "Perhaps this lack of recent analysis is because the topic lies at the intersection of labor economics, law, and industrial organization and thus does not fit easily within one of the subfields of the social sciences as they have evolved."

Kleiner explains the nuts and bolts of licensing. Usually it's the members of a profession themselves who lobby for licensing, reasoning that it's necessary to stipulate certain training and benchmarks of quality, especially as technology has grown, requiring higher-skilled labor. But there's another, less-publicized motivation: "The expectation from economic theory is that licensing may create windfall gains or rents, and that these prospective gains in income provide an important impetus for licensure," Kleiner writes. In other words, licensing may be more beneficial to those licensed than to consumers.

For high-income professions, like dentists and lawyers, regulation results in a kind of monopoly power because entry is limited in a variety of ways. (Licensing of this sort is not to be confused with the academic training that lawyers and doctors, among others, undergo — though, in some cases, obtaining such formal training may be a licensing requirement.) Professional associations justify resulting higher prices by explaining that expert supervisors and standardized practices bring about higher quality service on average. (Standard practices can also stifle innovation, though, Kleiner points out.)

Licensing and Consumer Welfare

Most of us assume licensing provides assurances of quality and safety in the case of medical professionals or home builders or furnace fixers. But when is the last time you checked a state regulatory Web site to make sure your doctor still had a license? Perhaps we depend too much on those pieces of paper on the wall. But most people would like for their furnace repairman to know something about boilers before hiring him. So it stands to reason that licensing would protect consumers, right?

Not necessarily. The impact of licensing on quality is unclear. Kleiner and others who have studied the issue say licensing shows "no effects on average consumer well-being relative to little or no regulation." What is clear, though, is that increased prices are associated with highly regulated services. Even when entry restrictions raise the quality of practitioners, fewer people may use their services as the price and wait time go up. So some consumers are made worse off. The wealthy, and in the case of health care, those with generous insurance plans may be exceptions because they can afford to pay the higher prices. As a result, licensing can raise significant distributional concerns.

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Could lack of regulation contribute to catastrophe, such as disease or building collapse? "Although there are many anecdotes that document worker negligence or incompetence that have led to major serious injury or even deaths, there is little evidence that licensing would have eliminated serious tragedies in any systematic manner," Kleiner writes.

Economists point out that licensing and restrictive rules limit supply and mobility across state lines in some professions. And everyone knows what limited supply can do: curtail consumer choices, especially if prices and wages have become unaffordable for some people, which sometimes happens with the poor and dental care, for example. For professions with higher education and earnings (dentists, lawyers, doctors, and so forth), Kleiner says, licensing "appears to have large effects through either limiting entry or restricting movement into the state. However, for other occupations such as teachers, nurses, and cosmetologists, the impact of licensing on earnings is murky, with some studies finding small effects and others finding none."

Licensing keeps out the competition, according to the "capture theory." If demand for a service is relatively inelastic, then higher prices will lead to higher income for the licensed professionals. That means the benefits are larger for dentists than for hairdressers, for example, because there are fewer substitutes for dentists than hairdressers.

Alternatives

Occupational licensing is often justified on the grounds that "information asymmetries" create market failures. In short, the consumer of a service may not be able to accurately judge the claims of a provider. Consider a person going to a mechanic to get his car fixed. Does the car really need all the repairs that the mechanic suggests? Or is he taking advantage of the consumer's relative lack of knowledge? And, assuming that all the repairs are necessary, is the mechanic capable of actually doing the job? These are tough questions for the average consumer to answer. Proponents of licensing argue that a third party is often necessary to set basic standards for providers so that consumers can be reasonably assured that they are going to get an accurate diagnosis and good service.

But, as has been discussed, licensing may be a costly way to achieve this goal. Kleiner suggests that it might be possible, instead, to use certification, a weaker form of regulation. Certification documents that providers have met specific standards yet does not carry licensing's restrictions on competition imposed through barriers to entry and mobility. Physicians, for example, can become "board certified" in specialties. Some 200 occupations have certification. Registration is another possibility, one that is even less restrictive. People file information and qualifications with an agency before practicing, which could also include posting a bond.

Kleiner compares licensing with certification in two states. Minnesota certifies physical therapists, respiratory care providers, and physicians' assistants, while Wisconsin licenses those professions. Evidence showed that licensing compared to certification in those professions "provides no obvious benefits to consumers as measured by complaints to regulatory boards."

But to change the current system, occupational licensing needs more visibility. As Kleiner points out in the book's final paragraph, "policies passed by legislatures on occupational licensing are back-burner issues."

Kleiner's book is a thorough examination of a topic that's not as exciting as interest rates or the stock market. But quieter economic trends need airing too. In simple prose that only occasionally strays into economic jargon, Kleiner makes a strong case against excessive licensing. Such rules can keep people out of occupations, raising prices and distorting labor markets. How much longer will we allow professionals, rather than consumers, decide who can provide the most competent service? **RF**