Presented to The Committee on Small Business, Subcommittee on Economic Growth, Tax, and Capital Access

"Occupational Hazards: How Excessive Licensing Hurts Small Business"

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Regulating Occupations

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Chair and members of the Committee on Small Business, Subcommittee on Economic Growth, Tax, and Capital Access

My name is Morris Kleiner. I testify before you today on my own behalf and not as a representative of the University of Minnesota or any other organization with which I am affiliated.

I have a Ph.D. in economics from the University of Illinois at Urbana-Champaign. I am a professor at the Humphrey School of Public Affairs at the University of Minnesota Twin-Cities. I also teach at the University's Center for Human Resources and Labor Studies. I am a visiting scholar at the Federal Reserve Bank of Minneapolis, a Research Associate at the National Bureau of Economic Research headquartered in Cambridge, Massachusetts, and a Visiting Scholar at the Upjohn Institute for Employment Research in Kalamazoo, Michigan. I have worked in government, including military service, and consulted for many public and private sector organizations. My research specialty includes the analysis of institutions, such as occupational licensing, in the labor market. I have published in the top academic journals in labor economics and industrial relations, and I am the author, co-author, or coeditor of eight books. Three of these books focus on occupational regulation and were published in 2006, 2013, and 2015 by the Upjohn Press. These books have been the leading volumes on occupational regulations based on sales and citations to the work in Google Scholar.

Let me start with my conclusions because it establishes that the wage and other benefits of occupational licensing are concentrated primarily among individuals who are already well paid.[1] Evidence indicates that occupational licensing can hamper mobility, making it harder for workers to take advantage of job opportunities in other regions. Moreover, there is relatively little evidence to show that occupational licensing has actually improved the quality of delivered services in many fields, although it has been shown to increase prices and limit economic output. Hence, governments should require cost-benefit analyses prior to new licensing rules, allow practitioners to cross borders without economic penalties, and reduce regulations on certain occupations.

Occupational licensure is the process by which governments establish qualifications required to practice a trade or profession, so that only licensed practitioners are allowed by law to receive pay for doing work in the occupation. During the early 1950s, occupational licensing in the U.S. covered about 4.5 percent of the workforce, but by 2015 it had climbed to 25 percent according to the U.S. Bureau of Labor Statistics. Below I enumerate these issues and suggest how these regulations influence the economy and small businesses. I also provide suggestions for improving current policies.

First, occupational licensing makes it more difficult to enter an occupation and move across political jurisdictions[2]. While licensing may be an effective means of boosting wages for some occupations, licensed workers are not always better off.[3] Empirical evidence indicates that licensing can hamper mobility, making it harder for workers to secure jobs in other states. Occupational licensing can thus act as a deterrent to geographical movements in several ways. For instance, because licensing is typically

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[1] Curr, Henry, 2018, “How to Rig an Economy: Occupational Licensing Blunts Competition and Boosts Inequality,” *The Economist,* February 17.

[2] See J. Johnson and M. Kleiner, 2017. “Is Occupational Licensing a Barrier to Interstate Migration?”, NBER Working Paper No. 24107. December.

[3] See both Kleiner, M. M. and A. B. Krueger (2010). “The Prevalence and Effects of Occupational Licensing," *British Journal of Industrial Relations*, 48, 676{687 and Kleiner, M. M. and A. B. Krueger, “Analyzing the Extent and Influence of Occupational Licensing on the Labor Market," *Journal of Labor Economics,* 31, S173-S202.

administered at the state level, workers may have to repeat many of the requirements and investments necessary to gain licensure when moving across borders. These requirements can include qualification criteria such as good moral character, passing exams, working with or for local practitioners, and engaging in ongoing professional development activities (an investment that continues throughout the worker's career). In the absence of reciprocity agreements—in which one state accepts occupational licenses granted by another—relicensing requirements can be prohibitive, in terms of both time and money, thereby discouraging workers from moving to other licensing jurisdictions where greater opportunities often exist.

Multiple studies have corroborated the negative link between occupational licensing and worker mobility. The licensing of manicurists, for example, can impede cross-state and even international migration—particularly from Vietnam (42 percent of all manicurists in the U.S. in 2000 were Vietnamese). A well-regarded study finds that the requirement of an additional one hundred hours of training reduces the likelihood of having a Vietnamese manicurist in the area by 4.5 percentage points, while states requiring some level of English proficiency were 5.7 percentage points less likely to have a Vietnamese manicurist[4]. In other words, policies that affect migration are not just limited to high-income individuals.

Beyond its detrimental effects on workers, this lack of mobility also can harm consumers—especially in rapidly growing areas. To the extent that licensing slows the influx of new workers and inhibits greater competition, consumers are unable to access services at the lowest cost. Small businesses are not as likely to be able to hire at going

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[4] Federman, Maya N., David E. Harrington, and Kathy J. Krynski. 2006. "The Impact of State Licensing Regulations on Low-Skilled Immigrants: The Case of Vietnamese Manicurists." *American Economic Review* 96 (2): 237–41.

wages creating what they perceive as "shortages." Taken together, these studies support the view that regulation may limit the number of practitioners in many fields, and that a policy of reducing barriers to state or national migration with respect to licensing requirements could benefit workers, small businesses, and consumers.

Second, occupational licensing can affect consumer prices via several channels, from restrictions on worker mobility to limitations on advertising and other commercial practices. The impact of licensing-related practices on prices ranges from 5 to 33 percent, depending on the type of occupational practice and location[5]. For example, estimates completed in the 1970s showed that the lack of reciprocity in dentistry raises prices by 15 percent. A restriction on the number of hygienists that a dentist may employ increases the average price of a dental visit by 7 percent[6]. More recent national estimates showed that restrictions on the tasks a nurse practitioner can perform without the supervision of a physician raises prices of healthy-child exams by up to 10 percent, with no effect on child mortality or insurance rates for malpractice[7].

These higher prices could be caused by government regulations intended to reduce the likelihood of poor service in the market[8]. The rationale is that higher prices cause consumers to perceive the service to be of higher quality (even if this is not actually the case) and thereby demand more of the service, which drives up the price further. On

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[5] See Kleiner, Morris M. 2006. "*Licensing Occupations: Ensuring Quality or Restricting Competition?*" Kalamazoo, MI: W. E. Upjohn Institute for Employment Research.

[6] See Kleiner, Morris M., and Robert T. Kudrle*. 2000. "Does Regulation Affect Economic Outcomes? The* Case of Dentistry." *Journal of Law and Economics* 43 (2): 547–82 and Kleiner, Morris M. 2006. "*Licensing Occupations: Ensuring Quality or Restricting Competition?*" Kalamazoo, MI: W. E. Upjohn Institute for Employment Research.

[7] Kleiner, Morris M., Allison Marier, Kyoung Won Park, and Coady Wing, 2016. "Relaxing Occupational Licensing Requirements: Analyzing Wages and Prices for a Medical Service." *Journal of Law and Economics*, Vol. 59, Vol. 2. May.

[8] See U.S. Executive Office of the President.2015. "Occupational Licensing: A Framework for Policymakers." Washington, DC: The White House.

the other hand, current practitioners could influence regulatory practices in order to raise their own wages by limiting entry or restricting information on service prices in the market (health care is a prime example of this type of use of regulations)[9]. Under this framework, occupational licensing creates a monopoly in the market, with the long-term impacts being lower-quality services, too few providers, and higher prices.

It is difficult to tell from the empirical studies which of the above causes are more likely. However, regardless of the exact cause, it is possible for regulated high-income occupations, such as dentists and lawyers, to raise prices in ways that may further shift income from lower-income customers to higher-income practitioners, thus potentially contributing to greater income inequality[10]. Furthermore, if wealthier consumers place greater value on (or can afford) higher quality licensed services, then lower-income individuals with less demand (or less ability to pay) might be adversely affected by tougher licensing standards, as they will have even less access to the increasingly higher priced services.

Third, occupational licensing reduces the ability of individuals to enter regulated occupations. For example, occupational licensing can reduce labor supply by between 17%-27%. Men respond to licensing with larger reductions in labor supply than women, regardless of race[11]. Longitudinal data show that the longer an occupation is licensed the

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[9] Kleiner, Morris M., Allison Marier, Kyoung Won Park, and Coady Wing, 2016. "Relaxing Occupational Licensing Requirements: Analyzing Wages and Prices for a Medical Service , *Journal of Law and Economics*, Vol. 59, Vol. 2. May.

[10] See Kleiner, M. M. and E. Vorotnikov (2017): "Analyzing occupational licensing among the states," *Journal of Regulatory Economics*, 1-27 for a detailed analysis of the issue.

[11] Blair, Peter, 2018, "How much of a barrier to entry is occupational licensing?" Working Paper. Clemson University.

greater its ability to limit entry and raise wages for its workers.[12] In addition, immigrants have lower levels of licensing than natives suggesting that it serves as a barrier for this growing group in the U.S. economy.[13]

New regulatory policies often include "grandparent clauses" that protect existing workers from having to adhere to changes in the licensure process; but, new entrants must meet these higher standards in order to gain entry into the occupation.[14] It takes time for older, less-educated workers to exit the labor market, and for newer workers who have met the higher entry requirements to enter. This process may limit the supply of labor and allow those who are already licensed to work in the occupation to gain economic benefits by limiting employment growth (and thereby competition) in their field. In addition, occupational licensing organizations that represent, for example, accountants, have ratcheted up the requirements to attain a license, in this case from 4 to 5 years of university training, which has served to further limit the supply of licensed practitioners.

Overall, occupational licensing and the lack of consistency across state borders with respect to the education and training of licensed practitioners can carry broad implications for the economic well-being of individuals. Evidence indicates that occupational licensing influences the allocation of labor in critical areas of the economy, such as health care, construction, and education, and has had an important influence on

[12] Han, S. and Kleiner, M.M., 2016. *Analyzing the Influence of Occupational Licensing Duration and Grandfathering on Labor Market Outcomes* (No. w22810). National Bureau of Economic Research.
[13] Hugh Cassidy and Tennecia Dacass, 2018. "Occupational Licensing and Immigrants," Kansas State University Working Paper, February.
[14] See Han, S. and Kleiner, M.M., 2016. *Analyzing the Influence of Occupational Licensing Duration and Grandfathering on Labor Market Outcomes* (No. w22810). National Bureau of Economic Research for further details.

employment, wage determination, employee benefits, and prices. Some even suggest that occupational licensing dampens the rate of innovation and misallocates resources within an occupation by setting fixed and in some cases arbitrary rules[15].

In order to enhance the benefits and reduce the costs of this form of regulation, the following three policies are recommended.[16] First, state governments should require and the federal government should encourage cost-benefit analyses prior to the approval of new occupational licensing standards. Second, licensed individuals should be allowed to move across political jurisdictions with minimal retraining or residency requirements. Third, where politically feasible, governments should reclassify certain licensed occupations to a system of certification or should remove regulation on some professions altogether. These proposals should lead to employment growth in affected occupations and a reduction in consumer prices. Replacing licensing with certification in certain occupations, thereby providing more competition, would, in most cases, result in substantial gains in economic growth and employment without measurable harm to consumers.

[15] Schmitz, James A.2012. "New and Larger Costs of Monopoly and Tariffs". Economic Policy Paper 12-5. Minneapolis, Minnesota. Federal Reserve Bank of Minneapolis.
[16] Kleiner, Morris M., 2015. Reforming Occupational Licensing Policies. Retrieved from the University of Minnesota Digital Conservancy, http://hdl.handle.net/11299/190817.

Addendum

Hierarchy of occupational regulations from least to most restrictive:

"Registration" means a requirement established by a legislative body in which an individual gives notice to the government that may include the individual's name and address, the individual's agent for service of process, the location of the activity to be performed, and a description of the service the individual provides. "Registration" does not include personal qualifications but may require a bond or insurance. Upon approval, the individual may use "registered" as a designated title. A non-registered individual may not perform the occupation for compensation or use "registered" as a designated title. "Registration" is not transferable and is not synonymous with an "occupational license."

"Certification" is a voluntary program in which the government grants nontransferable recognition to an individual who meets personal qualifications established by a legislative body or private certification organization. Upon approval, the individual may use "certified" as a designated title. A non-certified individual may also perform the lawful occupation for compensation but may not use the title "certified." "Certification" is not synonymous with an "occupational license."

"Occupational license" is a nontransferable authorization in law for an individual to perform a lawful occupation for compensation based on meeting personal qualifications established by a legislative body. It is illegal for an individual who does not possess an occupational license to perform the occupation for compensation. Occupational licensing is the most restrictive form of occupational regulation.