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Charles Wheelan

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# OCCUPATIONAL LICENSURE: THE ELEPHANT IN THE LABOR MARKET

CHARLES WHEELAN

Good morning and thank you for having me. This symposium addresses something that I consider to be a very important labor force issue. Let me begin with a question: How many of you got up this morning and told your friends or significant others that you were attending a symposium to discuss burning issues related to social justice? How many of you said you were going to a symposium to discuss fundamental issues at the core of human liberty that involve the most basic relationship between citizens and the state?

By now you are probably convinced that you are in the wrong room because licensing is not usually associated with social justice and the topic certainly seems more prosaic than something at the core of human liberty. But I am going to argue that it is both. This is an issue that should exercise libertarians—people who believe in a minimally intrusive government—because licensing involves the government telling you what you can and cannot do for a living. As a consumer, it tells you who you can or cannot hire to provide a given service.

The State is telling you that without a license you cannot practice certain professions, which is a very heavy-handed form of regulation. The State is also telling you that you cannot hire someone if he or she has not gone through a certain kind of training or passed a particular exam. This regulation overrides your judgment as an informed consumer. Government knows better than you do. This should be a “red meat” issue for libertarians and economic conservatives who believe that smaller government is better.

Licensing is also a social justice issue. If you are someone who cares passionately about what kinds of jobs low-skilled workers can do in the 21st century economy, or how ex-offenders can successfully re-enter society after leaving prison, then you also should care because licensing can often prevent disadvantaged groups from finding jobs. There are a lot of low-skilled professions, such as barbers, manicurists, or even hair braiders that could be done by people with few formal skills. Yet individuals are precluded by law from entering those professions without certain types of training that may or may not have a significant impact on their job

performance.

What I have described to you is an issue that should resonate across the entire political spectrum—from the economic libertarians who aggressively question the right of the state to limit your choices, to people who spend a lot of time thinking about policies that affect our most disadvantaged citizens.

If we leave the ideological poles aside, there are some pragmatic reasons to think deeply about the effects of licensing. I teach at a public policy school. The issues we are most likely to discuss in terms of “broken systems” are healthcare and education. Healthcare and education turn out to be two fields with the highest proportion of licensed workers.

Teaching requires a certificate, which is a misnomer, since it is really a license to teach. With very few exceptions, you cannot teach at any public school in America without a State-issued license. Healthcare is slightly different in that it is made up of many different licensed professions. Doctors are the most obvious, but we have nurses, nurse anesthetists, respiratory therapists, physician’s assistants and so on. Each one of those professions involves their own specified licensing process.

There are philosophical reasons that you should care about licensing. There are also pragmatic reasons if you care about some really important public policy challenges. For something that should really be a red meat issue for political ideologues and a concern for people who want public education and healthcare to improve, this is an issue that gets very little substantive attention and virtually no political traction.

#### THE ECONOMICS OF LICENSING

I am not unequivocally anti-government. I would describe myself as politically left-of-center. I think there is an important role for regulation throughout the economy. There are many ways in which government makes markets work better or can improve upon market outcomes. Having said that, I am convinced that licensing has become a form of stealth regulation that, in many cases, is doing more harm than good. We do not exercise much analytical rigor in deciding which professions should be licensed and which should not. At the minimum, I hope by the end of the symposium you are persuaded that this is an issue that deserves more public attention than it has been getting.

Let’s look from an economic standpoint: when, why, and how should a profession be licensed? There are three cases in which licensing can improve overall social welfare. The first is the case in which a profession poses some potential threat to a third party. An electrician would be a classic example. If you go out and decide to hire a cheap, unqualified electrician, his or her poor work is not merely your problem. The poor wiring in your house could easily end up burning down my house. Tree

trimming would be another example, even though it might not be considered a highly skilled profession. If someone goes out and cuts down a limb only on your property, it is only your problem. But in a lot of cases, particularly in a dense urban environment, if someone cuts down a tree limb on your property it can become my problem very quickly. There are cases where bad service provisions affect society beyond the consumer who has hired the service provider. This is a classic case of an externality. We can make society better off by passing regulation that makes that consumer more likely to act in a way consistent with the rest of our interests.

The second example where a compelling case for licensure exists is when there is a different kind of externality. The people harmed by a low-quality service provider are the people who are receiving that service. However, the fact they received that service poorly affects the rest of us. Teachers are a good example because they only do harm to the students they are teaching. However, society cares a lot about whether those students become literate, good citizens, and so on. A bad teacher in a bad school is not going to harm me directly as an electrician might. On the other hand, we in society have a stake in the quality of education that those students, many of whom we will never meet, receive in the classroom. Therefore, we can justify imposing some kind of regulation that might raise the quality of service being provided to other people.

The third case for licensing is more debatable, and that is a situation where society does not think that you or anybody else is capable of making a smart choice in terms of a service provider. It is paternalism, because if they make a bad choice, it does not affect the rest of us in any way. This is not an electrician or trimmer; it is something like a yoga instructor, a profession that has been considered for licensure. You choose a bad yoga instructor and as a result you will be harmed. So we as a society are imposing our preferences on that person because we have deemed them incapable of making a smart decision. I describe this as paternalism because we are overriding a decision that they might otherwise make. In some ways it is a little like seatbelt laws for adults or motorcycle helmet laws. Clearly, society in other realms has decided that we want to impose some change in your behavior.

Let me make two additional observations with regard to the theory of licensing. First, certification can solve many of the problems that are traditionally associated with licensing. I will explain the relevant terminology. Licensing is any case in which the government, usually a state government, requires that a service provider have a license. That license usually requires certain prerequisites, whether it is training, passing an exam, or the like. If you do not have the license, you cannot legally provide the service.

Certification merely signals that someone has received a certain kind of

training or has demonstrated a certain expertise, but individuals who are not certified are still allowed to practice the profession. Any one of us can hire someone who is certified or we can hire someone who is not certified. For example, you could have your computer serviced by someone who is certified by Dell, meaning that person has gone through training programs that Dell feels qualifies them to do good work. Or, you can have your computer serviced by your Uncle Al. If the Dell certification has some value then presumably you are willing to pay more in the marketplace for someone who is certified than for someone who is not. But it is optional.

I point this out because licensure is sometimes justified on the grounds that it helps rational consumers help themselves. You might not know whether a particular optometrist is qualified, therefore licensing is necessary to solve this information problem. That is a logical fallacy. Certification could do exactly the same thing in a less coercive way. The state government could simply set up a series of requirements to become certified as an optometrist. Imagine that the requirements are exactly the same as what is currently required by law to become licensed as an optometrist. Then when it came time to have someone check your eyes, you could choose someone certified by the state, and all the information about quality represented by that certification, or you could choose to go to someone else. Certification, even though it is voluntary, can provide any essential information to the consumer. The key is what economists refer to as an information asymmetry, meaning that service providers know more about the quality of service than consumers do. This is not a traditional economic rationale for licensure. A well designed certification program can provide whatever information consumers may need, assuming that they are rational decision makers.

Finally, for licensure to work in terms of improving overall quality in the profession, it has to actually improve the quality of service provided in the profession. It is true that a bad tree trimmer can cut down my neighbor's tree in a way in which the branch falls and crushes my roof. That argues in favor of some kind of regulation. However, the regulation put in place must actually make it less likely that the tree trimmer will cut down a limb in a way that crushes my roof. If we do something that does not truly improve quality in the profession, then we have not achieved our social objective, even if there is a compelling reason for people in this profession to be licensed. The fact that you might do harm to a third party is necessary but not sufficient to justify regulation. The regulation must also achieve its intended effect with regard to quality in order to improve overall social welfare.

That is a brief overview of the theory as to when we should license professions and when we should not. As you should recognize, there is nothing about the theory that says licensing is inherently bad. But like any

tool, it can be abused.

#### POSSIBLE ADVERSE CONSEQUENCES OF LICENSING

Licensing can also be a bad thing. It has legitimate economic purposes that can be used in a way that diminishes overall social welfare. How can regulation that ostensibly upgrades the quality of services provided end up making society worse off? There are a number of ways in which that might happen.

It is entirely possible within a profession to have “too much” quality. This might seem silly. More quality is presumably always better. In fact, that is not the case. Higher quality usually requires higher cost. Some consumers may prefer less quality at a lower cost. This point is best illustrated by an exchange that supposedly happened between Milton Friedman and a lawyer who was a member of the American Bar Association. Milton Friedman was a prominent opponent of licensing. He wrote his dissertation at the University of Chicago on the costs of overly restrictive licensing in the healthcare industry. Supposedly, Friedman had made the pitch to a group of lawyers that it should be much easier to practice law. One of the members of the Bar Association took issue with this position and asserted that all lawyers should be “Cadillacs.” Friedman retorted that if all lawyers are Cadillacs, many consumers will not be able to afford any vehicle at all.

Sometimes a Corolla is just fine. If the only choice for consumers is between a Cadillac and nothing, you may be unable to afford the Cadillac, in which case you get nothing. Using law as an example, there are a whole host of circumstances in which a “Corolla lawyer” may be fine. There are plenty of legal tasks that are important but not that sophisticated: drawing up a will for a simple estate, a simple divorce or bankruptcy, and so on. There is no reason you need someone who has graduated from Yale or clerked for the Supreme Court to carry out these tasks. Yet if you set the licensing bar too high, consumers are deprived of a more affordable choice, in which case they may not get the will or the bankruptcy assistance. If that is the case, then there is a social cost.

Let’s look at medicine as another example. If someone is going to do brain surgery you would like them to be as highly skilled as possible. However, most of medicine is not brain surgery. If you have children, you know that much of medicine is about stuffy noses, ear infections, basic immunizations, and flu shots. There are many relatively mundane but extremely important tasks that can be done well by nurses, physician’s assistants, or specially trained public health professionals. If you make it illegal for those individuals to do basic things like prenatal care or give immunizations, then it is less affordable to obtain that important medical care. Therefore, it is less likely they receive it, in which case the public

health costs can be quite significant.

Licensing may not improve quality. We should not assume that because we put a licensing law in place that we are upgrading overall quality in the profession. Nor can we assume that it will remove the worst service providers in the profession. There is an assumption that if a profession can harm the public then it ought to be licensed. I would concede that point. However, there is not sufficient skepticism as to whether the law subsequently put in place, passing an exam, or taking certain classes, actually improves quality.

Let me give you a powerful example. Beginning around the year 2000, Los Angeles was forced to hire thousands of new teachers as the result of a California law putting a cap on the student/teacher ratio. Los Angeles had to hire so many new teachers that the district was unable to fill all the positions with certified teachers. As a result, the district hired thousands of individuals who were either in the process of becoming certified or not certified at all.

There was a unique opportunity to observe the counterfactual. It is usually hard to compare the performance of certified teachers to non-certified teachers because uncertified teachers cannot legally practice in the classroom. Los Angeles is also unique in that the district collected classroom level data on student performance for many years so that it was possible to observe the impact of a particular teacher. Therefore, we can look at the students assigned to a particular teacher and determine their achievement gains over the course of the year. Then the next year the teacher will have a new group of students and we can do the same thing. Over time, it becomes possible to distinguish the most effective teachers from the least effective.

The Los Angeles experience was studied by several economists and they came to two very powerful conclusions.<sup>1</sup> First, good teachers matter enormously. If you are fortunate enough to have a good teacher several years in a row, your progress is dramatically better than students with average or below average teachers. Conversely, if you have a poor teacher for several years in a row, you will lose significant traction relative to other students.

Second, there was no statistically significant relationship between teacher certification and performance in the classroom. In other words, teacher quality matters, but what we demand of our teachers in order to become licensed has no discernible impact on that quality. Other research has come to similar conclusions with regard to licensure for other

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1. ROBERT GORDON, THOMAS J. KANE, & DOUGLAS O. STAIGER, *Identifying Effective Teachers Using Performance on the Job*, The Hamilton Project Discussion Paper 2006-01, April 2006.

professions. Just because quality in a profession matters does not mean that we can necessarily assume that the licensure requirements stipulated by a state legislature or licensing board will improve that quality.

Licensure can actually diminish the quality of professional training. To make this point, let me contrast journalism school, which is obviously not required by law, with teacher certification programs, which are provided by schools of education and are required in all states in order to become a public school teacher.

Journalism schools must add value for those who attend them or else they would disappear. Presumably, either journalism employers pay a premium for employees with journalism degrees, or it is easier to break into the profession. If that were not the case, then students would not pay to attend journalism school. There has to be some market-based reason for a person to seek out this kind of training. Therefore, journalism schools must constantly think about the skills that students need and employers demand in order to survive. There is a market mechanism forcing the training to be relevant and valuable. If this market mechanism breaks down, then people will cease to attend journalism school, and the schools will close down.

Education schools are the opposite in that you must go to an education school and take the prescribed courses because the law says that you have to. If you do not take those courses in those programs, you cannot become a teacher. Therefore, the courses themselves do not have to make you a better teacher. Their value lies in the fact that you cannot get a job without taking them. As a result, there is much less of a market mechanism forcing an improvement in the quality of those programs. Schools that are hiring teachers may still prefer the graduates that come out of one program as opposed to another, but to the extent you have come out of any program you are at least allowed to get a job. The fact that there is not much pressure to prove these programs produce great educators is consistent with the data from Los Angeles, where teacher licensing seems to have no significant effect on classroom quality.

Licensing restricts mobility, both within and across professions. Licensure laws are generally passed at the state level. As a result, someone who is licensed in Ohio may find it difficult to move to Wisconsin, even though he or she has worked successfully in Ohio for 20 years. States often have reciprocity laws for licensure, but not always.

Licensing can also reduce mobility across job descriptions. Someone who is licensed to teach high school may not be able to move to elementary school or even to middle school. The law may preclude a person who is a very good eighth grade teacher from moving to ninth grade, which is potentially ridiculous.

One less obvious effect on mobility is that licensure can prevent professionals from doing tasks that are the exclusive legal province of



another licensed profession. For example, a registered nurse may not be able to do certain tasks that are reserved for respiratory therapists in states that license respiratory therapists. The result is vertical silos in a field like healthcare which has a substantial number of licensed professions each with legally prescribed responsibilities. Hospitals and other healthcare providers have less flexibility in staffing. Healthcare workers have less mobility in the field, even across jobs that are broadly similar.

As I mentioned at the outset, licensing can prevent some individuals from entering the labor force at all, particularly in low-skilled professions that pose little harm to the public, such as cutting hair or grooming pets. Licensing can keep individuals out of the labor force. It can prevent workers from moving across state lines to pursue opportunities. It can also prevent workers from moving to similar jobs within the same basic profession.

Licensing can lower quality in a profession by creating barriers to entry that are most costly for individuals with the highest opportunity cost of time. This is arguably the least intuitive of all the potential adverse outcomes but one that is important to appreciate. You may assume that, worst case, if the requirements for licensure are completely useless then society is no worse off than if we did not have any licensing requirements at all. A law that has no effect on quality should not be any different than having no law at all. That is wrong. Any kind of training has some opportunity cost. If you are required to take two years of classes that turn out to be useless, you could have been doing something else with those two years. The time and the money obviously have value. It is also true that the most highly-skilled individuals in our society are the ones who have the highest opportunity cost of time. They are the most likely to be deterred by some kind of required training that is expensive in terms of time.

Think again about teaching. Suppose that we require two years of training that does not turn out to have much value in the classroom. That makes it significantly less likely that someone who is now a physicist at a federal laboratory or a chemist for Abbott is going to leave that job to teach because it would require two years of training. If that training has no value, it is particularly expensive to society if it keeps people who would otherwise be very good teachers out of the classroom. When you think about this subject, just remember that when Albert Einstein retired to Princeton, New Jersey, he was precluded by law from teaching high school physics unless he went back to school for eighteen months or two years to get a teaching license.

#### HOW DOES THIS HAPPEN?

How do we get licensing laws that do not necessarily make sense? We know there is a potential role for licensing, but we are seeing a lot of laws

that are not making us better off. On the face of it, licensing hair braiders just does not make a lot of sense.

Here, basic political economy can give us some intellectual traction. The reason that we see more licensing laws than is probably socially optimal is that there is a huge financial incentive for professions themselves to seek licensure. If you are a teacher, an optometrist, or a hair braider and you would like to raise your income, there are a number of ways you could go about doing it. One is working harder or more productively. Another would be to go to your state legislature and say, "Could you send us money?" On the other hand, you could go to the same state legislature and say, "Could you make it harder for potential competitors to enter my business?" You would not exactly describe it that way; you would talk about the importance of training and competency and so on. The end result would be to make it more difficult and/or costly to enter the profession.

At the same time, you would almost certainly ask the state legislature to exempt all current service providers from those new licensing requirements or "grandfather" them. So all new entrants to the profession have to take classes, pass an exam, and do an internship. However, if I am already practicing the profession at the time the law is passed, I am exempt. This will have same practical effect as the legislature sending me a check. By restricting the entry of new service providers, we can raise the incomes of those already in the profession. If supply goes down relative to what it would have been, then price goes up. In this case, the price is the wage of practitioners in the newly-licensed profession.

Consequently, no one speaks for consumers who now pay more. Many service providers do work for consumers who are not organized around this issue. Barbers have a professional association to look after their legislative interests, but people who go to barbers do not. When licensing legislation comes up in a general assembly, the profession involved usually has some kind of organized interest acting on their behalf. They often have a lobbyist tracking and promoting licensing legislation. Meanwhile, consumers do not pay a whole lot of attention. How many of you have ever gone to your state capital or called your state representative to say, "I am uncomfortable with hair braiders being licensed because it is going to raise the cost the next time I get my hair braided"?

It is perfectly rational for a profession that is seeking licensure to invest a lot of time and money in that process. Since the costs of licensure are generally diffused over a large group of busy, unorganized consumers, it is perfectly rational that none of us shows up in the state capital to question whether or not yoga instructors ought to be licensed. For the typical legislator, he or she can pick up the support of the barbers association, the teachers union, or the Bar Association by creating more rigorous licensing legislation. They will not pay a cost in terms of political capital with the rest

of us because we are not paying attention. Of course, that explains the explosion of licensing laws in recent decades; it does not justify them.

#### LEGISLATIVE SOLUTIONS

Let me conclude by talking about how we can make all of this better. We would like to pass a licensing law when: 1) there is a profession that poses some potential harm to the public, and 2) the law changes the entry criteria or training requirements for the profession in some way that successfully ameliorates the harm.

Having thought about this a great deal, I have composed what I would describe as my checklist for legislators and policy types.

The first and most important thing is to ask what the goal is. Next, seek the least costly means of achieving that goal. What are we trying to accomplish? For example, in the context of teaching, is it to simply weed out potentially dangerous teachers? If that is the case, then it can be accomplished with something far less costly and time-intensive than traditional licensure, such as a national criminal background check. There are teachers who have done horrible things to students; they should not be teaching.

Keeping a national database and checking names against it is a relatively cheap and quick way to accomplish that objective. For people with no prior criminal activity, it imposes virtually no cost. This does not keep the scientist from Abbott out of the classroom, where we need more science teachers.

We must always ask, "Will certification work instead?" If we are concerned that consumers cannot tell which service providers are of high quality and which are of low quality, but we trust them to make a sensible decision when they have such information, then we do not need to license the profession.

I cannot tell a competent eye doctor from an incompetent eye doctor. That does not mean that we need to license eye doctors. Instead, the State could stipulate what training produces qualified eye doctors. Everybody who does that training, or passes a certain exam, will be certified as competent by the State. I am still free to see whatever eye doctor I choose. If you visit a certified eye doctor, then you get exactly what you would get if that were a licensed profession. The state has helped you overcome a potential information barrier. On the other hand, if for some reason you want to go to an uncertified eye doctor, go for it! If you want to save money, or if you know enough about eye doctors that you can discern quality on your own, then you still have that right.

When providing information to consumers is the rationale for the state to inject itself into the labor market, we should always explore certification as a less coercive but still potentially effective option.

We should ask whether a licensing law will achieve what it is supposed to do. Will it actually improve the quality of service provided? Does it actually reduce the chance that someone will cut down a tree and crush my roof? To the extent that the whole point of this type of legislation is to improve the quality of some profession or to eliminate those who are really dangerous, there should be evidence that whatever is being required by law is likely to have that effect. Does this exam or training actually lead to better performance on the job? As you saw with teacher certification, this is not necessarily the case.

The burden of proof should be placed on the parties seeking licensure to demonstrate that it will make the public better off. When this idea reaches the legislature, someone is going to point out that members of the profession are in a position to do harm. That is step one. That is the necessary, but not sufficient, condition for licensure. Step two is to provide compelling evidence that what we are requiring of potential entrants to the profession will solve the problem that has been identified. If that answer is no, or even uncertain, then the State should not pass this law. You have identified something as dangerous but you have not ameliorated the danger.

A legislature should not exempt current service providers from new licensing requirements. For example, if there is an exam that is required to become a hair braider, then all hair braiders, old and new, need to pass the exam. If we say that someone who has been doing this for ten years must already be experienced and competent, that is fine. We can write that into the law. Therefore, anybody who has been doing it for 10 years in another state or country ought to be exempt from the exam as well.

Whatever is required of new entrants to the profession should be required of those who are already in the profession because this will ostensibly protect the public. This serves two purposes. First, if this requirement is really effective in protecting the public from low quality or dangerous service providers, then it will remove those people from the current workforce, which is presumably a good thing.

Second, it will remove the political impetus for groups to seek licensure merely to enhance their own economic interests by creating barriers to entry. Groups in a profession can no longer make it hard and costly for new entrants to the profession while exempting themselves from those same hard and expensive requirements. Therefore, a professional association has much less incentive to go to St. Paul or Madison to lobby for more rigorous licensing standards if they are imposing those costs on themselves.

Finally, any enlightened legislator ought to examine the licensure laws on the books and consider rolling many of them back. We ought to change the burden of proof. If there is no evidence that a current law leads to better outcomes, then there is a compelling reason to repeal it. We should not just assume that licensure is a good thing when I have provided many reasons

why it might generate social costs far in excess of the benefits.

I hope that I have persuaded you this is a really important topic. It may not be terribly sexy. I am sure we would have more people here today if we were talking about pornography and the First Amendment, but in terms of regulations that impact our everyday lives, you would be hard-pressed to find a more significant topic. Licensing has a profound impact on who enters what professions and on how entire industries operate. We need to be much more cognizant of the potential distortions that overzealous licensing can impose on our economy.