

A conversation with Morris Kleiner, March 23, 2015

Participants

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Note: These notes were compiled by the Open Philanthropy Project and give an overview of the major points made by Professor Kleiner.

Summary

The Open Philanthropy Project spoke with Professor Kleiner of the University of Minnesota as part of its investigation into the harms of and alternatives to occupational licensing in the U.S. Conversation topics included negative effects of licensing requirements, possible ways to quantify the costs of licensing, alternatives to licensing systems, and areas for further research and funding.

Problems of occupational licensing

Time and money costs to licensees

The procedure to become licensed is often costly and time-consuming, especially for lower-income entrants into the field. To become a licensed cosmetologist, for example, a person may have to pay thousands of dollars to a training institution (e.g., Aveda) and spend a year in school. Individuals who lack the necessary funds must borrow money for school fees and lose a year of income during their studies.

Inequality of impact on higher-income vs. lower-income workers

Becoming licensed in a certain profession translates to higher wages, better benefits (including better pensions and health care), and increased likelihood of finding a job. It is estimated that being licensed increases a person's wages by as much as 15–18% on average. However, as Professor Kleiner wrote in a February 2015 National Bureau of Economic Research working paper, study results consistently show that the gains are greater for workers in higher-income licensed professions, such as doctors and dentists, than for those in lower-income licensed professions, such as manicurists. (See <http://www.nber.org/papers/w20961>) Professions that have been licensed the longest, such as doctors and dentists, also tend to be more politically influential.

In another paper, published by the Brookings Institution in March 2015, Professor Kleiner found that licensing has no effect on income inequality (i.e., variations in income) within licensed occupations. (See http://www.brookings.edu/~media/research/files/papers/2015/03/11-hamilton-project-expanding-jobs/thp_kleinerdiscpaper_final.pdf) However, it is possible that occupational licensing compresses wages among lower-income occupations, while increasing variance in higher-income fields.

Wealth transfer from consumers to licensed workers

Licensing raises prices for services, resulting in a transfer of wealth from consumers to licensed workers. Professor Kleiner, along with Alex Mas and Alan Krueger of Princeton University, has estimated that 1% of total consumption expenditure is reallocated from consumers to licensed occupations. However, it is not clear how much of that reallocation goes to high-skilled workers as opposed to low-skilled workers.

Estimates by Professor Kleiner and others of “deadweight loss” or lost output from occupational licensing have generally found it to be proportional to wealth transfer. Because most of the wealth transfer goes toward higher-income licensed professions, it is reasonable to conclude that most deadweight loss results from higher-income professions as well.

Reduced access to services and trades

Occupational licensing reduces both workers’ ability to gain entry into certain fields and consumers’ access to the services of those workers. For example, if there are too few licensed practical nurses or too few physical therapists, prices for their services will go up and some consumers will choose not to use their services.

Reduced access could also include the need for consumers to travel greater distances to use services (i.e., if there is only one licensed practitioner in a given community instead of several, some consumers will have to spend time traveling to the sole licensed practitioner). This reduction in access is typically not covered by traditional calculations of deadweight loss from occupational licensing.

Licensing boards’ efforts to reduce access

Reduced access is exacerbated by licensing boards’ attempts to restrict trade among unlicensed workers they see as competitors. Occupations that have been licensed the longest frequently exert greater control over licensing boards. For example, the North Carolina Board of Dental Examiners is made up primarily of practicing dentists, some of whom have used their positions on the board to attempt to stop non-dentist businesses from providing teeth-whitening services. Because the dentists see the non-dentists as competition in a lucrative area of their business, the dental board argues that a dental license is required to practice teeth whitening. In the recently decided case *North Carolina Board of Dental Examiners v. Federal Trade Commission*, the Supreme Court ruled for the trade commission, finding that the dental board was attempting a restraint of trade.

Curtailed entrepreneurship and innovation

The Kauffman Foundation has conducted research that illustrates the role of licensing in inhibiting entrepreneurship by barring access to certain fields. For example, if CEOs were required to be licensed, Steve Jobs and Bill Gates, both of whom dropped out of college, would have been unable to head up their respective

companies, and much of their talent would have been underutilized or lost altogether. A paper recently published by the Kauffman Foundation focuses on the impact on low-income entrepreneurs in particular.

Increased inefficiency of business operations

Businesses become less efficient when they have to take into account directions from a licensing board or legislature on how to practice.

Obstacles for incarcerated individuals

Inmates often have the opportunity to learn trades while in prison, such as plumbing or cosmetology, but cannot find jobs in these professions after their release if the licensing statute for that field includes a “good moral character” clause. Having a good moral character is not relevant to every occupation, so this stipulation unnecessarily prevents formerly incarcerated individuals from practicing the trades they have studied. Because of the makeup of the inmate population in the U.S., these laws also disproportionately affect minorities.

Obstacles for veterans

Members of the armed forces receive training while serving, but when they reenter the civilian workforce, state governments often do not allow their military training to count toward fulfillment of licensing requirements. This is a more politically tenable cause than rolling back licensing restrictions as a whole, and Joseph Biden and Michelle Obama have recently made efforts to address these obstacles for veterans.

Quantifying the costs of licensing

Wealth transfer

The amount of the wealth transfer resulting from occupational licensing may be roughly estimated by assigning the average consumer an average wage, then finding the difference between this average wage and the relatively higher wages earned by licensed professionals controlling for human capital characteristics.

Access and innovation

So far there has been no attempt to quantify the access costs or innovation costs to society imposed by occupational licensing. One possible way to estimate the innovation cost would be to use patents as a proxy for innovation and compare two states, one with a licensing requirement for a given profession and one without, to see whether fewer related patents are issued in the state with the licensing requirement. To measure costs to access, one could find the number of practitioners in a given trade per the area population and examine the effect on prices when the number of practitioners increases.

Recent growth in licensed occupations

As the U.S. and other developed countries move increasingly toward service-based economies and away from manufacturing and industry, the opportunity for restricting entry through licensing increases. Occupations in the services sector are more dominated by licensing because manufacturing is generally done by companies rather than individuals.

Professor Kleiner has found that about 75% of the recent increase in licensing in the U.S. was due to an increase in preexisting licenses, and only 25% was due to the licensing of new occupations. This figure dates to 2006, so it would be useful to study how the number of professions requiring licensing has grown since then versus the number of total licensed practitioners.

It is also unclear whether this growth has been driven mainly by increased licensing among high-skilled professions versus low-skilled ones, another potential area of research. Licensing has expanded in both high-skilled and low-skilled areas, although health care in particular is dominated by licensed professions. Using census data, it is possible to look at how much growth has occurred in universally licensed occupations, such as doctors and dentists. However, in other growing fields, such as engineering and accounting, the licensed sector of the total number of practitioners is relatively small. For example, only 20% of engineers and about 45% of accountants are licensed, but practitioners in these fields are still legally able to practice these professions.

Alternatives to licensing

Professor Kleiner believes that certain occupations in which malpractice could have serious consequences should continue to be licensed. One example is doctors, who need to have the ability to recognize contagious diseases, such as Ebola. Certain businesses, such as restaurants, should also have to adhere to health standards. However, in many professions, a lower-skilled version (e.g., a legal technician instead of a lawyer) could provide many of the same services at a lower cost and thus expand access to legal services.

Certification vs. licensing

Some occupations could be subject to certification instead of licensing. Certification is an optional process that confers upon the holder a “right to title,” i.e., proof of having achieved a minimum standard of competency in a trade. However, it does not prevent those who do not hold certificates from practicing that trade. For example, only financial advisers who meet certain requirements can call themselves “Chartered Financial Analysts, CFAs” but anyone can dispense financial advice without a license. Licensing, on the other hand, grants the licensee a “right to practice” and prevents non-licensees from practicing a trade.

Moving to a certification-based system from a licensing system for many professions would be one way to reduce the number of licensed occupations, including high-skill occupations. Schools could be created to offer coursework in a given trade, and graduates from those programs would receive certification recognized by the state

to practice the occupation. However, licensed professionals in these trades would probably strenuously oppose a certification-based system.

Groups working on occupational licensing

- The **Institute for Justice (IJ)** has been actively campaigning for many years to raise public awareness, especially among judges, of the harms of occupational licensing. Most of its work focuses on licensing for low-skilled professions. In Indiana, IJ has worked with legislators to investigate either rolling back some licensing requirements or conducting a cost-benefit analysis of their efficacy.
- The **Goldwater Institute** in Phoenix, which advocates with Arizona state legislators
- The **Mackinac Center for Public Policy**, which does similar advocacy work with legislators in Michigan
- The **Brookings Institution**, through publishing Professor Kleiner's research
- The **Cato Institute**
- The **Obama administration**, which has set aside funds to examine the potential costs of occupational licensing
- The **Council of Economic Advisers** within the office of the President
- Individuals within the **Treasury Department and Department of Labor**

Professor Kleiner does not know of any organizations that focus specifically on the impact of licensing in high-skilled occupations.

Organizations that have occasionally publicized the potential harms to consumers from occupational licensing include:

- Common Cause
- AARP
- Consumers Union (the publisher of *Consumer Reports*)

Opportunities for funding around occupational licensing

Studying licensing in high-skill vs. low-skill occupations

Because the majority of wealth transfer and deadweight loss seems to stem from the higher-skilled licensed occupations, and because less attention is focused on licensing of these occupations, licensing of high-skilled professions seems to offer a better opportunity for philanthropists to begin rolling back or relaxing licensing requirements. However, groups representing high-skilled licensed occupations have significant political clout, making progress less feasible.

Studying impacts of occupational licensing on former inmates

No groups have studied these effects to date, but some of Professor Kleiner's PhD students at the Humphrey School are looking into it. One of them, Jason Hicks, is attempting to measure the effects of changes to some state laws that allow licensing requirements to be waived for formerly incarcerated individuals, especially in low-

income occupations. Mr. Hicks could use approximately \$40,000–\$50,000 in funding per year to cover his tuition, room, and board, which would allow him to focus exclusively on research and advance his work more quickly.

Professor Kleiner's research

Professor Kleiner is seeking funding for research into changes to licensing statutes over time. The Kauffman Foundation has funded a pilot study of a few occupations, which should conclude in June or July 2015, and will then decide whether it will fund a full study. Professor Kleiner would also like to investigate whether wealth is mainly reallocated from low-income consumers to high-income licensed practitioners. Another potential topic of study would be whether licensing results from a desire to restrict supply versus from consumers' perception that licensed services are of higher quality. In another study, Professor Kleiner is investigating the effects of occupational licensing in the European Union, which is facing similar challenges from licensing.

*All Open Philanthropy Project conversations are available at
<http://www.givewell.org/conversations>*