How to rig an economy

Occupational licensing blunts competition and boosts inequality

How high earning professions lock their competitors out of the market

Print edition | United States Feb 17th 2018 | WASHINGTON, DC

EVERY month Debbie Varnam of Shallotte, North Carolina, must pay a doctor's bill. It is not for treatment. Ms Varnam is a "nurse practitioner", a nurse with an additional postgraduate degree who is trained to deliver primary care. North Carolina, like many states, does not allow nurse practitioners to offer all the services they are trained to provide. Ms Varnam cannot, for example, prescribe the shoes diabetics often need to prevent the skin on their feet from breaking down. To do so, she needs the approval of a doctor. So Ms Varnam employs one. For about $1,000 a month, the doctor reviews and signs forms that Ms Varnam sends him. The doctor, she says, has a similar arrangement with five other offices.

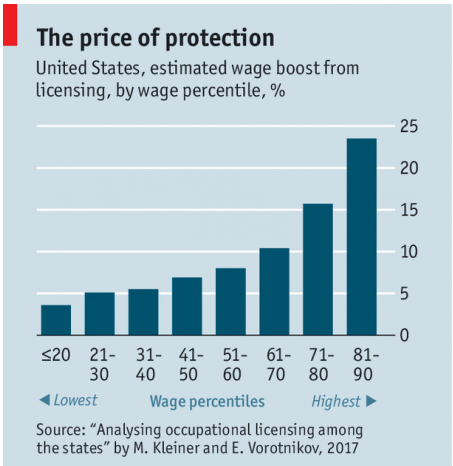
Occupational licensing—the practice of regulating who can do what jobs—has been on the rise for decades. In 1950 one in 20 employed Americans required a licence to work. By 2017 that had risen to more than one in five. The trend partly reflects an economic shift towards service industries, in which licences are more common. But it has also been driven by a growing number of professions successfully lobbying state governments to make it harder to enter their industries. Most studies find that licensing requirements raise wages in a profession by around 10%, probably by making it harder for competitors to set up shop.

Lobbyists justify licences by claiming consumers need protection from unqualified providers. In many cases this is obviously a charade. Forty-one states license makeup artists, as if wielding concealer requires government oversight. Thirteen license bartending; in nine, those who wish to pull pints must first pass an exam. Such examples are popular among critics of licensing, because the threat from unlicensed staff in low-skilled jobs seems paltry. Yet they are not representative of the broader harm done by licensing, which affects crowds of more highly educated workers like Ms Varnam. Among those with only a high-school education, 13% are licensed. The figure for those with postgraduate degrees is 45%.

More educated workers reap bigger wage gains from licensing. Writing in the *Journal of Regulatory Economics* in 2017, Morris Kleiner of the University of Minnesota and Evgeny Vorotnikov of Fannie Mae, a government housing agency, found that licensing was associated with wages only 4-5% higher among the lowest earning 30% of workers. Among the highest 30% of earners, the licensing wage boost was 10-24% (see chart 1). Forthcoming research by Mr Kleiner and Evan Soltas, a graduate student at Oxford University, uses different methods and finds no wage boost at the bottom end of the income spectrum, but a substantial boost for higher earners.

One way of telling that many licences are superfluous is the sheer variance in the law across states. About 1,100 occupations are regulated in at least one state, but

fewer than 60 are regulated in all 50, according to a report from 2015 by Barack Obama's White House. Yet a handful of high-earning professions are regulated everywhere. In particular, licences are more common in legal and health-care occupations than in any other (see chart 2).



These professions share two characteristics. First, it takes years of study—and often lots of student debt—to join them. Becoming a doctor takes a four-year undergraduate degree, a four-year postgraduate degree, and then a multi-year medical residency. Those barriers to entry mean that once the law requires the involvement of a doctor, costs soar. Yet it surely does not take all that training, argue nurse practitioners, to know when to prescribe diabetic shoes. The evidence is on their side. A review of the literature in 2012, paid for by the federal government, found that no study raised concerns about the quality of care offered by nurse practitioners. There are plenty of comparison points, because 22 states have overcome doctors' objections and given nurse practitioners so-called "full practice authority".

Second, it is often practitioners themselves who define—and expand—the boundaries of the regulated profession. For example, in North Carolina a board of dentistry, mainly elected by dentists themselves, regulates the profession. In 2006 it tried to stop hygienists and beauticians from whitening customers' teeth, after dentists complained that they were being undercut on price. (The Federal Trade Commission (FTC) objected, and in 2015 the Supreme Court put a stop to the practice by ruling that the board was not exempt from competition law.)

Occupy K Street

Both problems are acute in the legal industry. Almost every American state forbids those who do not have a three-year law degree from providing most legal services. Bar associations—composed of lawyers themselves—often define what counts as legal practice. In 2000 the American Bar Association, after rejecting a proposal to allow lawyers to split fees with non-lawyers, asserted that "the maintenance of a single profession of law" was a core priority. "In no other country does the legal profession exert so much influence over its own regulatory process," writes Deborah Rhode of Stanford University in her book "The Trouble with Lawyers". Outsiders typically cannot even invest in law firms, limiting funding for innovative new business models, such as providing fixed-fee legal advice over the internet, or through retailers. Even those who are qualified can struggle to compete across state boundaries, because of the need to pass a separate bar exam.

Advocates for reform compare America's model unfavourably with that of Britain. There, non-lawyers have a built in majority on legal regulatory bodies, which are tasked with promoting competition as well as protecting consumers. Outside court, anyone can offer legal advice, or provide basic legal services like drafting documents. The result seems to be cheaper access to justice, and more innovation. The World Justice Project ranks America 96th of 113 countries for access to and affordability of justice, sandwiched between Uganda and Cameroon. (It does not help that there is hardly any legal aid.)

American policymakers are increasingly aware of licensing's potential to chill competition. In 2017 the FTC launched a task force on "economic liberty" to campaign against unnecessary licensing. Some states have implemented reforms in recent years. Arizona rolled back some licensing requirements in 2016 and has since made it easier to challenge regulations in court. Last year Mississippi brought its licensing boards under closer supervision. Delaware, Nebraska and Wisconsin are considering proposals for reform.

State courts can also intervene. In 2015 the Texas Supreme Court struck down a law requiring eyebrow-threaders to obtain expensive and unnecessary training in cosmetology. The judges found that the Texas constitution guarantees a minimum level of economic freedom from regulation. Some scholars think such a right can be found in the federal constitution, implicit in the right to "due process". The

federal courts have mostly resisted this idea since a Supreme Court ruling in 1955 gave states plenty of room to regulate their economies as they themselves saw fit. But President Donald Trump's appointments to the federal courts might help "shift the centre of gravity" on the issue, says Dick Carpenter of the Institute of Justice, a libertarian legal charity, optimistically.

When it comes to medicine and law, however, it can be hard to convince the public that some licensing requirements are frivolous. California not only requires that nurse practitioners are supervised by doctors, but also bans doctors from overseeing more than four. Three liberalising bills, which would have given nurse practitioners full-practice authority, have failed since 2007. The California Medical Association, a trade group for doctors, has campaigned hard against reform.

The medical and legal professions account for around a quarter of the top 1% of earners, whose incomes have grown faster in America than in other rich countries in recent decades. A study published in *Health Affairs*, a journal, in June 2015 found that the average doctor earns about 50% more than comparably educated and experienced people in other fields. Another study, from 2012, put the wage premium from working in law at 23%.

Doctors are also unusually well-paid compared with those in other countries. The average general practitioner earns $252,000 and the average specialist $426,000, according to the Bureau of Labour Statistics. According to OECD data on a handful of other rich countries, the averages there were $130,000 for generalists and $273,000 for specialists in 2014. (These figures adjust for differences in living costs, and include only self-employed doctors, who tend to earn more.)

More competition would surely bring both wages and prices down. And less licensing across the board would make entrepreneurship easier. It might even palliate populism, which is partly driven by voters' sense that the economy is rigged to benefit the rich and powerful—a hypothesis which the evidence on licensing plainly supports. Politicians in distant Washington are usually the target of populist anger. But most licensing laws are local. Those looking to level the economic playing field could start closer to home.

This article appeared in the United States section of the print edition under the headline "How to rig an economy"