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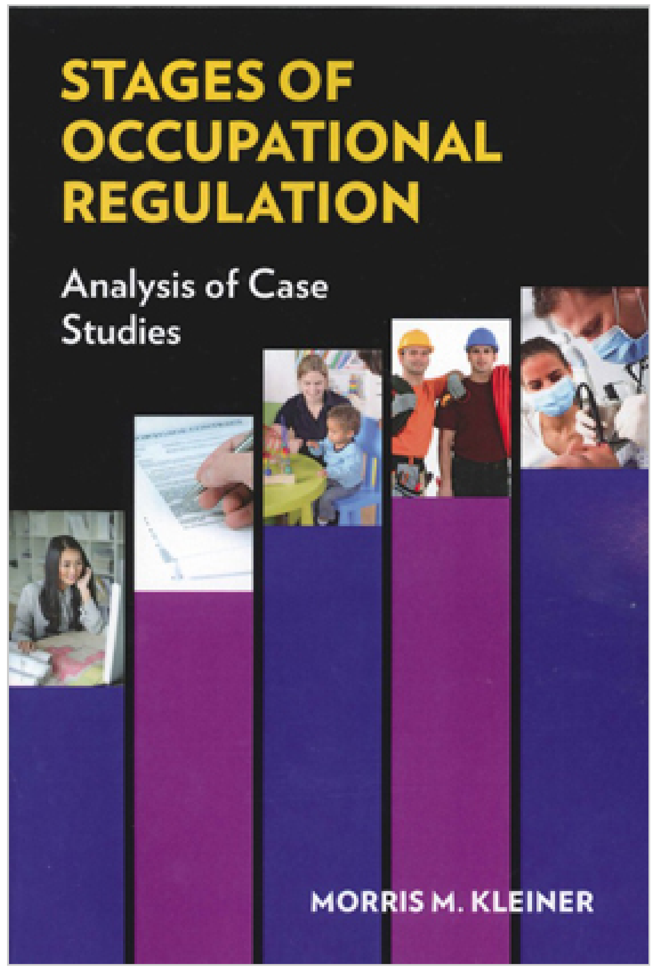
The public costs and private benefits of occupational regulation



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In *Stages of Occupational Regulation: Analysis of Case Studies,* author Morris Kleiner evaluates the effects of occupational regulation from two points of view: (1) the public as a whole, whose interests include health and safety, and (2) incumbent members of the occupation being regulated. Kleiner holds that the surest effect of occupational regulation is to restrict competition and increase wages for incumbents and, simultaneously, make entry into the occupation more difficult. He further observes that in most cases the party seeking to regulate an occupation is not a governmental agency or consumer advocacy group, but a representative of the occupation itself. This is an important book because occupational licensing is more pervasive than many realize: the author notes that nearly 30 percent of U.S. workers are licensed, more than double the number who belong to a union.

To support his position, Kleiner presents five case studies of professional occupations: mortgage brokers, interior designers, dentists and dental hygienists, electricians and plumbers, and preschool teachers. These occupations include the full spectrum of regulation, from interior designers, in the infant phase, to the universally licensed dentists and dental hygienists.

Each chapter provides convincing evidence in support of Kleiner's thesis that occupational regulation often serves private interests rather than the public good, but the chapter on mortgage brokers is particularly illustrative. Given the damage done by the housing crash of the first decade of the 21st century, there is an undeniable societal interest in establishing standards and maintaining order in the mortgage industry. Many mortgages that were originated during that timeframe were done so under highly questionable circumstances, which included misleading promotions, unrealistic appraisals, and risky financial instruments such as adjustable-rate mortgages. Consequently, many Americans took major financial damage: home values plummeted, credit scores were wrecked, and foreclosures skyrocketed.

To the extent that occupational regulation of mortgage brokers could rein in some of these abuses, it would be a worthwhile endeavor. Unfortunately, per Kleiner, there is scarce evidence that the regulation of mortgage brokers produces these types of benefits, because of the way such regulation is typically structured. One of the more common regulations is the requirement to purchase a surety bond—essentially an insurance policy in which brokers pay an annual premium on a bond paid to a third party in the event that the broker is found to be noncompliant with established performance duties. In theory, the bond incentivizes good conduct and safe loan origination. In practice, however, it works to the benefit of those already in the business and to the detriment of those attempting to enter: experienced brokers typically pay a premium of just 1 percent to 2 percent, while those with less experience pay up to 10 percent to 15 percent. Ostensibly, the difference is because less experienced brokers are riskier and thus carry a higher premium, but it also makes entry very difficult and expensive for younger professionals, driving many to reevaluate their decision to enter the occupation and thereby reducing competition. Although higher bonding requirements are in fact associated with a reduction in the number of subprime loans originated, they also are linked to higher interest rates on brokered loans. For brokers already in the occupation, higher interest rates equate to higher earnings, but the benefit to consumers is murky at best.

Interior designers provide another example of an occupation in which legislation has not accomplished its official, publicly stated goals. There is little evidence to suggest that regulating interior designers has improved building safety, for example. Fires, injuries from falling on slippery surfaces, and building collapse rates were found to be no lower in states where interior designers are regulated. There is a small upward wage effect, but because the regulation of this occupation is not overly restrictive (typically consisting of certification rather than licensure), the effect is minor.

Dentists and dental hygienists present an interesting case study. Traditionally, dental hygienists have been required by law to work under the supervision of dentists, but because dentists were the only legally permitted buyer of hygienist labor under the law, it created a monopsony (one buyer, many sellers). This situation enabled dentists to pay lower wages to hygienists than they otherwise would, with a consequent increase in dentists' earnings at the expense of hygienists. Beginning in the late 1970s, the American Dental Hygienist Association attempted to change the status quo by pushing for greater autonomy; in response, the American Dental Association passed a resolution reaffirming its intention to keep hygienists in an auxiliary status. A few states loosened their regulations on hygienists by allowing them to be self-employed and open their own teeth-cleaning offices, while others expanded the list of legally permitted tasks these workers could perform. In these two groups of states, the results were as hoped: hygienists' earnings increased, while dentist earnings simultaneously decreased. Consumers also benefited, as a wider range of service and product options became available. (For instance, patients could purchase sealants directly from a hygienist rather than fillings from a dentist, at about one-tenth the cost.)

Electricians and plumbers are somewhat distinct from the occupations discussed in the other case studies in that regulation is focused on promoting the safety of these workers, in addition to consumers. The results are nonetheless similar: regulation has a much clearer effect on wages than worker safety. There is limited evidence to suggest that regulation shows any improvement in injury rates or severity, for example, while licensing of electricians raises their wages. (The wage effect for plumbers is less clear.)

The case study of preschool teachers appears to run counter to Kleiner's theory, however: educational outcomes have shown improvement in response to certain regulations. In particular, stricter educational attainment requirements for preschool teachers are associated with higher test scores in reading and mathematics for their students. Moreover, wage effects are minimal to undetectable. This case study shows that it is possible for reasonable standards to be set so as to ensure a basic level of quality and safety while not being so restrictive as to deter entry and inflate wages.

One possible reason for the past inattention to this topic is limited availability of data. The author points to a suggestion from the Princeton Data Improvement Initiative which proposes that three simple questions regarding occupational regulation be added to federal statistical surveys (including the Current Population Survey). The addition of these questions to government surveys would provide a better understanding of the scope of occupational regulation and allow for more statistical analysis of the type provided by Kleiner:

1. Do you have a license or certification that is required by a federal, state, or local government agency to do your job?
2. Would someone who does not have a license or certificate be legally allowed to do your job?
3. Is everyone who does your job eventually required to have a license or certification by a federal, state, or local government agency?

This book is an easy read for both research economists and a general audience. The writing is clear, succinct, and well organized. Readers interested in statistical details will find plenty of them, as econometric models and output tables are presented throughout the book and data sources are detailed in the appendices. (No formal background in the field is needed, however, to appreciate the main points of the book.) *Stages of Occupational Regulation: Analysis of Case Studies* is an insightful, useful, and informative book on a topic worthy of more attention.