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Congress of the United States

U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6315

To: Members, Committee on Small Business
From: Committee Staff
Date: July 14, 2014
Re: Full Committee Hearing: "*Barriers to Entrepreneurship: Examining the Anti-Trust Implications of Occupational Licensing*"

On Wednesday, July 16, 2014, at 1:00 pm in Room 2360 of the Rayburn House Office Building, the Committee on Small Business will meet to examine whether the public safety benefits and assurances of competency provided by state licensure requirements outweigh the costs borne by society due to less competition, innovation, and job creation. Specifically, this hearing will focus on the role that the Federal Trade Commission (FTC) plays in combatting the rise in occupational licensure through the enforcement of federal anti-trust laws.

I. Introduction

Entry requirements for jobs and professions stretch back centuries. The notion that those already qualified in a field may seek to capitalize on those skills by self-regulating and requiring specific training, education, or payment of fees in order to gain admission into the field also has a long history. In Adam Smith's 1776 book, *An Inquiry into the Nature and Causes of the Wealth of Nations*, he discusses that learning is necessary for some occupations but how certain laws were enacted, such as the statute of apprenticeships, that "obstructs the free circulation of labour."[1] These statutes allowed certain professions to utilize government power to inflate their own worth by making entry into the profession difficult and ultimately restricting competition.[2]

Centuries later, the phenomenon identified by Mr. Smith has come into full bloom in the United States. In 1950, fewer than 5 percent of all occupations were licensed at the state level;[3] yet today, an estimated 29 percent of occupations are licensed, or approximately 1 in 3 occupations.[4] Today, a wide variety of occupations require licensure in some or many states

[1] ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS, bk. 1, ch. 10, pt. II (1776).
[2] *Id.* at ch. 10.
[3] Morris M. Kleiner and Alan B. Krueger, *The Prevalence and Effects of Occupational Licensing*, 48 BRIT. J. INDUS. REL. 651, 679 (2010), *available at* http://www.hhh.umn.edu/people/mkleiner/pdf/Prevalence_of_Occupational_lisc.pdf.
[4] *Id.* at 9; *accord* DICK M. CARPENTER, ET. AL., THE INSTITUTE FOR JUSTICE, LICENSE TO WORK: A NATIONAL STUDY OF THE BURDENS FROM OCCUPATIONAL LICENSING 6 (2012), *available at* https://www.ij.org/images/pdf_folder/economic_liberty/occupational_licensing/licensetowork.pdf.

including: animal trainers; barbers; bartenders; funeral attendants; home entertainment system installers; interior decorators; makeup artists; travel agents; and upholsterers.[5]

There are generally three forms of occupational regulation.[6] The least restrictive form is registration, in which individuals file their names, addresses, and qualifications with a government entity.[7] The next form is certification, in which a government agency or private entity administers an examination and certifies the individual's competency.[8] The most restrictive form is licensure;[9] this may include fees, education and training, examinations, minimum grade-level education requirements, and age restrictions.[10]

While the growth of licensing may provide benefits to the public, there also are potential costs associated with limiting competition in various businesses.[11] According to one study, the total cost of licensing regulations to the economy is between $34.8 billion to $41.7 billion per year.[12] Occupational licensing also may impede innovation and business development as would-be entrepreneurs focus their resources on meeting licensing board requirements rather than on meeting the needs of their businesses or customers.[13] A June 2014 study even found occupational licensing was the number one regulatory burden facing small firms.[14]

A Subcommittee hearing on March 26, 2014, examined whether the public safety benefits and assurances of competency provided by state licensure requirements outweigh the costs borne by society due to less competition, innovation and job creation.[15] Rather than repastinating the ideas elucidated in the memorandum accompanying the prior Subcommittee hearing, this memorandum will focus on the role that federal agencies, particularly the FTC, plays in combatting the rise in occupational licensure through enforcement of federal anti-trust laws.

II. Anti-trust Laws and State Action Immunity

The United States has three primary anti-trust laws: the Sherman Act, the Clayton Act, and the FTC Act. Broadly, "anti-trust laws proscribe unlawful mergers and business practices in general terms, leaving courts to decide which ones are illegal based on the facts of each case."[16] The Sherman Act prohibits agreements that restrain commerce and makes it unlawful to or

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[5] Carpenter, *supra* note 4, at 10-11. This is in addition to numerous learned professions that require licenses such as: physicians, attorneys, architects, public accountants, and professional engineers.
[6] Kleiner & Krueger, *supra* note 3, at 1.
[7] *Id.* In addition, the registration process may include posting a bond or filing a fee.
[8] *Id.* at 2.
[9] *Id.*
[10] Carpenter, *supra* note 4, at 7.
[11] http://www.econlib.org/library/Enc1/OccupationalLicensing.html.
[12] ADAM SUMMERS, REASON FOUNDATION, OCCUPATIONAL LICENSING: RANKING THE STATES AND EXPLORING ALTERNATIVES 36 (2007), *available at* http://reason.org/files/762c8fe96431b6fa5e27ca64eaa1818b.pdf.
[13] *Id.* at 22.
[14] http://www.thumbtack.com/survey#/2014/1/states; *see e.g.,* Gabrielle Karol, *Survey: Licensing Regulations Biggest Pain for SMBs,* FOXBUSINESS, June 11, 2014, *available at* http://smallbusiness.foxbusiness.com/finance-accounting/2014/06/11/survey-licensing-regulations-biggest-pain-for-smbs/.
[15] *Barriers to Opportunity: Do Occupational Licensing Laws Unfairly Limit Entrepreneurship and Jobs: Hearing Before Subcomm. on Contracting and Workforce of the H. Comm. on Small Business,* 113th Cong., 2nd Sess. (2014).
[16] http://www.ftc.gov/tips-advice/competition-guidance/guide-antitrust-laws/antitrust-laws.

attempt to monopolize competitive markets.[17] The Supreme Court has narrowed the breadth of the Sherman Act to those restraints of trade that are unreasonable.[18] The Clayton Act passed subsequently supplements the Sherman Act by, for example, clearly prohibiting anti-competitive mergers.[19] Finally, there is the FTC Act, which created the FTC and broadly empowers the FTC to prevent unfair methods of competition from being used in or affecting commerce.[20] Additionally, the Supreme Court has found that all violations of the Sherman Act also violate the FTC Act and therefore the FTC is broadly responsible for enforcing the Sherman Act.[21]

As more professions require occupational licensing, questions have been raised whether state licensing boards, typically made up of private actors within the profession, unfairly restrict competition and violate federal anti-trust laws. Under the FTC's aforementioned enforcement authority, the FTC has the power to question these state licensure laws. Using the power of the FTC Act, the agency has brought enforcement action against state licensure boards as potential anti-trust violations by private actors unlawfully restraining trade in various occupations.

However, the ability of the FTC to take action against state licensing laws is circumscribed by Supreme Court decisions that limit the scope and application of the anti-trust laws. This limitation is known as "state action immunity," articulated by Supreme Court in *Parker v. Brown*.[22] In that case, California passed the California Agricultural Prorate Act, intended to "conserve the agricultural wealth of the State."[23] As raisins were a crop primarily produced in California and the bulk was shipped to other states, California sought to restrict competition and maintain prices among growers and packers by restricting the quantity of raisins available in the market.[24] Despite, its anti-competitive effects on the market, the Supreme Court found that given the United States dual system of federalism, there was no evidence to suggest Congress had meant to limit states' ability to engage in anti-competitive activities.[25] Since California acting in its official sovereign state capacity sought to restrict competition, the Supreme Court ultimately found that it could not be subject to the anti-trust restrictions under the Sherman Act which applies to private actors.[26] However, "in holding that the Sherman Act does not apply to state government action, the Court found the identity of the actor – the state or private citizens – essential but provided no guidance on how to draw the line."[27]

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[17] 15 U.S.C. §§ 1-2.
[18] *State Oil Co v. Khan*, 522 U.S. 3, 10 (1997); *see e.g. Standard Oil. Co. v. United States*, 221,U.S. 1, 95-105 (1911).
[19] 15 U.S.C. §§ 12-27
[20] 15 U.S.C. §§ 41-58.
[21] http://www.ftc.gov/tips-advice/competition-guidance/guide-antitrust-laws/antitrust-laws. Together the Sherman, Clayton, and FTC Acts are referred to as the anti-trust laws. http://www.justice.gov/atr/about/antitrust-laws.html.
[22] 317 U.S. 341 (1943).
[23] *Id.* at 346.
[24] *Id.* at 344-47. A similar restraint is imposed on raisin markets through federal law. *See Horne v. United States Dep't of Agric.*, 133 U.S. 2053, 2054 (2013).
[25] *Id.* at 350-51.
[26] *Id.* at 350-52.
[27] Aaron Edlin & Rebecca Haw, *Cartels By Another Name: Should Licensed Occupations Face Antitrust Scrutiny?*, 162 U. PA. L. REV. 1093, 1119 (2014); *see also Parker,* at 352.

The state action immunity doctrine as articulated in *Parker v. Brown* was revisited in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum Inc.*[28] In that case, the Supreme Court expanded on the doctrine by articulating a two-prong test for state action immunity, particularly where private actors are involved.[29] "First, the challenged restraint must be 'one clearly articulated and affirmatively expressed as state policy'; second, the policy must be 'actively supervised' by the state itself."[30]

For the first prong of *Midcal* to be satisfied, instead of establishing a bright line rule, the Court has "described a general methodology and provided individual points of reference against which other fact patterns must be compared."[31] This prong generally is met if the state offers a clear articulation demonstrating that "the State as sovereign clearly intends to displace competition in a particular field with a regulatory structure."[32]

States have a more difficult burden in demonstrating the "active supervision" prong of *Midcal*. To satisfy this prong states must show that they play a "substantial role in determining the specifics of the economic policy."[33] The "purpose is to determine whether the State has exercised sufficient independent judgment and control so that the details of the rates or prices have been established as product of deliberate state intervention, not simply by agreement among private parties."[34]

III. Licensing Boards Under the State Action Immunity Doctrine

When examining occupational licensing boards in light of the two-prong test provided under *Midcal*, it appears evident that the majority of these boards will meet the first prong.[35] The majority of licensing boards are created by a state statute pursuant to a legitimate public policy goal. For example, states have a legitimate interest in protecting the health and welfare of their citizens. The need to protect health and welfare is patently obvious to ensure that a neurosurgeon is competent to operate on a brain or a professional engineer to ensure that buildings or bridges do not collapse. On the other hand, rational public policy articulation may be more challenging for occupations, such as interior designers or florists, whose occupations do not readily invoke images requiring public welfare protection.

However, the second prong proves far more burdensome as states may be unable to demonstrate active supervision. The theory underpinning occupational licensing is that those regulating entry are unbiased arbiters of standards and conduct. However, in many states a majority or even super-majority of these regulatory officials are comprised of practitioners.[36] To the extent that regulatory boards are made up of practitioners (who clearly understand the expertise needed to practice their particular profession or occupation), their personal vested

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[28] 445 U.S. 97 (1980).
[29] *Id.* at 97.
[30] *Id.* at 105.
[31] OFFICE OF POLICY PLANNING, FTC, REPORT OF THE STATE ACTION TASK FORCE 9 (2003).
[32] *Southern Motor Carriers Rate Conference, Inc. v. United States*, 471 U.S. 48, 64 (1985).
[33] *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 635 (1992).
[34] *Id.* at 634.
[35] Edlin & Haw, *supra* note 27, at 1123.
[36] SUMMERS, *supra* note 12, at 18.

interest in protecting their own income may lead them to impose conditions to entry that restrict potential competitors rather than protect health or safety of state citizens.[37] Furthermore, if regulatory boards are comprised of members of the particular profession or occupation, they may be reluctant to discipline their compatriots, thus undermining the argument that licensure protects consumers from bad actors.[38]

Given this, if a state allows occupational licensing requirements to be determined by private actors, it would appear that the necessary element articulated in *Parker v. Brown* - that the state actor be directing the anti-competitive policy - fails. If the state does not engage in active supervision, but rather allows various private actors to engage in anti-competitive activities under the "gauzy cloak of state involvement,"[39] the standard articulated under *Midcal* is likely not being met.

IV. FTC's Role

As previously mentioned, the nation's anti-trust laws, are enforced by the FTC,[40] although the FTC is more broadly authorized to challenge unfair methods of competition.[41] As occupational licensing boards have become more common place, the FTC has considered various approaches to ensure clarity and consistency in the application of the state action immunity doctrine. For example, the FTC's Office of Policy Planning convened a State Action Task Force and in 2003 released a report detailing various concerns over the anti-competitive effects of state licensure laws and made recommendations for improvement. Further, the FTC has utilized its ability to file amicus briefs and issue administrative complaints to attempt to prevent state occupational licensing boards from circumventing anti-trust laws and generally engaging in unfair methods of competition.

Recently, the FTC found the North Carolina Dental Board in violation of anti-trust laws, due to an exclusion of non-dentists from providing teeth whitening services.[42] The North Carolina Dental Board was established by the state to protect "public health, safety, and welfare."[43] The eight-member board is primarily composed of six dentists elected by state-licensed dentists, one dental hygienists elected by state-licensed dental hygienists, and one consumer appointed by the Governor.[44] The Board is funded by licensing fees paid by dentists and dental hygienists.[45] Given the Dental Board's state statutory creation, the Dental Board argued that it was exempt under state action immunity.[46] However, the FTC held and the Fourth Circuit agreed, that "when a state agency is operated by market participants who are elected by other market participants, it is a 'private' actor. Accordingly, it is required to satisfy both *Midcal*

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[37] *Id.*
[38] *Id.* at 11.
[39] *Midcal,* 445 U.S. at 106; *see also* OFFICE OF POLICY PLANNING, *supra* note 31, at 14.
[40] This authority is shared with the United States Department of Justice.
[41] The FTC is empowered to prevent unfair methods of competition from being used in or affecting commerce. 15 U.S.C. § 45.
[42] *In re N.C. Bd. of Dental Examiners,* 152 F.T.C. 640 (2011).
[43] *N.C. State Bd. of Dental Examiners v. FTC,* 717 F.3d 359, 364 (4th Cir. 2013), *cert. granted,* 134 S. Ct. 1491 (U.S. Mar. 3, 2014) (No. 13-534).
[44] *Id.*
[45] *Id.*
[46] *Id.* at 366.

prongs to obtain the *Parker* exemption."[47] Further, the Fourth Circuit upheld the FTC's ruling that the second prong of active-supervision could not be satisfied.[48] In this case, the court found a lack of active supervision because the Dental Board sent cease-and-desist absent any state oversight and without required judicial approval.[49] Given the implications this has on occupational licensing and more broadly the state action immunity doctrine, it was granted certiorari by the Supreme Court and will be heard later this year. It is likely the Supreme Court's ruling will have significant implications for occupational licensing boards moving forward.

V. Conclusion

America has always been a land of opportunity where competition and innovation have reigned supreme. But today, occupational licensing boards propped up through the colorable actions of a state yet ultimately run by individuals within that profession may utilize bureaucratic and unnecessary requirements to reduce entry and limit competition in the field. The impact on potential participants is obvious as an individual may be unable to pursue an entrepreneurial endeavor as they are unable to overcome various regulatory hurdles and increased costs. Yet, decreased competition in the market negatively affects consumers who are left with fewer options and alternatives. In certain instances, the public policy rationale for states to do this is common sense – competent and trained surgeons for example. But the concept of protecting public health and safety may have been utilized to permit self-regulation of occupations that achieve, not the protection of the public, but the economic health of the private actors in a particular occupation. Proper assessment of the state action immunity doctrine should ensure that occupational licensing is an active exercise of state sovereignty and not the imposition of an unreasonable restraint of trade by private actors.

[47] *Id.* at 370.
[48] *Id.*
[49] *Id.*