The Incidence of Occupational Licensing

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Abstract

Occupational licensing is a significant labor market institution, affecting directly at least one fifth of the US workers. For licensed occupations, professional practice without a license is illegal, and in the US, each state determines which occupations it licenses and which restrictions its licenses impose. Though licensing has the potential for extensive impacts on employment and consumption, little is yet know about its macroeconomic consequences. In this study, I quantify the incidence of licensing in the United States. For each occupation that is partially licensed, I quantify how licensing affects the consumption of households and earnings of workers of different income levels.

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1 Introduction

1.1 Occupational licensing is important to study

Occupational, or professional, licensing may be the most significant labor market institution, directly affecting at least one fifth of the American labor force (Kleiner, 2000). Allensworth (2025), a legal scholar, defines professional licensing as "a government-granted privilege to work that's given after a significant investment in human capital measured in months or years, without which professional practice is illegal." Because licensing regulates so many workers, it has the potential for great positive or negative effect on economic welfare. For instance, in *Federal Trade Commission v. North Carolina Board of Dental Examiners* the US Supreme Court opined that "professional licensing boards are cartels" such that "board members can be sued [...] for antitrust violations" when licensing restrictions benefit professionals at too high a cost to consumers (Allensworth, 2025). Economics literature, thus, has a great gap in its lack of understanding of how licensing affects households and workers of different income levels.

I contribute to our understanding of occupational licensing in two ways. First, I will estimate how licensing — across all states and occupations — affects the economic welfare of households and workers focusing on consequences to employment, affordability, and quality of services. Second, I will investigate the causes of variation in licensing policy across states and occupations in the US.

My hope is to contribute to what I see as the constitutional economics question facing occupational licensing (Brennan and Buchanan, 1985). Ostensibly, the purpose of occupational licensing is to ensure quality and safety. But there are alternatives to accomplish this purpose: from the broad tool that is tort law to the extreme specificity of safety regulations, such as codified rules about sanitation practices that restaurants must follow (Allensworth, 2025). Is the constitutional set up of licensing, which since *Dent v. West Virginia* (1899) has allowed states to form licensing boards that control entry into professions, ideal? Or can we improve upon it? For instance, the recent *Chiles v. Salazar* Supreme Court case has the potential to federally limit licensing insofar as licensing restrictions run against free speech (Barnett, 2024). It is pertinent to consider constitutional limits on the barriers of entry that licensing can impose. By studying the consequences of licensing, I hope to provide information on whether change is desirable. And by studying the causes of licensing policy, I hope to provide information on how change might be possible.

In posing the question at a broad, macroeconomic level, rather than investigating a selection of occupations, I am motivated by the ultimate goal of informing the public about the constitutional question facing licensing. At the level of an occupation in a state, licensing is already the result of political pressure mounted by occupational associations. We must assess how large are the possible net costs of licensing throughout the nation — so that society can decide whether it is desirable to effect better norms and incentives at the constitutional level, rather than adjusting licensing in each occupation and state.

1.2 Consequences: is change desirable?

I study the consequences of licensing by asking, for each state and each occupation, how are quality, employment, and affordability affected by licensing? To assess quality and affordability, I estimate demand for the services of an occupation and infer how licensing affects how much households in different income groups are willing to pay for such services. To asses employment, I put together estimates of demand and occupational labor supply to infer how licensing affects net earnings for workers with different skills. For each of partially licensed occupation, I leverage the variation in licensing status across states to identify structural parameters that allow me to compare outcomes of licensing status of some occupation in some state to the counterfactual. For fully licensed occupations, such as medicine and law, I am restricted to more to less strict licensing requirements.

Explicitly, my rhetoric is this: First, I wish to persuade you that my theory succeeds formally in identifying the relevant moving parts for determining the effect of licensing on household and worker welfare; Second, the theory is constituted quantitatively by micro data with variation across occupations, states, and metropolitan areas — which should help give you confidence that the theory's predictions are of adequate order of magnitude and direction; Third, I will show that the theory indeed gives adequate predictions about facts that are not directly targeted, and this should serve as inductive evidence that my theory is also adequate for the — by construction impossible to test — predictions on incidence.

2 Theory: market competition and licensing

2.1 Counterfactuals: licensed vs. unlicensed occupation in a state

The key features of the incidence of occupational licensing are captured by a simple model of supply and demand for occupations. The subscript U denotes the unlicensed counterfactual while the subscript L denotes the licensed counterfactual. Licensing affects economic outcomes in virtue of changing the quality perceived by consumers and the costs born by workers. Hence, the formal structure of the model is the same between the licensed and unlicensed case, with licensing exclusively affecting parameter values.

Our data will feature occupation markets segmented geographically by metropolitan areas (MSA). Hence, focus on an occupation i in an area a. For now we assume an exogenous distribution of workers across locations. Throughout, we normalize the lower bound of efficiency units for each occupation i to $z_{\min} = 1$.

2.2 Household choice

2.2.1 The theory of quality demand

We want to speak about the benefits to households of higher quality services against costs in terms of higher prices. To speak about quality, we must differentiate it from quantity. For some reason, different people choose to consume goods and services of different quality — rather than merely varying the quantity they consume of some given category. Some people spend hundreds of dollars on a single haircut while others spend USD $15 on a haircut.

It must be that quantity is not a perfect substitute for quality. There is no market for 5 minutes of a USD $200 haircut; and the person who pays hundreds of dollars for a haircut would not be satisfied with tens of USD $15 haircuts one immediately after another. Hair just doesn't grow that fast. The quality and quantity distinction is borne out of constraints on the quantity of consumption. Just like you cannot drive two cars at the same time, you do not get several haircuts one immediately after the other. This is the logic of the discrete choice model presented in Jaffe et al. (2019). In the simplest formulation, a consumer chooses which quality of a good or service they wish to buy, but she is physically constrained to buy at most one unit of it.

Moreover, much of quality variation seems intuitively to do with income. A rich person gets her tooth extracted by a well-reviewed oral surgeon while the extremely poor, even in America, often extract their own teeth[1]. Hence, letting income summarize heterogeneity between consumers, the problem of a consumer who chooses quality is

$$\max_{v} \; U(m - p(v), v)$$

where m is income, v is quality, and $p(v)$ is the price of quality. Following our observation that income determines much of quality consumption, we make one critical assumption: quality is a normal good. Formally, the higher income you have, the more you are willing to spend on a quality upgrade. This can be represented mathematically in two equivalent ways. The first is in terms of the equivalent variation: for two quality varieties of the same service, $\bar{v} > \underline{v}$, the price R which makes you indifferent between the varieties increases in income.

$$\frac{dR}{dM} > 0 \quad \text{where } R \text{ is defined implicitly by} \quad U(m - R, \bar{v}) = U(m, \underline{v})$$

By the implicit function theorem, normality is equivalent to the condition that the marginal utility of income be greater for the point with higher quality and lower leftover income y:

$$\frac{dR}{dm} > 0 \Leftrightarrow 1 - \frac{U_y(m, \underline{v})}{U_y(m - R, \bar{v})} > 0 \Leftrightarrow U_y(m - R, \bar{v}) > U_y(m, \underline{v})$$

Moreover, our condition on the marginal utility of income is equivalent to this: if I increase quality v along a consumer's indifference curve (so that I must be decreasing expenditure on other goods y), the marginal utility of income must increase. Mathematically, for R defined as above,

$$U_y(m - R, \bar{v}) > U_y(m, \underline{v}) \quad \Leftrightarrow \quad \frac{d}{dv} U_y(y(v), v)|_{U=\bar{U}} > 0$$

Finally, we can use this requirement to discover restrictions on our utility function. In particular,

$$\frac{d}{dv} U_y(y(v), v)|_{U=\bar{U}} > 0 \quad \Leftrightarrow \quad U_y U_{yv} - U_{yy} U_v > 0$$

This restriction becomes practically useful once we make an additional assumption: addi-

tive separability, $U_{yv} = 0$. Economically, this assumption keeps our framework simple by having that quality changes the level of utility (higher quality is preferred, ceteris paribus, by everyone) but it does not change the marginal utility of income. This way we focus on how income affects choices not through its effect on tastes but merely through the budget constraint. With additive separability, quality normality restricts us to diminishing marginal utility of income $U_{yy} < 0$. With these assumptions we arrive at

$$U(m - p(v), v) = u(m - p(v)) + v \quad \text{where } u \text{ is strictly concave}$$

2.2.2 Because quality is normal, licensing is a Regressive Regulation

We want to evaluate the consequences of licensing in terms of its ostensible purpose as well as important ostensibly unintended — though plausibly politically intended — economic consequences. Hence, we interpret licensing as regulation which has an ostensible purpose of increasing equilibrium quality v at a potential increase in the entry opportunity cost c. A strong implication of quality being normal, $R'(m) > 0$, is that any regulation which increases the only available quality will tend to be a Regressive Regulation. This comes from standard price theory.

In particular, define licensing as a regulation which affects parameters as follows: $\Delta c \geq 0$ and $\Delta > 0$. Without any extra assumptions, we can conclude that $\Delta S \leq 0$ and $\Delta D > 0$. Therefore, it must be that $\Delta p \geq 0$. Therefore, with very mild assumptions, as long as licensing accomplishes its ostensible goal, $\Delta v > 0$, it must also imply prices increase, $\Delta p \geq 0$.

Recall that quality normality is characterized by the equivalent variation $R(m)$ being a strictly increasing function. Welfare change from licensing is

$$\Delta W(m) = U(m - \bar{p}, \bar{v}) - U(m - \underline{p}, \underline{v})$$

Notice that for everyone whose income is high enough in baseline to buy $\underline{v}$ relative to not consuming the good,

$$\Delta W(m) \geq 0 \quad \Leftrightarrow \quad \Delta p \leq R(m)$$

We can conclude the following about the welfare effects of licensing. For everyone too poor to not buy the good at baseline, licensing has no effect. But for everyone with enough wealth that they buy the good in baseline, $\Delta p \leq R(m)$ characterizes the welfare effect of licensing. Licensing is a Regressive Regulation in that there are only three alternatives: either everyone is harmed, or everyone is benefited, or there is an income threshold such that all above it are benefited and all below it are harmed.

2.2.3 Probabilistic household choice over one service

A household in area a who has income m chooses whether to consume the services of occupation i by comparing

$$\max \{u_i(m - p_{ia}\bar{q}_i) + v_{ia}, u_i(m) + \mu_0\}$$

where u_i is a potentially occupation-specific utility of leftover income (e.g., u_i may be CRRA characterized by parameter γ_i), $\bar{q}_i$ are efficiency units per buying household purchases (assumed fixed across households for a given occupation i), and μ_0 is a household-specific taste shock. For mathematical tractability assume μ_0 is i.i.d. Type-I extreme value with normalized scale and location. A household buys the services of occupation i whenever

$$u_i(m - p_{ia}\bar{q}_i) - u_i(m) + v_{ia} \geq \mu_0$$

Define the utility cost of the service expenditure

$$\Delta u_i(m, p_{ia}) \equiv u_i(m) - u_i(m - p_{ia}\bar{q}_i) > 0$$

where the i index in Δu_i captures both how the curvature of u_i depends on the occupation as well as what is the fixed number of efficiency units per purchasing household for that occupation, $\bar{q}_i$. The probability that a household in area a who has income m purchases the services of occupation i is

$$\Pr_{ia}(\text{buy } i \mid v_{ia}, p_{ia}; m) = \Lambda\left(v_{ia} - \Delta u_i(m, p_{ia})\right)$$

The share of households who purchase the services of occupation i is

$$s_{ia}^D(p_{ia}, v_{ia}) = \int \Lambda\left(v_{ia} - \Delta u_i(m, p_{ia})\right) dF_a(m)$$

Where N_a is the number of households in the area and $F_a(m)$ is the income distribution of households in area a. Hence, the demand curve in efficiency units is

$$D_{ia}(v_{ia}, p_{ia}) = N_a \ \bar{q}_i \ s_{ia}^D(p_{ia}, v_{ia})$$

2.3 Worker choice

2.3.1 Probabilistic worker choice over one occupation

Similar to a Roy model, we look at a worker who chooses between occupation i and some general alternative. The worker is thus characterized by a pair of talent in occupation i denominated in efficiency units, z_i, and a taste (or pecuniary) shock for the alternative, z_0. We assume talent in i and the shock for the alternative are drawn independently. In particular, for mathematical tractability assume z_0 is i.i.d. Type-I extreme value with normalized scale and location. To work in occupation i, the worker must surmount a flow aggregate of barriers, $f_{ia} + \delta_{ia} r_{ia}$, where f_{ia} are any occupation-area specific fixed costs, δ_{ia} indicates whether area a licenses the services of occupation i, and r_{ia} are measured annualized fixed costs imposed by licensing (e.g., training, testing, fees). By working in occupation i, the worker earns a flow income of $p_{ia} z_i$. The value of the alternative depends on state characteristics such as the minimum and median wages, summarized by $\eta_i X_a$. Hence, the worker in area a chooses an occupation by comparing,

$$\max\left\{p_{ia} z_i - f_{ia} - \delta_{ia} r_{ia}, \eta_i X_a + z_0\right\}$$

Denote by $c_{ia} = f_{ia} + \delta_{ia} r_{ia} + \eta_i X_a$ the full non-random opportunity cost of working in occupation i. The worker chooses occupation i if and only if

$$p_{ia} z_i - c_{ia} \geq z_0$$

Therefore, the probability that a worker from area a who has efficiency units z_i chooses occupation i is

$$\Pr_{ia}(\text{choose } i \mid z_i) = \Lambda(p_{ia} z_i - c_{ia})$$

where $\Lambda(x) = \frac{1}{1+e^{-x}}$ is the logistic function. The share of workers of area a in occupation i is $s^S_{ia}(p_{ia}, c_{ia}) \equiv L_{ia}/L_a$ where L_{ia} is the number of workers in occupation i and L_a is the area employment count,

$$s^S_{ia}(p_{ia}, c_{ia}) = \int \Lambda(p_{ia} z_i - c_{ia}) dF_i(z_i)$$

We observe the wage-bill occupation i in area a,

$$Y_{ia} = p_{ia} L_a \int z_i \ \Lambda(p_{is} z_i - c_{ia}) dF_i(z_i)$$

Hence, the supply of efficiency units of occupation i in area a is

$$S_{ia}(p_{ia}, c_{ia}) = \frac{Y_{ia}}{p_{ia}}$$

2.4 Equilibrium

2.4.1 Market clearing

Given parameters $c_{ia}, v_{ia}, F_a(m), F_i(z), u_i, \bar{q}_i$, an equilibrium is a price p_{ia} and quantity of traded efficiency units of occupation i in area a such that markets clear

$$\frac{Y_{ia}(p_{ia}, c_{ia})}{p_{ia}} = S_{ia}(p_{ia}, c_{ia}) = D_{ia}(v_{ia}, p_{ia}) = N_a \ \bar{q}_i \ s^D_{ia}(p_{ia}, v_{ia})$$

2.4.2 Counterfactuals

We are interested in the extensive margin and intensive margin effects of occupational licensing. For occupations which are licensed in some states but not in others, the counterfactual for a state that licenses a given occupation and imposes a certain set of restrictions is that same state but with no license and therefore no legal practice restrictions. Instead, for occupations which are licensed in every state, such as doctors, the counterfactual can at most be a lower level of licensing. One such alternative is to compare a given state to what it would have been were it to have as many restrictions as the state with the fewest restrictions in that occupation.

We use the observed equilibrium price p_{ia}^0 and our identified model to solve for the counterfactual equilibrium price p_{ia}^1. The exogenous change that moves us from factual to counterfactual moves opportunity cost c_{ia} and quality v_{ia}. Opportunity cost changes according to $c_{ia}^1 = c_{ia}^0 - r_{ia}$, where we remove the added licensing burden r_{ia} in the case where we go from an area where the occupation is in fact licensed to the counterfactual where it would be unlicensed. Quality changes according to $v_{ia}^1 = v_{ia}^0 - \nu_i$, where ν_i is the licensing premium (which may be negative).

Welfare analysis depends on the price change, the licensing burden r_{ia} and the licensing quality premium ν_i. Since we observe r_{ia}, what we need is to identify ν_i and the price change $p_{ia}^1 - p_{ia}^0$.

Household welfare

For households, equivalent variation measures the consequences of licensing.

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Worker welfare

For workers, net income change measures the consequences of licensing.

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2.4.3 Caveats

3 Identification

Once we estimate structural parameters, our structural model constitutes a quantitative theory for how licensing affects equilibrium outcomes and economic welfare[2]. Identification relies on three types of variation in the data: occupation $i \in I$, state $s \in S$ and and metropolitan area $a \in s$.

3.1 Unknowns

3.1.1 Structural parameters

1. Occupation: quality parameters v_i^U, v_i^L; skill distribution F_i (e.g., Pareto shape ξ_i); utility function u_i (e.g., γ_i CRRA parameter); labor market index coefficient η_i.

2. Occupation-area: fixed cost f_{ia}.

3. Common or normalized: worker and household shock distributions assumed Type-I extreme value with normalized scale and location; Pareto minimum $z_{\min}^i = 1$.

3.1.2 Latent variables

The price in dollars per efficiency unit, p_{ia}, is not directly observed and must instead be inferred from an identity between observables.

3.2 Data

1. Area: household population N_a, household income distribution $F_a(m)$, employment L_a, labor market index X_a.

2. Occupation-area: occupational employment L_{ia}; occupational earnings distribution $G_{ia}(y)$, and total occupational income Y_{ia}.

3. Occupation-state: measured licensing burden $r_{ia} = r_i(s(a))$; licensing status $\delta_{ia} = \delta_i(s(a))$ (yes or no).

3.3 Mapping moments to parameters

3.3.1 Earnings distribution identifies skill distribution

Because $\Lambda(y - c_{ia}) \to 1$ as $y \to \infty$, we can identify the shape parameter, ξ_i, of the skill distribution F_i from the right tail of the earnings distribution. With limited data, we will approximate with the 75th and 90th quantiles. Then the ratio of quantiles identifies (approximately) the shape parameter ξ_i,

$$\frac{Q^y(0.9)}{Q^y(0.75)} = \left(\frac{1-0.75}{1-0.9}\right)^{1/\xi_i}$$

By assuming the latent skill distribution for an occupation F_i is common across areas, we can pool the right tails of occupation i's earnings distributions across all areas a in all states s to obtain a more robust estimate. In particular, given our rough final sample approximation, we can pick a relatively low quantile of the distribution of estimated ξ_i as our estimate.

3.3.2 Earnings scale identifies price

Based on the same asymptotic argument as above, for a high τ-quantile, $Q^y_{ia}(\tau)$ of the worker earnings distribution, we have

$$p_{ia} \approx Q^y_{ia}(\tau)(1-\tau)^{1/\xi_i}$$

We approximately identify the price of an efficiency unit, p_{ia}, from the 75th quantile (or 90th quantile).

3.3.3 Worker shares identify the non-random opportunity cost

Once we have identified F_i and p_{ia}, the occupation-area worker share can be inverted to identify the non-random opportunity cost of entry.

$$\frac{L_{ia}}{L_a} = \int \Lambda(p_{ia}z - c_{ia})dF_i(z)$$

3.3.4 State and area variation disentangles the opportunity cost of entry

From the non-random opportunity cost of entry, c_{ia}, we want to separately obtain the occupation-area cost f_{ia} and the index of labor market characteristics $\eta_i X_a$. Since r_{ia} and δ_{ia} are observed, we can write

$$c_{ia} - \delta_i(s(a))r_i(s(a)) = \eta_i X_a + f_{ia}$$

where f_{ia} empirically captures any and all variation in opportunity costs c_{ia} that is not explained by either local labor market characteristics X_a or licensing policy r_{ia}.

An alternative approach here is to let r_{ia} be the entire vector of observed licensing requirements (experience, training, fees, exams) and estimate the vector of coefficients β_i with the regression

$$c_{ia} = \eta_i X_a + \beta_i r_i(s(a)) + f_{ia}$$

3.3.5 Identify quality and utility from area and state variation

Expenditure per purchasing household, $p_{ia}\bar{q}_i$, is specific to an occupation and metro-area. We identify $\bar{q}_i$ and the vector (u_i, v_i^U, v_i^L) jointly from the cross-section. In particular, the wage bill divided by the total number of households lets us identify efficiency units per purchasing household $\bar{q}_i$ for a candidate vector (u_i, v_i^U, v_i^L):

$$\frac{Y_{ia}}{N_a p_{ia}} = \bar{q}_i \; s_{ia}^D(p_{ia}, v_{ia}) \; \forall i, a$$

Therefore, we can estimate the vector $(\bar{q}_i, u_i, v_i^U, v_i^L)$ by GMM on this system of equations. Recall that

$$s_{ia}^D(p_{ia}, v_{ia}) = \int \Lambda\left(v_{ia} - \Delta u_i(m, p_{ia})\right) dF_a(m)$$
$$\Delta u_i(m, p_{ia}) = u_i(m) - u_i(m - p_{ia}\bar{q}_i) > 0$$

4 Data

WIP Deprecated. Needs to be updated for MSA strategy.

4.1 Minimum data requirements

Table 1 clarifies the minimum data required for quantification. We use Archbridge Institute (2025) for licensing burden and status. The remaining data are available from the American Community Survey.

5 Results

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Table 1: Minimum Data Requirements by State and Occupation (2023)

Level	Object	Notation	Data source and variables
State s	Population	N_s	ACS (IPUMS): `HWEIGHT` by `STATEFIP`
	Income dist.	$F_s(m)$	ACS (IPUMS): `HHINCOME`, `HWEIGHT`, `STATEFIP`
	Labor force	L_s	ACS (IPUMS): `EMPSTAT`$\in \{1, 2\}$, `PERWT`, `STATEFIP`
	Wage shifters	X_s	ACS (IPUMS): `INCWAGE`, `PERWT` used to compute state median and p10 wages
$i \times s$	Occ. employment	L_{is}	ACS (IPUMS): `OCCSOC` (6-digit SOC), `EMPSTAT`=1, `PERWT`, `STATEFIP`
	Labor earnings dist.	$G_{is}(y)$	ACS (IPUMS): `INCWAGE` + `INCBUS00` + `INCFARM`, `OCCSOC` (6-digit SOC), `PERWT`, `STATEFIP`
	Total earnings	Y_{is}	ACS (IPUMS): $\sum$`PERWT` $\cdot$ (`INCWAGE` + `INCBUS00` + `INCFARM`) by i, s
	Lic. burden	r_{is}	Archbridge (2025): licensing cost index by occupation and state
	Lic. status	δ_{is}	Archbridge (2025): licensed indicator by occupation and state

5.1 Validation

A requirement for validation of my approach is that income must be quantitatively important in determining the demand for quality (quality upgrading). Moreover, we may validate the quantitative model on observed policy changes. That is, we can test whether we do a good enough job at predicting price and quantity movements which are actually observed following licensing events.

5.2 The effects of occupational licensing

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5.2.1 On prices and quantities

5.2.2 On household economic welfare

5.2.3 On worker earnings

Notes

[1]Cite the real case documented by Allensworth (2025).

[2]This identification strategy assumes household expenditure data is not available. However, for some occupations the Consumer Expenditure Survey does track household expenditures. Thus, the partial data on expenditures can serve for validation as well as for more precise estimation for a subset of occupations.

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