Perspectives
on current developments

ERISA, Thidwick, and the "Gotcha" Problem

One of the notions often included in "industrial policy" is that social programs are best provided through the work place instead of through free-standing government programs. For example, the government might tell employers to provide their own day-care centers as a substitute for government-run centers. Robert Reich writes that, in the neoliberal world of the future, "Government bureaucracies that now administer [social services] to individuals will be supplanted, to a large extent, by companies that administer them to their employees. . . . Business enterprises, therefore, will largely replace geographic jurisdictions as conduits of government support for economic and human development."

As Reich is the first to note, this is not a novel idea. Work-place social programs—better known as fringe benefits—have been encouraged, structured, and regulated by the government for years, through agencies ranging from the Internal Revenue Service to the National Labor Relations Board. But the results have not always been heartening. A notable example is federal regulation of private pension benefits—and in particular the Multiemployer Pension Plan Amendments Act of 1980, which makes companies responsible for bailing out their unions' shaky retirement plans.

Most fringe benefits become popular after some employers have begun offering them voluntarily, either to attract employees or as part of a collective bargaining agreement in which the benefit is traded off against other benefits such as higher wages. The details of benefit plans vary greatly from one employer to another, and some employers, especially small and entrepreneurial firms, will not offer even common benefits. Turning these multifarious voluntary benefits into a standardized mandatory-benefit system is not a simple matter. When Congress passed the Employee Retirement Income Security Act of 1974 (ERISA), for example, it did not require all employers to start pension plans, being unwilling to force every little tobacconist and dry cleaner to shoulder the paperwork and other burdens involved. Conceivably it could have mandated that larger but not smaller employers provide their employees with pensions, but such discrimination by size—aside from its fairness and constitutionality—would have engendered troublesome edge effects at the legal threshold.

ERISA's strategy, therefore, was to make existing pension benefits both more generous and more egalitarian. Internal Revenue Service rules on "nondiscrimination" already required that if a company offered tax-favored pensions to executives it had to offer them to all employees on similar terms. ERISA's rules on "vesting" were aimed not only at increasing benefits but at spreading them more widely among workers. Several provisions of the act were also meant to improve the perceived benefit of pensions to workers by shifting the burden of uncertainty of the plans to the employers. Thus the law forced pension plans into an insurance scheme and required up-front funding procedures, in order to reduce the risk that companies would go out of business leaving unpaid pension promises.

If regulations of this kind are pushed too far, of course, employers will take advantage of their right to stop offering the fringe benefit entirely. In the ERISA case, thousands of pension plans simply folded up rather than operate under its provisions. So more ambitious lawmakers are tempted to take away that freedom to drop out by adopting rules to compel firms to go on offering benefits they have offered in the past—rules that would turn temporary and voluntary or at least negotiable offerings into permanent, non-negotiable obligations, in what might be called a "gotcha" law. To use Robert

Nozick's example, it is as if the forest animals acquired a right to go on living in the antlers of Thidwick, the Big-Hearted Moose, even after Thidwick decided he wanted them to leave, while less generous moose remained free to do with their antlers as they liked.

Aside from any moral objections, and aside from the tendency of such laws to discourage employers from offering benefits in the first place, there is a big problem with a "gotcha" law: employers may get advance warning and pull out in the period before the law goes into effect. Thus there is a further temptation for Congress to pursue the logic to its ultimate conclusion and apply the law *retroactively.* That is how the lawmakers came to pass the Multiemployer Plan Amendments Act of 1980, recently struck down in part by a federal judge as unconstitutional and now up for review by the Supreme Court.

ERISA, passed in 1974, had made companies pay off the promises of the pension plans they ran—which, though a retroactive obligation in one sense, at least pertained to an obligation they had in some sense controlled. The 1980 amendments, however, forced companies to pay off the promises of the pension plans their *unions* ran. Although under federal law these funds were run by boards composed of half union and half management representatives, the companies had typically left the funds' operation to the union trustees—which was quite natural, since it was union members who had a stake in the funds' prosperity, while management's liability was thought to consist simply of chipping in a certain number of cents per hour for every participating worker. Moreover, particularly in fields like construction and entertainment, companies came and went while the union and its pension plan survived. True, union-dominated boards of trustees could and did unilaterally sweeten promised benefits—as a way of recruiting new union members, for instance—but management had no inkling it would someday be legally held to pay those benefits.

ERISA had set up a special insurance fund in 1974 for multiemployer plans. But during the 1970s it became clear that the amounts needed to bail out the plans would probably be large enough to strain the fund. Some plans had pursued unsound funding practices, and others were in declining industries such as hat making and milk delivering, where the base of new workers was disappearing. Yet ERISA had pledged that most pension promises would be paid off, come what may. Raising premiums sharply for the insurance fund would have harmed the healthy plans. Almost nobody supported taxpayer bailout.

That left employers. So Congress provided that any employer who stopped contributing to a multiemployer plan would have to pay an assessment entitled "withdrawal liability." This assessment would cover not only the unfunded liabilities attributable to the firm's own workers, but also a share of the liabilities that were attributable to the workers of *other* firms but that were not covered by plan assets (the share would be proportioned to the size of the participating firms). The trustees of the plan would get to assess the amount of the fine, despite the obvious conflict of interest involved. In industries where large sums were uncollectable, where trustees had made extravagant promises, or where there was a large actuarial deficit (which did not necessarily mean that a plan was in financial trouble), "withdrawal" could be ruinous. And a firm would be considered to have withdrawn from a plan not only if it stopped contributing, but also if it cut its contributions sharply, whether because of layoffs or for any other reason. To add a final Kafkaesque touch, a firm would incur withdrawal liability if its employees voted to decertify the union, although under federal law such a vote is not subject to employer consent.

Before the employers could be eaten, of course, they had to be pinned down. So Congress reached back to make withdrawal liability retroactive to April 1980, five months before its date of enactment.

The law led to widespread, though predictable, "horror stories." Elderly owners found themselves unable to close down their companies and retire because their "withdrawal liability" exceeded the value of their companies' assets. Some firms were assessed withdrawal liabilities that totaled more than the sum of the pension contributions they had made since they first went into business. Other employers complained that some boards of trustees were imposing illegally high withdrawal liabilities in order to punish firms for going non-union.

But the course of true expropriation never did run smooth. More than 140 suits have been

In Brief–

"Notice and Comment" on International Regulation. Business has many complaints about the regulatory endeavors of United Nations agencies, but one of its most elemental complaints is simply that it cannot see them coming. When the UN Economic and Social Council recently considered a set of consumer guidelines, for example, most businesses that would be affected by the guidelines were unaware that anything was going on.

The UN itself shows no sign of altering its procedures to provide any sort of advance warning to those its activities would affect. The U.S. government, however, is perfectly capable of letting Americans know what is going on. So says Senator Larry Pressler (Republican, South Dakota), who charged on September 30 that international organizations "have turned their attention from their primary goals to the dubious business of regulating economic activity." He thereupon introduced a bill (S. 1910) to require the State Department to provide timely notice and an opportunity for comment on UN regulatory proposals.

Specifically, under the terms of Pressler's proposed International Organizations Public Procedures Act of 1983:

- The secretary of state would put a notice in the *Federal Register* describing any proposal under consideration by an international organization that may affect U.S. interstate or foreign commerce.
- Interested persons would have an opportunity to comment, and the U.S. government would have to take their views into account before adopting a final position on the proposal.
- A detailed statement of that final position would have to be printed in the *Federal Register.*

Senator Pressler has already introduced a sense-of-the-Senate resolution calling on U.S. representatives to international organizations to oppose restrictions having an "unnecessary adverse impact" on the free flow of goods and information in the world marketplace. That resolution was adopted by the Senate Foreign Relations Committee as an amendment to the State Department's authorization bill.

Update: Computer Crimestopper's Notebook. Some time ago we reported on a social abomination practiced by thousands of Americans despite strict federal laws—namely, knitting at home for pay. It was made illegal back in the 1940s. In October 1981 the Department of Labor revoked its rule against "homework" for knitted ski caps, after a well-publicized lawsuit filed by Vermont knitting women, while keeping its rules against six other categories of needlework and related trades.

Unfortunately, criminal ingenuity knows no bounds, and an estimated 10,000 to 20,000 budding cottage industrialists—their numbers increasing rapidly—have found a new way to violate the spirit, if not the letter, of the Labor Department's ban. They work at home on computer terminals hooked up by phone to other computers. This "telecommuting" has aroused the wrath of some labor unionists. "We think it should be banned," says Denise Mitchell, a spokeswoman for the Service Employees International Union—at least unless its abuses can be contained, she adds. Not so incidentally, Mitchell's union, which represents some 50,000 office workers, will find it harder to recruit members if the telecommuting trend continues. There is no law compelling people to admit union representatives to their front parlors.

It may not be easy to convince these victims of high-tech peonage that they need to be liberated and sent back downtown. According to *Forbes*, employees volunteered in droves for a pioneering work-at-home experiment at Continental Illinois National Bank.

Even so, it is not hard to imagine where support for a crackdown on this newest of computer crimes would come from. Working at home undermines mass transit systems and central city business districts, both of which have been the subject of much federal solicitude. Besides, the Internal Revenue Service has long taken a dim view of deductions for offices at home. If all else fails, the Feds could nab the outlaw telecommuters, like Al Capone, on an income tax rap.

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filed in federal court to challenge the law's constitutionality. There was no solace for employers in Article 1, section 9 of the Constitution, which states, "No bill of attainder or *ex-post-facto* law shall be passed," because courts routinely say it applies only to criminal legislation; but they could still challenge the revision of contract obligations as a deprivation of property without due process.

In a May 1983 case (*Shelter Framing et al.*) the Ninth Circuit Court of Appeals held that the retroactive provisions were unconstitutional. Although the court took a rather relaxed view of the due process requirements, implying that a finding of sufficient inconvenience might set them aside, it found that the law violated the requirements nonetheless. "The trust fund and covered employees have not relied heavily on these employers' contributions," it said. The employers, it added, had been made "to pay a sum that seriously threatens their solvency, without a specific showing of the proportionate need on the part of the pension trust funds." (Shelter Framing Corporation had been assessed $797,648, which amounted to 180 percent of its net worth.)

The Supreme Court agreed on October 17 to resolve the question. But note that even if retroactivity is struck down, it will have served its purpose of preventing defections. Firms that stayed in the plans will be permanently on the hook.

The 1980 law has come under intense legislative challenge from small business, especially in such industries as trucking. Still, Congress failed to act on more than half a dozen proposals for reform last session, and it appears that defenders of the 1980 act are strong enough to block any serious change. That will leave a lot of businesses continuing to pay for other companies' pensions—and wondering who will be the victims next time Congress drafts business into a surrogate welfare system.

DOE Walks into a Better Mousetrap

If there is any truly thankless task in government, it must be that of carrying out projections and simulations under the glare of hostile press scrutiny. Take the risk analyst who is charged with assessing the remote hazards of nuclear power. If he follows his mandate to assess the most unlikely contingencies, including "worst-case" scenarios, he may read in the next morning's headlines that "Government Says Nuclear Power Could Kill Thousands; Refuses to Shut Down Plants." Or take the defense analyst instructed to predict whether the United States would or would not fight in reaction to a nuclear attack on its cities, and who is faced with a choice of headlines: "U.S. Planning Surrender in Nuclear War" or "U.S. Planning to Fight Nuclear War."

The Department of Energy is the latest agency to be mouse-trapped by the need for contingency planning. In May and June of this year it took part in the Fourth Allocation Systems Test run under the auspices of the International Energy Agency, an organization of twenty-one industrial countries. The exercise simulated the results of a major oil supply disruption in the Persian Gulf, the object being to test the workability of the international oil-sharing procedures that the IEA treaty would require in such an event. In line with Reagan administration policy, the United States took the position throughout the test that it would meet its oil-sharing obligations and respond to the disruption generally without resorting to coercive measures like rationing or allocation.

Now, any model of how process A will operate necessarily devotes most of its detail to process A itself, while greatly simplifying the tangentially related processes B and C. In this case, since the test was meant to assess the narrow issue of whether the United States could come up with oil to share with its treaty partners, DOE paid less heed to modeling how such a disruption would affect U.S. consumers in general, except insofar as it related to our IEA obligations.

Moreover, the key assumptions on which the test was based were thoroughly unrealistic. The participating countries used two-year-old supply and demand data, although U.S. demand had dropped by 1 million barrels/day in those years and Strategic Petroleum Reserve holdings had more than doubled to 327 million barrels. One reason was that complete data were not available for more recent years; another was that using contemporaneous data would have raised antitrust questions.

The simulation of the subsequent events was less realistic than the starting point. For one thing, the Energy Department interpreted the IEA test conditions to mean, as Assistant Secretary of Energy William Vaughan said later, that "[n]o responses of any kind—international or domestic—by the U.S. or any other participant, were allowed between the beginning of the hypothetical disruption in December 1982 and the beginning of the actual exercise play on May 2, 1983." (Later this interpretation came into question.) Aggregate oil inventories, public and private, in participating countries were assumed by IEA to have been drawn down by 20 percent during the preliminary period through May. The IEA also specified that, however much prices might rise, *no* surge production could be considered available to compensate for the oil shortfall, even though DOE has estimated that 2.5 million barrels/day were available worldwide within a few months of the disruption. On top of that, DOE ruled out any drawdown of the Strategic Petroleum Reserve. Thus it was essentially impossible for price rises in the test to call forth supply, either from the public stockpile or from additional production.

The structure of the exercise thus guaranteed that the price of oil during the hypothetical disruption would rise to an absurdly high level. The figure reached $98 a barrel by the end of the test, up from $29 at the beginning. Had the test assumed, more realistically, that the United States would draw down the strategic reserve and private inventories to offset some of the shortfall, oil prices would have been kept at a far more moderate level for at least six to eight months. That would have been long enough for producers to bring significant new production to market, for consumers to implement extensive conservation measures, and even possibly for governments to unblock the Persian Gulf or find some alternative route of egress for its oil. Just the Strategic Petroleum Reserve, if used to make up two-thirds of the hypothetical shortfall, would have lasted for six months.

The oil sharing worked as planned. The simulation raised more than twice as much oil as necessary, and the Energy Department was incautious enough to declare that it all had been a success. They should have known better. On September 19, the *Washington Post* ran a front-page story summing up the results of the test. "In the most realistic test of how the U.S. government would deal with a new world oil crisis, the Reagan administration's free-market approach turned an oil shortage into a national 'economic disaster,' according to reports by ten states that participated." The article did not report the peculiar assumptions on which the test was based, although all of this had been made public from the beginning, or make clear that the exercise was not seriously intended to assess the domestic effects of an oil disruption. It did, of course, cite the striking $98/barrel price projection, a figure that was soon picked up in other news stories.

One can only imagine what was going through the mind of Vaughan, who is in charge of emergency preparedness, as he read the paper that morning (to add insult to injury, the *Post* had repeatedly spelled his name "Vaughn"). At any rate, it happened that he was scheduled to be hauled before a House subcommittee that very Thursday to answer questions on the test. He spoke at some length about the unrealistic assumptions, and then added that any disruption was by its nature going to be disruptive, and that the mandatory allocation measures that the department's critics were calling for might redistribute those costs, but could not prevent them. He might have added that allocations can drive the costs underground, since the time spent waiting in gas lines, for example, is rarely reckoned officially at the hourly wage of the average worker.

DOE says that even such an unrealistic simulation is useful in identifying bottlenecks and management problems before an emergency occurs. But the degree to which the results were liable to distortion points up the need to assume a more realistic set of test conditions—or not run such simulations at all.

Boxcar Decontrol: No Empty Gesture

"As far as I can tell, never in the history of the commission has there been such an outcry over an ICC decision." Those are the words of Interstate Commerce Commission Chairman Reese Taylor, Jr., and he is speaking, not of trucking decontrol or antitrust exemption, but of the obscure issue of railroad boxcar deregulation. On April 29 the ICC voted by a three-to-one margin to deregulate some aspects of railroad boxcar traffic, over bitter objections from many shippers and smaller railroads. Part of the controversy is over the commission's deregulation of the rates that shippers pay railroads for shipping goods in boxcars. But the most controversial aspect of the decision was the portion in which the commission partially deregulated the terms of boxcar *interchange*—what railroads pay when they use boxcars owned by other railroads or by shippers. The amounts at stake are considerable. The railroad cars in use today are worth an estimated $30 billion, and close to half of that consists of boxcars.

The controversy has been a long time in building. Nowadays we take it for granted that one railroad can send its cars onto another's tracks and eventually get its empty cars back. Until the latter decades of the nineteenth century, however, it was not so easy. Carriers had differing track gauges or were even physically unconnected with each other, so that freight had to be moved laboriously from one railroad's cars to another's at a connecting point; and if one railroad did send its cars onto another's tracks, it sometimes had trouble getting them back. Track gauges began moving toward standardization during the Civil War. The process was completed around 1890, and in 1902 a trade association set uniform rules for car interchange.

Eight years later Congress came along to enshrine in law what had already been going on voluntarily for decades. In the 1910 amendments to the Interstate Commerce Act, it gave the ICC broad powers to require the "interchange and return of cars." It was only much more recently, however, that the commission's regulation of car interchange became really pervasive.

Under the current system, when a railroad sends its car onto another railroad's tracks and it is unloaded, the car begins earning a fee, paid by the railroad that has custody of it, until it is returned. The ICC sets the formula by which these fees are computed, which can be per day or per mile or both. It also sets the fees that railroads must pay to private car owners for using their cars.

The ICC-set payments were generous to boxcar owners, for at least two reasons. First, the agency read the Interstate Commerce Act as encouraging it to set its formula at a level that allowed car owners to recover their investments. Second, penalty charges were imposed in order to curb car shortages by giving carriers a reason not to dawdle in returning other lines' cars after they unloaded them.

The boxcar shortage has turned into a glut since then, but the old car interchange regulations remain and are having a number of perverse effects. Many carriers have made a profitable sideline of buying or leasing extra cars and routing them onto the tracks of connecting carriers to collect fees. In fact, there are a number of short-line railroads that try to live at least in part off boxcar rentals.

In addition, since the ICC's current formula amounts to rate-of-return regulation, the commission responds to a car glut the same way the utility regulators in textbooks respond to a drop in demand: by raising the payment per car, in order to compensate boxcar owners for lower levels of usage. This tends to add to the surplus, which is the very opposite of what would happen in an ordinary market. The fixed charges give carriers odd incentives at times of surplus and shortage alike. In times of surplus, a railroad has an incentive to get competitors' cars off its tracks quickly, even if the cars have to travel empty—which leads to the obviously wasteful circumstance of two railroads' exchanging empty cars. In times of shortage, a carrier can simply fall back on its right to insist that other carriers return its cars at once, so that empty cars still crisscross the map.

In a market situation, different railroads would bid different amounts for car hire, depending on how badly they needed cars. In certain circumstances, in fact, the "origin carrier" might even pay the "destination carrier" to take or to keep its cars, in order to defray the costs of storage or empty return.

Incidentally, the ICC has the statutory power to force the transfer of boxcars by issuing "car service orders." For example, if Railroad A runs short of cars, the agency can compel Railroad B to send it empty cars, including cars from other lines, as fast as it can. The commission has delegated this power to the Association of American Railroads (AAR), a trade group, but the association stopped issuing orders after conducting a study that found that the orders led to needless car movements.

The big loser from the system, and the leading advocate of deregulation, is the northeastern railroad Conrail, which receives more freight from other carriers than it sends to them. As Conrail has had to pay more and more to send empty cars back, its boxcar traffic has dropped precipitously, from 796,000 cars to 288,000 from 1977 to 1982. According to Conrail, the nationwide percentage of boxcars that returned empty increased from 56 percent in 1979 to 81 percent in 1981.

Some of the empty car movement is clearly necessary to make up for the overall west-to-east flow of traffic. But much of it seems unnecessary, according to a 1980 study for Conrail by transportation consultant Alain L. Kornhauser. In fact, Kornhauser found that about 70 percent of the 1.4 billion empty car-miles that took place in that year were needless. He used a computerized model of car flow to compare empty mileage under the current system with empty mileage under the assumption that the railroads were operated as an integrated system in which each railroad took into account the full consequences of its loading decisions on other railroads. Since the variable cost of moving a car one mile has been estimated (by Conrail) at around 35 cents, a 70 percent reduction would have saved about $340 million. (That does not include the value of the added traffic that now does not move at all because of the current inefficiencies.)

The Kornhauser study was not perfect: critics say it did not reflect up-to-date routings and operating practices, and part of the inefficiency he found may already have been cured by the Staggers Rail Act of 1980. Moreover, the several end-to-end railroad mergers that have occurred since the study have probably reduced the amount of interchange that goes on and thus the amount of waste. Still, even allowing a significant margin for error, the loss seems to be considerable.

The Staggers Act loosened up the system by allowing railroads and shippers to set their own contract terms. The Burlington Northern, for example, has been offering discounts to shippers on other railroads that load Burlington cars with goods to ship back in its direction. In November 1982, furthermore, the commission abolished its system of car-hire charges for the interchange of the "piggyback" containers that are transferred from or to trucks. Despite predictions of doom from AAR and others, piggyback traffic is still moving normally and is continuing its strong growth trend. Most railroads have reached agreements with their connecting railroads on piggyback shipments, and Conrail and the Norfolk Southern continued to interchange piggyback cars even without such an agreement. Railroads have also reached interchange agreements with the many truckers that carry piggyback shipments; the Santa Fe alone has arrangements with at least fifty-one such firms.

In 1980 the ICC allowed railroads to cut the car-hire rates they charge when their cars are on the tracks of another railroad, and it is also considering letting them raise the rates as well. Of course, freeing up the car-hire rates A could charge B when A's cars are on B's tracks would be only half-deregulation. In the final rule it adopted April 29, the commission increased the "destination carrier" B's ability to bargain with the "origin carrier" A over the terms of B's acceptance of A's cars. Specifically, B can apply an empty movement charge if A demands its cars back before B can arrange a return load. Moreover, if A decides not to ask for its cars back, B can store them without paying A a car-hire fee. Finally, railroads are allowed to negotiate with each other over any of the current terms of car interchange.

Smaller railroads naturally worry about imbalances of bargaining power in these negotiations. (Perhaps to placate the smaller lines, the ICC postponed the rule's application to them to July 1, 1984; for cars owned or leased by Class III railroads it goes into effect January 1.) But it is far from clear how the ICC could design car interchange terms that mimicked the results of perfect competition—as opposed to rules that simply subsidized shippers and small carriers—without falling back into some extremely messy regulation. The commission would have to monitor a vast number of interchange situations and a variety of conditions of supply and demand for cars. Conceivably the ICC might placate small boxcar owners by retaining a residual regulatory power to enforce some set of "reasonable" car-hire terms. But any such terms could easily become the standard terms, since they would give one or the other side an incentive to hold out in the bargaining process—which would bring us back to regulation. In any case, most boxcar interchanges in a deregulated market would take place between the seven large systems that carry the most freight (Norfolk Southern, CSX, Conrail, Burlington Northern, Southern Pacific, Santa Fe, and the newly merged Union Pacific/Missouri Pacific/Western Pacific system).

Some railroads fear that negotiated agreements will be more costly to administer than the ICC's old rules. The Norfolk Southern told the ICC that the deregulation of piggyback traffic would force it to boost its clerical staff at least 20 percent to administer agreements for interchange of such traffic. That would cost $458,000 in start-up costs plus about $519,000 annually. The latter figure comes to about one-third of 1 percent of Norfolk Southern's 1982 piggyback revenue of $151 million, a percentage that should shrink if piggyback continues its rapid growth.

A liberal construction of the antitrust laws, or even an exemption, could help curb these administrative costs by allowing those railroads that want to do so to continue or expand cooperative car arrangements. AAR, for instance, maintains a central car interchange accounting system and sets equipment standards for interchange.

Deregulation notwithstanding, the Interstate Commerce Act still requires railroads to accept boxcars from connecting carriers whether they want to or not. It is interesting to speculate what would happen if Congress or the ICC lifted this mandatory interchange rule, too, and left the market for car interchange completely deregulated. Such an entirely deregulated market would not be purely competitive in the textbook sense of having a large number of buyers and sellers. The terms of interchange would instead be set through case-by-case bargaining between two (or at most a few) connecting railroads at a time. Any one-on-one bargaining system, as in the case of labor-management relations, is vulnerable to breakdown, leading to service interruptions. Would this one be different? Probably, because the basic incentive to reach interchange agreement would be powerful: no railroad wants to have to load goods from one car to another at a junction point. Any breakdown in the interchange system would harm the joint line business of both railroads.

Professional Licensure— One Diagnosis, Two Cures

An ever-growing body of empirical scholarship, some of it collected in the September issue of *Law and Human Behavior*, supports the idea that occupational licensure is an anticompetitive barrier to entry. The controversies surrounding licensure, however, point up the division in the regulatory reform movement between what Jonathan Rose describes as its "control" and "anti-government" wings—between those who want to harness regulatory power and those who want to end it. The two sides agree that self-regulation in the professions has harmed consumers, but the former group would replace that self-regulation with regulation by outside parties acting in the name of the public interest, while the latter would remove most regulations entirely in the name of consumer sovereignty.

Both sorts of reformers agree, by and large, that occupational licensure has tended to serve the interests of the regulated profession, and indeed, as a historical matter, was enacted at its behest. For instance, William White demonstrates in a history of nursing licensure that only the nurses have been for it: individual consumers have taken little interest in the issue, while large institutional consumers of nursing services such as hospitals have been strongly opposed.

Quality of Service. The customary rationale for licensure is that it protects consumers from incompetents, quacks, and charlatans—or, to put it more scientifically, that it repairs a market failure caused by consumers' lack of information about the quality of service. And the recent scholarship does in fact suggest that licensure may raise the average quality of *practitioners*—which, unfortunately, does not necessarily mean that it raises the average quality of the service that consumers receive. One study found that restrictive licensing improved the average quality of lawyers as judged not merely by the (possibly circular) measures of peer evaluation and number of disciplinary actions, but also by the more objective test of the level of malpractice insurance rates. Other investigators have found that licensure improved the average quality of optometrists and either improved or left unchanged the quality of pharmacists.

The problem is that the less-qualified practitioners that a licensing law lops off may have been doing more good than harm overall, so that the overall decline in the *amount* of service rendered harms consumers on balance. In their study of dentists, for example, Sidney Carroll and Robert Gaston found evidence that "strong forms of licensing such as the requirement for U.S. citizenship or the lack of reciprocity agreements [between states] are associated with reduced numbers of practitioners, which in turn are associated with proxy measures for low quality of dental care." Carroll and Gaston also found that houses tend to stay on the market longer where real estate brokers are tightly regulated, and that the incidence of rabies and brucellosis is higher where there are strict limits on veterinary practice. Sometimes there are geographic differentials: restrictions tend to lower the number of sanitarians in isolated rural areas and inner cities, while leaving suburbs and small towns practically unchanged.

Carroll and Gaston's research indicates that people in underserved areas are more likely to turn to often injurious self-help methods or help from friends and neighbors, presumably owing to the scarcity of lawful service. There is more do-it-yourself plumbing, as measured by retail sales of plumbing supplies, in states with strict laws regulating plumbers, and accidental electrocutions occurred ten times more often in states with the most restrictive licensing rules for electricians. They sum up: "for all the [seven] professions listed here, restrictiveness was carried far enough to encounter negative results *in at least some states*. Further, no professions were encountered that demonstrated a significant relation in the opposite direction."

The behavior of licensing boards, which have traditionally been dominated by the regulated profession, is also difficult to square with the consumer protection rationale. According to Elton Rayack's study of licensing in southern New England, "When labor market conditions worsen, licensing boards tend to fail a higher percentage of applicants for licensure, irrespective of the qualifications of the applicants, in order to reduce the flow of new entrants into the market and thereby strengthen the competitive position of the licensed." In 1934 the president of the American Medical Association, Dr. Walter Bierring, warned that a rising physician population threatened "the economic welfare of the future practitioner" and said that a "fine piece of educational work could well be done if we were to use only half of the seventy-odd medical schools in the United States." Medical schools cut acceptances by 17.8 percent between 1933 and 1939 even though applications remained almost unchanged in that period.

Entry. Both the "public interest" and the "consumer sovereignty" reformers generally concur in criticizing many types of anticompetitive restrictions in the professions, such as minimum fee schedules, bans on advertising and group practice, and curbs on the use of allied professionals such as paralegals and lab technicians. But when it comes to the central question of whether and how to allow more practitioners into the profession, there is no such consensus. The consumer sovereignty view, the classic statement of which is found in Milton Friedman's *Capitalism and Freedom*, would let the market decide who should practice, with the law invoked only against those actually guilty of malpractice. Another version of this view is, to quote Daniel Hogan, that "licensing laws should only restrict the use of certain titles, not the right of a person to practice." Alternatively, he says, the government could require anyone who wants to practice a profession simply to register and make full public disclosure of detailed information about himself. Any person that the registration board struck from the register for "good cause" would be forbidden to practice. The "public interest" side, for its part, has not settled on a single recommendation: its general view seems to be that the number of new entrants would rise to the "right" level once public-spirited representatives were appointed to a licensing board.

Present-day licensing boards tend to require applicants to pass a written exam, and sometimes they specify minimum levels of education and work experience as well. This "credentialism" is often said to present a special obstacle to minorities and the disadvantaged, whose skills may not be embodied in formal education, and to the elderly, who grew up at a time when undergraduate and graduate degrees were far less common than now. The critics range all the way across the political spectrum from Milton Friedman ("the effect of restricting [practice] and defining it as we tend to do to a particular group, who in the main have to conform to the prevailing orthodoxy, is certain to reduce the amount of experimentation . . . and hence to reduce the rate of growth of knowledge in the area") to civil rights enforcers (in California they have charged that the state's nursing and psychologist tests are biased against blacks).

What might be called the nihilist position on credentialism is not without empirical support: a 1964 study by P. B. Price and others found that "performance in formal education, as measured by grade-point averages, comes out as a factor almost completely independent of all the factors having to do with performance as a physician." But credentialism is not just some invidious scheme cooked up to punish those with low test scores. It is the inevitable consequence of replacing a regime of consumer sovereignty with one of entry restriction. If the general public is not to be allowed to practice medicine, then some way must be found to exclude applicants. And while consumers are free to reject a would-be doctor for subjective or ineffable reasons, the government, in our system, is not. If there is one thing that government employment law makes clear, it is that officials must fill a record with evidence, preferably of a quantifiable variety, before they take away someone's livelihood. A system in which the wisdom of job allocations must be defended with a paper trail is, no matter what its name, credentialism. If tests are made less important, the likeliest other sorts of screening mechanisms might keep out just as many minorities but be even less job-related.

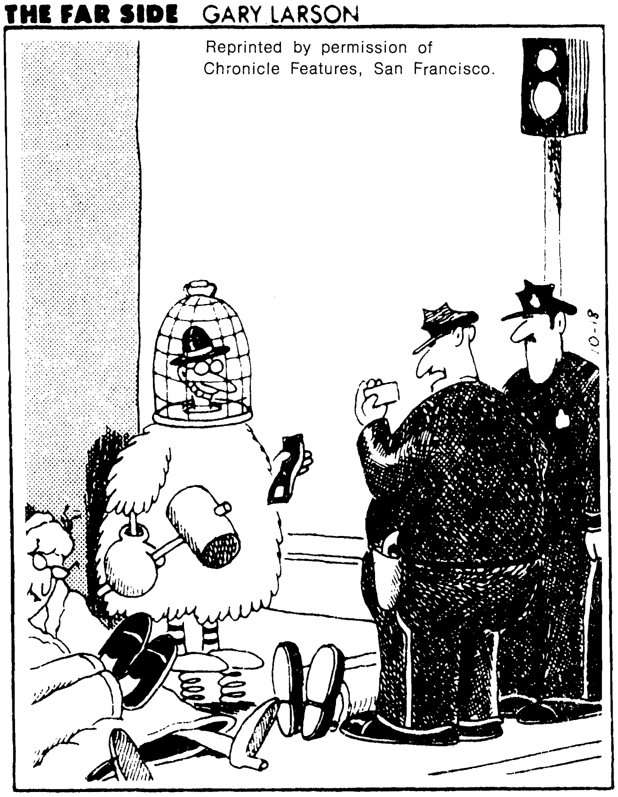
Policing Existing Practitioners. Another division between the two sets of reformers concerns recurrent proposals to test existing practitioners periodically or require them to take continuing education courses, so as to make sure they know the same things that new applicants are expected to know. The deregulation side is rather cool to these proposals, probably because tossing out existing practitioners would make the perceived shortage worse. The public interest side, however, often supports such requirements, finding it ironic that licensure boards avidly enforce restrictions on new entrants while showing a great reluctance to apply the same standards to established members of the professional fraternity.

Dr. Robert Derbyshire, formerly president of the Federation of State Medical Boards, writes that the average doctor faced only a 0.06 percent chance of being disciplined by a state medical board in the late sixties, narcotics violations being the major single cause. By 1981 the number had inched its way up to 0.14 percent, but fifteen states still disciplined no physicians at all. (Incidentally, stringent Nebraska provides thirty-four reasons for disciplining doctors, while free-wheeling Nevada concerns itself with just four.)

When disciplinary boards do act, Derbyshire says, doctors are often unwilling to testify against their colleagues even where major crimes are involved. Since there is not much disciplinary reciprocity between states, he adds, a suspended doctor can often engage in "state-hopping" and continue practicing. Ten states have passed laws that require physicians to report colleagues whom they know to be incompetent.

Andrew Dolan and Nicole Urban, in research on state medical boards, found that the principal determinant of disciplinary activism is the degree to which a board is *not* controlled by doctors. Jerome Carlin's research looked at the legal profession and found that the degree of disciplinary action taken by the organized bar in a case depends, not just on the severity of the misdeed, but also on the degree of publicity the case has received. The implication, Carlin concluded, is that formal disciplinary proceedings serve in part to fend off public scrutiny of the bar.

THE FAR SIDE GARY LARSON



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"Well, I'll be darned! I guess he does have a license to do that."

An even more notable divergence between consumer-autonomy and public-welfare approaches is exemplified in the proposal by Senator Arlen Specter (Republican, Pennsylvania) and others to write into federal law the proposal that the American Bar Association recently failed to adopt: known as the "lawyers' squeal rule," it would require attorneys to rat on their unethical clients. The acrimonious arguments over whether such a rule would purge lawyers of complicity in the crimes and near-crimes of their clients, or turn lawyers into agents of the state against the interests of their clients, or do both, should warn us that the wrangling does not end—and in fact just begins—when self-regulation is replaced by other-regulation.