Introduction

Following the Great Recession, job creation has become a central issue in American politics and media. As the government struggles to promote job creation from above, entrepreneurs around the country are pioneering new businesses that are stimulating job growth from the ground up. Yet, all too often, burdensome regulations suppress such entrepreneurship, and governments are preventing rather than promoting local job growth.

Start-ups account for almost 20 percent of gross job creation (Haltiwanger, Jarmin, and Miranda 2010). Cities with more small start-ups have significantly more employment growth; indeed, an entrepreneurial culture in a city is self-sustaining and fuels job growth for decades (Glaeser et al. 2012). Small and young businesses have important ripple effects. They are more likely to keep the jobs they create close to home and buy from local suppliers, building and keeping wealth in the community (Les Miserable, Economist July 28, 2012; Glaeser et al. 2012).

Given the importance of start-ups in job growth and economic development, it seems intuitive that state or local governments would aim to encourage local entrepreneurship rather than outlaw it. Yet, in the face of logic, common sense, data, and the public interest, state and local governments have accreted unnecessary business licensing requirements that make entrepreneurship impossible, costly, slow, or onerous. For example, a leading national expert estimates that the job loss attributable to occupational licensing is between .5 and 1 percent (Kleiner Testimony 2011). By trimming or eliminating harmful licensing requirements, state and local governments can boost job growth without spending any money from their tight budgets. Indeed, they might even save money on the administration and enforcement of counter-productive laws.

By way of introduction, this paper will give an overview of business licensing laws, their origins, their purposes, and their outcomes as a general matter. Then, I will identify four features of business licensing laws that often inhibit job creation and economic growth, so that state and local governments can identify the biggest culprits in their codes. I will discuss real life stories of entrepreneurs that were handicapped by
these laws, in order to explore more deeply why governments regulate, how regulations affect individual entrepreneurs and entire markets, and how removing regulatory barriers to entrepreneurship can make job creation possible. All but one of the entrepreneurs I profile are in Chicago, where I direct a legal aid clinic advocating for lower-income entrepreneurs. Even though the geography is somewhat narrow, the problems these four entrepreneurs have faced are commonplace.

First, I will describe the dangers of overbroad and excessive training requirements in a typical occupational licensing structure. The story of a traditional African hair braider, Melony Armstrong, will show how the training requirements in a cosmetology licensing scheme can suppress entrepreneurship and how lifting the burden of the licensing requirements can create jobs. Second, I will explain the effects of laws that require entrepreneurs to spend money on needless facilities instead of on creating jobs. The phenomenon is illustrated clearly by the story of an entrepreneur in Chicago who was told he could not hire employees if his business headquarters were located in his home.

Third, I will explain how narrow categories of business licenses can lead administrative agencies to turn away innovative businesses founded by creative entrepreneurs thinking out of the box. Because inspectors and bureaucrats in Chicago did not know how to license a commercial kitchen shared by several small food start-ups, the business’s resources were spent on negotiating with the city government instead of building up the business. The kitchen shut down instead of serving its function of incubating the kinds of start-ups that create new jobs.

Finally, I will discuss rules embedded in licensing schemes that are blatantly anti-competitive and protectionist. Though they may appear to protect existing jobs, they stunt economic growth and deprive consumers of the freedom to choose where to spend their hard-earned money. As an example, I will tell the story of a food truck entrepreneur in Chicago, who fears the harsh laws prohibiting him from operating too close to restaurants could destroy the business and, with it, his plans to open a restaurant himself someday.

I. CONTEXT OF BUSINESS LICENSING

What do business licensing laws look like?

Business license requirements take many forms (Carpenter et. al. 2012; Young 1987). Almost every business needs to register and pay a fee to operate legally. Many businesses, especially service businesses, must also satisfy a checklist of additional requirements specific to their line of work before the government will give them permission to operate. Individuals working in the business might need to get a degree or hours of education, spend time in apprenticeship, pass a test, demonstrate skills for an inspector or judge, have a clean record, evidence good character, or more. In addition, the business itself may need specific equipment
or facilities or insurance to get a business license. To keep a license, there may be ongoing requirements such as reporting, recordkeeping, continuing education, or the like. In fact, as will be discussed later, the business may even be required not to create jobs.

Where do business licensing laws come from?

The ostensible (and only constitutional) purposes for most business licensing laws are consumer protection and protection of the public. As the United States Supreme Court stated in 1889, “The power of the State to provide for the general welfare of its people authorizes it to prescribe all such regulations as in its judgment will secure or tend to secure them against the consequences of ignorance and incapacity as well as of deception and fraud. As one means to this end it has been the practice ... to exact in many pursuits a certain degree of skill and learning upon which the community may confidently rely.” (Dent v. West Virginia 1889).

Licensing laws are supposed to create standards for businesses, to give consumers confidence that the service providers are qualified and properly equipped, as well as to eliminate quacks (Adams et al. 2003). They are justified as a solution to asymmetrical information problems (Cox and Foster 1990, Leland 1979), especially in cases where a practitioner’s incompetence, though difficult for the consumer to detect, would have irreparable consequences (Hollings and Pike-Nase 1997, Leland 1979). They also provide a profession with sufficient prestige and salary to attract high-quality practitioners (Leland 1979). Finally, they can assure that a customer will not choose an incompetent service provider who will end up creating irreparable externalities for others, such as a fire hazard or a building that might fall down (Wheelan 2010).

The so-called learned professions were the first to be licensed in the United States, particularly the medical profession (Gellhorn 1976, Hollings and Pike-Nase 1997). Lawyers and doctors are thought to have specialized and esoteric expertise, so that customers cannot evaluate their competence well, even after service is provided. At the same time, lawyers and doctors can severely harm customers if they are not competent. Customers’ health, liberty, and fortune may be at stake when hiring a doctor or lawyer. To keep a license once earned, a member of a learned profession is required to follow a code of ethics and hold the public welfare in trust.

The 20th century saw a steady proliferation of new and stricter occupational licensing laws for many occupations beyond the traditional learned professions (Hollings and Pike-Nase 1997). According to the Council of State Governments, more than 800 occupations required licensure in at least one state in 2003 (Kleiner and Krueger 2008). Kleiner and Krueger determined that, in 2006, 29 percent of the workforce was required to hold an occupational license from a government agency—federal, state, or local (Kleiner and Krueger 2008). Some hypothesize that the 20th century called for more occupational licensing because the urbanization of America made it harder for consumers to know service providers by experience and reputation, and so the government stepped in to assure customers of service providers’ competence (Kim and Law 2004). In other words, the anonymity of city life made information asymmetries a serious issue for
relationships with ordinary tradespeople like barbers or cabinet makers. Others have suggested that
government oversight was more and more necessary as America evolved from a manufacturing economy,
where workers’ competence was determined by expert employers, and both firms and unions enforced rules
on workers, to a service economy, where individual customers must trust the quality of independent service
providers (Kleiner and Krueger, 2008).

The public interest explanations for many business licensing laws are, however, feeble. As scholars and
theorists dating back to Adam Smith have noted, most business licensing laws are driven by a lobby of
existing businesses, rather than demand by consumers for protection or independent legislative findings
about the public interest (Gellhorn, 1976, Wheelan 1999, Young 1987). Milton Friedman wrote:

> The declaration by a large number of different state legislatures that barbers must be approved by a
committee of other barbers is hardly persuasive evidence that there is in fact a public interest in
having such legislation. Surely the explanation is different; it is that a producer group tends to be
more concentrated politically than a consumer group (Friedman 1962).

Incumbents have clear incentives to ratchet up the requirements for licensure over and over again to limit
competition from new entrants, as long as they are shielded by grandfather clauses (often the case)
(Gellhorn 1976; Rottenberg, 1962). In 1962, Rottenberg demonstrated how the requirements for barbers in
Illinois had become stricter every few years since they took effect in 1909 (Rottenberg 1962); they have
become even stricter since. More recently, empirical analyses have shown that the size, strength, and
budget of a trade association often determines whether a licensing law passes, rather than the risks posed
to the public if there is no licensure system to exert quality control (Benham and Benham 1975; Kim and

States and municipalities, with little-to-no resources for economic analysis of legislation, defer to the
“industry experts” who claim legislation is necessary to protect the health and safety of consumers (Young
1987). They respond to the courtship of professional lobbyists who represent groups of passionately
invested constituents who want to protect themselves from competition. Legislators do not often get the
other side of the story: that onerous business licensing requirements will suppress job growth, squeeze out
innovation, make it harder for minorities and low-income people to create jobs for themselves, and impose
higher costs on consumers, shutting the poor out of vital services completely.
Do licensing laws serve their ostensible public purposes?

Rather than ensuring quality or addressing information asymmetry, occupational licensing accomplishes these results: (1) fewer people working in the licensed occupation, (2) higher incomes for the people in business, (3) higher—sometimes prohibitive—prices for consumers, and (4) the pride that people derive from membership in an exclusive profession (Kleiner 2006).

Given the anti-competitive motivations and incentives driving the adoption of many licensing laws, it follows that some of them are poorly designed to ensure quality services for entrepreneurs (Leland 1979). Indeed, several studies have shown that particular licensing schemes served to increase the income of licensed practitioners without any increase in the quality of the services to the public (Cox and Foster 1990). Kleiner and Kudrle determined that the dental health of Air Force recruits from states with strict dental licensing standards was no better or worse than that of recruits coming from states with laxer standards (Kleiner and Kudrle 2006). Carpenter found that experts could not tell the difference between floral arrangements created by licensed florists, who had to pass an exam and reviewed by a panel of judges, and florists from a state without a licensing system (Carpenter 2010). According to Barker's study, higher education requirements for real estate brokers in some states raise those brokers' incomes, costing consumers $5.4 billion per year, but do not lower the rate of customers’ complaints about brokers’ services (Barker 2008). Adams et al. calculated that states with stricter licensing rules for certified midwives restricted the supply of midwives but did not improve quality assurance and consumer confidence proportionately, so consumers simply used midwives much less frequently in more heavily regulated states (Adams et al. 2003).

Business licensing laws are not often targeted to address pressing problems of information asymmetry either. Though urbanization may have presented new problems for customers trying to learn about the quality of tradespeople, technology has decreased those problems significantly. Information about the quality of many goods and services is readily available today due to abundant consumer reviews on the Internet. It is as hard or harder for a charlatan or incompetent to get away from his bad reputation today as it was in small-town 19th century America. Yet, instead of decreasing in the information age, occupational licensing is increasing significantly. In 2008, nearly 30 percent of the U.S. population required a license to work, up from 10 percent in 1970 (Kleiner 2009). Many occupations, such as hair braiders or landscape architects, have been licensed initially or more strictly in recent years, even though previous customers can understand and make accurate assessments of the quality of services to decide whether or not to repeat the transaction, and potential customers can easily research providers’ quality using customer reviews.

It is also hard to believe that business licensing is primarily or proportionally used to prevent harms that could not be compensated by damages or do-overs. In a study of 102 occupations commonly held by low- to moderate-income Americans, Carpenter et al (2012) gave a comprehensive overview of state licensing laws that limit the job opportunities of people with little money. Fifty states require specialized licenses of
manicurists, barbers, and cosmetologists, even though it has often been said that the remedy for a bad haircut is to wait two days (or a week, depending on how patient you are) (Kleiner 2006). Auto mechanics, whose mistakes could lead to fatal accidents harming their customers and others, are not licensed by any state. Instead, they have the option to establish their qualifications by getting certified by an independent association and informing customers of their seal of approval (Carpenter et al 2012). Interior designers are subject to the most burdensome average requirements when licensed by states, with average fees of $364 and an average of 2,190 days of training required. Barbers are ranked 13 in the list of burdened occupations, having to pay an average of $130 and spend 415 days in training. Meanwhile, an emergency medical technician is at rank 67, and a child care worker is at rank 71. States are screening businesses involved in aesthetics and grooming more strictly than businesses that play a serious role in the health and safety of citizens.

What does business licensing do to job creation?

When there are regulatory barriers to entry in an occupation, there are fewer jobs in that field. Some individuals cannot afford the cost of meeting the regulatory requirements and simply do not enter the workforce. Even those who do commit to meeting the requirements lose time and money that they could have spent on starting a business and hiring others. Kleiner 2006 calculated that the growth rate in an occupation is 20 percent less in a state where the occupation is licensed than in a state where it is not. Other studies have also shown that licensure depresses the numbers of people working in an occupation (Harrington and Treber 2009, Timmons and Thornton 2012).

Licensing requirements that apply to the business itself and not just the individual workers also make it hard for businesses to start up and develop new jobs. They drain resources that the business could spend on personnel. Plus, because business licensing requirements are often implicitly—and sometimes explicitly—anti-competitive, they discourage new entrants from trying to build a business by improving upon existing goods and services. They handicap the process of creative destruction, whereby entrepreneurs with innovative businesses woo customers away from their passé predecessors. Though creative destruction has been shown to yield growth, and the high-growth startup “gazelles” are essential to creating new jobs, the laws written by incumbent businesses sometimes make the next big thing illegal.

Plus, because the regulations lock in the standards and the contours of business practices that are customary at the time when the law is written, they can sometimes unintentionally outlaw new, creative business models (Harper 2003). By inflexibly requiring that businesses conform to the expectations of legislators, they prohibit new businesses that will build on unanticipated technological change or market shifts. For example, laws that strictly define a livery service, as distinct from a taxi service, have blocked the high-growth start-up Uber, which is a mobile app through which customers can hire an available car in the
neighborhood, from entering certain markets. In the end, some business license schemes outlaw, delay, discourage, or burden entrepreneurs with innovative business models to the point that they never start or cannot succeed. By artificially suppressing the success of those creative start-ups (who generate the most net new jobs), localities lose jobs in those businesses and the businesses that might grow around them.

In fact, we can never quantify the jobs lost to excessive, unnecessary business licensing schemes. We cannot count the individuals who were discouraged or could not afford licensure and never tried. We cannot count the potential jobs that were lost when a creative innovator was not allowed to succeed.

II. FOUR HARMFUL ASPECTS OF LICENSING

Unnecessary Training Requirements

One of the most common regulatory barriers to entry in an occupation is an education or experience requirement, which is often coupled with an exam or two. Of course, the “learned professions” have required specialized degrees for well over a century in this country (Young 1987). As documented by Carpenter et al. 2012, states also have extensive education and experience requirements for many occupations that are commonly held by low- to moderate-income Americans. Alabama requires 385 days of training to be an auctioneer. Arkansas requires 1,825 days to be a door repair contractor. Texas mandates 1,465 days of training to be a sports coach in a school.

The wide variety of these requirements, with scarce evidence of varying quality across states, begs the question of whether these requirements are in fact required to preserve health and safety. Connecticut has no manicurist license; Alaska requires three days of training to be a manicurist; California requires 90; Alabama requires 163. Arizona requires 1,460 days to be a carpenter or cabinet maker, but Colorado has no license requirement. It is hard to understand why there is so little consensus on the minimum training required for a person to be competent enough that the government will allow him or her to pursue the vocation. It certainly seems plausible that some states are requiring more days of training than is necessary.

Education and experience requirements are potentially troubling for several reasons. By their very nature, they delay a person’s employment opportunities, resulting in lost wages and opportunity costs. Vocational schools also cost tuition dollars, which many people can ill afford in this economy and no people should be forced to pay unnecessarily in any economy (Schlomach 2012). Such costly requirements are hardest on the poor or disadvantaged in our economy. And they may be harsher on minorities, who often have less financial security. Harrington and Treber (2009) showed that blacks, Hispanics, and people wishing to switch careers later in life are disproportionately excluded from interior design jobs in the states that require licenses (which require an average of 2,190 days of experience or education).
Even apprenticeship or supervised experience requirements, though they might allow people to work for a wage, have the potential to suppress job creation because they forbid people from starting their own businesses offering distinctive services and creating jobs for others if the business grows. Given that new businesses dominate in job creation, preventing people from starting their own businesses quickly is shortsighted in trades or professions where the apprenticeship is not necessary to train a novice in safe practices.

Education and apprenticeship requirements also give the people who are already established in an occupation authority to decide who will be allowed to enter the occupation as their competitors. Schools for licensed trades often have to be licensed too, and teachers may need to have the licenses their students are seeking. Licensed schools are often represented on the board that oversees the occupation’s licensure requirements for the state (Rose, 1980). The schools have a direct financial stake in the state’s educational requirements, and they are more likely to advise legislators to increase than decrease requirements (Harper 2003).

Any requirement that someone work for a licensee before getting a license creates a suspicious conflict of interest. The people most threatened by potential competitors are the very gatekeepers for the license. The existing businesses might discriminate in whom they take on as apprentices, or they might refuse apprentices altogether. The Illinois Supreme Court has said such apprenticeship requirements are unconstitutional because they give the incumbents a monopoly over the occupation (People v. Brown 1950). To make sure people can create jobs for themselves instead of being shut out by the old boys club, states and local governments should scrutinize apprenticeship or experience requirements carefully.

Finally, it is demeaning and wasteful to require people to spend lots of valuable time taking classes that they do not need to provide customers with what they want. Because the licensing boards, full of licensees, tend to want to expand their power and eliminate competition from businesses that customers might view as alternatives to the licensed businesses, they interpret their statutory authority broadly (Carpenter et al. 2012). As a result, people for whom the license was never intended and the educational program is not designed are often still required to meet the requirements. Carpenter et al. (2012) supply numerous examples. Cosmetology boards in several states have insisted that eyebrow threaders and hair braiders and makeup artists need to get cosmetology licenses, even though the extensive coursework required has nothing to do with the services they provide. The Connecticut dental association claims that people who are not licensed dentists should not be able to help people apply over-the-counter teeth whitening products. Texas decided that a computer repair person who would look at data on computers had to get a private investigator license. Someone with an entrepreneurial spirit and a drive to be independent—the kind of person most likely to start an innovative new business that could create new jobs—might be the least likely person to give up weeks or years sitting through irrelevant classes just to get the government’s permission to start a business.
Melony Armstrong’s story, as told in Carpenter and Ross 2009, demonstrates the entrepreneurial and economic potential that can be unleashed when inappropriate or excessive training requirements are lifted.

Melony’s drive to start a hair braiding business in her hometown of Tupelo, Mississippi, started in a classic fashion. It’s a textbook example of Kirznerian alertness: simply put, she spotted an opportunity to provide a quality service at a profitable price in her own hometown where it was not available.

The vision came in a rush. Her husband had driven her an hour and a half into Memphis to get her hair braided as a special treat. She paid $75 for a simple hairstyle. And suddenly she realized there was an opportunity to build a successful business braiding hair in Tupelo if she worked hard to provide great service.

She learned her trade the way people have learned how to braid hair for centuries. She sought guidance from experienced braiders, and she practiced. And practiced and practiced. Eventually her models started to pay her for her skillful braiding. She was in business right at home.

Melony’s skills and eager customers were not enough for her to get permission to start a “legitimate” business in Tupelo, however. She had to sit through 300 hours of classes that were unrelated to braiding in order to get a wigology license so she could open a natural hair care and braiding shop. From there, she grew her business gradually by creating demand for a service that Tupelo women were not used to buying. She had to prove to potential customers that her braiding skills were worth an investment. And she succeeded.

As demand grew for Melony’s business, she saw that there was opportunity in the market for more women to make a living and support their families by braiding. Melony created jobs for several other people to work in the shop. She wanted to share all she had learned about braiding and business and teach her trade to still more people so they could build businesses in their own towns and create jobs for themselves and others. But again, her government dashed her hopes of expanding her own business and helping people create new jobs.

To teach others to braid, Mississippi required Melony to spend 1,200 hours in classes to get a cosmetology license and then spend 2,000 hours in classes to earn a cosmetology instructor’s license. (These requirements are not unusual. Carpenter et al. ranked cosmetology as the fourth most burdened low-income occupation in the country when taking both the breadth of requirements and number of states burdening the occupation into account. For comparison’s sake, it is notable that a firefighter in Mississippi needs only 240 hours of class time to learn about safety and proper procedures.) In all that time away from her growing business and her family, she surely would have lost money and momentum, but she would not have learned anything about braiding or braiding instruction. The classes were totally unrelated to the work she wanted to do. Indeed, it was precisely because there were no braiding classes available in Mississippi that Melony wanted to start teaching.
One might wonder why common sense did not prevail and why no one determined that a braiding teacher should be exempt from these training requirements unrelated to braiding. As is common (Rose 1980), the cosmetology licensing system in Mississippi is overseen and enforced by a state board comprised of licensed cosmetologists. There are official advisory roles for licensed cosmetology schools. When confronted with the question of whether their licensing requirements apply to braiders, the board is invested in saying yes. The licensed cosmetologists on the board do not want competitors styling hair without losing time and money on training like cosmetologists do. After all, any entrepreneurs who are allowed to start their businesses and hire others who did not lose money to years of training might charge lower prices. And the schools on the board are not inclined to suggest that braiders should be exempt from requirements to pay tuition. So they strive to convince the legislators that the braiders do pose a threat to uninformed consumers or, more frankly, to the beauty salons that are established as the legislators’ constituents (E.g., N.C. Legislative Committee 2009).

The injustice and foolishness of Mississippi’s training requirements incited Melony, and she applied all her entrepreneurial spirit and passionate persistence to changing the system. Every week, she made a seven-hour round trip to the capitol to talk to legislators about changing the law. She also bravely joined with some other braiders to sue the state for its unconstitutional restrictions on her freedom to earn an honest living. Her hard work and sacrifice paid off. In 2005, the governor of Mississippi signed a law declaring that braiders need only to register with the state, pay a $25 registration fee, and follow health and sanitation laws to ply their trade.

Melony knew that allowing braiders to work without forcing them to receive costly, unnecessary training would create important opportunities for people in her community, including people who did not previously see a realistic path to employment. As Chervy Lesure, a hair braider who trained under Melony and worked in her salon, said, “The results of the lawsuit have given an opportunity to people who had the talent to braid but couldn’t and were on public assistance.” Jackie Spates, another hair braider who learned from Melony and worked in her salon, agreed. She said, “Other braiders now know they can open their own business and take care of themselves.” Indeed, women who were scraping by braiding in their kitchens for friends and family were enabled by the law reform to start businesses in the open that could serve the general public, and they began to earn a good living.

Melony also knew that opening up the market for competition would be good for her hair braiding business as well as her teaching opportunities. The more that braiders established themselves in Mississippi, and the better they became at providing attractive natural hairstyles, the more demand there was for braiding services. The braiders built demand and the demand built opportunities for more braiders.

As of 2009, when Carpenter and Hoss profiled Melony, she had employed 25 women in her salon, 12 of whom went on to open their own salons, and she had taught 125 women how to braid. In the four years
since the registration system had been created, 300 individuals were registered hair braiders in Mississippi. Who knows how many others—braiders or not—were inspired by Melony because they saw it was possible to start a business and succeed?

It is true that eliminating training requirements might have destroyed some jobs in the trade schools. It seems probable that those lost teaching jobs are far outnumbered by the hundreds of braiders who were able to pursue jobs efficiently under the new system, in turn building demand for their services and patronizing other businesses such as accountants, contractors, and suppliers. States that maintain extensive education requirements for braiders out of deference to the schools, even if they are lower than those required for cosmetologists, will probably not see the increase in licensed braiders that Mississippi has experienced (Adams et al. 2003; Barker 2008).

However, sometimes regulation creates a compliance industry that does create jobs. For example, when environmental standards are tightened, some jobs are lost in businesses that cannot afford as many employees while meeting the new requirements, and other jobs are created in companies that help businesses meet the standards. It is contentious whether specific environmental regulations have resulted in net job growth or loss (Broder and Rich 2011). Nonetheless, the environmental laws are legitimate only if they were passed for legitimate health and safety reasons, and their benefits were seen to outweigh their costs.

Requiring needless coursework before permitting someone to earn an honest living has no public benefit and presents a serious cost of liberty. It’s worse than breaking windows to create jobs repairing them; it’s like breaking arms to create jobs repairing them. Courts have repeatedly found such irrational training requirements to be an unconstitutional deprivation of due process (St. Joseph Abbey v. Castille 2013).

Moreover, it is simply bad policy to force businesses to buy something they don’t need just to prop up jobs in the businesses supplying the useless item. For example, an artisanal ice cream business in Chicago called Nice Cream was shut down because it did not use a $20,000 pasteurizing machine. Instead, Nice Cream pasteurized (or, rather, repasteurized) milk on the stove in small amounts. Requiring Nice Cream to buy the machine may have been good for a fraction of a job in the business (probably in some other region) that makes the machine, except for the fact that Nice Cream shut down because it could not afford the machine. Taking the logic a bit further, the state could require all businesses to buy pasteurizing machines, and that might support jobs at the manufacturer too, but it seems clear that it would not create job growth overall. Businesses cannot even start when they are forced to pay for training that has no value to the business. When the businesses can’t start, they have no chance to create jobs.

Hair styling and many other occupations that currently require licensing can be performed successfully, safely, and economically without any training requirements or with significantly reduced requirements. By
allowing people to get to work faster and build markets for their services, governments will allow them to create jobs for themselves and others. To facilitate job creation, states and local governments should reduce or eliminate training requirements for jobs wherever possible. They can start by reviewing Carpenter et al. 2012 to see which occupations do not require as much training in other states. And they can eliminate the trade schools, whose conflict of interest is manifest, from positions of influence or leadership in the decisions about training requirements. The lobby of licensed schools and predecessors who had to run the gauntlet of unnecessary training themselves will squeal. But legislators owe it to their constituents to serve the economy as a whole instead of the small, noisy special interests.

**Unnecessary Facility Requirements**

Many businesses are required to have specific layouts, equipment, amenities, and facilities before they can start serving customers. Some requirements are clearly tied to health and safety, such as hand washing sinks and working drains in a restaurant. Others arise when legislators react to a particularly salient story about a business engaged in crime or fraud. For example, massage establishments in Chicago, if there are ever more than five people present in the establishment, have to have separate bathrooms for men and women (Chi Mun. Code 4-92-052(a)(3)), because some massage establishment at some point must have used the bathroom in furtherance of its illicit sex trade.

Still other businesses are subject to extremely specific requirements about the space they use and its layout, because established businesses convinced the lawmakers to codify the way they were already doing business. Not surprisingly, some of the businesses with strict facilities requirements are the same businesses with licensure schemes that are overseen by boards made up of licensed practitioners. Barbers in Arizona are under strict requirements for their shops (Rose 1980). In many states, funeral homes have to have embalming rooms, even if the business will not embalm on the premises (Harrington 2007). Such requirements are costly and may pointlessly incapacitate businesses that otherwise could employ people. For example, in states where funeral homes are required to have embalming rooms, funerals cost $546 more on average, and fewer alternative or innovative services are taking hold (Harrington 2007). Harrington calculates that the embalming room requirement results in $58 million in welfare losses each year. Where such requirements are imposed on businesses that do not have any conceivable need for those facilities, the requirements might be irrational and unconstitutional (St. Joseph Abbey v. Castille 2013).

Like any other costly threshold requirements for start-ups, specific requirements for facilities can be especially unwieldy and inappropriate when applied to innovators. An online business selling caskets may not succeed in a state where funeral services require the maintenance of an embalming room (Harrington 2007). A green energy start-up trying to convert restaurants’ leftover cooking grease to fuel for automobiles
is stopped in its tracks when it learns it needs to build a standard oil refinery. The requirements can impede job growth if they are blunt instruments instead of tailored regulations that simply ensure health and safety.

On top of licensing requirements, zoning codes impose a separate set of rules about where businesses can set up shop. Before a business can get a license, it must typically demonstrate that it will be in a location that is zoned for that business. Up until recently, an urban farm in Chicago could not possibly get a business license because no land in Chicago was zoned for farming. The zoning rules can hamper a business’s activities. For example, a bakery in a location zoned for retail may not legally sell cakes wholesale for someone else to sell online. The bakery’s business has a harder time growing and creating jobs, and so does the online business.

Numerous American cities have strict rules about what businesses can operate as home-based businesses. Zoning departments loyally adhere to an aesthetic ideal of residential neighborhoods that are havens from the workplace (Garnett 2001). Under this rationale, a business in a home should not produce noises or smells that disturb the neighbors. Homes should not have the outward appearance of businesses, because that would change the character of the neighborhood, so they are often not allowed to hang signs, and they are not allowed to park commercial vehicles on the street or perhaps even in the home’s garage. Indeed, even internally, homes should not be used for a business purpose that domineers the residential purpose, so home-based businesses are limited to 15 or 20 percent of the space in the residence. Residential streets should not be crowded with traffic, so the numbers of customers visiting or employees working in the home are limited. Any work taking place in homes should be hidden, and is perhaps altogether illegal (Cates and Merriam 2006, Beale 2004).

But these restrictions are outdated. Women, in particular, are interested in finding ways to create jobs that allow them to attend to duties at home too (Garnett 2001; Clowney 2009). Technology makes it possible for many businesses to operate in home offices without any impact on the character of the neighborhood. Indeed, data collected by the U.S. Census Bureau shows that the population working exclusively from home increased from 4.8 percent of all workers in 1997 to 6.6 percent of all workers in 2010, and nearly half of home-based workers were self-employed, running their own businesses (Mateyka et al. 2012).

Flat restrictions on home-based businesses regardless of their externalities or impact on the neighborhood ban the very kind of low-budget, experimental market testing that is necessary for an innovative start-up. Chicago’s rules against operating a business in a garage or making a product that is sold elsewhere would have outlawed Amazon, Dell, Microsoft, and Chicago’s own The Pampered Chef. If those businesses had never started, America would have lost hundreds of thousands of jobs.

Even more surprising, many cities explicitly prohibit job growth by home-based businesses (Beale 2004; Garnett 2001). Zoning codes often proscribe hiring anyone who does not live in the home or, as in Chicago’s
case, more than one non-resident. In spite of the fact that a business might serve customers off-site, so the employees never need enter the home office, or a business might have employees working remotely via internet or telephonic connections, the business is not allowed to create those jobs unless it moves out of the home prematurely (Beale 2004).

The fact is, of course, that Amazon, Dell, Microsoft, and the Pampered Chef did start. Their founders probably did not check the zoning code before experimenting with their business concepts. And many dot coms have started since, operating out of basements and coffee shops, without regard for the law or thought of applying for a business license. After all, the most creative entrepreneurs are rule breakers by their very nature. They are not thinking of getting permission in City Hall to set up a home office but planning to take over the national or global marketplace by doing things differently than everyone else.

It seems clear that many home-based businesses start up without a business license or a zoning review. Chicago’s records show that 604 businesses have current home occupation licenses, yet the Small Business Administration says more than half of America’s businesses are home-based (Beale 2004).

Obviously prohibitions on home-based businesses are not wiping them out, but they may still be depressing job creation unnecessarily. The only people who may be discouraged from starting a business at home are the people who actually check the law, including those with lawyers. And such people do exist.\(^1\) Over-broad restrictions on business activity, even if their intention is to give an enforcement option to the government in extreme circumstances, can penalize the law-abiding citizens unintentionally. It is a waste of human potential to lose any start-ups or jobs to unnecessary, outdated laws.

Moreover, laws prohibiting beneficial home occupations or outlawing employees who work outside the home make the government look frivolous. They deteriorate respect for the rule of law. And they express a callous disinterest in people’s ability to earn a living in a prudent, creative way. Yet, entrepreneurship is most likely when people grow up in a family and in a city where small businesses are valued and experimentation is prized (Glaeser et al. 2012).

The story of Mark Andrews and his visit to City Hall should serve as a cautionary tale.

Mark Andrews is a kindly, mild-mannered, middle-aged man. He has worked for several different companies as a security officer. After being laid off from his most recent job, however, he decided to create his own job security by starting a business. He had often taken painting jobs on for family and friends, to their great satisfaction, and he decided to build a business out of his talent, work ethic, and experience. He christened the business Cosmetic Interior Concepts.

\(^1\) I am sometimes the person who discourages them with the information about the laws, which I doubt are ever enforced. In the last few months, I spoke to a woman who decided not to sell vintage jewelry on Etsy because Chicago would load her down with disclosure requirements like she was a pawn shop, and I counseled another woman who questioned her business plan to make organic pet food because Chicago would not allow her to sell it wholesale without a commercial location.
Mark had a clear goal, not only to be his own boss, but to provide jobs from the start for two other men he knew who were in need of work. He also looked forward to training his teenage sons in the business, so they would learn his meticulous standards and principles of professionalism and eventually take leadership roles in the company. Because Mark wanted to have tight quality control over the work done in his company and the nature of the customer service, he planned to train all his workers and supervise them closely. As a result, they would be classified by the IRS or the Illinois Department of Employment Security as employees, not independent contractors.

Mark was determined to do everything right. He enrolled in classes about business planning and computer literacy. He worked with a legal clinic to set up a corporation in the state of Illinois. He learned about the pamphlets that Illinois requires home repair businesses to hand out to customers to explain their rights. And he made an appointment in Chicago's Department of Business Affairs and Consumer Protection ("BACP") to get a business license.

Mark explained to the business consultant that he planned to start a painting business with a home office. The consultant asked where he planned to keep his tools (presumably his paint rollers and ladders) and his van. When he suggested he would keep them in his own garage, the consultant told him that was not allowed by the zoning department. He was not allowed to keep them in a garage space rented from a neighbor, either, because that building was also zoned residential. He was not allowed to park his van on a residential street or a commercial street, either, except when he is unloading. The only acceptable storage for a van and ordinary home equipment was a storage facility in a part of the city zoned for parking and storage. That storage would cost CIC around $200 a month.

Next, the BACP bureaucrat asked Mark if he would have employees. Mark brightly answered that he planned to hire two people. The business consultant shook his head. “You cannot hire more than one person.” Mark pointed out that his employees would never have need of coming to the house. The licensing code on home occupations says only that home occupations may not have more than one nonresident employee working at the home. But, the city responded, the zoning code says there may not be more than one nonresident employee “in connection” with the home occupation.

A deputy suggested CIC could just hire subcontractors instead of employees. But, as a matter of law, it is not at CIC’s discretion to call workers subcontractors if the company controls the way in which they work so that customers will get the best service. Plus, a court might decide that independent contractors are also prohibited as employees by the zoning code (Windsor Charter Twp. v. Remsing, 2004). The only legal way for Mark to hire people would be to rent office space for his business. The money wasted on office space and commercial parking for his business could instead be spent on wages for an employee.
The impact of these unnecessary expenses on Cosmetic Interior Concepts is not yet known. Mark just started his business recently, under the handicap of extra expenses. Nonetheless, it was rather stunning to learn that the City of Chicago is telling people not to hire employees when the unemployment rate is 10.5 percent as of July 2012 (the third highest of any major city in the nation, the national average being 8.6 percent). It is even more stunning that cities across the country are sending the same message to entrepreneurs who are trying to follow the law. Though cities might argue that employees of a home-based business, like customers, increase traffic undesirably in a residential neighborhood, that is not a reason why employees working at alternating shifts, employees who take public transportation, or employees who never come to the home office at all, should be prohibited (Beale 2004).

As with training requirements, state and local governments should scour facilities requirements to make sure they include no more than is necessary for health and safety. If specific facilities or equipment are necessary to conduct a certain activity safely, then they should be tied to that activity, not to the general category of business. For example, an embalming room might be required of businesses that will embalm, rather than all businesses that provide funeral services. Zoning codes should limit home businesses only as necessary to prevent externalities that affect the neighbors, so that home businesses can spend money on hiring workers instead of useless office space. Any limitations on home businesses’ employees should be reviewed carefully. At the very least, the law should not outlaw home businesses from hiring people who do not work at the home office (Model Home Occupation Ordinance 2009).

**Unnecessary Classification**

By their nature, business licensing laws identify specific categories of businesses and outline the requirements for any entrepreneur starting such a business. Inversely, they prohibit businesses that fall within that category but do not meet the requirements. As a result, business licensing laws present the serious risk that the legislators will unintentionally outlaw an innovative way of doing business that they did not anticipate, perhaps because it was not yet invented when they drafted the law.

Harper (2003) explains, citing Hayek, that laws should be broad and general to promote equality and freedom and, therefore, entrepreneurship. In a society governed by the rule of law in its ideal form, the laws are principled rules that are abstracted from any one situation or set of people, and they apply equally to everyone. For example, there are rules prohibiting all businesses from harming their customers or their neighbors, such as proscriptions of fraud, assault, and pollution. Entrepreneurs with creative new ideas are free to pursue them as long as they are not breaking the rules that govern everyone in society.

When laws are written to govern specific groups of businesspeople, in contrast, the laws make innovation very difficult. Licensing laws are perfect examples. A business licensing scheme sets forth how a specific
kind of business, such as a salon, a private detective agency, or a law firm, can operate and whom it can hire. The scheme discriminates against everyone who does not fit the mold, based on an assumption that the nonconformists would hurt their customers or their environment. As a consequence, the licensing law eliminates the possibility that the person who does not fit the legislators’ expectations could start a business that hurt no one and in fact served customers in a new, efficient, affordable way. Even if licensing laws are written with great attention to the health and safety of the public, they embed the legislators’ understanding of how businesses operate safely in a specific industry, and they freeze the model in time (Maxwell 1998).

But the whole nature of innovative entrepreneurship is that it cannot be predicted! Who would have guessed that a mold would be the miracle cure for infections or that a kid who hadn’t graduated college would fiddle around in his garage and eventually create software that the entire world uses? The individual who does the most unexpected thing is the one who can do us the most good, if given the freedom to do so (Hayek 1960). Laws that mandate all businesses to continue using the best practices at the time the law is drafted deprive us all of better practices.

The hazard of outdated, overspecified business licensing laws has been especially apparent in recent years, as entrepreneurs have figured out new ways to provide services and goods on the Internet. Naturally, licensing schemes that predate the Internet were written for in-person services and sometimes have requirements that are irreconcilable with dot com innovations. For example, many states have license requirements for nutritionists or dieticians, who give people customized advice about what they should eat to improve their health. Creative programmers who figure out an algorithm for offering customized dietary advice over the Internet might not be allowed to serve customers in some states without a license. It is not even clear whether the business could get the required licenses since the algorithm could not get the requisite degree in nutrition science. Another dot com that matches babysitters to customers online, like SitterCity, could be prosecuted in some jurisdictions because it fits their definition of a day labor agency and does not have a waiting area for applicants. It would be a shame to stop SitterCity from creating jobs internally and playing its part in helping babysitters get jobs, just because it does not fit a traditional, but legally required, model.

If legislators wanted to update a licensing law in light of recent innovations or new technology, they might face serious pushback. Imagine what the professional association of nutritionists and the board overseeing licensure would say if legislators wanted to open their profession up to anyone with an internet connection. As Harrington 2007 lays out, the incumbents in the funeral profession have convinced Arizona’s legislature to keep its rules in place for all businesses in the funeral industry, in spite of the fact that independent commissions have recommended changes to open the market up to innovators. As he wrote, “The economic chemicals needed to preserve the status quo are harsh, leading to higher funeral prices and often poorer-quality services.” (Harrington 2007).
When lawmakers target specific groups of people, with a burden or a benefit, they also give that group a serious stake in the way those laws are written. The targeted group is likely to get more involved in the legislative process, and the law will be influenced by the intense voice of the small minority instead of the public interest as a whole. Private interest groups will also come to understand that they have the chance to get special benefits from the government in the form of laws, so they may draft up new laws to benefit their groups and try to get them passed.

Special interest legislation, or regulatory capture, is indeed rampant in the area of business licensing, as I have pointed out throughout this paper. As Djankov et al. (2002) determined, laws regulating the entry of new enterprises into the marketplace are much more about the goals of private interests and the legislators looking for campaign contributions from the private interests than about protecting the public. They are hard to change once in place (Young 1987).

The pressure on legislators to have highly specified licensing requirements that exclude new business models can be great. Consider the experiences of Uber, a young company that is using the creative and analytical powers of mathematicians, statisticians, and programmers to put a new twist on the car service business. Customers can use Uber on their mobile phones to find out what sedans are for hire in the neighborhood and book them. Uber provides independent drivers with information about where it is best to be at different times to get hired. Uber’s sales pitch is that it provides rides with convenience and class. Uber is not only creating jobs in its start-up for programmers, analysts, sales agents, designers, and others, but it is helping independent car companies grow their businesses as well. It is building a demand for a new kind of “smart” transportation service, and other companies are following its lead, creating more jobs with the goal of improving transportation with technology.

Uber has had regulatory battles in every city where it has tried to establish its business, either because the existing categories of limos (reserved in advance and paid by the hour) and taxis (hailed and paid by the mile) did not have a place for Uber’s model (reserved and paid by the mile) or because the taxis pushed the lawmakers to change the rules after Uber arrived to make Uber’s model illegal (McArdle 2012). The taxi companies have built up political influence over years of lobbying, donating, sitting on the commissions that make the rules, and building relationships with city councils. They are normally much more influential on questions of taxi regulation than the customers. Uber, however, is engaging its customers in the debate, and it may be able to keep the exclusionary licensing rules at bay in markets where it is operating. Other cities, where the rules were too hostile for Uber to enter, will not benefit from the economic development of Uber’s fast-growing company.

The story of Logan Square Kitchen in Chicago is another pointed example of how overspecified business license categories can suppress innovation and cost a city jobs. I have learned the story through conversations with the business founder, as well as newspaper articles and blogs (Bayne 2010).
Zina Murray was on the forefront of the locavore movement in Chicago. She wanted to encourage local food production, because she believes that locally produced food is healthier for consumers, the local economy, and the environment. As entrepreneurs tend to do, she put her passion into action. She developed a plan for the Logan Square Kitchen, which would include a state-of-the-art commercial kitchen, where small food businesses could rent space by the hour to experiment with recipes or prepare food for sale legally, and a lovely event space for food markets, pop-up restaurants, or private parties. She wanted the space itself to be healthy for consumers, the economy, and the environment too, and she committed to using green construction materials in an old building on an under-utilized commercial strip in her neighborhood.

Zina and her husband took out a mortgage and bought a vacant, foreclosed former furniture store in walking distance of their home. They applied for building permits to transform the space. After reviewing their plans and the description of the business plan, the Buildings Department classified the business as a restaurant, which did not need a parking lot due to its size. The Zoning Department signed off on preliminary construction plans in March 2008 and on final plans in January 2009.

As the build-out took shape, Zina hired an expediter—a licensed professional license and permit seeker—to help her apply for business licenses. The expediter described the multifaceted business model to the Department of Business Affairs and Consumer Protection: Logan Square Kitchen would rent out its kitchen facilities by the hour, it would host markets where customers could come discover local food producers, it would allow chefs to cook food in the kitchen and serve in the dining room, and it would rent the facility out for private events like weddings or other celebrations. After consulting with the Department, Logan Square Kitchen applied for a retail food establishment license (as a kitchen where food would be prepared for sale to customers), a liquor license (for any events where liquor was served), and a public place of amusement license (for any large markets where customers would buy tickets to attend).

Logan Square Kitchen received its retail food establishment license in August 2009, but an inspector who visited in September decided the business actually fit into the category of a banquet hall rather than a restaurant. Zina was informed by the city that she needed to provide off-street parking spots adjacent to her business, because the business was now considered a banquet hall. Because large groups of people arrive at once at a banquet hall, the city code requires parking spaces. Logan Square Kitchen could not serve liquor or receive the PPA license until it provided parking. Given its location in an old building on a dense city block, however, the kitchen simply had no parking spaces to provide. So began a long, drawn-out battle over whether the business fit in the restaurant category or the banquet hall category.

Then, in February 2010, the whole business model of a shared kitchen was called into question, because it did not fit in any of the city’s food establishment categories. In a surprise inspection of a shared kitchen called Kitchen Chicago, inspectors asked to see the licenses of the little businesses who rented the kitchen by the hour, but the entrepreneurs did not have their own food establishment licenses. Some of them had
contacted the city to apply for licenses and had been told they could not get food establishment licenses at an address that already had a food establishment license. So everyone believed the kitchen’s license covered the users. After all, the city had licensed the shared kitchen and inspected it, knowing that the kitchen space would be rented to other businesses by the hour. And the city told the renter businesses that they could not get their own licenses.

The inspectors declared all the food prepared in the kitchen to be unlawful, and they poured bleach over beautiful fruit purees made there by a confectioner. A Chicago Tribune reporter happened to be there that day researching a story on the local food movement, and she videotaped the destruction. The video went viral.

In response, the city announced that it was happy to license multiple food businesses operating at the same address. From then on, each budding entrepreneur that wanted to rent time in Logan Square Kitchen had to be licensed as a retail food establishment for a $660 fee. The facility was inspected each time as if it were a brand-new restaurant. (Logan Square Kitchen was inspected top to bottom about 20 times in two years.) Renters preparing food to sell at farmer’s markets, however, fit in a different category and did not need a food establishment license at all.

There was a lot of demand for Zina’s business among people who wanted to start a business legally but could not afford to build or buy a kitchen as a first step, as well as among people who wanted to host events in a green space, but the uncertainty of the city’s enforcement of licensing laws was dragging the business down. Zina had to convince clients that they should invest heavily in licenses to operate at the Logan Square Kitchen, even though the city was threatening the business with closure if it did not produce parking spaces where there were no parking spaces. She could not allow liquor to be served unless it was served by a caterer with its own liquor license. By necessity, she spent a lot of her time working with lawyers and negotiating with the city and repeatedly walking inspectors through her gleaming, new space, instead of building the business.

In November, 2010, the Zoning Board of Appeals heard the question of whether Logan Square Kitchen was a restaurant or banquet hall. A crowd of supporters attended the hearing, and Zina presented 275 letters of support. The Board asked the Zoning Department’s representative why the private parties were not simply an accessory use to the primary use of the space as a retail food establishment. The Board pointed out that other restaurants rent out their spaces occasionally for private parties without transforming into banquet halls. And the Board decided, just in time for Thanksgiving, that Logan Square Kitchen could continue as a restaurant.

The city also rolled out its reforms to the code to allow for shared kitchens. Instead of broadening the categories in existence, so that innovators would not fall through the cracks, the Department of Business
Affairs proposed a new 15-page law, with four new license categories. The City Council passed the law, creating a lot more cracks for innovators to fall through.

Under the new law, a potential client of Logan Square Kitchen could get a Shared Kitchen User license, which was less expensive than a full retail food establishment license and was available for a short term. The kitchen was not inspected for every new client, but other problems arose. Here is Zina’s description of the new regime:

“In place of site inspections, Shared Kitchen Users now have a consultation with a Health Department Supervisor. Ironically, this inspector is the same person that destroyed thousands of dollars worth of food at Kitchen Chicago two years ago (captured on video). With the advent of the consultation, businesses are taking longer to get licensed, often having to make multiple trips to City Hall for reasons that don't make sense. We have seen licenses held up for food labeling reasons, despite the fact that the STATE approves labels, and the City has no role. I've taught my clients to nod at the bad direction, and we'll do it right after they get their license.”

In addition, the Department of Business Affairs required the Shared Kitchen Users to get badges identifying them and to be present at all times when operating in the kitchen. So a small catering company could not hire certified chefs to cook in the shared kitchen without the owner being present. Again, because the lawmakers had a very specific sort of business in mind for the category of Shared Kitchen User—namely, a sole proprietor—they wrote laws that made it difficult for any other variety of business.

In May, 2012, Zina announced that the Logan Square Kitchen would close. She explained that the delays, uncertainty, expenses, and distractions created by the city’s management of her business licensing made her business financially unviable. Mayor Rahm Emanuel had taken steps to improve business licensing since taking office, but he had not yet managed to reform food business licensing. And damage to Logan Square Kitchen was already done.

As Zina had said earlier:

“'When I looked at building this place and I looked at all the risk and all the things that could go wrong, it never, ever occurred to me that the city would be my greatest problem,'” says Murray. “'I thought, the City of Chicago’s going to love this business. It’s green, it helps the economy, it helps the environment—it’s a local, long-term person investing in where they live. How could it get any prettier than that?’” (Bayne 2010).

When Logan Square Kitchen closed, the city lost countless jobs. The Kitchen itself might have hired only a few people, but it was meant to be a small business incubator. Chicago has already seen some restaurants and growing companies blossom after starting out in a shared kitchen. One of Chicago’s top restaurants, The Girl and The Goat, was even preceded by a pop-up restaurant in Logan Square Kitchen. It was meant to be a
place where entrepreneurs could test the market affordably and legally. But those entrepreneurs have fewer options now, and those who want to start legally may not be able to start at all. We will never know how many jobs they might have created if they had the chance.

Zina herself continues to advocate for reforms of the city’s licensing regime. In a hearing in July of 2012, where a committee was considering adding another two categories to the list of food licenses in Chicago, she urged them to limit business licenses to two categories: food enterprises and food facilities. She explained that a business making chocolate chip cookies might need one or two of eight different license types, depending on where it makes them and where it sells them. As a result, the licensing system is designed to create confusion and delay rather than permitting businesses to create jobs.

To avoid the needless job losses that Chicago suffered when Logan Square Kitchen closed, cities and local governments should take Zina Murray’s advice. Avoid drafting business license laws for specific categories of business models. Liberally allow creative entrepreneurs to try out new business models. Let experts in administrative agencies implement necessary, clear health and safety rules that apply to all businesses regardless of license type. Interest groups that argue that everyone serving the same customers should be regulated in the same way, even if they have different business models and present different risks, should be heard with skepticism; they may be trying mostly to protect their market shares rather than the public.

Cities and state governments might also follow Chicago’s lead by creating an avenue for licensure for new business models that do not fit comfortably in existing categories. Chicago recently created the “emerging business license,” which allows the Commissioner of the Department of Business Affairs to give a temporary license to a business that presents hazards but has no laws restricting its operation (Chicago Municipal Code 4-4-022). The Department can condition the license on health and safety rules. Then the City Council has some time to draft up the amendments to the code necessitated by the new business model without delaying an innovator’s start-up as much. If the City Council does not write new laws, the business loses its license after two years.

Yet, this reform should be handled delicately. Chicago’s approach is over-reaching and possibly unconstitutional. If a business is not restricted by laws written by elected officials, unelected administrators should not be allowed to prohibit it or restrict it based on their own individual preferences. Entrepreneurs who see a clear field in the law for a new business idea should not be upended by the decision of one official who thinks the business should be regulated. For this reason, Chicago’s process might be an unconstitutional delegation of legislative authority to an agency (Hanna v. City of Chicago 2009). A local government could, however, create a valuable process whereby innovative entrepreneurs could apply for exemption from certain inappropriate licensing requirements when they do fall within a regulated business category, similar to the process for a zoning variance. The government’s focus should be on moving out of
the way of new businesses so they can create jobs, rather than enforcing irrelevant or out-of-date laws that suppress competition.

Always Unnecessary Protectionism

As explained above, many business licensing laws are heavily influenced by existing businesses. They wind up being anti-competitive. They make it harder for new businesses to enter the market, and the businesses that are in the exclusive set of privileged service providers can raise their prices and make more money. They actually cap the jobs that can be created, rather than opening the market to new jobs. Some licensing laws go even further to include explicitly anti-competitive or protectionist provisions. Such provisions are clear targets for reform and repeal efforts.

Anti-competitive, protectionist provisions can take different forms. Sometimes they place a cap on the number of businesses that can compete. Sometimes they require businesses to show that the current businesses are not adequately serving customers—these are called “convenience and necessity” requirements. In Illinois, a household goods moving company has to present evidence at a hearing to prove its service is necessary, including the testimony of two sworn witnesses who say they cannot move to a new home unless the new company is authorized to perform the service (625 ILCS 5/18c-4202(2)). Sometimes, the licensing system gives existing businesses an opportunity to object to the entry of a new competitor (Carpenter et al. 2012).

As an example, taxicab industries are often stifled by anti-competitive provisions, like caps on the number of taxis allowed to operate (Greene 2011). Caps not only drive up the price of the medallion or license for a taxi, making it hard for any entrepreneur without extensive capital to create jobs, but they also directly limit the number of jobs in the industry. When Indianapolis lifted its cap on taxicabs, along with some other restrictions on pricing and staffing, 32 new companies started in six months, and 158 new taxis were operating within two years (Buckeye Institute 1999; Hardaway 1996). “In 1998 Dublin suffered from a distorted licensing system. Demand had doubled in the previous 20 years but the number of licenses had not kept up. Waiting times were over an hour. Deregulation in 2000 reduced entry costs (the cost of a car and a licence) by 74 percent. The result was more than three times as many cabs on the roads, lower waiting times, maintained cab quality and higher passenger satisfaction—all in two years.” (Barrett 2003; The Economist 2012). In 1974, the Department of Transportation published a study concluding that deregulating the taxi industry would create 38,000 jobs (Webster et al. 1974).

Protectionist laws may be passed out of concern for the ill effects of competition on existing businesses, but they can suppress job growth. When France set up local zoning boards to decide whether big retail stores would be allowed, the intention was to protect small shopkeepers, but the result was to prevent increases in
retail employment between 3 and 15 percent (Bertrand and Kramarz 2002). The legislative process is naturally biased in favor of the existing businesses, who can plead with the legislators for protection, as opposed to the future businesses, who are unrepresented. Yet the future businesses are necessary for job creation, and they should never be shut out if the government wants job growth.

Across the United States, food trucks are a hot trend. When allowed to flourish, they create significant jobs. One study determined that employment in street vending grew at an annualized 8.9 percent to 15,523 employees between 2007 and 2012 (concentrated in a few states), due to the surge in demand for food trucks, even though the recession pushed many households to reduce spending on food services (Samadi 2012). Food trucks also led to jobs in the traditional food retail industry. A food truck (or trailer) allows an entrepreneur to start with a small budget and then build capital and a customer base. For example, Torchy’s started six years ago as a trailer in Austin, Texas, selling gourmet street food, and the company now employs about 450 people. Food trucks also build up the entire food industry. In Austin, which has relatively few restrictions on mobile food, street food has contributed to the branding of Austin as a great culinary city and has drawn tourists and new residents. The number of employees in the metro area’s food industry rose from 58,838 to 68,635 between 2006 and 2010, with annual payroll jumping from $820 million to more than $1 billion (Gaar 2012). As food trailers are multiplying, more restaurants are opening and hiring people. Moreover, the food trucks’ suppliers, mechanics, and engineers experience growth.

Yet, in the name of protecting restaurants from “unfair competition,” many cities (including Austin) have laws in place that make it hard for mobile food vendors to operate. The story of Manny Hernandez and his Tamale Spaceship illustrates what happens when a city puts the brakes on food trucks. Manny told his story at a hearing in July, 2012, when Chicago’s City Council committee on License and Consumer Protection was deciding whether to recommend a new law governing food trucks. The proposal maintained a blatantly anti-competitive rule that food trucks have to stay 200 feet away from restaurants. Restaurants are defined as any place that prepares and serves food for consumption, so they include some Starbucks’ locations and 7-11 convenience stores. With the 200-foot rule in place, the areas of Chicago with the most customers for food trucks, most notably the downtown Loop, are off limits to food trucks, except for a few designated parking spots that the city promised to establish for the trucks. Moreover, the proposed law would tighten the screws on the 200-foot rule, hiking the potential fines for violations to $1,000-$2,000. It suggests that it is worse for a truck to park 175 feet from a restaurant than it is to serve unsanitary food, for which the fine is $250-$500.

Manny worked for high-profile restaurants in Chicago for years, but, like so many Americans, he was laid off during the recent recession. He decided to take his future into his own hands and start a food truck with the dream of opening a restaurant someday. Like some of the original food truck pioneers, Manny decided to sell gourmet updates of Mexican street food, but he is hardly a copycat. He called the truck Tamale
Spaceship and turned it into a tribute to the luchadores, the masked wrestlers and science fiction characters who were heroes to Manny and his business partners when they were children. The staff on the Tamale Spaceship are dressed in traditional wrestling masks and sombreros. The presentation may be quirky, but the food is magnificent. The truck was featured recently on a TV program dedicated to Chicago’s Best. (http://www.youtube.com/watch?v=vvTAbEtE-vM).

By the end of their first year of business, the truck was a stable business, hitting hotspots downtown just about every day and letting fans know its whereabouts through Twitter. Manny had gone from unemployed to being an employer of five. But, as the restaurants started urging the city to enforce its existing 200-foot rule, the police started ticketing trucks who were serving the office buildings downtown. They began to marginalize the food trucks. And then the mayor’s office proposed the new law that would increase penalties on food trucks for being too close to restaurants.

As Manny (and many other food truck owners) testified, the prospect of strict enforcement of the 200-foot rule and $1,000-$2,000 penalties for violations made him fear for his business. One parking mistake could wipe out a day’s earnings and require a food truck owner to spend another day in a hearing instead of on the road. Manny’s hopes of building the business into a brick-and-mortar restaurant (or perhaps many, as Torchy’s did in Austin) were dashed. But the City Council committee did not hear Manny’s testimony. After the committee members spoke, and the representatives of the Illinois Restaurant Association spoke, most of the committee members left the room. Someone was sent to fetch one more member to make quorum at the end of the meeting, so they could vote to recommend the new law.

Instead of letting Manny add to the five jobs he created, the city decided to squelch those jobs, even though there was no data suggesting restaurant employment would decrease with liberal food truck laws. Indeed, Austin’s data suggests the opposite. Chicago chose to be a city with 100-200 food trucks creating jobs instead of thousands like there are in Los Angeles, where the city has no anti-competitive laws squeezing them out.

To make sure that entrepreneurs like Uber, Tamale Spaceship, and Torchy’s can start and create jobs, state and local governments should purge their codes of anti-competitive rules such as caps on the number of businesses, convenience and necessity requirements that ask an entrepreneur to prove a new business is necessary to serve customers, and proximity restrictions that limit how closely businesses can compete.
Conclusion

To ensure that entrepreneurs and start-ups are free to create jobs, state and local governments should avoid business licensing laws that make innovation difficult or illegal. Here are some recommendations:

1. Pass a law providing standards for new licensing laws, so that the legislature is bound to confirm that they are necessary to protect health and safety of consumers (Schlomach 2012, citing Arizona example). Model laws are available (IJ Model Legislation; ALEC Occupational Licensing Relief and Job Creation Act).

2. Create a process for auditing current licensing laws to find outdated or unnecessary requirements. Michigan, for example, has an Office of Regulatory Reinvention that boasts it has eliminated 762 rules since April 25, 2011.
   a. Review Carpenter et al. 2012 to determine whether your state has heavier requirements than others for common occupations held by lower-income workers. Analyze whether the costs of job suppression and administrative expense can be safely reduced by matching the state with the lightest requirements.
   b. Focus reform efforts on licensing laws that apply to businesses providing services that customers (or employers) can understand and evaluate for themselves, so that there are minimal concerns about asymmetric information. If online reviews of the businesses abound, that is one good sign that customers can evaluate the quality of the services and decide whom to hire without government involvement. Licensing is not necessary if the worst of those businesses will only wreak temporary damage on the customer who chose them. Examples include cosmetologists and barbers, door repair contractors, makeup artists, cabinet makers, auctioneers, painters, interior designers, and landscapers. If workers are hired by specialized businesses rather than direct customers, the employers can often evaluate the workers’ qualifications without government-mandated licensure. Examples include veterinary technologists, crane operators, and bartenders. If there are still concerns about information asymmetry, consider converting the licensure requirement to a certification program, so customers and employers can learn whether service providers have passed a screen, but entrepreneurs are still free to start businesses without passing the one-size-fits-all requirements (Wheelan 2011). Professor Kleiner estimated that Minnesota would open up 15,000 jobs if it passed a law preferring certification to licensure (Kleiner Testimony 2011).
   c. Take an especially hard look at training or facilities requirements that determine whether a business is allowed to open. If necessary, require the training or facilities for a particular hazardous activity but not for a whole category of businesses just because they serve the same market segment. Examples include requiring extensive coursework about dying hair for
all people who will style hair, requiring embalming rooms in every location where funeral services or products are provided, and requiring an office or storage facilities in a commercial zone when a business would have no impact on neighbors in a residential zone.

3. If an occupational licensing board is necessary to bring expertise to bear on a hazardous, specialized, opaque industry, then require it to have members from the general public in significant numbers to ensure the consumers are represented (Schlomach 2012, citing Arizona example). Unfettered self-regulation by the incumbents in an industry usually results in barriers to entry for new businesses that are too high (Leland 1979). If possible, save money by eliminating occupational licensing boards. If a test is necessary, use a standardized test or have one created by objective experts to cover only the topics necessary for public safety, instead of by local industry incumbents who have a conflict of interest (Shimberg et al. 1973).

4. Create a process for entrepreneurs with non-traditional business models to apply for an exemption or variance from licensing laws that impose restrictions that do not protect the public, when applied to the particular business plan.

5. Amend zoning codes to allow home occupations to have unlimited numbers of employees who do not work at the home (Model Home Occupation License 2009).

6. Remove caps, requirements for certificates of convenience and necessity, proximity restrictions, and any provisions designed to limit competition directly.

By removing barriers to entry, government can create an open field for innovation and job growth. By sending a message to entrepreneurs that they are welcome as long as they follow fair and impartial rules, instead of a message that they are hazards to be restricted, the government can contribute to a culture of entrepreneurship that will create job growth for generations to come.
References


Dent v. West Virginia, 129 U.S. 114 (1889).


About the Big Ideas for Job Creation Project

Big Ideas for Job Creation, a project of the Institute for Research on Labor and Employment at the University of California, Berkeley, with the support of the Annie E. Casey Foundation, tapped into the innovative thinking of leading experts across the nation to develop job creation proposals. Every idea had to meet the following criteria: designed for implementation by cities and/or states and will lead to net new job creation in the short-term; practical, sustainable, scalable and already tested; and all jobs created should be accessible for low-skilled workers and offer some career opportunity. Taken together, these Big Ideas can create millions of new jobs for our country.