PERCEPTION AND ADOPTION OF OCCUPATIONAL LICENSURE BY ENTREPRENEURS

THE CASE OF TAX PREPARERS IN THE U.S.

Kyle Albert
Harvard University

Roman V. Galperin
Johns Hopkins University

Aleksandra Kacperczyk
Massachusetts Institute of Technology
ENTREPRENEURSHIP AND OCCUPATIONAL LICENSURE
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- Entrepreneurship is a labor market phenomenon
  - Engine of job creation
  - Results from individual career decisions
ENTREPRENEURSHIP AND OCCUPATIONAL LICENSURE

▸ **Entrepreneurship** is a *labor market* phenomenon
  ▸ Engine of job creation
  ▸ Results from individual *career* decisions

▸ **Occupational licensure** is a large labor market institution—a structural determinant of wages and employment
  ▸ Affects about a third of all U.S. workers
  ▸ Raises barriers to entry into an occupation
  ▸ Predicts about 18% higher wages
WHAT IS THE RELATIONSHIP BETWEEN ENTREPRENEURSHIP AND OCCUPATIONAL LICENSURE?
LICENSING MAY PLACE SPECIAL BURDENS ON [. . . ] THOSE WITH CRIMINAL RECORDS, MILITARY SPOUSES, TELEWORKERS, ENTREPRENEURS, AND LOW-WAGE WORKERS

OCCUPATIONAL LICENSING “FENCES OUT” ENTREPRENEURS, LIMITS BUSINESS INNOVATION, RAISES CONSUMER COSTS, AND EXACERBATES INCOME INEQUALITY

Kauffman Foundation Growthology blog, Feb. 4, 2016
THE BURDEN OF OCCUPATIONAL LICENSING IS STIFLING ENTREPRENEURSHIP IN AMERICA

Slivinski, S. 2013 “Bootstraps tangles in red tape”
ENTREPRENEURSHIP AND OCCUPATIONAL LICENSURE

- The assumed relationship is negative:
ENTREPRENEURSHIP AND OCCUPATIONAL LICENSURE

- The assumed relationship is **negative**: 
  - Licensing is a *barrier* that impedes entrepreneurial entry
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- A license provides incumbents with
  - Higher occupation legitimacy
  - Credible quality signal to individual practitioners
ENTREPRENEURSHIP AND OCCUPATIONAL LICENSURE

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  - The stated goal of licensure is insuring quality/safety
  - To the extent *legitimacy is a scarce resource* for nascent entrepreneurs, license is *valuable* to them
ENTREPRENEURSHIP AND OCCUPATIONAL LICENSURE

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  - To the extent legitimacy is a scarce resource for nascent entrepreneurs, license is valuable to them

We may therefore expect two opposing effects:
- The cost of obtaining a license \(\rightarrow\) negative relationship between entrepreneurship and adoption of license
- The value as a quality signal \(\rightarrow\) positive relationship
No studies test this directly or even consider the two opposing effects

- Slivinski (2013) report is the only empirical study of the negative effect
  - Correlates the extent of licensure in a state with entrepreneurial entry in low-wage occupations
  - Finds a negative relationship
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Measuring the value of license as a quality signal for nascent entrepreneurs is especially tricky

- Licensure is usually implemented as a universal requirement for an entire labor market
- Difficult to observe whether nascent entrepreneurs value it, e.g., through their proclivity to adopt it
THE CASE OF TAX PREPARERS IN THE U.S.
REGISTERED TAX RETURN PREPARER (RTRP) INITIATIVE

- Tax preparation does not require any license or credential in all but four U.S. states
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- Tax preparation does not require *any* license or credential in all but four U.S. states

- Following a GAO report, the IRS moved to institute a federal-level, mandatory credential (RTRP) in 2012
  - RTRP required passing a test, paying a fee, and taking continuing education
  - Effectively—a license
  - But phased in gradually—was not to become mandatory until 2014
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- We analyze who were the voluntary early adopters, and whether the adoption by nascent entrepreneurs is consistent with cost and value perspectives on licensure
ZIP CODE AREAS WITH EARLY RTRP ADOPTERS

- 2,795 tax preparers (about 0.4% of the 780K preparers in the U.S.) adopted RTRP in 2012, across 2,139 ZIP code areas.
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Including OR, CA, MD, and NY – states where tax preparers were licensed prior to RTRP
ESTIMATION STRATEGY: ADOPTION CONDITIONAL ON NEED FOR SIGNAL

Model: \( Pr(Adoption_i) = \beta_0 + \beta_1(\text{Entrep}_i \times \text{NoStateLicense}_s) + \beta_2 \text{Entrep}_i + \beta_3 \text{NoStateLicense} + X'_i \delta + C'_z \gamma + \mu_s + \varepsilon_{is} \)
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- **Data source:** 2012 and 2014 cross-sections of all tax preparers in the U.S.
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  \[
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  \]

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- **Sample:** case-control 1:2 sampling with geographic matching on ZIP code (2 randomly selected controls for each early RTRP adopter in a ZIP code), restricted by age - between 18 and 65
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- **Predictors** of adoption: career outcome within two years
  - No change in employment in 2014
  - Started or joined as owner his/her new practice by 2014
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- **Controls:** age, gender, professional credentials, competition in ZIP code
### Descriptive Statistics

<table>
<thead>
<tr>
<th></th>
<th>State requires license</th>
<th>No state licensure</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adopts RTRP in 2012</td>
<td>33% (by design)</td>
<td>33% (by design)</td>
<td>33% (by design)</td>
</tr>
<tr>
<td>Mean age in 2012</td>
<td>50</td>
<td>49</td>
<td>49</td>
</tr>
<tr>
<td>Mean number of tax returns filed in ZIP code in 2011</td>
<td>15,853</td>
<td>11,281</td>
<td>12,262</td>
</tr>
<tr>
<td>Tax returns filed with a paid preparer in ZIP code in 2011</td>
<td>9,929</td>
<td>5,972</td>
<td>6,821</td>
</tr>
<tr>
<td>Mean number of tax preparers in ZIP code</td>
<td>114</td>
<td>75</td>
<td>83</td>
</tr>
<tr>
<td>Percent of tax preparers with credentials in ZIP code</td>
<td>49%</td>
<td>35%</td>
<td>38%</td>
</tr>
<tr>
<td>Male</td>
<td>56%</td>
<td>46%</td>
<td>48%</td>
</tr>
<tr>
<td>No professional credentials</td>
<td>56%</td>
<td>74%</td>
<td>70%</td>
</tr>
<tr>
<td>Will start own practice by 2014</td>
<td>25 (2.19%)</td>
<td>87 (2.08%)</td>
<td>112 (2.10%)</td>
</tr>
<tr>
<td>Will leave occupation by 2014</td>
<td>197 (17%)</td>
<td>959 (23%)</td>
<td>1156 (22%)</td>
</tr>
<tr>
<td>Observations</td>
<td>1,144</td>
<td>4,190</td>
<td>5,334</td>
</tr>
</tbody>
</table>
DO PROFESSIONAL CREDENTIALS MATTER?
### Professional Credentials in the Sample

**Table 1.** Distribution of professional credentials across early RTRP adopters and non-adopters

<table>
<thead>
<tr>
<th>Professional credentials</th>
<th>Adopt RTRP in 2012</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No</td>
</tr>
<tr>
<td>JD or CPA</td>
<td>1,138</td>
</tr>
<tr>
<td>EA</td>
<td>218</td>
</tr>
<tr>
<td>Other</td>
<td>92</td>
</tr>
<tr>
<td>None</td>
<td>2,120</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>3,568</strong></td>
</tr>
</tbody>
</table>

*Note:* The category “Other” includes Certified Acceptance Agents, Enrolled Actuaries, Enrolled Retirement Plan Agents, and Supervised Registered Tax Preparers.
PREDICTED VALUES: BY PROFESSIONAL CREDENTIALS

Predicted probability of RTRP license early adoption by professional credentials and intent to start a tax preparation business

(For a 50 y.o. male preparer in a state with no licensure)
MAIN RESULTS
# EARLY ADOPTION CONDITIONAL ON NEED FOR QUALITY SIGNAL

Logit regression of RTRP adoption in 2012 by a tax preparer on availability of state license and entrepreneurial intent

<table>
<thead>
<tr>
<th></th>
<th>(2)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Will start own practice by 2014</td>
<td>-0.054</td>
<td>-2.100*</td>
<td>-2.009*</td>
</tr>
<tr>
<td></td>
<td>[0.165]</td>
<td>[0.971]</td>
<td>[0.989]</td>
</tr>
<tr>
<td>Will leave occupation by 2014</td>
<td>-1.302***</td>
<td>-0.537</td>
<td>-0.541</td>
</tr>
<tr>
<td></td>
<td>[0.131]</td>
<td>[0.370]</td>
<td>[0.366]</td>
</tr>
<tr>
<td>No professional credentials</td>
<td>2.508***</td>
<td>2.542***</td>
<td>2.578***</td>
</tr>
<tr>
<td></td>
<td>[0.285]</td>
<td>[0.295]</td>
<td>[0.303]</td>
</tr>
<tr>
<td>No state licensure</td>
<td>-0.168</td>
<td>-0.173*</td>
<td></td>
</tr>
<tr>
<td></td>
<td>[0.092]</td>
<td>[0.070]</td>
<td></td>
</tr>
<tr>
<td>No state licensure * Will start own practice by 2014</td>
<td>1.014**</td>
<td></td>
<td>0.952**</td>
</tr>
<tr>
<td></td>
<td>[0.311]</td>
<td></td>
<td>[0.303]</td>
</tr>
<tr>
<td>No state licensure * Will leave occupation by 2014</td>
<td>-0.109</td>
<td></td>
<td>-0.080</td>
</tr>
<tr>
<td></td>
<td>[0.339]</td>
<td></td>
<td>[0.352]</td>
</tr>
</tbody>
</table>

Observations: 5334 5334 5334
Number of state clusters: 49 49 49
State fixed effects: Yes

Note: Logit coefficients shown. Standard errors in brackets are clustered at state level. States with tax preparer licensure are CA, MD, NY, and OR. The omitted controls include age (quartic polynomial), gender, and ZIP-code-level characteristics of competition.

* p<0.05,  ** p<0.01,  *** p<0.001
ILLUSTRATION: PREDICTED VALUES BY STATE LICENSURE

Predicted probability of RTRP license early adoption by availability of state-level licensure and intent to start a tax preparation business

(For a 50 y.o. male preparer without credentials)
WHEN IT CAME OUT, I THOUGHT [THE RTRP] WOULD BE A VERY GOOD SELLING POINT, A VERY GOOD WAY TO SHOW [TO CLIENTS] THAT THE IRS IS CONFIDENT THAT I HAVE THE KNOWLEDGE LEVEL THAT I NEED

An early RTRP adopter who started own practice in 2012 in a state without preparer licensure
WHAT DO THESE RESULTS MEAN?

▸ The findings are mostly descriptive, but illuminate important and heretofore ignored relationships.
▸ Occupational licensure may be valuable to entrepreneurs who lack other signals of quality, but may still be costly otherwise.
▸ Licensure thus may have competing effects on entrepreneurial entry—as a barrier and an enabler.
▸ A fruitful direction of future research is assessing the trade-off between the two effects and the conditions that affect it.
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THANK YOU!

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