Is protectionism a legitimate state interest?

A Private Auction of Opportunities

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Protectionism is probably as old as government. In 1621, the great English jurist Sir Edward Coke told Parliament that the private interest groups that lobbied in favor of tariffs and other trade barriers were like a man in a rowboat: "They look one way and row another: pretend public profit, intend private." In other words, although the lobbyists claimed that banning "cheap imports" or "unfair competition" would protect consumers or "create jobs," their real interest lay in prohibiting competition and thus keeping their own prices artificially high.

Over the years, England developed a startlingly severe system of protective tariffs. In his *Wealth of Nations,* published over a century and a half after Coke's death, Adam Smith reported that under one of these laws, it was illegal to export sheep, and an offender could be punished by having his left hand cut off and nailed up in a public square. Politically powerful businessmen, Smith wrote, "extorted" laws like these from Parliament "for the support of their own absurd and oppressive monopolies."

Although such draconian penalties have gone out of fashion, economic interest groups continue to clamor for legislation that will protect them from having to compete. In Tampa, Fla., for example, a county ordinance prohibits limousine companies from charging customers less than $40 per trip. The head of the county's Public Transportation Commission explained that this rule was designed to protect taxi companies from having to compete against limousine services. The minimum rate rule "create[s] a balance between the different transportation service 'markets,'" he wrote, and ensures that they are "not directly competing against each other. This way, both manage to survive in their respective market area and the 'balance' is maintained." Meanwhile, federal bureaucrats, enforcing the "Byrd Amendment," prohibit foreign manufacturers from "dumping" goods on the market at lower prices than their American counterparts. Any company that does so can be fined—and the fine is then handed over to the American company that filed the complaint. From mundane local politics to the high stakes of international relations, legislators enact rules forbidding competition so as to benefit some businesses against others.

The notion that such laws protect the consumer is laughable. Although politicians often claim that they "protect jobs," they do so only by allowing the preferred businesses to keep their prices artificially high—essentially taxing consumers to subsidize businesses that cannot compete. This is why protectionist laws are rarely created at the behest of consumers: consumers do not usually ask the legislature to proscribe less expensive goods and services. Instead, protectionist laws are a consequence of "rent-seeking," a process whereby lobbyists expend time and resources trying to convince lawmakers to enact legislation that will ultimately return a profit for those lobbyists—a profit that comes from the consumer's pocket.

PROTECTION AND THE CONSTITUTION

While the economic case against protectionism is well known, the constitutionality of such laws has been taken for granted for decades. But four recent decisions by federal courts have revived serious consideration of this question for the first time since the Supreme Court's 1934 decision in *Nebbia v. New York*. *Nebbia* was the case that began the constitutional "revolution" of the New Deal by holding that a state tariff on the sale of milk was constitutional under the Fourteenth Amendment (which asserts that no state shall deprive any person of life, liberty, or property without due process of law). New York bureaucrats had set the minimum price of milk at nine cents a quart on the theory that allowing milk producers to sell for less would

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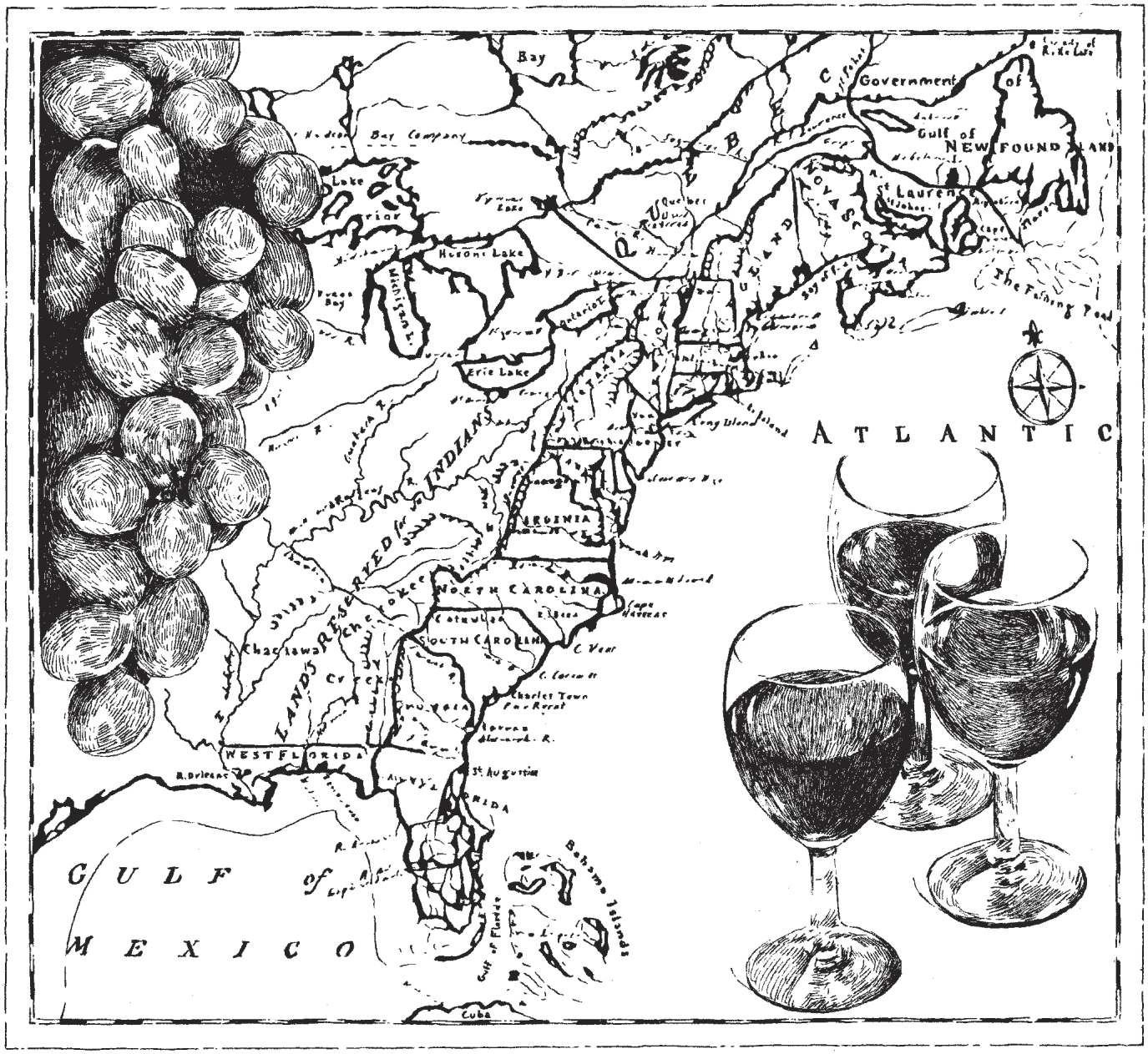

spawn a "price war" that would eventually bankrupt the industry and permit the few surviving dairies to boost their prices to monopoly levels. Of course, basic economics reveals the flaw in this theory: in a free market, any such attempted "monopoly" would be immediately undercut by new competitors charging less than the "monopoly" price—all of which would result in more milk for consumers at lower prices. So long as we keep in mind Smith's dictum that "consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to only so far as it may be necessary for promoting that of the consumer," such a price competition can be seen as a social benefit.

The Courts saw it differently. New York convicted Leo Nebbia for selling two quarts of milk and a five-cent loaf of bread for 18 cents—well below the legal minimum. On appeal, he argued that the law deprived him of the liberty to sell his milk at the price he chose, in a way that did not benefit the public but simply protected the income of dairies that were unable to compete with him. But the Supreme Court ruled against Nebbia. Overturning 50 years of precedent, it held that from now on states would be "free to adopt whatever economic policy may reasonably be deemed to promote public welfare," even if their policies put the interests of politically influential businesses above those of consumers or competitors. If the legislature decides that "unrestricted competition is an inadequate safeguard of the consumer's interests, produce[s] waste harmful to the public, threaten[s] ultimately to cut off the supply of a commodity needed by the public, or portend[s] the destruction of the industry itself, appropriate statutes passed in an honest effort to correct the threatened consequences may not be set aside." The Constitution, the Court concluded, "does not secure to any one liberty to conduct his business in such fashion as to inflict injury upon the public at large"—such as charging low prices for milk.

Not long after *Nebbia* was decided, law professor J.A.C. Grant wrote that it and similar cases indicated a revival of the

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medieval guild system, a system that "makes use of government for its own purposes" by forbidding competition with cartelized industries. The guild system's "principal interests lay in minimum prices and maximum wages," wrote Grant, and it enforced the price restrictions by creating "artificial scarcity of labor": essentially criminalizing competition against state-authorized industries. Grant applauded New Deal legislation that gave "sovereign powers to business groups" and "confers upon them all the types of power normally exercised by government." But at the same time, he recognized that the increasing cartelization of American industry meant that economic regulations "will be primarily in the interests of the group rather than of the public as a whole."

Despite this warning, no federal court ever struck down a state economic regulation for violating the Due Process Clause in the years following *Nebbia.* That changed in the 2002 case of *Craigmiles v. Giles,* when the Sixth Circuit Court of Appeals held that an occupational licensing law violated the Due Process and Equal Protection clauses because it had no connection to public safety, but merely prevented competition for the benefit of preferred producers. The law required Tennessee casket retailers to obtain funeral director licenses before selling caskets, urns, or other funeral merchandise, even though the casket sellers did not officiate at funerals or handle bodies. The licensing law required applicants to spend two years and thousands of dollars learning skills such as embalming or grief counseling. But the trial judge found that "the purpose of promoting public health and safety is not served by requiring two years of training to sell a box." The Court of Appeals agreed, finding that the licensing law had nothing to do with protecting the public; it was simply designed to prevent innovative competition from companies that could provide coffins at a lower price. "Protecting a discrete interest group from economic competition is not a legitimate governmental purpose," the court declared.

A NEW LOW

This statement was vital because the Fourteenth Amendment requires that everything government does, no matter how minor, must serve a "legitimate governmental purpose." But deciding what purposes are legitimate is a complicated matter. In support of its holding, for instance, the *Craigmiles* court cited three cases, *Philadelphia v. New Jersey* (1978), *H.P. Hood & Sons v. DuMond* (1949), and *Energy Reserves Group v. Kansas Power & Light* (1983), none of which actually involved the Fourteenth Amendment at all. *Philadelphia* and *DuMond* were decided under the Interstate Commerce Clause, a provision long interpreted as forbidding states from discriminating against businesses that sell across state lines. Such trade is solely within the purview of federal regulators. *Energy Reserves Group,* on the other hand, dealt with the Contracts Clause, which is rarely implicated in cases involving protectionist laws.

These weaknesses were exploited only days afterward, when a federal district court in Oklahoma held that that state's almost identical funeral director licensing law *did* satisfy the Constitution. That decision, *Powers v. Harris,* was upheld by the Tenth Circuit Court of Appeals, which declared that the *Craigmiles* decision was wrong to say that states could not act simply on behalf of private groups. On the contrary, "intrastate economic protectionism constitutes a legitimate state interest." Thus, even laws that have no relationship at all to the public's health and safety are constitutional. "While baseball may be the national pastime," the court noted, "dishing out special economic benefits to certain in-state industries remains the favored pastime of state and local governments…. [A]dopting a rule against the legitimacy of intrastate economic protectionism and applying it in a principled manner would have wide-ranging consequences." Although *Powers* was directly contrary to *Craigmiles,* the United States Supreme Court decided not to take the case.

Powers adopted a far more extreme degree of judicial deference than the Supreme Court's *Nebbia* decision. *Nebbia* had held that while states may establish price-fixing laws, they may not do so in ways that are "arbitrary or discriminatory." But under *Powers,* even laws that are designed to be discriminatory will still satisfy the Constitution. *Powers* set a new low: in the past, courts upholding protectionist laws had struggled—sometimes desperately—to rationalize special-interest laws as somehow benefiting the public. *Powers* shrugged off any such pretense, allowing legislators and interest groups to admit their private intentions without embarrassment. Protectionists were no longer forced to "pretend public profit" while "intending private."

Craigmiles and *Powers* set up a neat division between two fundamentally differing views of the nature of government. In 2004, the Ninth Circuit joined the debate when it decided *Sagana v. Tenorio.* That case upheld the constitutionality of the discriminatory Nonresident Worker Act in the Commonwealth of Northern Mariana Islands (which is required to abide by the Fourteenth Amendment as if it were a state). The act imposes various burdens on the employment of legally admitted, non-resident aliens, solely to protect resident workers from having to compete in the labor market. Among other things, the act requires that at least 10 percent of an employer's work force must be made up of residents. Employers must post a bond covering three months of wages, medical coverage, and repatriation expenses for each nonresident employee; must pay them biweekly, in cash; and must obtain government pre-approval of all nonresident employment contracts. For some occupations, the law forbids the hiring of nonresidents entirely.

Despite several Supreme Court decisions striking down similar laws—including one decision that held that "discrimination…against aliens as such in competition [for jobs]…clearly falls under the condemnation of the fundamental law"—the Ninth Circuit upheld the act. It concluded that the legislature's purposes were "bolstering the [local] economy, giving job preference to its residents, and protecting the wages and conditions of resident workers while enforcing a system to control and regulate its visiting laborers. These are reasonable, important purposes." Once again, providing benefits to particular groups, rather than the public at large, was held to be a legitimate government interest. And once again, the Supreme Court ignored the decision.

MISCHIEF OF FACTION

Laws like those upheld in *Powers* and *Sagana* represent some of the most disgraceful tendencies of representative government. As America's founders well understood, government exists to protect citizens against the arbitrary force of thieves or bullies who would do them harm. Unfortunately, government itself can all too easily be co-opted by private interest groups that seek to exploit its coercive power for their own aggrandizement. This is the problem James Madison called "the mischief of faction." Preventing that mischief, he explained, was one of the primary goals of any wisely written constitution: "In framing a government which is to be administered by men over men, the great difficulty lies in this: you must first enable the government to control the governed; and in the next place oblige it to control itself."

The basic way of obliging government to control itself is to require some degree of generality in all of its laws. As Friedrich Hayek put it, "when we obey laws, in the sense of general abstract rules laid down irrespective of their application to us, we are not subject to another man's will and are therefore free." But when legislation is devised to benefit private groups rather than the public at large, government's power to coerce, which ought to be used in the interest of the whole society, becomes perverted into a weapon that one group can use against another. This is why an older generation of courts called such laws "special" or "partial" legislation, and held that they were not actually law at all. After all, law is the opposite of arbitrariness. But government regulation that serves nothing more than the private desires of successful groups are fundamentally arbitrary; they are based on nothing more than fleeting popularity and are as likely to be repealed tomorrow as promulgated today. They are mere acts of will, rather than deliberate reason.

In *Loan Association v. Topeka* (1876), the Supreme Court explained that legislation that lacks generality and merely transfers wealth between private groups is "none the less a robbery because it is done under the forms of law. . . . This is not legislation. It is a decree under legislative forms." And because it is not law, such legislation deprives its victims of liberty and property without due process of law, in violation of the Fourteenth Amendment. The "substantive due process" theory articulated in *Loan Association* and later in *Craigmiles* is rooted in the Madisonian understanding that if a citizen's rights may be revoked whenever the legislature changes partisan hands, then citizens are really no safer than they would be without government. "In a society under the forms of which the stronger faction can readily unite and oppress the weaker," wrote Madison, "anarchy may as truly be said to reign as in a state of nature, where the weaker individual is not secured against the violence of the stronger." Such a situation can hardly be called a rule of law. What the *Loan Association* and *Craigmiles* courts recognized was that the Due Process Clause imposes a sort of "publicness" requirement on a state's laws.

The same is true of the Equal Protection Clause in the Fourteenth Amendment. By requiring states to accord people the "equal protection of the laws," it ensures that government does not give preferred groups special favors that are not extended to other groups. When government does distinguish between people, it must do so for some objective reason, not merely as an act of will. For the legislature to treat people differently on the basis of age, for example, might make sense in the case of traffic laws or health care regulations. But to grant benefits or impose burdens on people merely because legislators like one group instead of another, or have received more campaign contributions from one instead of the other, serves no rational public purpose; it is every bit as arbitrary as theft or robbery.

FLIMSY EXCUSES

Although *Nebbia* effectively overruled *Loan Association* by adopting a rule of extreme deference in favor of the legislature, courts continued to recognize that the Constitution at least requires legislators to base their decisions on public considerations, not private ones. Laws that merely benefit particular groups for no public reason have routinely been declared invalid under *Nebbia*'s "rational basis" test because they do not serve a "legitimate state interest." For example, in *Romer v. Evans* (1996) the Court declared that government may not enact laws simply for "the purpose of disadvantaging the group burdened by the law." And while courts have never denied that legislatures do pass protectionist laws and have usually upheld them against constitutional challenges, the courts that have done so have at least regarded such laws as abusive and tried to conceal their arbitrariness with some public rationalization.

Two recent decisions by federal trial courts provide startling examples of the flimsy excuses that courts employ in upholding protectionist laws that, in reality, do nothing more than protect established businesses against competition from entrepreneurs. In *Meadows v. Odom,* a federal court in Louisiana held that the state could require florists to obtain professional licenses before practicing floristry. Getting such a license is a burdensome affair, requiring applicants to pass a one-hour written exam and a four-hour performance exam, during which their flower-arranging skills are evaluated for "balance," "harmony," "unity," and other subjective variables. This law, which appears to be unique in the United States, excludes entrepreneurs who would otherwise try to compete in the market for floral services, and the state's commissioner of agriculture and forestry admitted as much when he testified that he had made a campaign pledge to "support [the] desires" of licensed florists, whatever they might be—whether it meant "having or get[ting] rid of the [licensing] law." The trial court, however, ignored those details and held that the licensing scheme satisfied the rational basis test because unlicensed florists would lack training and expertise, and therefore harm the public. What sort of danger do unlicensed florists present to the public? The court found that unlicensed florists might not know how to use the wires that florists employ to hold flower arrangements together, and thus consumers might prick their fingers. The florist licensing law therefore protected public safety. *Meadows* is currently on appeal before the Fifth Circuit.

Also on appeal is *Merrifield v. Lockyer,* a case challenging the constitutionality of a California law that requires the licensing of people who install anti-pigeon spikes on buildings or

use other mechanical devices against pigeons, rats, and mice. This requirement only applies to people who work on pigeon, rat, and mouse infestations—meaning that a person installing spikes on a building to keep pigeons away must get a license, but if the same person installs the same spikes on the same building to keep seagulls away, he is not required to have a license. Getting a license requires an applicant to spend two years working for a person who has a license, and then to pass a 200-question examination. Yet the examination does not have a single question about pigeons. Instead, it is devoted almost entirely to questions about the use or storage of pesticides, or about ways of eradicating insects. Although Alan Merrifield, the 66-year-old owner of Urban Wildlife Management in San Mateo, has been installing spikes and other devices on buildings for some 30 years, state bureaucrats have threatened to fine him unless he gets a license—meaning that he must close his business and become an apprentice for two years, studying pesticides he never uses and insects he never treats.

When challenged to defend the law, California regulators offered as their expert witness Eric Paulsen, a representative of a group of licensed pest-control companies that might face competition from Merrifield if the licensing scheme were not in place. Paulsen—who admitted under oath that the law was "irrational" and "a political piece of legislation in order to make a particular constituency happy"—explained that he was present when the law was written and that he had proposed the final language as a way to divide up the marketplace for pest-control services. The position of his organization, he said,

> was that the trapping and excluding of all these birds really should [require] a structural pest control license. I said, well, where could we find a middle ground here? I said, well, what are the primary vertebrate pests and primary bird pests in structures? And what are some that are not of the greatest importance? And arguably rats, mice and pigeons are...a larger percentage of the . . . [pest control business]. I said, well, you guys keep the pigeons. Will that keep you happy so you will not oppose our bill? Keep rats, mice, and pigeons, and we'll take these others. . . .

Acknowledging that the law was really a protectionist device, Paulsen concluded that "as it pertains to the specific rationale for separating [pigeons, rats, and mice from other animals] . . . from a public perspective, it might be irrational." The phrase "from a public perspective it might be irrational" is an elegant way to sum up the *Powers*, *Sagana*, *Meadows*, and *Merrifield* cases. If mere protectionism is a legitimate goal for the legislature to pursue, then economic regulations do not need to be rational from a public perspective—an entirely private law-making scheme would be permissible. But the better understanding of the Constitution requires that all laws be rational from a public perspective.

Despite Paulsen's admissions, the trial court upheld the pest-control licensing law, ruling that the legislature might have believed that people like Merrifield should be aware of the dangers posed by pesticides that might have been applied by other pest control workers. The fact that people who treat seagull or starling infestations are not required to be licensed, even though they do identical work, was ignored. The court's decision—now on appeal before the Ninth Circuit—is another desperate rationalization for a law that is admitted, even by one of its authors, to be a purely protectionist device.

CONCLUSION

For many years, courts held that all laws must serve some public goal. That is not a very stringent requirement because legislators can conjure up some plausible public justification for virtually anything they do. Yet *Powers* and *Sagana* threaten to overthrow even this modest restraint, and allow even avowedly private, arbitrary legislation to satisfy the Constitution. Although *Meadows* and *Merrifield* do not go quite that far, they reveal the lengths to which courts are willing to go to concoct disguises for blatantly protectionist legislation. Taken together, these cases endanger the continued viability of the rule of law and threaten to transform representative government from a forum in which competing views of the public good are deliberated and resolved, into a private auction of opportunities and monopolies.

Four centuries ago, Edward Coke complained that a government-protected monopolist "engrosseth to himself what should be free for all men"—namely, the right to earn a living. That right is a precious liberty, one that today is threatened by a barrage of protectionist schemes, sometimes disguised as consumer protection laws and sometimes without any disguise at all. But if the rule of law means anything, courts must ensure that lawmakers confine their efforts to serving the public interest and not merely granting preferences to their favored constituents. R

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