Appendix 3

Slicing and Dicing the NIPA Measure of Corporate Profits

In the National Income and Product Accounts (NIPA) compiled by the Bureau of Economic Analysis (BEA) in the US Commerce Department, corporate profits represents the total income earned from current production that is accounted for by US corporations. NIPA profits includes all incorporated businesses—both publicly traded and privately held—and all industries, while financial-accounting tabulations cover a subset of the corporate universe. It covers all entities required to file federal corporate tax returns, including mutual financial institutions and cooperatives subject to federal income tax; nonprofit organizations that primarily serve business; Federal Reserve banks; and federally sponsored credit agencies.

When available, BEA uses data collected on a tax-accounting basis as the primary source of information on corporate "book" profits. BEA also reports "profits from current production." It includes the Inventory Valuation Adjustment and the Capital Consumption Adjustment to restate the historical-cost basis used in profits tax accounting for inventory withdrawals and depreciation to the current-cost measures used in GDP. It is necessary to make these adjustments to calculate profits' contribution to GDP and to the share of National Income.

NIPA corporate profits includes the profits of both C and S corporations. C corporations pay corporate taxes on their earnings. Their shareholders report any dividends they receive on their personal tax returns. S corporations are legal entities that pay no federal corporate profits taxes; instead, all of their earnings are treated as taxable income of shareholders, regardless of whether the income is distributed as dividends or retained by the corporation. As a result, most income is paid out as dividends.

In the early 1980s, C corporations produced almost all business income. In 2013, only 44% of the income of business owners was earned through C corporations. Owners of S corporations and partnerships now earn about half of all income from businesses. The shift occurred because of tax and legal changes that benefitted pass-through business owners and made the pass-through form more attractive to file. For instance, in 1986, the top individual income tax rate fell below the corporate tax rate. This created significant incentives for a business to un-incorporate and for new businesses to organize as pass-throughs.*

NIPA dividends as a share of corporate profits is much larger than the share reported in private-sector estimates. One of the most important factors accounting for the difference in the estimates of dividend-to-profits ratios is the inclusion of S corporations in the NIPA estimates; they are excluded from many of the private-sector estimates.

* See Aaron Krupkin and Adam Looney, *9 facts about pass-through businesses*, Brookings, May 15, 2017.
Source: Yardeni Research, Inc.