

## **Proprietors' Income**

Proprietors' income with inventory valuation and capital consumption adjustments is the current-production income of sole proprietorships and partnerships and of tax-exempt cooperatives.<sup>1</sup> Proprietors' income includes corporate directors' fees and the imputed net rental income of owner-occupants of farm dwellings, but it excludes the imputed net rental income of owner-occupied nonfarm housing as well as the dividends and the monetary interest that are received by nonfinancial business and the nonfarm rental income received by persons not primarily engaged in the real estate business.<sup>2</sup>

Proprietors' income accounted for approximately 8.6 percent of total personal income at the national level in 2000 (table D). The estimates of proprietors' income are prepared in two parts-- nonfarm proprietors' income and farm proprietors' income. Nonfarm proprietors' income accounted for approximately 96 percent of proprietors' income, and farm proprietors' income, for approximately 4 percent.

### **Nonfarm proprietors' income**

Nonfarm proprietors' income consists of the income that is received by nonfarm sole proprietorships and partnerships and the income that is received by tax-exempt cooperatives.

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1. A sole proprietorship is an unincorporated business owned by a person. A partnership is an unincorporated business association of two or more partners. A tax-exempt cooperative is a nonprofit business organization that is collectively owned by its customer-members.

2. The dividends are included in personal dividend income, the monetary interest in personal interest income, and the nonfarm rental income in rental income of persons.

The national estimates of nonfarm proprietors' income are primarily derived from income tax data. Because these data do not always reflect current production and because they are incomplete, the estimates also include four major adjustments--the inventory valuation adjustment, the capital consumption adjustment, the "misreporting" adjustment, and the adjustment for the net margins on owner-built housing.<sup>3</sup>

The inventory valuation adjustment offsets the effects of the gains and the losses that result from changes in the prices of products withdrawn from inventories; this adjustment for recent years has been small, but it is important to the definition of proprietors' income.

The capital consumption adjustment changes the value of the consumption, or depreciation, of fixed capital from the historical-cost basis used in the source data to a replacement-cost basis.<sup>4</sup>

The "misreporting" adjustment adds an estimate of the income of sole proprietors and partnerships that is not reported on tax returns. This adjustment accounted for almost half of nonfarm proprietors' income in 2000.

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3. For other adjustments to the tax data, see NIPA table 8.23, "Relation of Nonfarm Proprietors' Income in the National Income and Product Accounts (NIPA's) to Corresponding Measures as Published by the Internal Revenue Service (IRS)," Survey 81 (August 2001): 118.

4. The capital consumption adjustment also reflects the differences between the depreciation schedules used for tax accounting and straight-line depreciation based on economic service lives.

See also "Capital consumption adjustment" and "Inventory valuation adjustment" in the "Glossary."

The adjustment for the net margins on owner-built housing is an addition to the estimate for the construction industry. It is the imputed net income of individuals from the construction or renovation of their own dwellings.

The source data necessary to prepare these adjustments are available only at the national level. Therefore, the national estimates of nonfarm proprietors' income that include the adjustments are allocated to States, and these State estimates are allocated to the counties, in proportion to tax return data that do not reflect the adjustments.

In addition, the national estimates include adjustments made to reflect decreases in monetary and imputed income that result from damage to fixed capital and to inventories that is caused by disasters, such as hurricanes, floods, and earthquakes. These adjustments are attributed to States and counties on the basis of information from the Federal Emergency Management Agency. These adjustments include those for Hurricanes Andrew and Iniki in 1992, for the Midwest floods and the East Coast storms in 1993, for the Northridge Earthquake in 1994, for Hurricane Opal in 1995, and for Hurricane Floyd in 1999.

**Income of nonfarm sole proprietorships and partnerships.**--Both the State and the county estimates of the income of nonfarm sole proprietorships and partnerships for 1992-98 are based on data for those years that were tabulated by the Internal Revenue Service (IRS) from Schedule C of form 1040 for sole proprietorships and from form 1065 for partnerships.<sup>5</sup>

The national estimates excluding the misreporting adjustment for 1992-98 were allocated to States in proportion to the IRS data for "net profit less loss" at the Standard Industrial

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5. The geographic coding of the data is by tax-filing address. This address is assumed to be the same as the address of the place of residence. For additional information, see the section "Geographic characteristics of the source data" in the introduction to "Sources and Methods."

Classification (SIC) two-digit level, and the national estimates of the misreporting adjustment were allocated to States by the IRS data for "net gross receipts" (gross receipts less refunds) at the SIC two-digit level.

However, the IRS county data at the SIC two-digit level for 1992-98 could not be used to prepare the county estimates because the usefulness of the data would have been severely impaired by the large number of the suppressions to these data that would have been required to prevent the disclosure of confidential information. Further, the IRS data for net profit less loss could not be used, because of the volatility of these data.<sup>6</sup> Consequently, the IRS data for net gross receipts at the SIC division, or "one-digit," level were used to allocate the State estimates to counties. These data were supplemented by the use of the previous county estimates for 1992-97 for SIC two-digit industries, which are based on extrapolations of IRS data for 1983.<sup>7</sup>

The 1992-98 county estimates were prepared in two major steps. First, the State estimates were aggregated to the SIC division level. The aggregated State estimates were allocated to counties in proportion to the net gross receipts.

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6. The volatility is frequently indicated by fluctuations between positive and negative values, which usually leads to anomalous results when the data are used in an allocation.

7. For information about the preparation of the county estimates using the 1983 IRS county data for SIC two-digit industries, see U.S. Department of Commerce, Bureau of Economic Analysis, Local Area Personal Income, 1984-89, vols. 1-5 (Washington, DC: U.S. Government Printing Office, 1991): M12-M13; or see the Regional Economic Information System CD-ROM for 1969-91 (May 1993).

Second, the county estimates for each SIC division were apportioned among the SIC two-digit industries through the use of a dual allocation procedure.<sup>8</sup> In this procedure, the State estimates for each SIC two-digit industry in a division were used for the primary control totals (in the columns), and the county estimates for the division were used for the secondary control totals (in the rows). The State estimates were initially allocated to counties in proportion to the previous county estimates for 1992-98 in order to generate initial county estimates at the SIC two-digit level. Then, each county estimate for a division was allocated to the SIC two-digit industries in the division in proportion to the initial county estimates for the SIC two-digit industries. Finally, the State estimates for each SIC two-digit industry were allocated to counties by the output of the previous step.

The 1998 county estimates for each manufacturing industry were extrapolated to 1999-2000 by the corresponding estimates of wages and salaries, and the 1998 estimates for oil and gas extraction, for real estate, and for holding and other investment offices were extrapolated by the estimates of dividends (from all industries) received by individuals. These extrapolations were used to allocate the 1999-2000 State estimates for these industries to counties. For each of the other industries, the 1999-2000 State estimates were allocated to counties in proportion to the 1998 estimates.

**Income of tax-exempt cooperatives.**--The income of tax-exempt cooperatives consists of the income that is received by rural electric cooperatives, rural telephone cooperatives, and agricultural cooperatives.

The estimates of the income of rural electric cooperatives and of rural telephone cooperatives are based on annual data for the net margin, or profit, of these cooperatives that have

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8. See "Dual allocation" in the "Technical notes."

outstanding loans from the Rural Utilities Service (RUS) of the Department of Agriculture.<sup>9</sup> The net margin of each cooperative is allocated to States and counties in proportion to the distribution of its customer-members that is reported by the RUS. The allocated amount for each type of cooperative is summed to State and county totals, and these totals are then used to allocate the national estimates to States and counties.

Agricultural cooperatives are mainly farm marketing cooperatives and farm supply cooperatives; they are classified in the SIC in wholesale trade. The State estimates of the income of these cooperatives are based on data provided by the Agricultural Cooperative Service of the Department of Agriculture. Because no source data for counties are available, the State estimates of the income of these cooperatives are allocated to counties in proportion to the estimates of the income of the sole proprietorships and partnerships in wholesale trade.

### **Farm proprietors' income**

Farm proprietors' income consists of the income that is received by the sole proprietorships and the partnerships that operate farms. It excludes the income that is received by corporate farms.

The national and State estimates of farm proprietors' income are primarily derived from the national and State estimates of the income of all farms that are prepared by the U.S. Department of Agriculture (USDA). The concepts that underlie the USDA national and State estimates of farm income are generally the same as those that underlie the BEA estimates of farm

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9. The data for the electric cooperatives are for the total number of the customer-members, including businesses; the data for the telephone cooperatives are for the number of residential customer-members.

proprietors' income. However, the USDA estimates of farm income include the income of corporate farms, and the USDA measures of depreciation differ from the BEA measures.<sup>10</sup>

To prepare the county estimates of farm proprietors' income, BEA first prepares county estimates of the income of all farms, and it uses primarily the USDA State estimates of the components of farm income as control totals. Then, the USDA State estimates are adjusted for the differences in the measures of depreciation and to include the sales and purchases of livestock between farms, which are excluded from the USDA estimates of two components of farm income--cash receipts and expenses.<sup>11</sup>

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10. For the differences between the USDA and the BEA estimates of net farm income at the national level, see NIPA table 8.24, "Relation of Net Farm Income in the National Income and Product Accounts (NIPA's) to Net Farm Income as Published by the U.S. Department of Agriculture (USDA)," Survey 81 (August 2001): 118.

For information on the BEA estimates of depreciation, see Barbara M. Fraumeni, "The Measurement of Depreciation in the U.S. National Income and Product Accounts," Survey 77 (July 1997): 7-23.

11. These transactions are excluded from the USDA State estimates of the cash receipts from marketing livestock and of the expenses for livestock purchases because in the aggregated State estimates of farm income the cash receipts from intrastate interfarm sales offset the expenses for intrastate interfarm purchases.

Because these transactions may not be intracounty transactions, BEA estimates the transactions for each State and adds the estimate to the USDA State estimates of these cash receipts and of these expenses.

The county estimates of farm proprietors' income are calculated in three major steps. First, estimates of "realized net income" of all farms are computed as the gross receipts of all farms less the production expenses of all farms. Second, the estimates of realized net income are modified by the inventory change adjustment so that only the income from current production is measured; this modification yields the estimates of "total net income" of all farms. Third, the income of corporate farms is estimated, and the estimates are subtracted from the estimates of total net income to yield the estimates of farm proprietors' income.<sup>12</sup>

The county estimates of farm proprietors' income for 1992-2000 were primarily derived from county data from the 1992 and 1997 Censuses of Agriculture and from selected annual county data from the State offices that are affiliated with the National Agricultural Statistics Service (NASS) of the USDA. In addition, data from other sources within the USDA, such as the Farm Service Agency, were used.

For 1992 and 1997, the county estimates of 30 components of gross receipts, 13 categories of production expenses, and 2 categories of the value of the net change in inventories were derived mainly from the census of agriculture for those years. For 1993-96 and for 1998-2000, the county estimates for each State were prepared in the component detail that corresponded to the best annual county data available for the State.

**Farm gross receipts.**--The estimates of the gross receipts of all farms consist primarily of the following items: (1) The cash receipts from farm marketing of crops and livestock, (2) the receipts from other farm-related activities, including recreational services, sales of forest products, and custom-feeding services performed by farm operators, (3) the payments to farmers under several Federal Government farm subsidy programs, (4) the imputed value of

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12. The derivation of the estimate of farm proprietors' income for each county is available in table CA45, "Farm Income and Expenses."

home consumption, which is the value of the farm products produced and consumed on farms, and (5) the imputed gross rental value of farm dwellings.<sup>13</sup>

The largest component of gross receipts is the cash receipts from marketing. The USDA State estimates include estimates of the cash receipts from the marketing of about 150 crop and livestock commodities, but the county estimates are prepared in much less detail.

Annual county estimates of cash receipts--usually for total crops and for total livestock--for 15 States are prepared by the NASS-affiliated State offices. BEA uses these estimates to allocate the USDA State estimates to the counties in these States.<sup>14</sup>

For the other States, the USDA State estimates of cash receipts from the marketing of each commodity are summed into the 13 groups of crops and the 5 groups of livestock for which county data for value of sales are available from the censuses of agriculture. The State

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13. Receipts for recreation services are received for providing facilities for recreational activities, such as fishing, hunting, and camping.

The inclusion of the imputed gross rental value of farm housing in gross receipts offsets the expenses--including interest, taxes, and depreciation--that are associated with the operation of the housing. These expenses are included in farm production expenses, but they cannot readily be distinguished from nonhousing expenses of the same type.

The net effect of including both the imputed gross rental value and the associated expenses in the farm income accounts is to add the net rental value of farm housing to farm income. The net rental value of the housing occupied by farm proprietors is part of proprietors' income; the net rental value of the housing occupied by farm employees is part of pay-in-kind.

14. The county estimates of cash receipts are currently available for Alabama, Arizona, California, Hawaii, Illinois, Kansas, Kentucky, New Mexico, New York, North Carolina, Ohio, Oregon, Pennsylvania, South Carolina, and Utah.

estimates of cash receipts for these groups for 1992 and for 1997 were allocated to counties by the related census data.

For the counties of some of these States, the county estimates of cash receipts for selected groups of commodities were interpolated between 1992 and 1997 and extrapolated to 1998-2000 by the value-weighted series for the annual production of selected crops and for the inventories of selected categories of livestock; these series were constructed from supplemental NASS data using marketing year average prices for each commodity as the weights. The State estimates for 1993-96 and for 1998-2000 were allocated to counties in proportion to the interpolated and extrapolated county estimates for those years.

For the remaining commodities and for all commodities in States for which no annual county data are available, the 1992 and 1997 State estimates of the cash receipts were allocated to counties in proportion to the corresponding census data for those years. The 1993-96 county estimates reflect interpolations between the 1992 and 1997 census data, and the 1998-2000 estimates reflect the 1997 census data.

The State estimates of the receipts from other farm-related activities for 1992-2000 were similarly allocated to counties in proportion to the data for the receipts from these activities from the censuses or from interpolations between the censuses.

The State estimates of the Federal Government payments to farmers for 1992-2000 were allocated to counties in proportion to annual tabulations of the payments from the Farm Service Agency, USDA.

County source data that reflect the imputed value of home consumption and the imputed gross rental value of farm housing are unavailable. The county estimates of the imputed value of home consumption are based on the distribution of the number of farms reported in the censuses, and the county estimates of the imputed gross rental value are based on the distribution of the value of farm land and buildings from the censuses.

**Farm production expenses.**--The State estimates of the production expenses for most items for 1992 and 1997 were allocated to counties in proportion to the data for the item from the censuses for those years; the 1993-97 county estimates are based on interpolations of the data from the censuses, and the 1998-2000 estimates are based on data from the 1997 census.<sup>15</sup>

The county estimates of the production expenses for three items are based on series that are related to the items from the censuses. The estimates of the rent paid to landlords who are not farm operators are based on the acreage of the farms operated by tenants.<sup>16</sup> The estimates of the depreciation of machinery are based on the value of the machinery and equipment. The estimates of the depreciation of buildings are based on the value of the farm land and buildings.

**Inventory change adjustment.**--This adjustment is an estimate of the value of the net change during the year in the farm inventories of the livestock and crops that are held for sale. This estimate is added to the estimate of realized net income in the second major step in the calculation of the estimates of farm proprietors' income, so that the estimate of farm proprietors' income for a year will include only the farm income from production during the year, or from

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15. Direct allocators for the following expenses are available from the 1992 and 1997 censuses: Purchases of feed, livestock including poultry, seed, fertilizer and agricultural chemicals including lime, and petroleum products; cash wages, perquisites, and social security taxes; contract labor expenses; machine hire and custom work; electricity; interest; taxes; repair and maintenance; and a miscellaneous category that includes animal health costs.

16. The rent paid by farm operators to landlords who are also farm operators is omitted from production expenses and from gross receipts because it is assumed that the tenant and the landlord usually operate farms in the same county and that the rent paid usually offsets the rental income received.

"current" production. The sum of realized net income and the value of the net change in inventories is total net income.

The role of the inventory change adjustment in the derivation of net farm income is illustrated by the following examples. For crops, the value of the net change in inventories is negative when farmers feed more crops to their animals or sell more crops than they produce during the year, so that the amount held in inventory declines and the realized net income overstates the income from current production by the value of the net withdrawals from inventory. For livestock, the value of the net change in inventories is positive when the number of animals that are born or that farmers purchase is greater than the number that they sell during the year, so that the size of the herds increase and the realized net income understates the income from current production by the value of the net increase in the herds.

Annual county data for the number of cattle, swine, sheep, and chickens on farms are available from the NASS offices of some States. The 1992-2000 State estimates of the value of the net change in livestock inventories on farms for these States were allocated to the counties in these States in proportion to the number of livestock of each type in farm inventories at the end of each year. The county estimates for the other States are based on the county distribution of the number of livestock units in farm inventories reported in the 1992 and 1997 censuses.

The State estimates of the value of the net change in crop inventories were allocated to counties by the annual data for crop production from the NASS State offices. If the NASS data were unavailable, the 1992 and 1997 State estimates were allocated by the data for crop production from the censuses for those years, the 1993-96 State estimates were allocated by the interpolations of the data from the censuses, and the 1998-2000 State estimates were allocated by the data from the 1997 census.

**Adjustment to exclude the income of corporate farms.**--This adjustment is made in the third major step in the calculation of farm proprietors' income, because the estimates of the total net income of all farms that are calculated in the second major step include the income of corporate farms.

The adjustment is calculated in four steps. First an adjustment ratio is computed as the ratio of the acreage of corporate farms to the total acreage of all farms in each county; the data for the acreage are from the 1992 and 1997 censuses and from interpolations between the censuses; the 1997 ratio is used for the 1998-2000 estimates. Second, the adjustment ratio is multiplied by the county estimate of the total net income of all farms in order to derive the initial estimate of corporate farm income for each county. Third, the State estimates of corporate farm income are allocated to counties in proportion to the initial county estimates. Fourth, the allocated county estimates of the income of corporate farms for each county is subtracted from the estimate of the income of all farms to yield the estimate of farm proprietors' income.

Table D.--Relative Importance to Personal Income of Proprietors' Income,  
by Component, United States, 2000

	Millions of dollars	Percent of personal income
Personal income..	8,314,032	100.00
Proprietors' income/1/..	716,222	8.61
Farm..	31,833	0.38
Nonfarm..	684,389	8.23
Agricultural services, forestry, fishing..	8,409	0.10
Mining..	17,539	0.21
Construction..	85,601	1.03
Manufacturing..	42,025	0.51
Transportation and public utilities..	64,449	0.78
Wholesale and retail trade..	69,598	0.84
Finance, insurance, and real estate..	105,187	1.27
Services..	291,581	3.51
Business services..	140,120	1.69
Professional, social, and related services..	151,461	1.82

1. Shown with inventory valuation and capital consumption adjustments.

NOTE.--Detail may not add to totals due to rounding.