Fair Value Accounting and Measures of U.S. Corporate Profits for Financial Institutions

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Paper Abstract: Quarterly source data are used to measure quarterly corporate profits in the U.S. national accounts. Consistent with international guidelines, the source data are adjusted to remove holding gains and losses; however, fair value accounting (FVA) practices call into question the completeness of the adjustments. This paper evaluates quarterly source data on financial institutions and the resulting published quarterly corporate profits series to identify FV gains and losses that may generate measurement error during the 2008 financial crisis. The core results of the paper reveal significant FV losses reported in the quarterly source data during the recessionary period 2007Q4 to 2009Q2. In addition, evidence suggests that not all FV losses are removed, which has a negative effect on the resulting published series. The results indicate that source data currently available to measure quarterly corporate profits for financial institutions are inadequate without significant efforts made to adjust the data, which are often not practical or possible during a typical estimation cycle. The extent of the inadequacy was highlighted during the 2008 financial crisis. Thus, quarterly source data based on surveys designed for statistical purposes would be a valuable alternative to source data currently available to measure quarterly U.S. corporate profits for financial institutions.