GAAP vs Statutory Accounting

Every industry has a given set of principles for the preparation of financial statements. These principles define how financial transactions should be accounted for in accordance with the rules and regulations of the statutory bodies. Two of these statutory bodies are known as GAAP and SAP. Statutory Accounting Principles, also known as SAP, are used to prepare the financial statements of insurance companies. In the United States, authorized insurers are required to prepare financial information according to SAP. These principles are designed for the insurance departments of different states to help them regulate the solvency of insurance companies.

On the other hand, Generally Accepted Accounting Principles or GAAP provides a common set of accounting standards, procedures and rules that are defined by the professional accountancy body. Almost every publicly traded company in the United States has adopted GAAP. These principles provide authoritative accounting standards as well as commonly accepted methods of recording and reporting accounting transactions. Companies are required to follow GAAP in order to take the investors into confidence who use financial information of the company for investment purposes. However, GAAP and SAP are not same. There are differences between these two accounting frameworks and these differences are discussed below.

Difference between GAAP and Statutory Accounting

Industry Difference

It is mandatory for all the companies in the United States to use GAAP. When the companies file their financial reports, they are required by the Security and Exchange Commission of the U.S. to follow these Generally Accepted Accounting Principles. Financial Accounting Standards Board, also known as FASB, set the GAAP rules and accounting standards. These rules are same everywhere in the U.S., which makes it easier for investors to compare the financial information of different companies using the same set of principles. Statutory Accounting, on the other hand, is specific to insurance companies. The National Association of Insurance Commissioners (NAIC) provided the framework for SAP in order to record the financial transactions of insurance companies. The filing under Statutory Accounting is used to determine how insurance companies are performing.

Purpose of Accounting Principles

Financial statements of the insurance companies are prepared under the guidelines of statutory accounting and this financial information helps investors to see whether insurers are in a position to pay insurance claims. Moreover, it allows investors to assess the total worth of an insurance company in case the company ceases its operations. On the contrary, an entity is considered as a going concern as per GAAP. Therefore, financial statements are prepared on the basis of matching concept and investors can measure the profitability of a business. It also allows investors to assess the value of a company and compare its future and present value.

Value of Asset

The financial statements prepared under Statutory Accounting and the financial statements prepared under GAAP have different purpose. Statements prepared under the statutory accounting are used to find the current value of a company, and therefore, it doesn't include a lot of non liquid and intangible assets. For example, goodwill, supplies, furniture, tax credit etc., are not included in the financial statements of SAP. But, under the GAAP rules, these items form part of the financial statements under the category of asset, which increases the overall value of the asset.

Matching Principle

GAAP follows matching principle when preparing the financial statements of the companies, but in Statutory Accounting, no matching principle is followed. The matching principle allows an entity to record the expense related to a product only when the sale of the product is recorded in the financial statements. For example, if a company books its quarterly sales, the expense related to those sales is apportioned on a quarterly basis to match the quarterly earnings. But in the case of statutory accounting, insurance companies have to book the expenses as they occur. Therefore, as soon as the insurance policy is sold, the expenses related to that policy are accounted for immediately regardless of when the related premiums will be earned.

Value of Equity

The value of the entity is recorded as stockholder equity under GAAP, whereas in case of statutory accounting, it is recorded under statutory policyholder surplus. The value recorded in statutory policyholder surplus is not the same as stockholder's equity because statutory accounting has strict rules related to recording the assets, and the net income of an insurance company is calculated differently as compared to the calculation of net income under GAAP.