

# FASB Interpretation No. 5

Note: This Statement has been completely superseded

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## Applicability of FASB Statement No. 2 to Development Stage Enterprises

an interpretation of FASB Statement No. 2

February 1975



**Financial Accounting Standards Board**

of the Financial Accounting Foundation

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# FIN 5: Applicability of FASB Statement No. 2 to Development Stage Enterprises

## an interpretation of FASB Statement No. 2

### INTRODUCTION

1. The FASB has been asked to explain the applicability of *FASB Statement No. 2*, "Accounting for Research and Development Costs," to development stage enterprises.
2. In July 1974 the FASB issued an exposure draft of a proposed Statement titled "Accounting and Reporting by Development Stage Companies, Subsidiaries, Divisions and Other Components." A final Statement on this subject has not yet been issued.
3. Broad guidelines about the activities to be classified as research and development and the elements of costs to be identified with those activities are set forth in paragraphs 8-11 of *Statement No. 2*. Paragraph 12 of that Statement provides that research and development costs shall be charged to expense when incurred. However, some costs associated with research and development activities shall be capitalized if the item has alternative future uses in research and development or otherwise (see paragraphs 11(a) and 11(c) of *Statement No. 2*). The costs of materials consumed, the depreciation of equipment and facilities used, and the amortization of intangibles used in research and development activities are research and development costs.
4. Some development stage enterprises have adopted special accounting practices or forms of financial statement presentation and types of disclosure that are different from those used by established operating enterprises. Special accounting practices include deferral of preoperating costs (sometimes including general and administrative costs and interest costs), non-assignment of dollar amounts to shares of stock issued for consideration other than cash, and offset of revenue against deferred costs. Special financial reporting formats may consist of presentation of statements of (a) assets and unrecovered preoperating costs, (b) liabilities, (c) capital shares, and (d) cash receipts and disbursements; or other formats.

5. Other development stage enterprises prepare financial statements like those of established operating enterprises that present financial position, changes in financial position, or results of operations in conformity with generally accepted accounting principles.

## **INTERPRETATION**

6. *Statement No. 2* applies to the accounting for research and development costs of development stage enterprises whose financial statements present financial position, changes in financial position, or results of operations in conformity with generally accepted accounting principles. *Statement No. 2* also applies to the accounting for research and development costs of a development stage enterprise when the financial statements of that enterprise are included, either by consolidation or by the equity method, in financial statements of others that present financial position, changes in financial position, or results of operations in conformity with generally accepted accounting principles.

7. Pending the issuance of a Statement on the subject (see paragraph 2), a development stage enterprise that issues financial statements that do not purport to present financial position, changes in financial position, or results of operations in conformity with generally accepted accounting principles need not apply *Statement No. 2* in accounting for its research and development costs. However, at such time as a development stage enterprise commences issuing financial statements that present financial position, changes in financial position, or results of operations in conformity with generally accepted accounting principles, *Statement No. 2* shall apply. At that time, the requirement of paragraph 12 of *Statement No. 2* that research and development costs be charged to expense when incurred shall be applied retroactively by prior period adjustment (described in paragraphs 18 and 26 of *APB Opinion No. 9*, "Reporting the Results of Operations"). If financial statements that present financial position, changes in financial position, or results of operations in conformity with generally accepted accounting principles are not also presented for prior periods, the disclosures specified by paragraphs 15 and 16 of *Statement No. 2* and by paragraph 26 of *APB Opinion No. 9* shall be limited to the effects of the prior period adjustment on retained earnings at the beginning of the period.

## **EFFECTIVE DATE**

8. This Interpretation shall be effective on March 31, 1975 for fiscal years beginning on or after January 1, 1975. Earlier application is encouraged, except that this Interpretation shall not be applied prior to initial application of *Statement No. 2*. When initially applied, this Interpretation shall be applied retroactively as described in paragraphs 15 and 16 of *Statement No. 2*.

*This Interpretation was adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board following submission to the members of the Financial Accounting Standards Advisory Council.*

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