

Accounting Standard (AS) 8  
(issued 1985)  
Accounting for Research and Development

*(This Accounting Standard includes paragraphs 7-16 set in **bold italic** type and paragraphs 1-6 set in plain type, which have equal authority. Paragraphs in bold italic type indicate the main principles. This Accounting Standard should be read in the context of the Preface to the Statements of Accounting Standards<sup>1</sup>.)*

The following is the text of the Accounting Standard (AS) 8 issued by the Council of the Institute of Chartered Accountants of India on 'Accounting for Research and Development'. The Standard deals with the treatment of costs of research and development in financial statements.

In the initial years, this accounting standard will be recommendatory in character. During this period, this standard is recommended for use by companies listed on a recognised stock exchange and other large commercial, industrial and business enterprises in the public and private sectors.<sup>2</sup>

### Introduction

1. This Statement deals with the treatment of costs of research and development in financial statements.
2. The Statement does not deal with the accounting implications of the following specialised activities:
  - i. research and development activities conducted for others under a contract;
  - ii. exploration for oil, gas and mineral deposits;
  - iii. research and development activities of enterprises at the construction stage.

<sup>1</sup> Attention is specifically drawn to paragraph 4.3 of the Preface, according to which Accounting Standards are intended to apply only to items which are material.

<sup>2</sup> It may be noted that this Accounting Standard is mandatory. This standard stands withdrawn from the date of Accounting Standard (AS) 26, 'Intangible Assets', becoming mandatory, for the concerned enterprises (see AS 26).

Reference may be made to the section titled 'Announcements of the Council regarding status of various documents issued by the Institute of Chartered Accountants of India' appearing at the beginning of this Compendium for a detailed discussion on the implications of the mandatory status of an accounting standard.

### Definitions

3. The following terms are used in this Statement with the meanings specified:
  - i. *Research* is original and planned investigation undertaken with the hope of gaining new scientific or technical knowledge and understanding;
  - ii. *Development* is the translation of research findings or other knowledge into a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services prior to the commencement of commercial production.

### Explanation

#### 4. Cost of Research and Development

- 4.1 There can be practical difficulties in deciding the amounts of the costs specifically attributable to research and development. In order to achieve a reasonable degree of comparability between enterprises and between accounting periods of the same enterprise, it is necessary to identify the elements comprising research and development costs.

4.2 Costs incurred for research and development include the following:

- i. salaries, wages and other related costs of personnel;
- ii. costs of materials and services consumed;
- iii. depreciation of building, equipment and facilities which have alternative economic use, to the extent that they are used for research and development;
- iv. an appropriate amortisation of the cost of building, equipment and facilities which have no alternative economic use, to the extent that they are used for research and development;
- v. a reasonable allocation of overhead costs;
- vi. payment to outside bodies for research and development projects related to the enterprise; and
- vii. other costs, such as the amortisation of patents and licences.

4.3 Costs incurred to maintain production or to promote sales of existing products are excluded from the costs of research and development. Thus, the costs of routine or periodic minor modifications to existing products, production lines, manufacturing processes and other ongoing operations as well as routine or promotional costs of market research are excluded.

## 5. Accounting Treatment of Research and Development Costs

5.1 The allocation of the costs of research and development activities to accounting periods is determined by their relationship to the expected future benefits to be derived from these activities. In most cases there is little, if any, direct relationship between the amount of current research and development costs and future benefits because the amount of such benefits, and the periods over which they will be received, are usually too uncertain. Research and development costs are therefore usually charged to expense in the period in which they are incurred.

5.2 If it can be demonstrated, however, that the product or process is technically and commercially feasible and that the enterprise has adequate resources to enable the product or process to be marketed, it may be appropriate to defer the costs of related research and development to future periods. Research and development costs previously written off are not reinstated because they were incurred at a time when the technical and commercial feasibility of the project was too uncertain to establish a relationship with future benefits and they were therefore proper charges to those past periods.

5.3 Deferred research and development costs are amortised on a systematic basis, either by reference to the sale or use of the product or process or by reference to a reasonable time period. However, technological and economic obsolescence create uncertainties that restrict the number of units and time period over which deferred costs are to be amortised.

5.4 Wherever research and development costs are to be deferred, the appropriate legal requirements are also taken into account, for example, in the case of companies the need to provide depreciation on fixed assets used for purposes of research and development in accordance with the provisions of Sections 205 and 350 of the Companies Act.

## 6. Disclosure

6.1 The accounting policy adopted for the costs of research and development is included in the statement of accounting policies (see AS 1 on 'Disclosure of Accounting Policies'). Information about amortisation practices is also disclosed when research and development costs are deferred.

6.2 The disclosure of

- i. research and development costs, including the amortisation of deferred costs, charged as an expense of each period, and
- ii. the unamortised balance, if any, of deferred research and development costs,

enables the users of financial statements to consider the significance of such activities in relation to those of other enterprises as well as to the other activities of the enterprise itself.

### **Accounting Standard**

**7. Research and development costs should include:**

- i. **salaries, wages and other related costs of personnel engaged in research and development;**
- ii. **costs of materials and services consumed in research and development;**
- iii. **depreciation of building, equipment and facilities which have alternative economic use, to the extent that they are used for research and development;**
- iv. **an appropriate amortisation of the cost of building, equipment and facilities which have no alternative economic use, to the extent that they are used for research and development;**
- v. **overhead costs related to research and development;**
- vi. **payment to outside bodies for research and development projects related to the enterprise; and**
- vii. **other costs related to research and development such as amortisation of patents and licences.**

**8. Amount of research and development cost described in paragraph 7 should be charged as an expense of the period in which they are incurred except where such costs may be deferred in accordance with paragraph 9.**

**9. Research and development costs of a project may be deferred to future periods, if the following criteria are satisfied:**

- i. **the product or process is clearly defined and the costs attributable to the product or process can be separately identified;**
- ii. **the technical feasibility of the product or process has been demonstrated;**
- iii. **the management of the enterprise has indicated its intention to produce and market, or use, the product or process;**
- iv. **there is a reasonable indication that current and future research and development costs to be incurred on the project together with expected production, selling and administration costs are likely to be more than covered by related future revenues/benefits; and**
- v. **adequate resources exist, or are reasonably expected to be available, to complete the project and market the product or process.**

**10. Wherever research and development costs are deferred, the appropriate legal requirements should also be taken into account.**

11. *If an accounting policy of deferral of research and development costs is adopted, it should be applied to all such projects that meet the criteria in paragraph 9.*
12. *If research and development costs of a project are deferred, they should be allocated on a systematic basis to future accounting periods by reference either to the sale or use of the product or process or to the time period over which the product or process is expected to be sold or used.*
13. *The deferred research and development costs of a project should be reviewed at the end of each accounting period. When the criteria of paragraph 9, which previously justified the deferral of the costs, no longer apply, the unamortised balance should be charged as an expense immediately. When the criteria for deferral continue to be met but the amount of unamortised balance of the deferred research and development costs and other relevant costs exceed the expected future revenues/benefits related thereto, such excess should be charged as an expense immediately.*
14. *Research and development costs once written off should not be reinstated even though the uncertainties which had led to their being written off no longer exist.*

#### **Disclosure**

15. *The total of research and development costs, including the amortised portion of deferred costs, charged as expense should be disclosed in the profit and loss account for the period.*
16. *Deferred research and development expenditure should be separately disclosed in the balance sheet under the head 'Miscellaneous Expenditure'.*

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