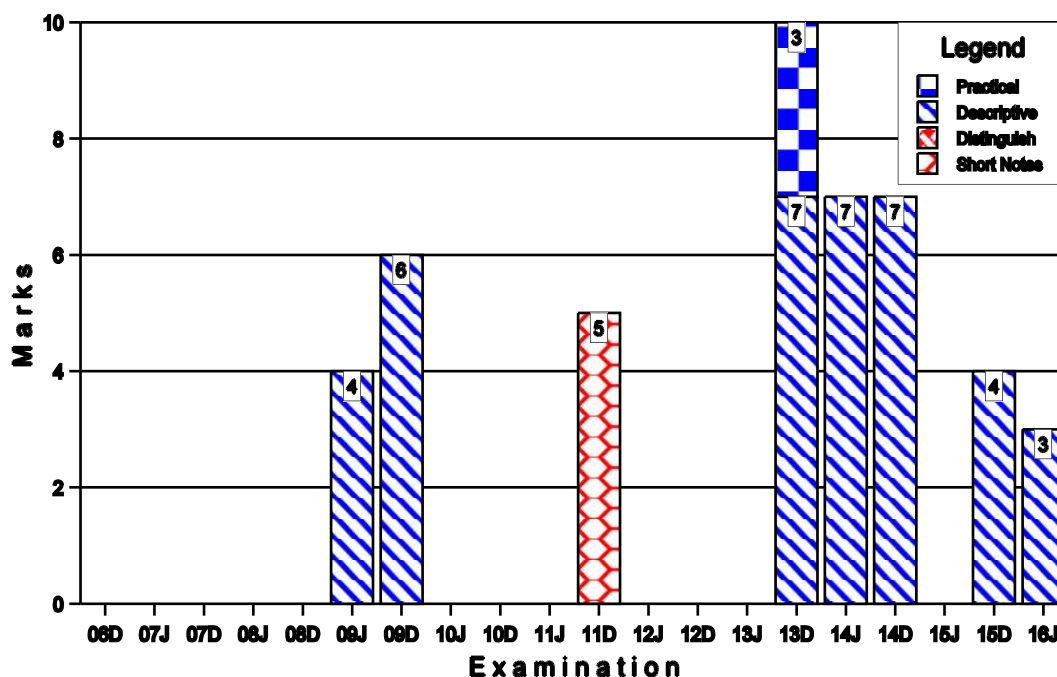


1

Cost Audit

This Chapter Includes : Cost Audit - Basics, Origin, Relevance, Objectives, Features; Genesis of Cost Audit in India, Provisions Under Companies Act.

Marks of Short Notes, Distinguish Between, Descriptive & Practical Questions



SHORT NOTES

2011 - Dec [3] (b) Write a note on 'social objectives' of Cost Audit.

(5 marks)

Answer :

The following are the social objectives of cost audit:

1. It helps in improving productivity of all the resources employed by the enterprise.
2. It helps in using the resources in most beneficial manner as all the areas are studied by the company.
3. It helps in fixation of reasonable prices of goods and services produced by the concern.
4. It helps in highlighting areas of inefficiency and mismanagement and thus increases the overall profits of the company.
5. It helps in contract costing particularly where the price is subject to escalation due to inflation.
6. It helps in cost plus contracts where records of cost play a very important role.
7. It also helps the government in setting prices for regulated goods.
8. It acts as an ethical standard.

DESCRIPTIVE QUESTIONS

2009 - June [4] (b) Define Cost Audit and state its purposes. (4 marks)

Answer :

Cost audit means audit of cost accounting records. According to CIMA London, cost audit is “the verification of the correctness of cost accounts and of the adherence to the cost accounting plan”.

The Institute of Cost Accountant of India on the other hand, defines cost audit as “a system of audit introduced by the Government of India for the review, examination and appraisal of the cost accounting records and attendant information, required to be maintained by specified industries.”

The purpose of cost audit can be understood by the definition itself. In India cost audit is more specific and lays emphasis on the evaluation of the efficiency of operations and the propriety of management actions.

The purpose of cost audit can be summarized by the following points:

1. To ascertain that T&F COP is worked out.
2. To ensure that inefficiencies, bottlenecks etc are resolved.

3. To bring out areas of wastage, possibility of cost control & reduction.
4. To bring out areas of inefficiency, deficiencies etc. and suggest remedial measures.

2009 - Dec [2] (a) What are the Social objectives of Cost Audit ? (6 marks)

Answer:

The following are the social objectives of cost audit:

1. Improvement in productivity of all resources of the enterprise.
2. It helps in using the resources in most beneficial manner as all the areas are studied by the company.
3. It helps in fixation of reasonable prices of goods and services produced by the concern.
4. It helps in highlighting areas of inefficiency and mismanagement and thus increases the overall profits of the company.
5. It helps in contract costing particularly where the price is subject to escalation due to inflation.
6. It helps in cost plus contracts where records of cost play a very important role.
7. It also helps the government in setting prices for regulated goods.
8. It acts as an ethical standard.

2013 - Dec [4] (a) What review should be made by a Cost Auditor of Cost Accounting Records? (7 marks)

Answer:

The cost auditor during the course of audit reviews the Cost Accounting Records of the company. Such review may include:

1. The manner in which cost centers are identified and established.
2. The accounting procedures followed for raw materials, packing materials, and spares, etc.
3. Method of accounting of wastes, rejections and defectives.
4. Methods of costing used by the company batch, job, process etc.
5. The accounting system for recording of wages, salaries, overtime and their allocation.
6. The manner in which overheads are allocated/ apportioned for utilities and service departments.
7. The Method of accounting for depreciation, sales & purchases and

- charging depreciation to cost centers.
8. The basis for reapportioning of service department to production departments.
 9. Internal audit system implemented by the management.
 10. The procedure of stock-taking.
 11. The method of valuation of inventories and WIP.

2014 - June [2] (a) What procedure are to be followed for appointment of cost auditor? (7 marks)

Answer:

PROCEDURE FOR APPOINTMENT OF COST AUDITOR

1. The category of companies specified in rule 3 and the threshold limits laid down in rule 4 of Companies (Cost Records and Audit) Rules, 2014, shall within one hundred and eighty days of the commencement of every financial year, appoint a cost auditor.
2. The audit committee, if constituted by the company shall ensure that the cost auditor is free from any disqualifications.
3. The audit committee shall obtain a certificate from the cost auditor certifying his independence.
4. Every company referred to in sub-rule (1) shall inform the cost auditor concerned of his or its appointment as such and file a notice of such appointment with the Central Government within a period of **thirty days** of the Board meeting in which such appointment is made or within a period of **one hundred and eighty days** of the commencement of the financial year, whichever is earlier, through electronic mode, in form CRA-2, along with the fee as specified in Companies (Registration Offices and Fees) Rules, 2014.
5. On filing the application, the same shall be deemed to be approved by the Central Government, unless contrary is heard within **thirty days** from the date of filing of such application.
6. If within **thirty days** from the date of filing of such application, the Central Government directs the company to re-submit the said application with additional information the period of **thirty days** for deemed approval of the Central Government shall be counted from the date of re-submission by the company.

7. After the expiry of **thirty days**, the company shall issue formal letter of appointment to the cost auditor.
8. The audit committee, if constituted by the company recommends to the Board a suitable remuneration to be paid to the cost auditor. In the case of those companies which are not required to constitute an audit committee, the Board shall consider and approve the remuneration of the Cost Auditor which shall be ratified by shareholders subsequently.
9. Every cost auditor appointed as such shall continue in such capacity till the expiry of **one hundred and eighty days** from the closure of the financial year or till he submits the cost audit report, for the financial year for which he has been appointed.
10. Every cost auditor, who conducts an audit of the cost records of a company, shall submit the cost audit report along with his reservations or qualifications or observations or suggestions, if any, in form CRA-3.
11. Every cost auditor shall forward his report to the Board of Directors of the company within a period of **one hundred and eighty days** from the closure of the financial year to which the report relates and the Board of directors shall consider and examine such report particularly any reservation or qualification contained therein.
12. Every company covered under these rules shall, within a period of **thirty days** from the date of receipt of a copy of the cost audit report, furnish the Central Government with such report alongwith full information and explanation on every reservation or qualification contained therein, in form CRA-4 along with fees specified in the Companies (Registration Offices and Fees) Rules, 2014.
13. The company shall disclose full particulars of the cost auditor, along with the due date and actual date of filing of the cost audit report by the cost auditor, in its Annual Report for each relevant financial year.
14. In those companies, where constitution of Audit Committee is not required by law, then the role of Audit Committee shall be discharged by the Board of Directors.
15. The provisions of sub-section (12) of section 143 of the Act and the relevant rules made thereunder shall apply mutatis mutandis to a cost auditor during performance of his functions under section 148 of the Act

and these rules.

2014 - Dec [2] (b) For what purposes the Cost Auditor refers to financial records while conducting the Cost Audit of the Company. (7 marks)

Answer:

A Cost Auditor is appointed to express an opinion whether the:

- (1) company has maintained proper cost accounting records;
- (2) cost accounting records give a true and fair view and depict the correct cost of production.

While doing so the cost accountant has to verify the details of materials, employee cost, labour cost, power & fuel consumption, stock consumption, depreciation, royalty etc.

The annexure to cost audit report requires disclosure of information in respect of capital employed, net worth, sales, profit, cost of fuel and power, wages and salaries paid etc.

We know that all these information are maintained in the financial records.

Therefore the cost auditor has to verify the financial records as well.

Schedule III of the Companies Act, 2013 requires:

1. disclosure of various expenses like consumption of material, labour;
2. disclosure & classification of material into raw material, WIP and finished goods;
3. disclosure of costs related to production.

Further the annexure to Cost Audit Report Rules requires Reconciliation statement which indicates the reasons for difference in profit as per cost accounting and financial records.

Therefore in view of above it is quite clear that cost auditor will have to refer to financial records. Unless this is done completion of cost audit will not be viable.

2015 - Dec [1] Answer the question:

- (b) (i) What are the duties of the companies in relation to provisions of section 148 of the Companies Act, 2013 and Rules framed thereunder? (4 marks)

Answer:

1. Every company shall appoint a cost auditor within 180 days of

Commencement of every financial year.

2. Inform the cost auditor concerned of his appointment.
3. According to Section 148 of Companies Act, 2013 a company shall within thirty days from the date of receipt of a copy of the cost audit report prepared in pursuance of a direction under sub-section(2) furnish the Central Government with such report along with full information and explanation on every reservation or qualification contained therein.

If after considering the cost audit report referred to under this section and the information and explanation furnished by the company under sub-section(6), the Central Government is of the opinion that any further information or explanation is necessary, it may call for such further information and explanation and the company shall furnish the same within such time as may be specified by Government.

4. If any default is made in complying with the provisions of this section:
 - (a) The company and every officer of the company who is in default shall be punishable in the manner as provided in sub-section(1) of Section 147.
 - (b) The cost auditor of the company who is in default shall be punishable in the manner as provided in sub-section(2) to (4) of Section 147.

2016 - June [8] (b) Who can be appointed as a “Cost Auditor” of a company? (3 marks)

PRACTICAL QUESTIONS

2013 - Dec [3] (d) Company having turnover above ₹ 100 crore undertakes works contracts for pipe line execution for Drinking, Sewerage and Irrigation purpose. The required pipes for the projects, falling under Chapter 68 of CETA, are manufactured by the Company itself. A part of the production is also sold outside. Whether Cost Audit is applicable for pipe manufacture.

(3 marks)

Answer:

Cost audit is applicable on the basis of total turnover of the company.

19.8

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So the focus for applicability will be on **turnover of entire company and not just an individual activity.**

If the activity of pipe manufacturing in question is covered under the cost audit circular no. 52/26/CAB-2010 (it means cost audit is ordered by Central Government) then cost audit will apply.

The company will attract cost audit for its pipe manufacturing activity if captive consumption is made for a product which is under cost audit.