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# Nature and significance of cost audit

It is an audit process for verifying the cost of manufacture or production of any article, on the basis of accounts as regards utilisation of material or labour or other items of costs, maintained by the company. In simple words the term cost audit means a systematic and accurate verification of the cost accounts and records and checking of adherence to the objectives of the cost accounting.

As per **ICWA London**’ “Cost Audit is the verification of the correctness of cost accounts and of the adherence to the cost accounting plan.”

The **ICWAI** defines cost audit as “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”

From above definition of cost audit, it is clear that cost audit is a systematic examination of cost accounts to verify correctness of cost accounting records.

For **companies** under item A: Every **company** having annual turnover from all its products and services in the immediately preceding financial year of Rs. 50 crore or more and the aggregate turnover of the individual product or products or service or services of Rs. 25 crore or more..

**Objectives of Cost Audit**

The following are some of the objectives for which cost audit is under taken:

1. To establish the accuracy of costing data. This is done by verifying the arithmetical accuracy of cost accounting entries in the books of accounts.
2. To ensure that cost accounting principles are governed by the management objectives and these are strictly adhered in preparing cost accounts.
3. To ensure that cost accounts are correct and also to detect errors, frauds and wrong practice in the existing system.
4. To check up the general working of the costing department of the organization and to make suggestions for improvement.
5. To help the management in taking correct decisions on certain important matters i.e. to determine the actual cost of production when the goods are ready.
6. To reduce the amount of detailed checking by the external auditor if effective internal cost audit system is in operation.

**Advantages of Cost Audit:**

**To The Management**

1. Cost audit helps in detection of errors and frauds.
2. The management gets accurate and reliable data based on which they can make day-to-day decisions like price fixation.
3. It helps in cost control and cost reduction.
4. It facilitates the system of standard costing and budgetary control.
5. It helps the management in inter-unit / firm comparison.
6. It enables the management to identify loss making propositions.

**To The Government**

1. Cost audit ensures efficient functioning of the industry. This in turn, nurtures a healthy competition among the different companies and paves a path for fast progress.
2. It helps in identification of sick units and enables the Government to make relevant decisions.
3. It helps in fixing prices in the case of essential commodities and checking undue profiteering.
4. It enables to take decisions as to granting of subsidies, incentives and protection to various industries.
5. It helps to take decisions as to levies, duties and taxes.

**To the Society**

1. Cost audit enables the Government to fix prices of essential commodities. This safeguards the interests of the society.
2. Cost audit enables the Government to keep a check on undue profiteering by the manufacturers and avoids artificial price rise due to monopolistic tendencies.

**To the Shareholders**

1. Cost audit reveals whether any of the products of the company are making losses. Thus though the company making an overall profit, a loss making line may eat up the company’s profits. This is brought to the notice of the shareholders and the management is forced to take remedial measures, thereby making optimum utilisation of resources.
2. Cost audit ensures that the shareholders get a fair return on their investments.

**Disadvantages of Cost Audit:**

1. Holding a Cost Audit can be expensive. This is because a company will often bring in an independent auditor who are normally charging higher price.
2. A Cost Audit can be a long process which will likely involve more time. This extra time and effort can impact an employee’s day to day routine work.
3. If a Cost Audit is carried out in order to find fraudulent activity it can take a long time by which time people stealing could have covered their tracks.
4. Cost Audits involve a large amount of estimation and so there is the possibility that figures will be incorrect and if record keeping from the company is not good to start with then inaccuracies will be arises

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**When cost audit is required:-**Centralgovernment may direct to conduct cost audit in respect of companies engaged in the production of such goods or providing such services and have a net worth or turnover as may be prescribed.

Note: If company is regulated by any special act then central government can direct to conduct cost audit only after consulting with regulatory body constituted under special act.

**Appointment of cost auditor:-**Costauditor shall be appointed by board whereas remuneration of cost auditor shall be determined by members.

**Who can be appointed as cost auditor:-**Costaudit shall be done by cost accountant in practice.

**Qualifications, disqualifications, rights and duties of cost auditor:-**Costauditor shall have same qualifications, disqualifications, rights and duties as that of a company auditor. Further, it is the duty of cost auditor to comply with cost auditing standards and to submit his report to BOD.

**Duty of company:-**Afterreceiving the cost audit report, company shall furnish full information and explanations on every reservations or qualifications to CG within 30 days of receipt of cost audit report. If CG requires any further information then it is the duty of company to furnish such information within given time.

**Punishment for contravention in case of company:-**Ifcompany contravenes any of the above mentioned provisions then company shall be punishable with fine of Rs. 25,000 to Rs. 5, 00,000 and officers of company shall be liable for fine of Rs. 10,000 to Rs. 1, 00,000 or imprisonment for a term which may extend to 1 year.

**Punishment for contravention in case of cost auditor-**IfCost auditor contravenes any of the above mentioned provisions unknowingly then he shall be punishable with fine of Rs. 25,000 to Rs. 5, 00,000. Whereas, he contravenes any of the above mentioned provisions knowingly then he shall be punishable with fine of Rs. 1,00,000 to Rs. 25,00,000 along with imprisonment for a term which may extend to 1 year. Further, he shall be liable to refund the remuneration and pay damages to company.