

CMA FINAL

Group IV

Paper 17: Cost and Management Audit.

Hand written notes

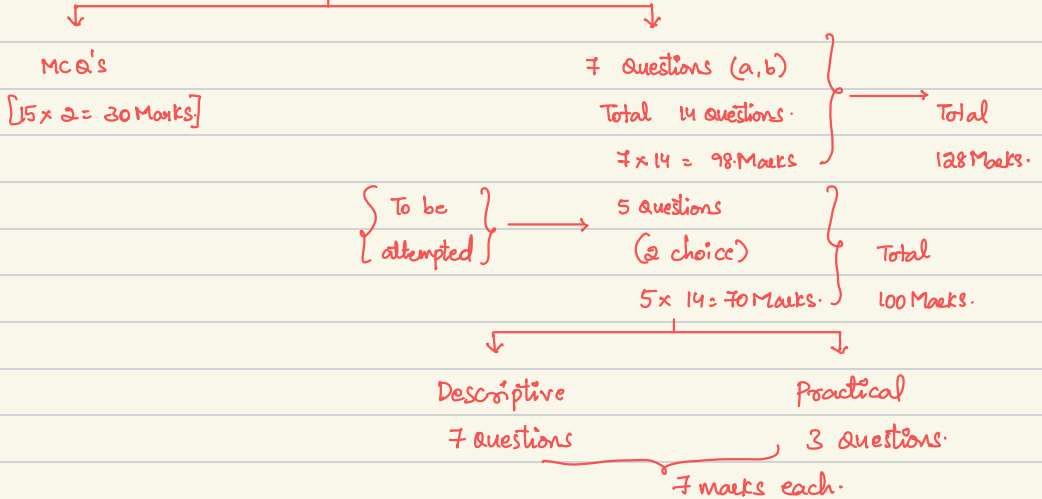
CMA PARVATHI



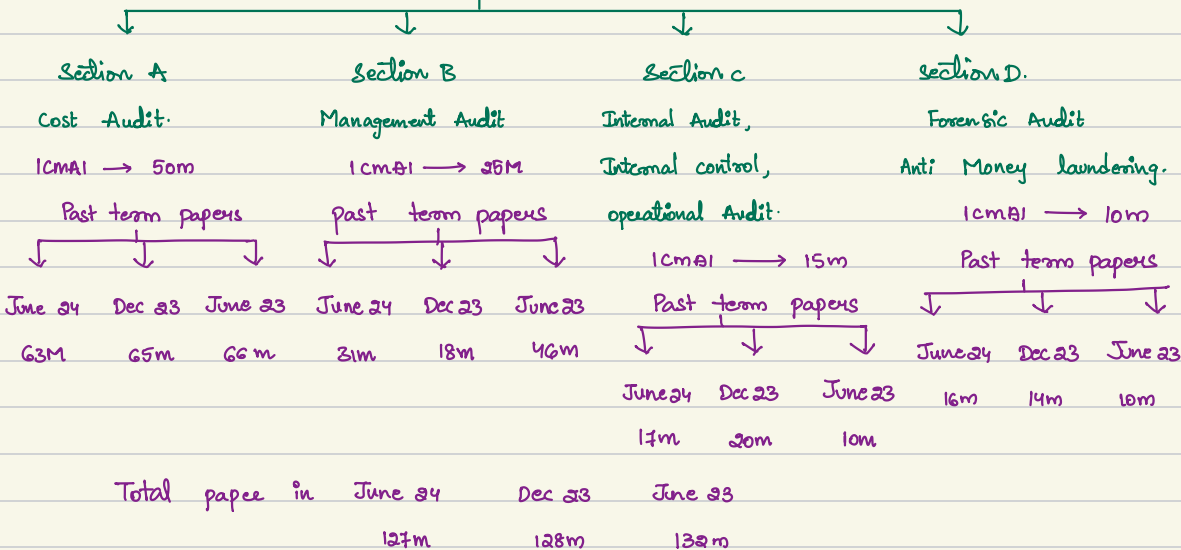
CMA FINAL GROUP IV

Paper 17 : Cost and Management Audit:

Paper Pattern



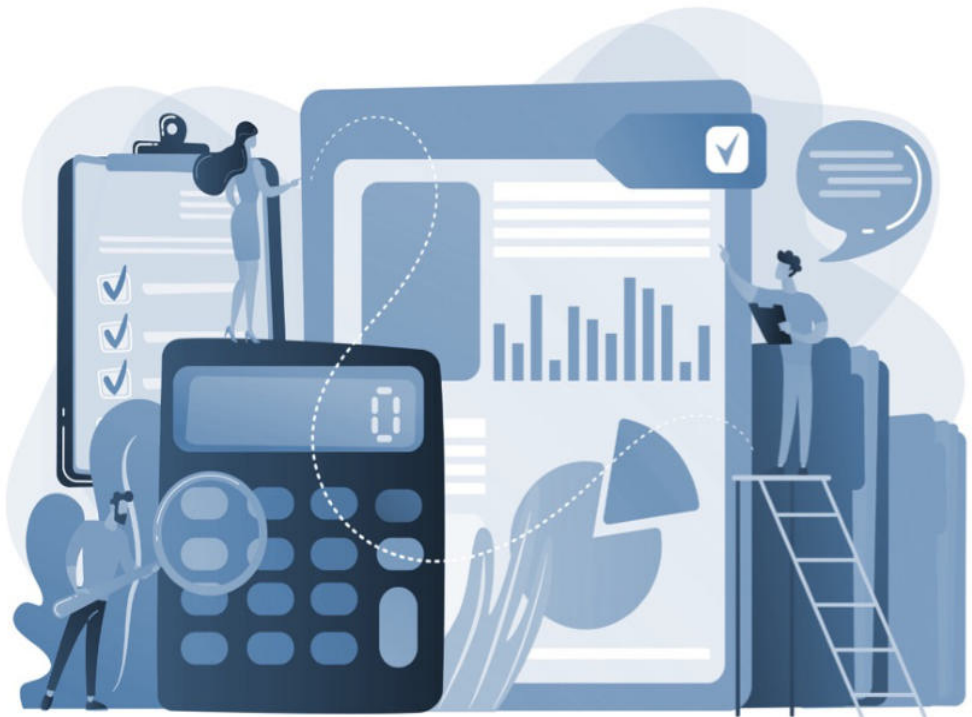
Syllabus



Section A

Cost Audit

- Basics of Cost Audit
- Companies (Cost Records and Audit) Rules, 2014 (as amended)
- Cost Auditor
- Overview of Cost Accounting Standards and GACAP
- Cost Auditing and Assurance Standards
- Cost Audit Programme
- Cost Audit Documentation, Audit Process and Execution
- Preparation and Filing of Cost Audit Report



SECTION-A: COST AUDIT

UNIT-1: Basics of cost Audit

- 1. Cost : - A price that must be paid for something or to cause loss of something
- 2. Audit - official examination of present state of something, especially financial records & Books
- 3. Cost Audit - examination of cost statements, cost records & other cost related information of entity

4. Cost Accounting : Process of Identification, classification, measurement & assignments of cost to various cost objects

Management → will take proper steps in preparation & presentation of cost records & cost statements

*

cost Accounting



Cost Accounting standards



Guidelines / Rules for companies

- 1. cost accounting treatments
- 2. disclosure requirements
- 3. ensure comparability, consistency & completeness of cost records

cost auditing



Standards on cost auditing



Guide for cost auditor

- 1. Procedures to be followed,
 - 2. Responsibilities & cost reporting
- Streamline audit, Better planning & Documentation, effective implementation



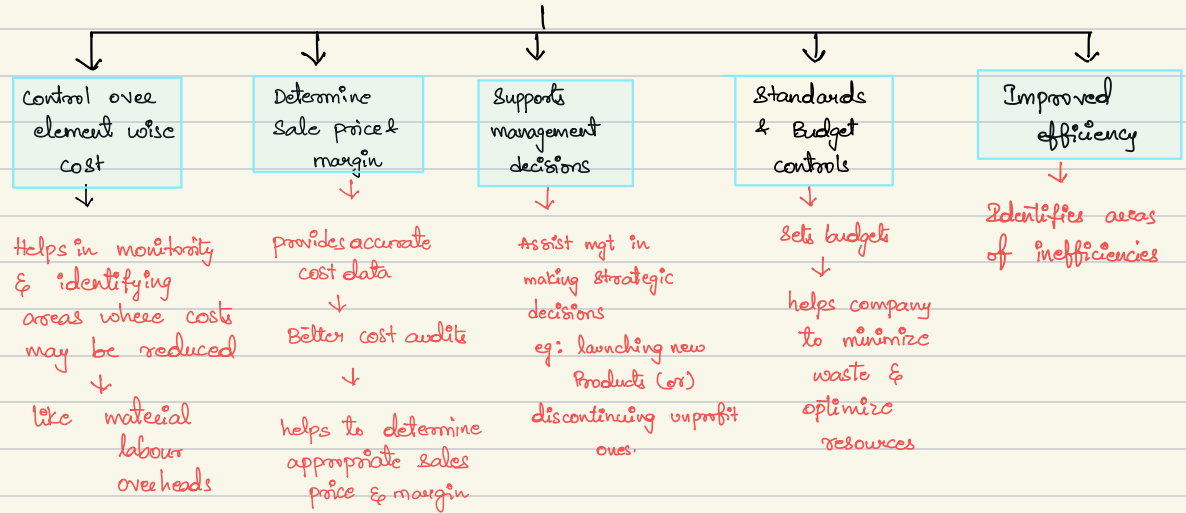
following both will improve the overall quality of audit

* If Required & Satisfied the cost auditor can rely on work done by another auditor

* Scope of cost audit

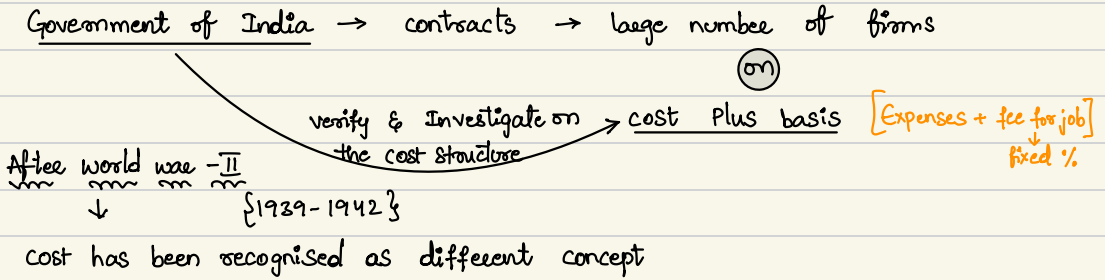
objective \longrightarrow Accuracy & exact
of cost data computation of
cost of a product

\implies cost audit is not just a compliance tool
It has a very wider scope.



Genesis of cost Audit

→ Methods & Techniques of cost accounting & audit of cost accounts can be traced back to pre independence era.



In mid 1950's → case of corporate fraud in Dalmia jain Companies

1. This company was involved in fraud & other commercial crimes
2. falsified its accounts
3. Tampered records for personal gains &
4. Tax evasion etc.

however, obtaining evidence was difficult because accounts books have been destroyed & the companies involved were no longer in existence.

* Vivian Bose Commission
Dutta Commission &
Daphatary Sastri Committee

appointed by government → Recommended effective system of cost accounting & cost audit & to improve system of corporate disclosures

↓

After which a mechanism of cost audit & maintenance of cost data were considered as important instruments

1944 — Institute of cost and work Accountants of India [ICWAI] was set up
 Renamed as ICAI (Institute of cost Accountants of India) in 2012
 under companies Act 1913 as company
 objective → Promote, regulate & develop cost Accountancy in India

1959 — ICAI incorporated as statutory body by Act of parliament
 under cost & works Accountants Act 1959.

History of Cost Audit

1965 — Cost Audit was introduced

Sec 233B of companies Act 1956
 → Cost Audit

Sec 209(1)(d) for maintenance of Cost Records

1965-2008 — Under cost record maintenance & cost audit of company →

around 44 Industries are covered

2008 — To study existing system of maintenance of cost Accounting Records and audit

Expert group was set up.

2009 — Report on Study — was submitted by expert group to central government.

2011 — Mandatory cost Audit of cost records maintained by companies for Manufacturing, mining & processing operations

2014 — Companies (Cost Records & Audit Rules) 2014 issued under companies Act 2013.

Cost Audit ——— Tool for price control mechanism

Objective ———

Initial years

1. To meet government requirements for regulating the administered price mechanism in industries
2. To provide an authentic data to the government to regulate demand & supply through price control mechanism

General objectives.

Verification of cost accounts	ensuring Prescribed Procedures are followed.	Determine Inventory valuation
periodic reconciliation of CA & FA	Detect & correct abnormal loss.	To Facilitate fixation of prices of Goods & services.
		ensure optimum utilisation of resources.

social objectives.

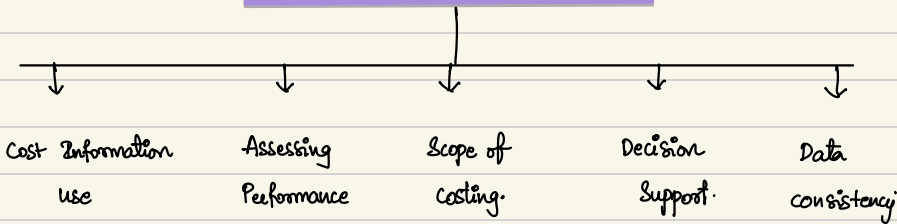
Verifying pricing of products are justified	→ Preventing overpricing/underpricing. (Cost as per quality)
when products are in global market looking into no cost based economic imbalance	Removing differences b/w prices of products
efficient utilisation of resources	→ Reducing waste & promoting practices that benefit Society.

Benefits of cost Audit

As per International Federation of Accountants:

- Helps to ascertain whether organisation records are maintained to give true & fair view of
 - cost of production
 - Processing
 - Manufacturing
 - Mining of Product.
- Helps to identify weakness in cost accounting system.
- Helps to drive down costs by detecting wastage & inefficiencies
- Assists government in helping to formulate taxation policies.

Benefits of cost Information



Section 148 of Companies Act, 2013.

Central government to specify audit of items of cost in respect of certain companies

1. Central Government → order → class of companies



Production of such goods/
Providing services such
as may be prescribed.

To include in Books of Accounts ←



utilisation of material / labour / other
items of cost

If companies are regulated
by special act



Central
government



consult such regulatory
body before issuing order.

2. Central Government if
is of opinion to
do so,



Manner of
conducting



Audit of cost
records of
class of companies
{ having (to or) n/w as
may be prescribed }

3. Audit → conducted by →

cost Accountant in
Practice



shall be appointed by
Board

* Auditor of company cannot be appointed as

cost Auditor.

shall ↓ always comply with cost auditing
Standards

4. Cost Accountant → Submit → Report on Audit of cost records → Board of directors of the company.

5. within 30 days

from Receipt of Report

Company → To furnish with central government

[Report along with full explanation & information]

6. central government → may ask for additional information if needed.

7. Default



Company & every officer of company (punishable)

as per Section 147(1)

Cost auditors of company (Punishable)

as per Section 147(2) & 147(5) -

Section 148 (Companies Act 2013)

Gave Powers to central government

(to)

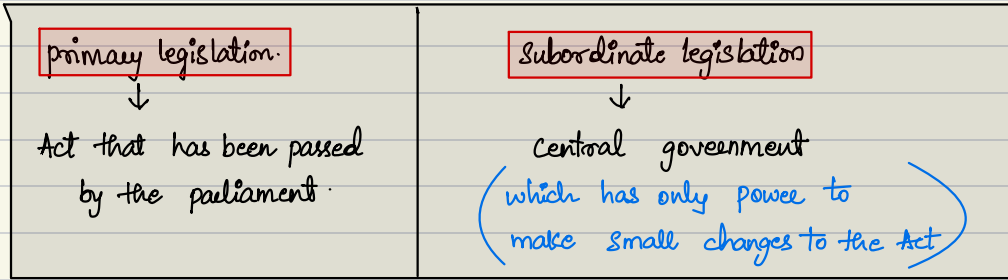
Make Rules regarding maintenance of cost records

for companies engaged in specified industries, Manufacturing/providing goods / services.

Central government

Subordinate legislative power

It is a process by which executive is given powers by primary legislation to make laws in order to implement & administer the requirements of primary legislation.



CG

→ from time to time issues

notifications (or)

orders

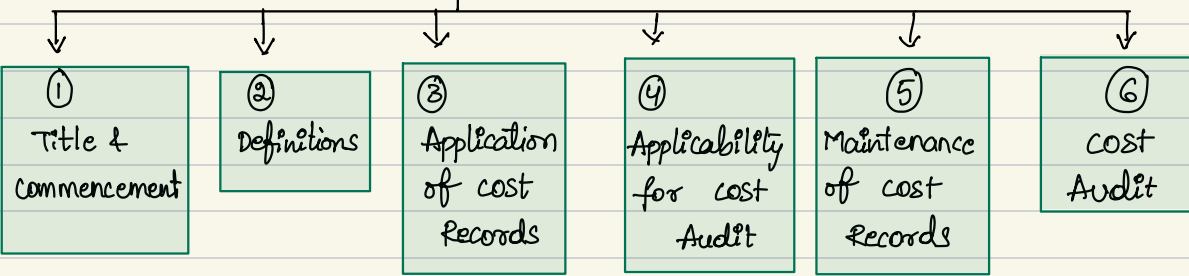
Providing information

- 1. Guidance/classifications on law provisions
- 2. prescribe procedures for compliance
- 3. Introduce changes in provisions/regulations

Specific order Passed by Gov. which is intended to be followed by target group

Cost Records & Audit Rules

6 Rules



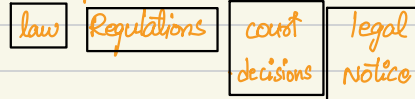
Rule 1: Title & Commencement.

Companies cost records & Audit Rules 2014. came into force as on 30-06-2014.

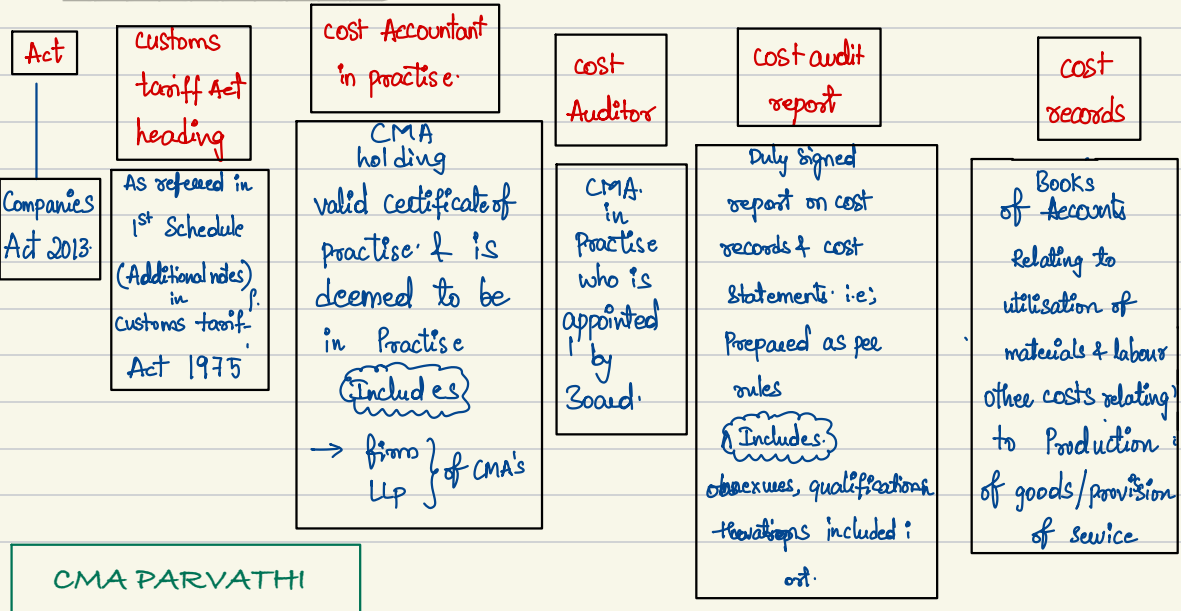
By publishing in

official Gazette

legal newspaper that publishes → new



Rule 2: Definitions



Form

INDAS

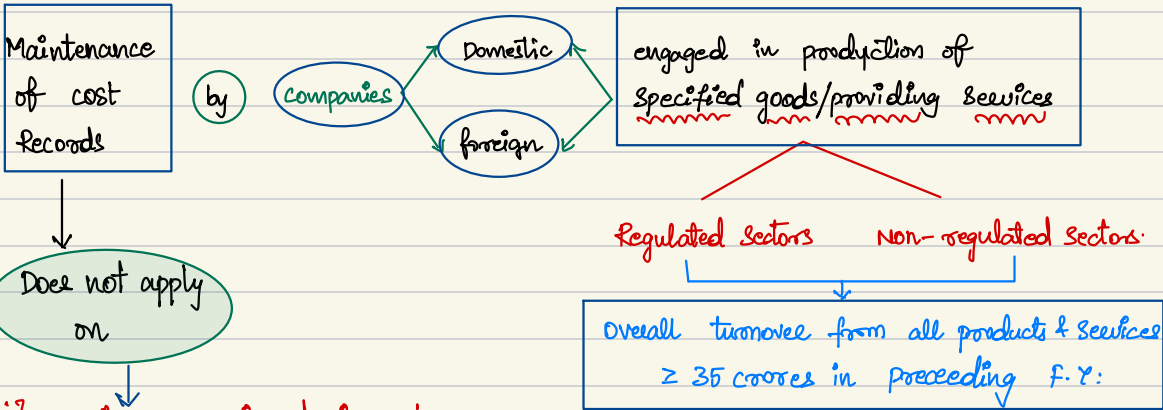
Institute

form annexed to these rules

IND AS referred in companies INDAS (Rules) 2015.

ICAI under ICWAI Act 1959.

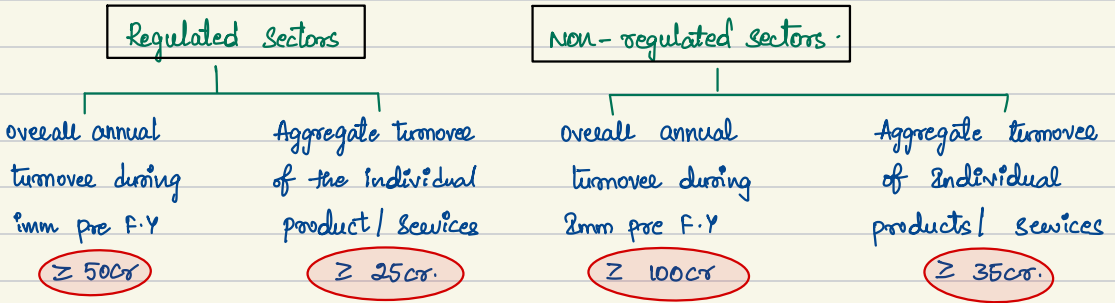
Rule 3: Applicability of cost Records.



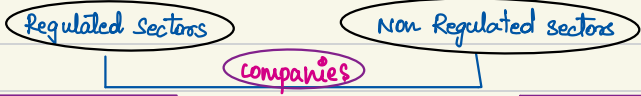
[i] foreign companies having only liaison offices → Representative office.
 connection (or) bond. eg: parent company (foreign) → Business parties (India)
 helps to facilitate close working relationships

[ii] companies classified into Micro (or) small enterprise
 As per Micro, small & medium enterprises Development Act, 2006.

Rule 4: Application of Cost Audit.



Non applicability of Rule 4 {Only Rule 3 will apply}



If Revenue from exports (foreign exchange) > 75% of total revenue

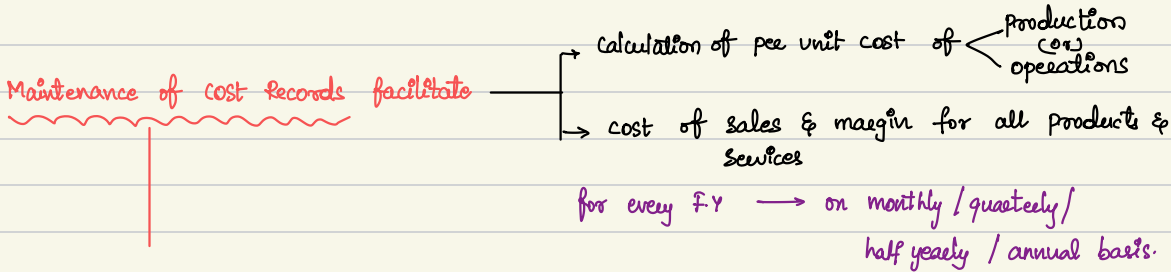
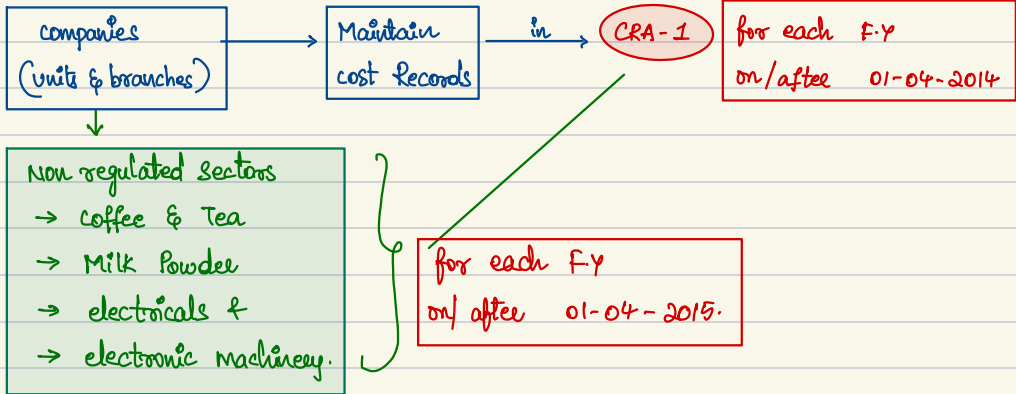
If operating from special economic zone (SEZ)

engaged in generation of electricity for captive consumption through captive generating plant.

meaning
 goods manufactured by 1 division/unit consumed by another division/unit for producing another product.

captive consumption through CoP → owner of power plant uses atleast 51% of the electricity. it generates for own consumption

Rule 5 : Maintenance of cost Records.



helps company to exercise

- * control over various operations
- * control over costs to achieve optimum utilisation of resources &
- * To provide necessary data which is required to furnish under these rules.

Rule 6 : Cost Audit

1. Board meeting → within (180 days of commencement of F.Y)
 Appoint Cost Auditor.

2. Company → inform → Cost Auditor
 About his/ her appointment & obtain consent letter & certificate from him

3. Certificate → cost auditor → Individual or firm
 * is eligible for appointment & not disqualified.
 * Satisfies the criteria provided in (qualifications, disqualifications
 Section 141 & Responsibility of auditor).
 * Appointment is within limits & as per rules.
 * Matter disclosed in certificate is true & correct.

4. Company → file notice → central government
 within

30 days of Board meeting
 in which such appointment
 is made.

(or)

180 days from commencement
 of the financial year

whichever is earlier.

In Form CRA-2. through electronic mode along with
 prescribed fee.

5. Auditor → to continue in his office.

till expiry of 180 days
 from closure of F.Y

(or)

till he/she submits
 the report.

6. Cost Auditor Appointed → Can be removed from his office (before expiry of his term)

↓
through boards resolution & ROBT to be given to cost auditor
Board → shall also record the reasons in writing for such removal.

7. For appointing another auditor also.

company → file CRA-2 → central government.

8. Nothing contained in this rule shall prejudice the right of cost auditor to resign from such office.

9. casual vacancy to be filled by BOD within 30 days.

↓ whether due to resignation, death or removal

* company → shall inform in CRA-2 → central government.
(within 30 days of appointing new auditors)

10. Cost Statements, & other statements to be annexed to Cost Audit report.

↓
shall be approved by BOD before signed.

11. Cost Auditor → Submit → cost audit Report → duly signed.

in CRA-3.

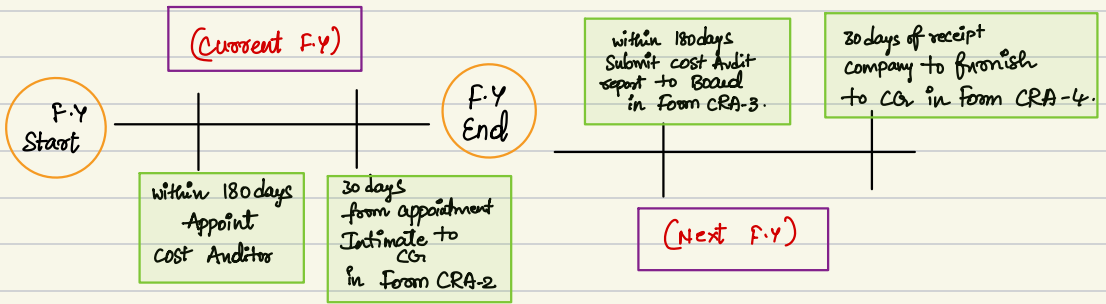
Along with reservations / qualifications / observations / suggestions

12. Cost Audit Report → Submit to BOD → within 180 days.

13. company → within 30 days form

receipt of copy of → furnish CO in
Cost Audit report CRA-4.

Time line for Rule 6:



CRA Forms

Form CRA-1 Maintenance of cost Records.

Specified Requirements in 31 headings

heading 18 - Capacity determination.

can be measured

- how many products made
- Amount of service
- Machine hours
- Man - hours

Installed Capacity

Theoretical maximum production

Normal Capacity

Realistic output after accounting for holidays, maintenance & other factors

Capacity utilization

It shows how efficiently a plant is using its installed capacity based on actual output

$$\frac{\text{Actual production}}{\text{Installed capacity}} \times 100\%$$

Installed capacity → Maximum possible output of production unit under ideal conditions.

- Determined based on →
1. Manufacturers, Technical Specifications
 2. Capacities of individual production centers
 3. Capacity of critical machines
 4. Number of shifts.

Normal capacity vis a vis installed capacity.

↓

Practical output after some adjustments to installed capacity like.

①	②	③	④	⑤
holidays, Shutdowns & Idle time	Time lost in Batch changes	Time lost in Maintenance & Break downs	loss in efficiency due to Aging of Equipment	Number of Shifts.

heading 24 Related party transactions.

- Normal price** →
- * price charged for comparable & similar products.
 - * in ordinary course of business
 - * price charged in sole consideration of sale
 - * sale is not made to related party.
 - * Transaction is not clouded due to proximity.
 - * Transaction is not made under any influence

Basis adopted to determine Normal price

Cup method	Resale price method	cost plus method	Profit split method	Transactional net margin method
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Form CRA-2 Intimation of appointment of cost auditor by co. to CG.

1. Corporate Identity Number (or) Foreign company Registration number

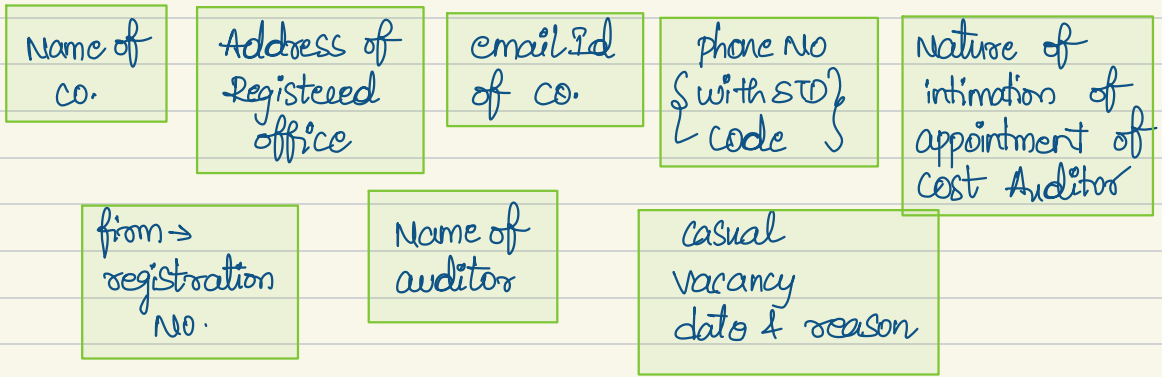
Global location number → 13 digit unique identification

NO. assigned to entity

* to identify physical locations, legal entities etc.

common in retail & logistics industries

2. General Information →



3. Regulated Sector or Non Regulated Sector.
Industry / Sector / product / Services

4. details of cost auditor



5. Financial year to be covered
6. details of previous cost auditor who has not been appointed.
7. Attachments:

copy of Boards
Resolution of
Company.

other
Attachments

Form CRA-3 cost Audit report

Part A
General
Information

Part B
For manufacturing
Sector

Part C
For Service
Sector

Part D.
other details
& Statements.

↓

Name of co.
Address
email Id.
Date of Start & end of
→ reporting F.Y &
→ previous F.Y.
IND AS applicability
No. of cost Auditors
Date of Board meetings.
Related party transactions.

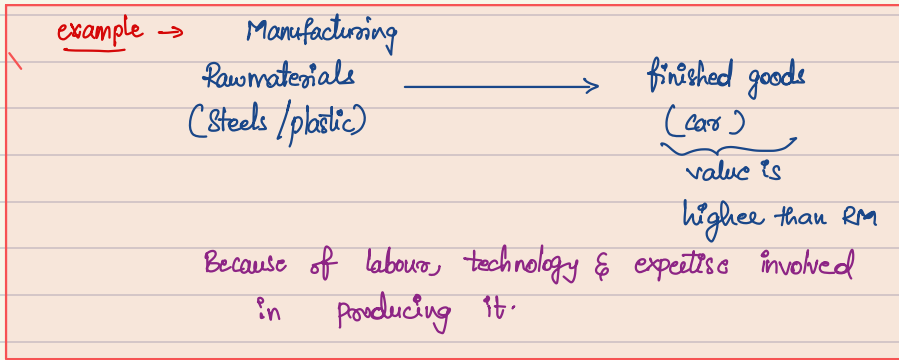
General details of
cost Auditor

Category
registration No.
Name
PAN, Address
email Id, membership
NO.
Name of product/Service

Quantitative Information

- * Available capacity
- * Actual production
- * Capacity utilisation
- * Stock & other Adjustments
- * Actual Sales.

- value addition** → Increase in value of business by transforming raw materials / inputs into finished goods / services
- It is difference b/w cost of inputs & price at which FG are sold.
 - process of enhancing value of product / service through various activities
 - Manufacturing, Processing, Packaging, branding, customer service



Form CRA 4 : Company to file cost Audit Report to central government.

1. corporate Identity NO, (Or) foreign co. registration Number
Global location Number
2. General Info
3. Details of Industry / sector / product / service

Covered in cost Audit Report

Not covered in cost audit Report.

4. observations of cost auditor
5. Attachments

XBRL Documents

other attachments

Work Book Questions:

Q1.

Sinjini Ltd.

Step-1: calculation of value addition.

Particulars.	Amount ₹ (in lakhs)	
	2023	2022.
Net Sales	4,800	3,840.
Add: Export incentives.	—	—
Add: Increase in stock of finished goods.	<u>20</u>	<u>10.</u>
	4,820	3,850
less: Stock of bought out inputs:		
Raw materials consumed.	1,760	1,440.
Power & Fuel	240	192.
Stores & spares	160	140
other Administrative overheads	260	220.
Packing & forwarding	20	16
other selling & distribution overheads	250	200
other manufacturing overheads.	430.	370.
working capital loans from bank.	60.	25.
Audit fees.	<u>36.</u>	<u>30.</u>
	<u>3,216.</u>	<u>2,633.</u>
value addition-	1,604	1,217.

Step 2 : calculation of Earnings available for distribution.

particulars	(Amount ₹ in lakhs)	
	2023	2022.
value addition.	1,604	1,217.
Add: other Income	<u>300</u>	<u>200.</u>
Earning available for distribution.	<u>1,904</u>	<u>1,417.</u>

Step 3 : Distribution of Earnings to different claimants.

Particulars.	Amount (₹) in lakhs	
	2023	2022
Salaries, wages, bonus & gratuity.	524.	422.
cess & local taxes.	436.	300.
Total Depreciation.	120.	120.
Dividend to shareholders.	450.	220.
Interest on debentures & fixed loans.	120.	105.
company as retained funds.	<u>284.</u>	<u>240.</u>
	<u>1904</u>	<u>1417.</u>

Q2.

Vennela Ltd.

step-1 calculation of value added.

Particulars.	Amount ₹ in lakhs	
	2023	2022.
Net Sales.	7,120	5,700.
Add: Export incentives.	80.	60.
Add: Increase in value of stock of finished goods.	<u>30.</u>	<u>15.</u>
	<u>7,230</u>	<u>5,775.</u>
less: Cost of stock of bought out inputs.		
Raw materials consumed.	2,640	2,160.
Power & fuel	360.	288.
Stores & spares	240	210.
other manufacturing overheads	645	555.
Audit fees.	54	45.
other administrative overheads	390	330.
Packaging & forwarding other overheads	30	24
	375	300
Interest on working capital loans.	90	75.
	4824	3987.
value addition.	<u>2406</u>	<u>1788</u>

Step 2: Calculation of earnings available for distribution.

Particulars.	Amount ₹ (in lakhs)	
	2023	2022.
value addition.	2406.	1788.
Add: Income from other sources.	<u>450</u>	<u>300.</u>
Earnings available for distribution.	<u>2856.</u>	<u>2088.</u>

Step 3: Distribution of earnings to different claimants.

Particulars	Amount (₹) in lakhs	
	2023	2022.
Direct wages, salaries, Bonus & gratuity.	786.	633.
Total Depreciation.	180	180.
Interest charges on fixed loans.	135	105
Interest charges on Debentures.	45	45.
Tax paid including provision.	474.	300.
Shareholders dividend.	630.	345.
Dividend distribution tax.	110	60.
Company as Retained funds.	<u>496.</u>	<u>420.</u>
	<u>2856</u>	<u>2088</u>

Q3.

ABC Hd.
calculation of operating profits.

Particulars.	Amount (₹) in lakhs.		
	2023	2022	2021
Net Sales.	1,745.	1,705.	1,610.
less: cost of sales.			
Raw materials consumed.	1140	1060	975.
Direct wages.	35	32	27.
Stores & spares	6	5	4.
Power & fuel	30	27.	24.
Factory overheads.			
wages.	5	4	3.
Rates & taxes	1	1	1
overheads other	6	5	4.
Administrative overheads.			
wages	10	9	8
Rates.	2	2	2.
other overheads.	162	154	148.
Selling & distribution.			
wages	7	6	5.
Packaging & forwarding	6	6	5.
other overheads.	124	118	108
Bonus & gratuity	12	10	9.
	<u>1,546.</u>	<u>1,439.</u>	<u>1,323.</u>
operating profit.	199.	266.	287.

calculation of value addition.

Particulars	Amount (₹) in lakhs.		
	2023	2022.	2021.
Net Sales.	1745	1705	1610.
less: Cost of Stock of bought out inputs.			
Raw materials consumed.	1140	1060	975.
Power & Fuel	30	27	24.
Stores & Spares	6	5	4.
Factory overheads.	6	5	4.
Administrative overheads.	162	154	148.
packaging & forwarding.	6	6	5.
Selling & distribution overheads	124	118	108.
	11474	1375	1268.
value addition.	271	330	342.

(i) operating profit to the percentage of value addition.

<u>199</u>	<u>266</u>	<u>287</u>
271	330	342.
73.43%	80.60%	83.92%

(ii) value addition as percentage of net sales

<u>271</u>	<u>330</u>	<u>342</u>
1745.	1705	1610.
15.53%	19.35%	21.24%

Reconciliation.

Q4).

Trincus Textiles mills Ltd.

Reconciliation of profit between cost & financial Accounts.

particulars	Amount (₹)	Amount (₹)
Profit as per financial Accounts.		22,14,100.
Add: Expenses not considered in cost Accounts.		
loss on sale of Investments.	33,600.	
voluntary Retirement compensation.	50,25,000	
Donation paid.	75,000	51,33,600
less: Incomes not considered in cost Accounts-		
profit on sale of fixed Assets.	2,05,000.	
Insurance claim received during year.	5,08,700.	
profit from Retail trading Activity	32,02,430	
Interest Income from inter corporate deposits	6,15,000.	
Difference in valuation of stock	806070	5337200
		<u>20,10,500</u>

Q5. Auto parts manufacturing company Ltd.

particulars	Amount (₹)	Amount (₹)
profit as per financial Accounts		35,46,700
Add: Expenses not considered in cost Accounts		
CSR committee Expenditure	58,000	
loss in Trading activity	48,500	
4/5th of Renovation expenses	6,20,000	
undervaluation of closing RM.	29,600	75,6100
less: Incomes not considered in cost Accounts.		
profit from sale of old machine	2,76,000	
dividend Income.	84,500	
overvaluation of closing Inventory	65,400	4,25,900
		<u>38,76,900</u>

Stock Adjustments.

overvaluation of opening Inventory	Add.
undervaluation of opening Inventory	Less.
overvaluation of closing Inventory	Less.
undervaluation of closing Inventory	Add.

Q6) M/s Kaling Pong Himalaya Private Limited.
 Reconciliation of financial Accounts and cost Accounts

particulars	Amount (₹)	Amount (₹)
profit as per financial Accounts		1,54,28,642
Adjustments of valuation of stock:		
Add: overvaluation of opening WIP.	2,96,605	
less: undervaluation of opening FG.	(26,71,403)	
less: overvaluation of closing WIP.	(5,39,294)	
Add: undervaluation of closing FG	62,65,719	33,51,600.
Add: Expenses not considered in cost Accounts		
Donations given.	4,85,560.	
loss on sale of fixed assets.	1,22,546.	
voluntary retirement compensation	16,76,540.	22,84,646.
less: Incomes not considered in cost Accounts		
Interest Income from inter corporate deposits.	(6,15,340)	
value of cement taken for own consumption	(17,584)	
cost of power drawn from own W.M.	(13,35,955)	
Non operating Income	(45,36,770)	
Insurance claim	(14,85,620)	(79,41,219)
		<u>1,31,23,669</u>

UNIT - 3 COST Auditor

As per companies (cost Records & Audit Rules) 2014

Cost Auditor \longrightarrow 1. cost Accountant in practice
 {Rule 2(c)} 2. who is appointed by Board.

cost Accountant in practice \longrightarrow 1. cost Accountant
 as defined in \longrightarrow ICWAI Act 1959
 2. holds valid certificate of practice
 3. deemed to be in practice
 4. Individual, {firms and LLP} of CMA's.

As per
 ICWAI Act 1959 & Regulations \longrightarrow Every member \longrightarrow follow certain
 * professional ethics
 * code of conduct.

Professional/misconduct:

- \rightarrow act or omission given in Schedules
- \rightarrow Not to constraint powers or duties of Individuals
- \rightarrow Inquire on conduct of any member.

code of conduct:

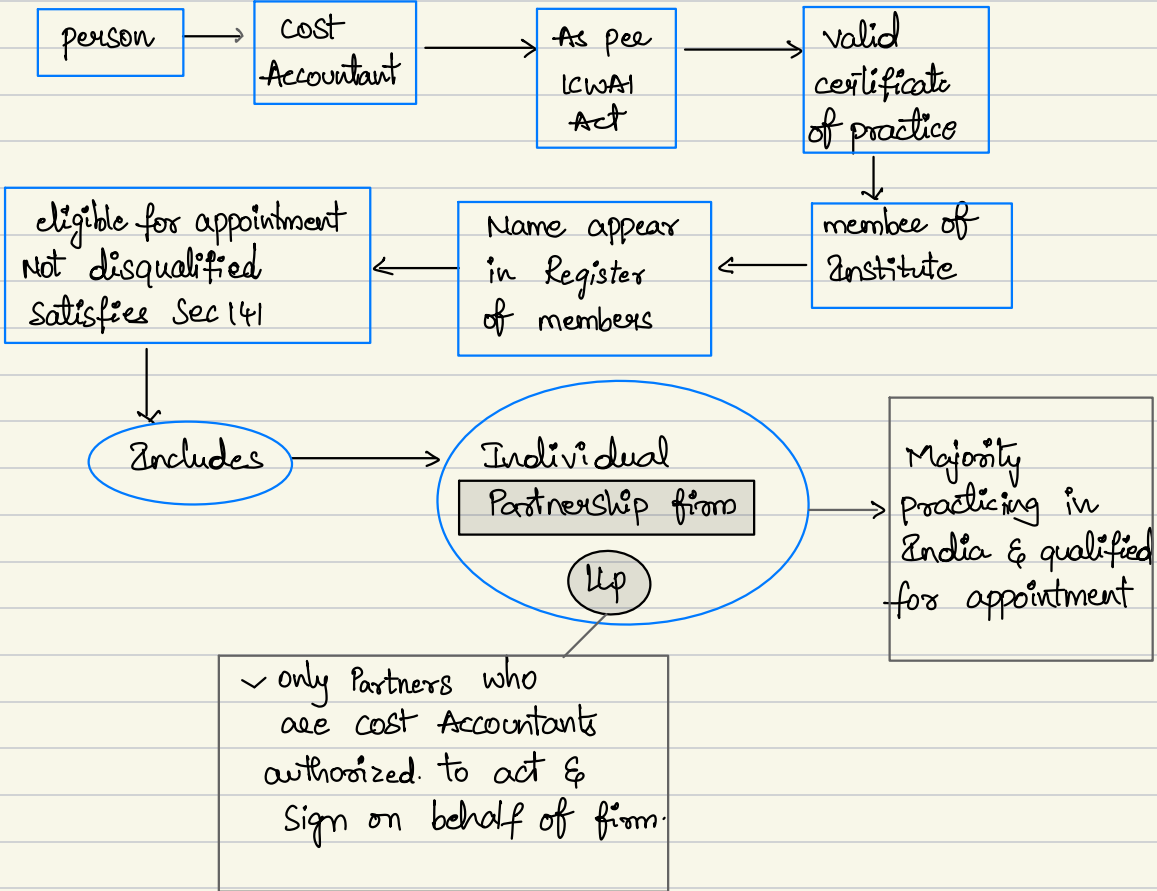
- \rightarrow guidelines & expectations on behavior of individual within org. (or) community.
- \rightarrow ensure compliance of law prevent misconduct.
- eg: workspace behavior interactions with clients, colleagues. & company values.

Qualifications of cost Auditor

Companies Act 2013 Section 141 } Qualifications eligibility & disqualifications of auditors in company's

Read with Section 148 of Companies Act 2013 along with Cost Records & Audit Rules, 2014.

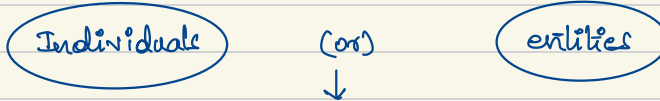
Cost Auditor:



Disqualifications of cost auditor:

Companies Act, 2013 (Section 141)

read with, (Rule 10) of Companies Audit & Auditors Rules 2014
& Section 148 of Companies Act 2013.



Body corporate except → LLP.

person associated with officer or employee

Person/relative/partner holds securities/has interest in C/A/S/H.

companies officer or employee

Relative of any partner of audit firm holds securities in company > ₹ 1 lacs

Person/relative/partner indebted to C/A/S/H > 5 l ₹

Person/relative/partner given guarantee for indebtedness of third party in C/A/S/H/sofH for > 1 l ₹

Person/ firm D/E Business relationship with C/A/S/H/sofH

Relative as Director or Kmp.

Full time employment elsewhere & exceeded Auditor limit

convicted for fraud & 10yrs period not elapsed

Engaged in specialised services

* **C/A/S/H** → company / Associate / subsidiary / holding / subsidiary of holding.

* **Auditors limit** → Companies Act 2013 limits number of companies an auditor can audit to 20.

exceptions → OPC, Small companies, Dormant company, private limited company if paid up share capital is < 100 crores rupees

* **Body corporate** → group of persons incorporated to carry out specific enterprise, includes All entities registered in India or outside India.

* **Business relationship:**

Any transaction entered into for a commercial purpose

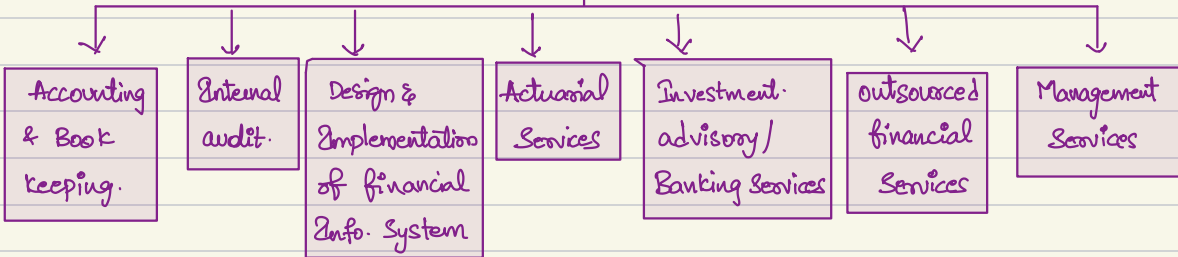
except → ① transactions which are in the nature of professional services permitted to be rendered by an auditor / audit firm

② commercial transactions which are in ordinary course of business of company at arm's length price
eg: sale of products / services to auditor as customer

* Where any person appointed as auditor of company incurs any disqualifications after appointment, he shall vacate his office as such auditor, such vacation shall be deemed to be **casual vacancy**

* Specialized Services.

Person/its
Subsidiary/
Associate/
other entity. → Providing Services. → to Company/
Subsidiary as
date of appointment
disqualified.



1. Accounting Services

- financial statements preparation.
- Tax planning and preparing tax returns
- Auditing (Internal/ External)
- Financial analysis.

Book Keeping Services

- General ledger maintenance
- Payroll Services
- Accounts Payable and Receivable
- Bank Reconciliation
- Recording transactions.

2. Internal Audit : → Improve & focus on Internal Controls of company
→ check company operations are efficient
→ compliance with laws and regulations.

3. Design and implementation of financial information System

- enhance company's ability to manage financial data
- ensure accuracy & streamline operations
- helps in accounting, budgeting, forecasting & reporting.

4. **Actuarial Services :** → Applying mathematical & statistical techniques.
 → uses models to predict future events.
 → helps business in making decisions regarding risk management, pricing & strategic planning.

Areas :- Insurance, pensions, Retirement, Risk management, health & health care, Investment & finance.

5. **Investment Advisory Services**

- providing clients with professional advice on managing their Investment.
- financial planning
- portfolio management, Asset Allocation
- Retirement planning.

Banking Services

- Savings A/c
- loans
- wealth management.

6. **outsourced financial Services :**

- Maintaining financial records.
- Preparing financial statements
- Making journal entries &
- trail balances
- filing tax returns
- Audit Services.

7. **Management Services :**

- | | |
|--------------------------|----------------------|
| → project planning | → Recruitment |
| → Executing project | → Staffing |
| → Resource Allocation | → payroll management |
| → performance monitoring | → Training. |
| → Risk management. | |

* Appointment of cost auditor

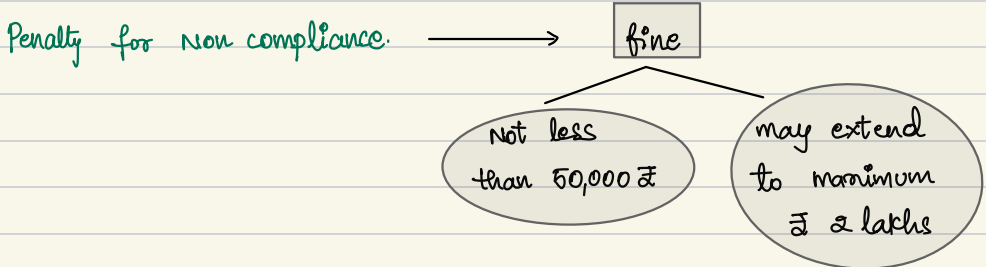
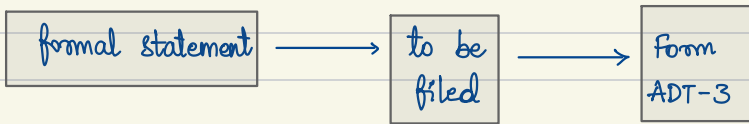
Written Notes ——— Refer Section 148 from
Unit 2 companies cost records & Audit rules 2014

Concept ——— Refer Concept : 4 Appointment of Cost Auditor.
from concept Book.

* Resignation Section 140(a) of companies Act 2013.



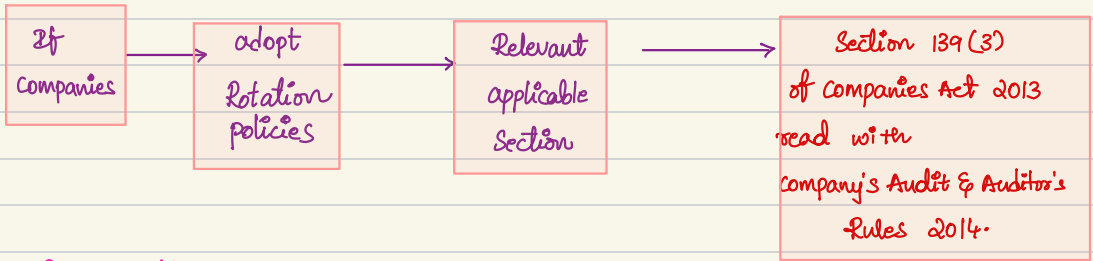
As Per Rule 8 of companies (Audit & Auditors) Rules 2014.



* Rotation :

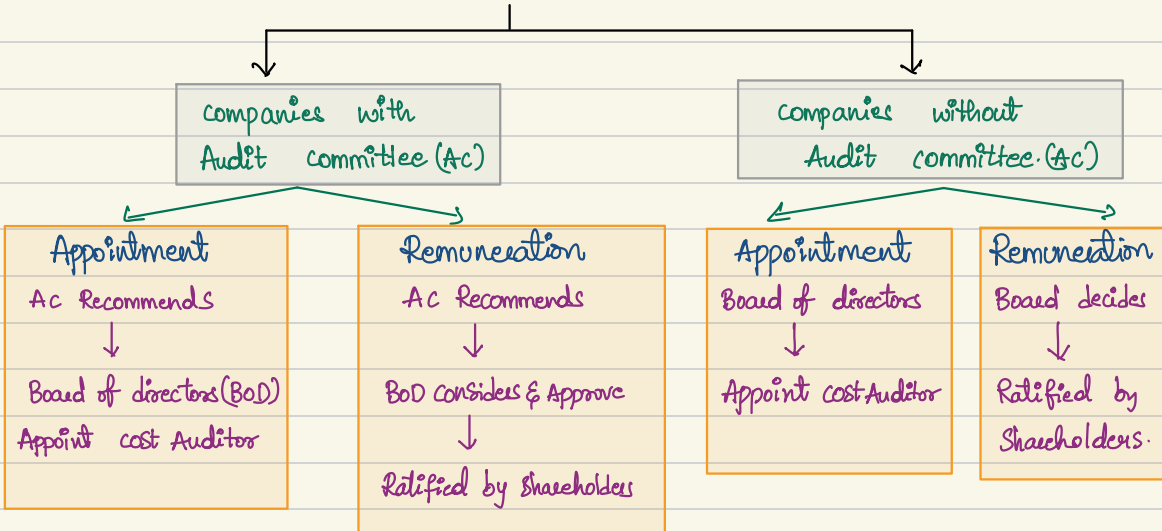
Cost Auditors $\xrightarrow{\text{Same}}$ Rights $\xrightarrow{\text{as}}$ financial
governed by qualifications auditors

There is no legal requirement for their rotation
Companies may choose to adopt their own rotation policies



* Remuneration :

Appointing & determining remuneration of cost Auditor
Section 148 (3) of companies Act 2013 &
Rule 14 of companies (Audit & Auditor's) Rules 2014.



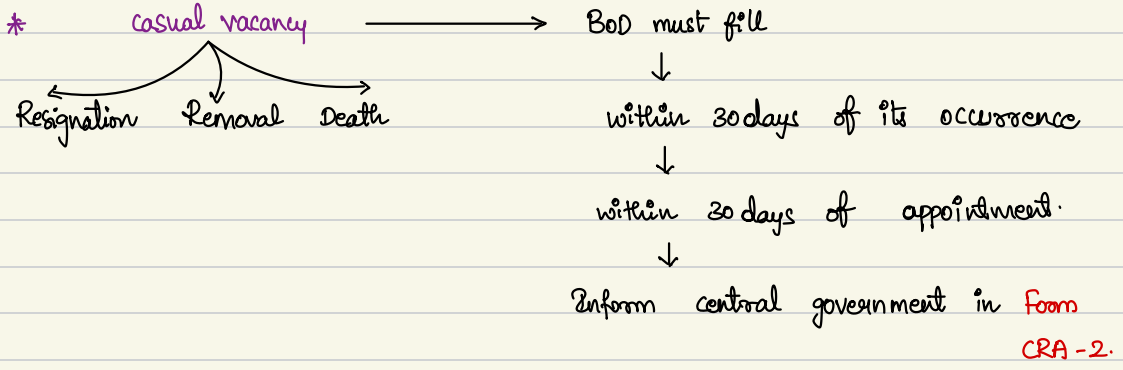
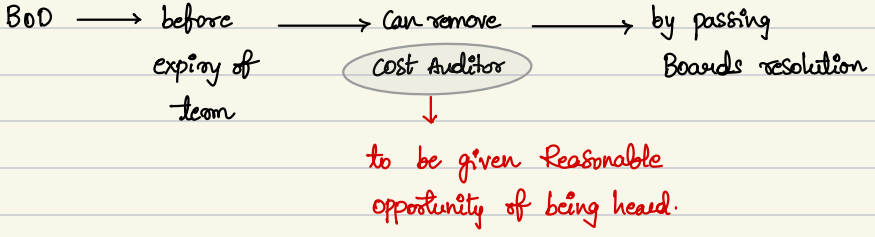
Ratified Means : Confirmation or sanction
 Agreement officially accepted by voting or signing it

Audit committee : Section 177 of Companies Act 2013

- listed companies
- Public companies having
 - Paid up share capital of at least 10 Crores
 - turn over of at least 100 Crores
 - outstanding loans, debentures / deposits at least 50 Crores.

*** Removal :**

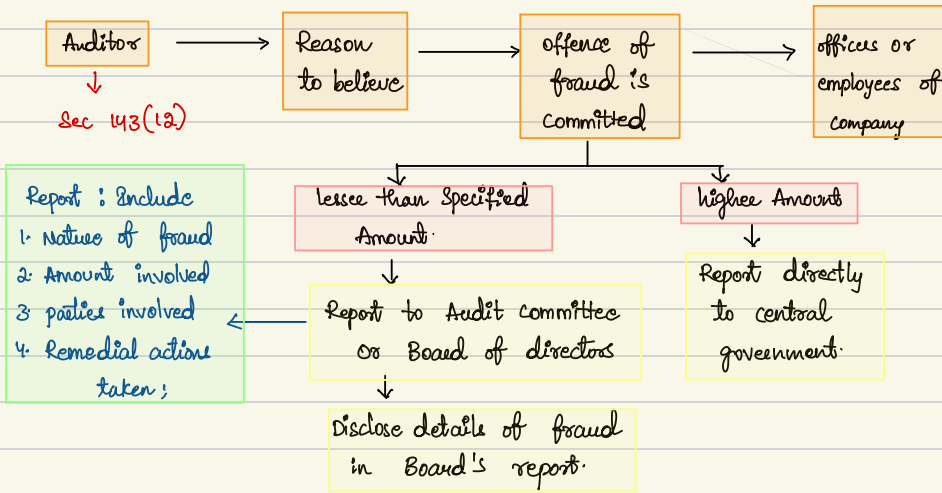
As per Rule 6 of Companies Cost Records & Audit Rules 2014.



Cost Auditor Section 148(5) of Companies Act 2013.

Rights	Duties.
1. Access to Records & information	1. compliance with Standards
2. Assistance from the company	2. Submission of Report
3. Independence	3. contents of Report.
4. Reporting of fraud	4. Reporting fraud
5. protection from liability.	5. Timely Reporting

Section 143 of companies Act 2013:



contents of Report →

- Confirmation : Information is obtained only annexures to cost audit report gives true & fair view
- Verification : cost records are maintained unit wise cost statements are kept.
- Assurance : Received Returns from branches not visited
- opinion : Books & records provide information as per law Adequate internal audit system is maintained

Sec 143(12) → Auditor → Reporting to Central government
 ↓
 In good faith → is protected by law.

⇒ Auditor has to report fraud immediately, but not later than 2 days after he/she becomes aware of that fraud.

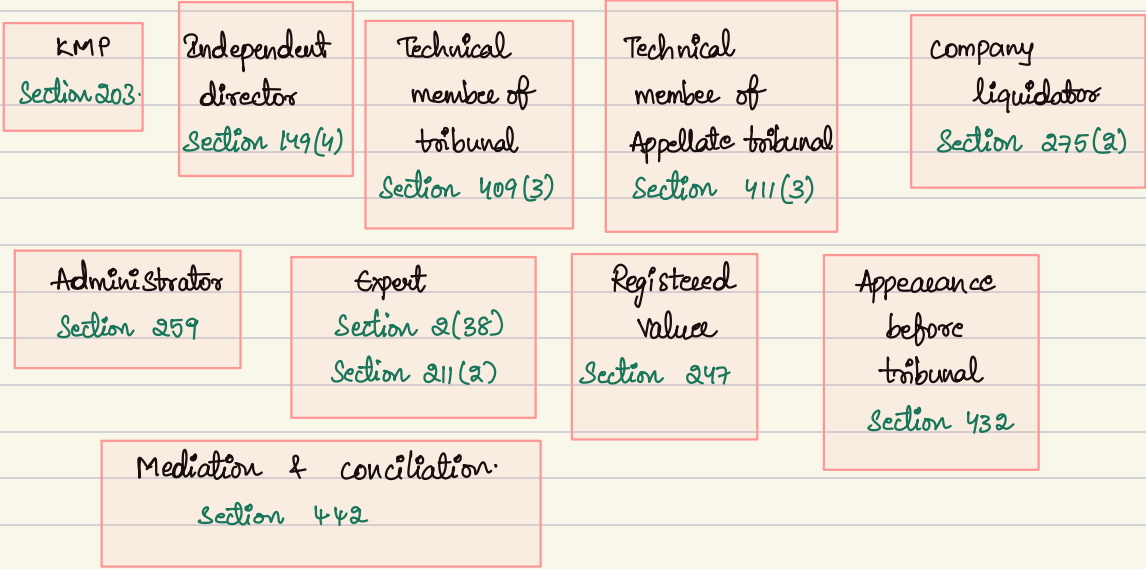
If cost Auditor, cost Accountant, company Secretary in practice

contravene

- listed companies → penalty 5 lakh ₹
- other companies → Penalty 1 lakh ₹

Maximum fine can be ₹ 25 lakhs.

⇒ strategic positions for cost Accountants.



9. Mediation

helps disputing parties
 Mediator → communicate and negotiate to reach voluntary agreement.

↓

Does not offer solutions but facilitates discussions.

conciliation

↓

conciliator → takes more active role by offering solutions or recommendations to resolve dispute

final decision → parties.

1. Key managerial personnel → Managing director (or) CEO (or) manager (or) WTD
 Company Secretary
 CFO.

2. Independent directors :

Public Companies

Listed

At least $\frac{1}{3}$ rd of total

No. of directors

Unlisted

paid up SC — 100crs / more

Turn over — 100cr / more

outstanding loans, deposits

50 cr / more

→ At least 2 directors
 upon total shall be
 Independent.

3. Technical member →

Tribunal

cost Accountant in practice

at least 15 years of service

Appellate tribunal.

cost Accountant in employment

or practice

experience at least 25 years

4. company liquidator:

CA, advocates, CMA, CS

having at least 10 years experience

in panel maintained by CG

5. Administrator

Appointed by tribunal

from data bank maintained

by CG / any institute / agency

authorised by CG

6. Expert

CG → establishes

SFO

headed by director

& Experts in

Banking, finance etc.

7. Registered valuers.

Appointed by Audit committee

or Board of directors

to value property, shares,

stocks.

8. Appearance before tribunal

NCLT (or) NCLAT

in matters of merger, amalgamations

winding up, Revival of sick companies

liabilities of cost auditors

Statutory liabilities

contractual liabilities

under companies Act 2013

under other Acts

civil liabilities

criminal liabilities

- Income tax Act 1961
- Cost Accountants Act 1959
- Life Insurance Act 1956
- Banking Regulation Act 1949.

1. Misstatements in prospectus
2. Liability for Misfeasance

Misstatement in prospectus.
Punishment Under Section 447

Punishment for Non compliance by Auditors.
Sec 139 Appointment
Sec 144 prohibited services
Sec 145 Duty to sign Reports

Punishment for Refusal or failure to produce Documents
→ 6 months imprisonment
→ fine : 25,000 to 1,00,000 ₹
further ₹ 2000/day for continuation

Fraud in relation to company in winding up
Imprisonment - Min 3 years
Max 5 years
fine : Min ₹ 1,00,000
Max ₹ 3,00,000

Fraud for false statement
Punishment U/s 447.

Punishment for false evidence
Imprisonment:
Min 3 years, Max 7 years
fine : upto ₹ 10,00,000

General

Min: 25000

Max: 5 lakhs/
4 times of remuneration

willful fraud

Jail 1 year

fine :
Min: 50000
Max: 25 lakhs/
8 times of Remuneration

Refund of Remuneration +

pay for damages if any.

Audit firm

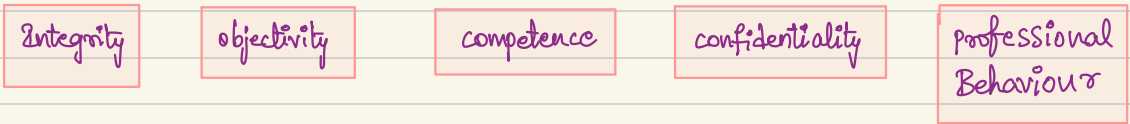
- fines both firm & partners are liable.
- imprisonment - only partners.

* Professional ethics :

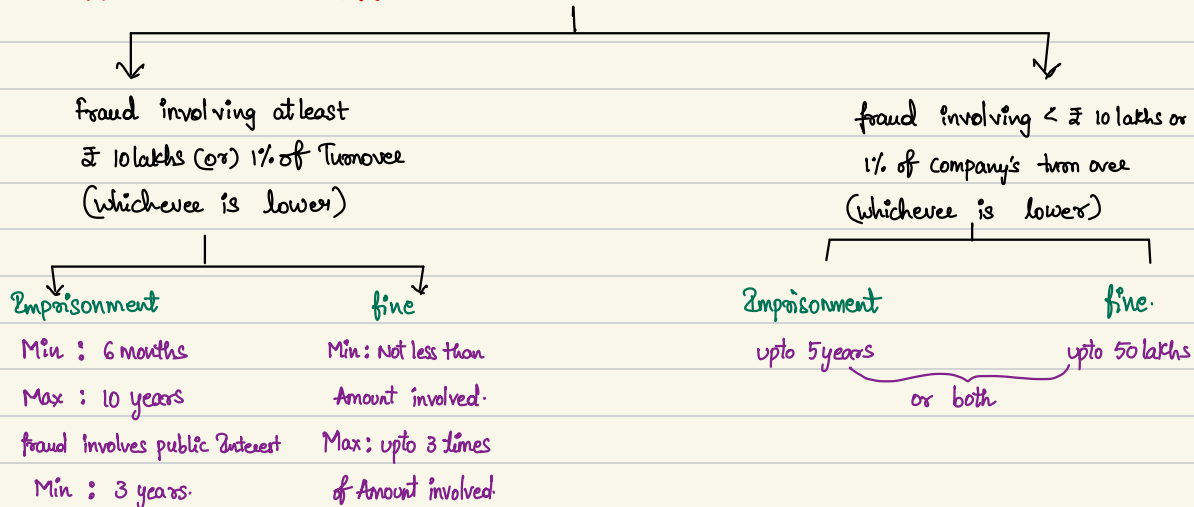
objectives of accountancy profession :



fundamental principles



* Section 447 of Companies Act 2013 : Punishment for fraud.



Professional and other misconduct.

Cost and Works Accountants Act 1959.

- Act → for regulation of profession of cost & management Accountants
- Council → for Management of affairs & to discharge functions assigned to it by Act.
- Institute → Council finds prima facie case of professional / other misconduct.
- Institute enquiry → Investigate matter & take disciplinary actions.

Schedules to Act.

↓
First Schedule
↓

- Part 1 : Relation to cost Accountants in practice
- Part 2 : Relation to Members of institute in service
- Part 3 : Relation to Members of institute generally
- Part 4 : Other misconduct Members of institute generally

↓
Second Schedule.
↓

- Part 1: Relation to cost Accountants in practice
- Part 2: Relation to members of institute generally
- Part 3: other misconduct in relation to members of institute generally.

* Penalties under the Act

Section 24	Section 25	Section 26	Section 27	Section 28	Section 29
falsely claiming to be member	using name of Council & awarding degrees	Companies not to engage in Cost Accountancy.	unqualified person not to sign documents	offences by Companies.	Sanction to Prosecute.
↓	↓	↓	↓	↓	
fine - upto ₹ 1000 Subsequently Imprisonment - 6 months fine upto ₹ 5000/ Both.	fine - upto ₹ 1000 Subsequently Imprisonment - 6 months fine upto ₹ 5000/ Both.	fine upto ₹ 1000 Subsequently fined upto ₹ 5000	fine - 5000 to ₹ 1,00,000 Subsequently - Imprisonment - 1 year fine - 10000 to ₹ 2,00,000 or Both.		

UNIT-4: Overview of Cost Accounting Standards & GACAP.

1. Difference between Standard & Principles.

- Standards are specific, detailed & often mandatory rules or guidelines that must be followed, They are instructions on how to handle specific tasks / situations.
- They are like recipe with precise measurements & instructions that must be followed to achieve consistent result.

example: CAS dictate specific methods to classify & allocate costs. { CAS 1-24 }

- Principles are fundamental concepts / guidelines that provides general framework for decision making.
- They are based on accepted norms or common practices. they does not enforce any strict rules.
- Principles are like guidelines for cooking - i.e; we have basic idea of dish but you can adjust ingredients & techniques based on Preferences.
- GACAP are general concepts like cost behavior, classification but doesnot give exact method.

2. What is cost Accounting standards :

- guidelines for companies to manage their cost accounting practices.
- Rules to govern how costs should be measured, reported & analyzed.

The Institute of Cost Accountants of India (ICAI)

to have systematic approach in both manufacturing & service sectors.



established the cost Accounting standards Board (CASB)

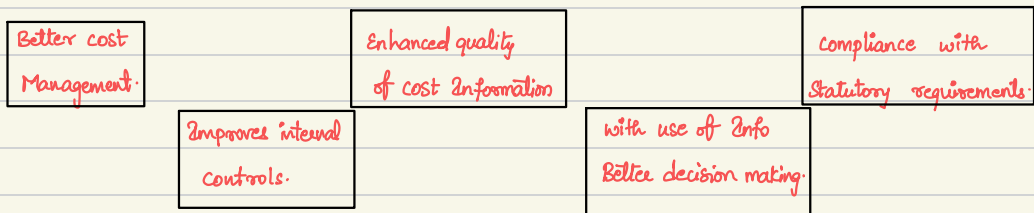
→ It is responsible for issuing, formulating & regulating standards related to cost Accounting.



Issued CAS cost Accounting standards (CAS) { 1-24 }.

* CAS should be followed to ensure — consistency } in financial data of
 comparability } organisations, concerning
 & transparency } cost information.

3. * Advantages :



4. Do all companies have to follow cost accounting standards? :

NO

Companies Subject to → Applicability of cost Records: Rule - 3
 Applicability of cost Audit: Rule - 4.

companies (cost Records & Audit Rules) 2014.

Example :

Manufacturing industries

→ cement, steel,

fertilizers & pharmaceuticals.

Service Sector.

telecommunications, electricity &

healthcare.

5. objectives of CAS.



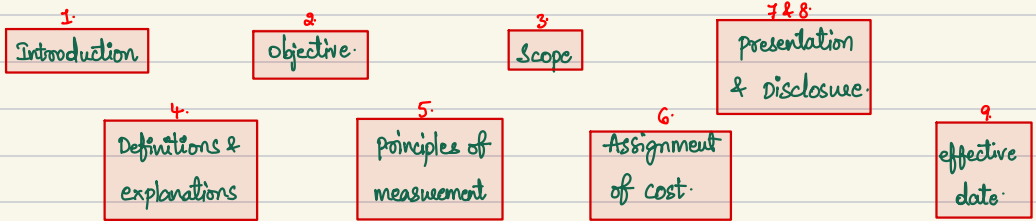
Uniformity in Cost Accounting practices

Transparency & Disclosure

Guidance for cost measurement.

Adopting to legal & Industry changes.

Structure of cost Accounting standards.



CAS - 1 : Classification of Costs.

Introduction
 Guidelines for Cost classification w.r.t cost of Products/Services.

Objective

- Uniformity
- Consistency
- Clarity & accuracy in Cost Statement.
- Disclosure & presentation of Cost.

Scope
 classification, presentation & disclosure of Costs.

Definitions
 33

① Cost :

Monetary value $\xrightarrow{\text{of}}$ Resources $\xrightarrow{\text{in}}$ production of goods/ services.
 (in terms of money)

Price	cost
Amount of money charged to Products/ services.	Amount incurred by business in production of goods/ services either in Making/ purchase of materials.

Cost

Normal cost

usual cost incurred during cost of business

2. abnormal cost:

unusual or unexpected cost/ expense. irregular & often due to abnormal conditions in production / operations.
 eg: accident, natural disasters, & unusual events.

3. Conversion cost :

Raw materials $\xrightarrow{\text{transform into}}$ finished goods.

Cost incurred during this period is conversion cost.

Includes

labour & other production costs.

excludes

cost of Raw materials bought in.

4. classification of cost :

organizing costs into logical categories.

cost

By nature (subjective)

Based on type of cost:

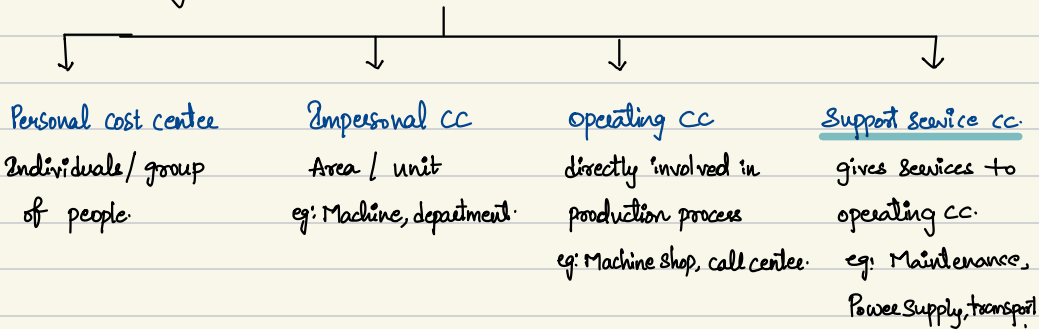
eg: Material, labour.

By purpose (objective)

Based on why cost is incurred.

eg: production, administration.

5. Cost center: Any part of company where costs are incurred. but doesn't directly contribute to revenue. (eg: division, department, employees)



6. Cost object: Anything for which costs are measured.
 eg: Activities, contracts, Cost centers, products, services, customers

7. Cost unit.

Measure of volume of production/ Services.

eg: power → Megawatt (Mw) cement → metric ton (MT) Automobiles → Number (units) Transportation → Tonne - Km.

Example: Adithiya. Motors. → Car Manufacturing company.

<u>cost unit</u>	<u>cost center</u>	<u>cost driver</u>	<u>cost object</u>
single car.	Paint department.	factor which cause change in entire cost of activity.	Any model of car
	incurs expense of labour, material & equipment but doesn't directly relate to product (car)	eg: Number of cars painted.	eg: SUV Model.
		↑ Painted cars	electric vehicle
			luxury cars.
			↑ cost of paint / labour.

8. overheads Indirect costs that could be.

9. Indirect material → costs cannot be directly linked to cost object
oils, cleaning supplies, screws, bolts, packaging materials

10. Indirect Employee cost →

examples → cost incurred to pay employees who directly do not work on product.

Salaries to Supervisors, managers, maintenance staff, quality control inspector,
human resource staff cost.

11. Indirect Expenses :

Rent, utilities, depreciation, office supplies, Marketing & advertising.

12. production OH : Indirect costs associated with producing goods / services.

(or)
Manufacturing

Includes → factory overheads

→ works overheads.

→ Manufacturing overheads

→ Administrative costs related to production.

eg: factory rent, Depreciation of machinery, factory utilities, Maintenance Repairs, salaries of supervisors.

13. Selling overheads :

expenses $\xrightarrow{\text{or}}$ Selling products / Services $\xrightarrow{\text{}}$ Includes all indirect costs incurred in Selling process.

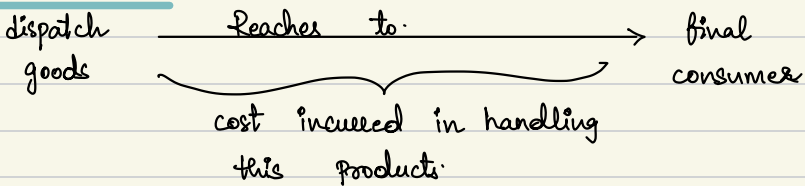
eg: sales commission, Advertising & promoting cost
salaries of sales staff, Travel expense for sales.

14. Marketing overheads :

Selling overheads + Distribution overheads.

eg: Branding expense, promotional events, website maintenance, social media advertising costs, content creation, Digital marketing etc..

15. Distribution overheads:

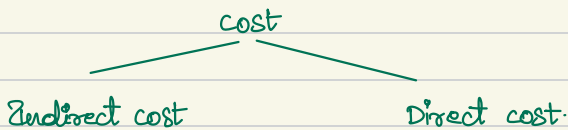


Includes \rightarrow Inter unit transfers.

eg: secondary packaging, outward transportation cost, warehouse cost clearing & forwarding cost.

16. Administrative OH: expenses incurred to manage & support general operations of business, not directly related to production / sales.

eg: Salaries, office rent, utilities, Administrative Supplies.



17. Direct materials:

costs of materials that can be directly linked to product.

eg: car manufacturing \rightarrow steel. furniture \rightarrow wood.
 clothing production \rightarrow fabric. Bread Baking \rightarrow flour

18. Direct employee cost: employee cost that can directly be attributable to cost object.

employee \rightarrow operates machinery / assemble products in cars \rightarrow Salaries / wages paid to him \rightarrow Direct employee cost.

19. Direct Expense : costs other than direct material / employee cost.

eg: Royalties, Job charges, hire charges for equipment used for particular job, Software services needed for specific task.

20. employee cost : All benefits paid/ payable to employees.

includes → temporary, part time, contract employees.

→ can be paid in cash / kind.

(i) contract employees.

hired directly/ through contractors but exclude employees of contractors in jobs.

(ii) compensations paid

due to past disputes/ court orders will be employee cost but not production cost.

(iii) prior period costs.

recognized in current period will form part of current employee cost but not production cost.

21. fixed cost.

→ costs do not change with level of activity or production volume.

→ If fixed costs → Indirect
↓
fixed overheads.

22. variable cost.

→ changes directly with level of activity

→ variable → Indirect costs
↓
variable overheads.

23. Standard cost : Predetermined cost based on technical specifications & efficient operating conditions.

Reference → compares actual costs to identify variances & control costs.

24. Semi variable cost :

fixed elements + variable elements.

eg: electricity bill → Monthly fixed charge + variable based on usage.
Telephone Expenses, Maintenance cost.

25. Research cost:

Cost of planned investigation aimed at gaining new scientific or technical knowledge.

26. Prime cost

Direct material cost + Direct employee cost + Direct expenses.

27. Packing material cost:

Cost of material used for packaging product.

Primary packaging material
essential for holding & preserving
the product for customer use.

Secondary packaging material
used for storage, transport &
Marketing of product.

28. Material cost : Cost of material used for
production of goods or services.

29. Normal capacity : Average level of production achievable under normal
conditions

30. Development cost :

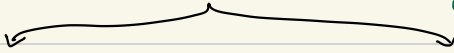
Apply research results / new knowledge $\xrightarrow{\text{to create}}$ new/improved materials, products, process / services
Cost incurred.

31. Cost of production : Material cost, Direct employee cost, Direct expenses,
production OH, Quality control cost, packaging, R&D.

32. Cost of transportation:

Includes costs like freight, cartage, transit insurance, fleet other incidental transportation charges.

excludes - Detention / demurrage charges.



Inward transportation cost:

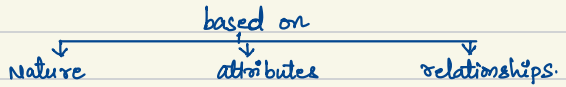
cost of bringing materials in

outward transportation cost:

cost of transferring finished goods out.

5. Principles of classification of costs.

①. Cost should be organized $\xrightarrow{\text{by}}$ grouping similar cost components.

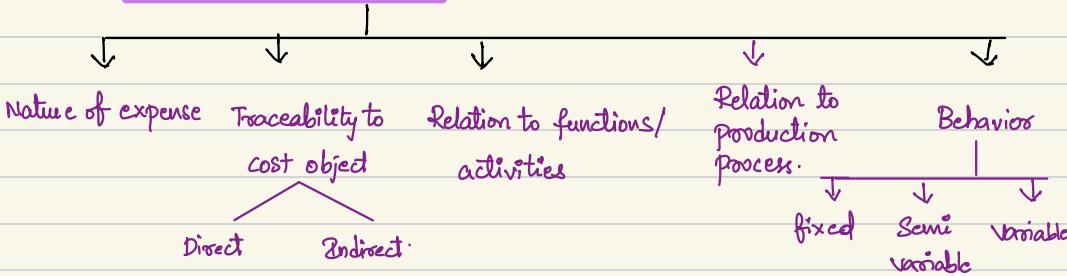


②. further classified according to their fundamental differences.

③. costs \rightarrow should be $\xrightarrow{\text{identified}}$ & placed $\xrightarrow{\text{with}}$ similar items based on shared features.

④. There could be Multiple classification & purpose driven classification.
 some costs can fit into different classifications.
 costs to be aligned with how costs reports will be used.

⑤. Factors of classifications:

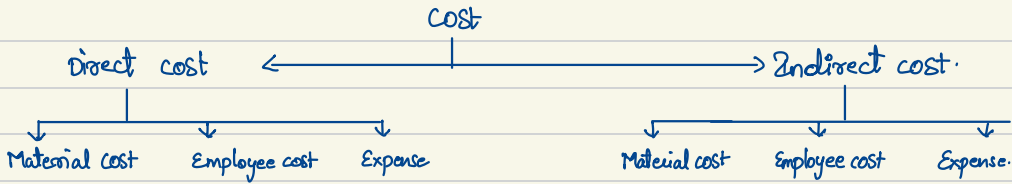


6. classification of cost

a) By Nature of expense.

<u>Material cost</u>	<u>Employee costs</u>	<u>Expenses.</u>
cost of materials	All forms of compensation	utilities
- trade discounts	wages, salaries	purchased services
rebates	& benefits.	
refundable taxes/duties.		

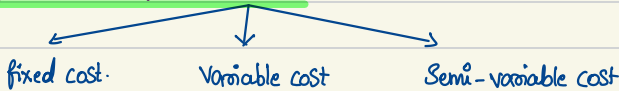
b) By Nature of Traceability to cost object



c) By function:

production/
project: Administration selling Distribution Research Development.

d) By nature of Behavior:

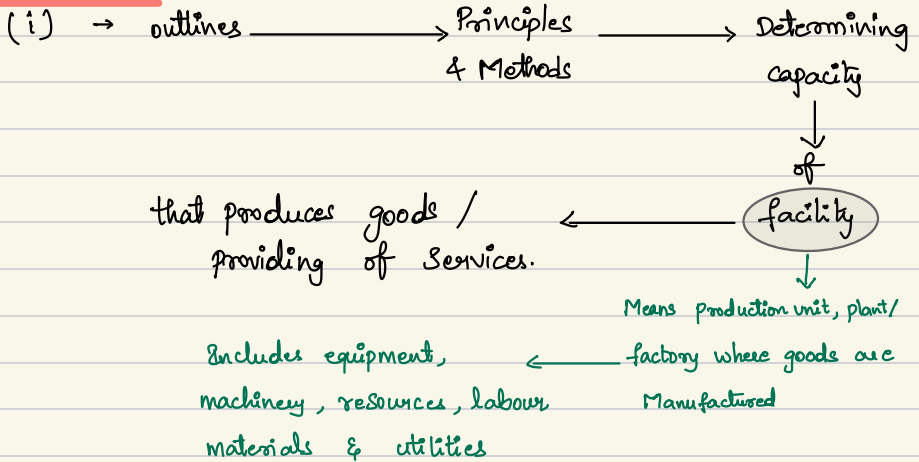


e) By nature of production / operation Process.

Batch cost Process cost operation cost contract cost Joint costs.

CAS - 2 Capacity determination

1. Introduction :



(ii) determines the capacity of entity ~~so to~~ → determine the cost of product / service.

(iii) guides ; presentation & Disclosure of Information in → cost statements.

2. objective :

- uniformity
- consistency
- Determine capacity across entities
- ensuring accuracy in process.

3. Scope :

Applies to cost statements.

↓

where Capacity determination is necessary to assign overheads.

4. Definitions :

(i) capacity -

Maximum level of output or production → facility, machinery system → can achieve over specific period under normal conditions.

(ii) Normal capacity :

Capacity → achieved/achievable → on an average → over several periods under normal circumstances

(iii) Actual capacity utilization :

volume of production or services → Provided during specific period.
 expressed as % of Installed capacity.
 can be measured in
 units produced Services provided Equivalent machine or man hours.

(iv) Installed capacity :

Maximum output a facility can produce → by operating continuously under ideal conditions } Fuller utilization of available machinery & resources without any interruptions.

(v) Achievable/practical capacity:

Maximum productive capacity $(-)$ inevitable internal interruptions
 → preventive maintenance, Repairs, Setups, Normal delays, weekly off days, holidays.
 Does not include external factors (lack of orders)

(vi) Idle capacity:

Installed capacity - Actual capacity
 (only when Actual < Installed capacity)

(vii) Excess capacity:

Installed capacity - Actual capacity.
 (when Actual > Installed capacity)

(viii) Bottleneck:

A point → Restricts flow of production process

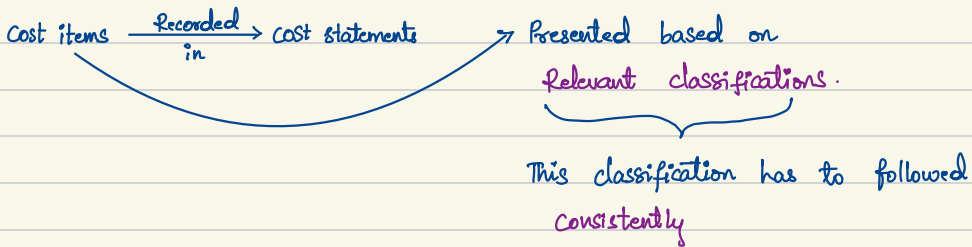
* Reducing the capacity of overall system.

eg: Machine with lower processing speed can cause backlog & slows the entire process.

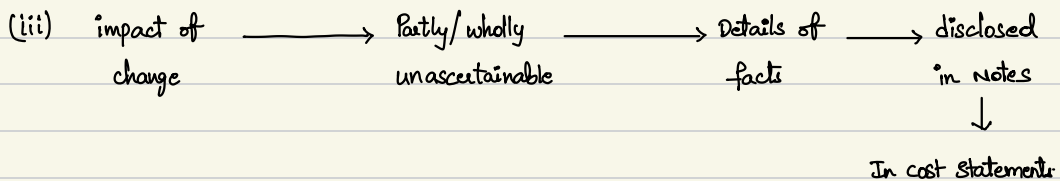
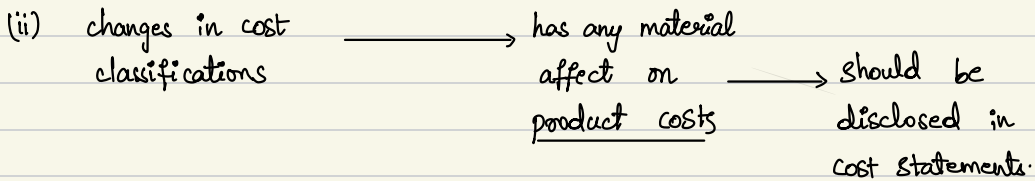
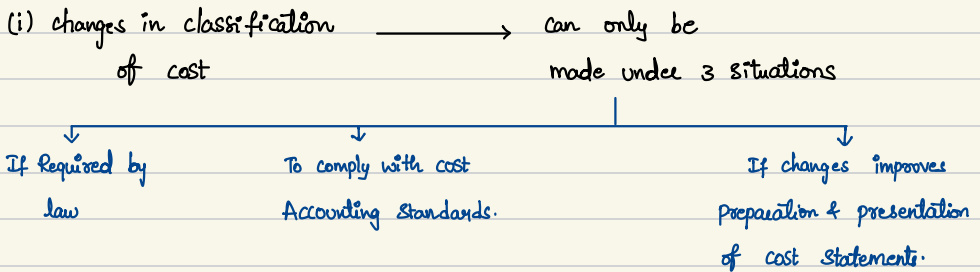
(ix) licensed capacity:

Appropriate authority → Issues license for → Allowed capacity / Allocated capacity.
 license capacity.

7. Presentation :

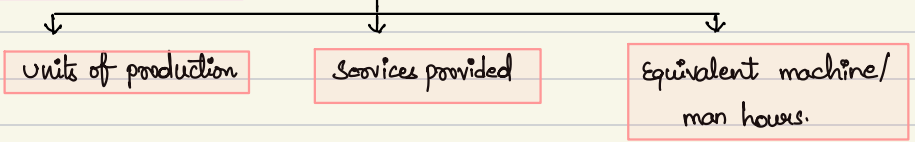


8. Disclosures :

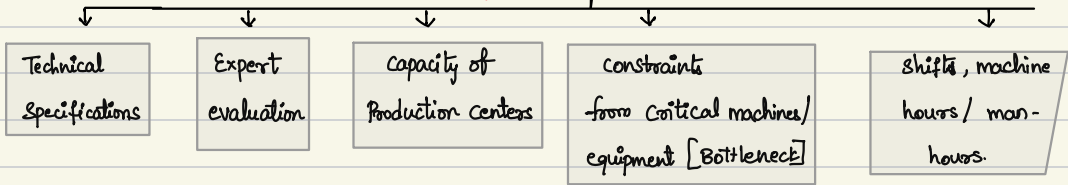


5. Determination of capacity:

(i) Measurement of capacity: → based on



(ii) determine. Installed capacity: → Based on



Key points

* If technical specifications are unavailable consider estimates from technical experts.

* If Authority assessed capacity then follow those guidelines [Licensed capacity]

* When determining Installed capacity consider bottle neck.

(iii) calculate. practical capacity:

Installed capacity adjusted for → Maintenance time
downtime, holidays,
setups, efficient losses.

(iv) If there are changes due to:

Addition, deletion, modification of facilities → Reassess Installed Capacity.

(v) calculation of Normal capacity

: Based on Average capacity over 3-5 normal years excluding Interruptions / abnormal periods

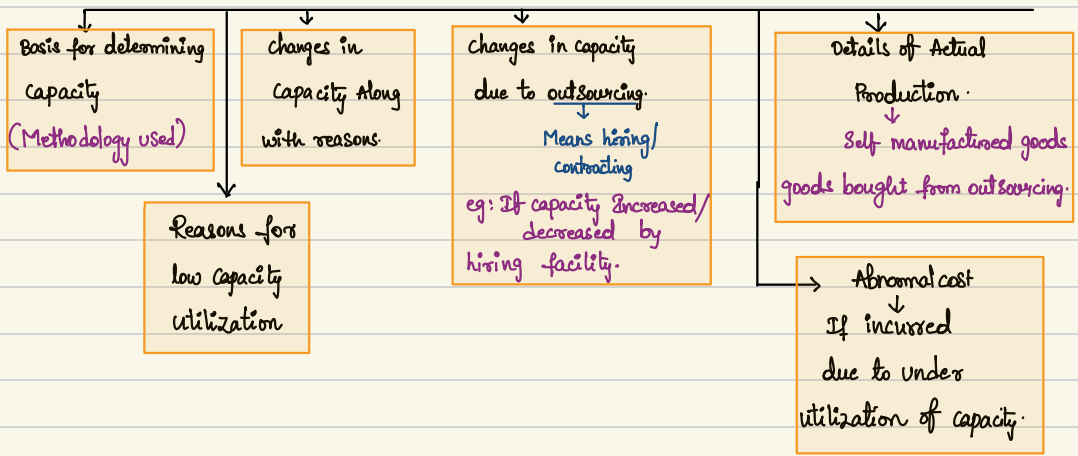
6. presentation :

* Installed capacity
normal capacity &
Actual production: $\left\{ \begin{array}{l} \text{should be} \\ \text{presented} \\ \text{in} \end{array} \right. \rightarrow \text{Absolute terms.}$

Means giving fixed/ standalone number without any reference/comparison.

* Actual capacity utilization: expressed as % of installed capacity:

7. Disclosures :



8. effective date : 1st April 2024.

CAS - 2 Problems

① (i) Installed capacity :

$$1200 \text{ units per hour} \times 3 \text{ shifts} \times 8 \text{ hours} \times 365 \text{ days} \\ = 10512000 \text{ units.}$$

(ii) Practical capacity :

$$1200 \text{ unit per hour} \times (365 - 52 - 8) \times 3 \text{ shifts} \times \\ (8 \text{ hrs} - 1 \text{ hr}) \\ = 1200 \times 305 \times 3 \times 7 \\ = 76,86,000 \text{ units.}$$

(iii) Actual capacity = $\frac{\text{current production}}{\text{Installed capacity}}$

$$= \frac{69,90,000}{10512000} = 66.50\%$$

(iii) Ideal capacity

= Installed capacity - Actual capacity.

$$10512000 - 69,90,000 \\ 3522,000 \text{ units.}$$

Ideal capacity as % of Installed capacity is

$$\frac{35,22,000}{1,05,12,000} = 33.50\%$$

(iv) Normal capacity =

$$\frac{69.4 + 72.6 + 71.4 + 70.5 + 70.8}{5}$$

5.

70.94 lakh units.

(v) Abnormal Ideal capacity = practical capacity - Actual capacity.

$$(76.86 - 69.9) \text{ lakh units.}$$

6.96 lakh units.

② (i) Installed capacity =

$$1500 \text{ units} \times 3 \times 8 \times 365 \\ 13140,000 \text{ units.}$$

(ii) practical capacity =

$$\text{Installed capacity} - \text{Interruptions.} \\ 1500 \text{ units} \times \{3 \times (8-1)\} \times (365-52-12) \\ 9481500 \text{ units.}$$

(iii) Actual capacity = 81.50 lakh units.

Actual capacity as % of installed capacity.

$$\frac{81.50}{131.40} = 62.024\%$$

(iv) Normal capacity = Average data of production in past 5 years.

$$\frac{75.70 + 87.42 + 65.38 + 77.97 + 76.08}{5}$$

$$\frac{382.55}{5} = 76.51 \text{ lakh units.}$$

(v) Ideal capacity = Installed capacity - Actual

$$131.40 - 81.50$$

49.9 lakh units.

(vi) Abnormal capacity = Practical - Actual capacity.

$$94.815 - 81.50$$

13.315 lakh units.

$$3. (i) \text{ Installed capacity} = 2500 \text{ units} \times 8 \text{ hrs} \times 3 \times 365 \\ 219 \text{ lakh units.}$$

$$(ii) \text{ practical capacity} = \\ 2500 \text{ units} \times (8 \text{ hrs} - 0.5 \text{ hr}) \times 3 \times \\ (365 - 52 - 10) \\ = 17043750 \text{ Units.}$$

$$(iii) \text{ Actual capacity} = \frac{\text{Actual production}}{\text{Installed capacity}} = \frac{158.80}{219} \\ = 72.51\%$$

$$(iv) \text{ Normal capacity} = \frac{\text{Average of Sales expectancy in past 3 yrs}}{3} \\ \frac{154.50 + 159.54 + 166.66}{3} \\ 160.23 \text{ lakh units.}$$

$$(v) \text{ Ideal capacity} = \text{Installed capacity} - \text{Actual capacity.} \\ (219 \text{ lakh} - 158.80 \text{ lakh}) \text{ unit} \\ 60.2 \text{ lakh units.}$$

$$\text{as \% of Installed capacity} \\ \frac{60.2 \text{ lakh units}}{219 \text{ lakh units}} \times 100 \\ 27.48\%$$

$$(vi) \text{ Abnormal capacity} = \text{practical capacity} - \text{Actual capacity} \\ = 17043750 \text{ units} - 15880,000 \\ 1163750 \text{ units} \\ (08) \quad 11.6375 \text{ lakh units.}$$

4.

Particulars	2020-21	2021-22	2022-23
Installed capacity - Ton	250	250	250
Production - Ton	240	230	125
Actual capacity utilisation			
$\frac{\text{Actual production}}{\text{Installed capacity}} \times 100$	96%	92%	50%
cost per ton (₹)	1000	1077	1660.
Base year cost price.	100	105.	107.
cost.	1000	1077 → 105	1660 → 107
		9 100	100
		$1077 \times \frac{100}{105}$	$1660 \times \frac{100}{107}$
		1026.	1551.
cost of production (cost × production Ton)	2,40,000.	2,35,980	1,93,875.
variable cost.	402	402	401.
Fixed cost (Total cost - vc)	1000-402	1026-402	1551-401
	598.	624.	1150.

100% fixed cost utilization is 574.08.

$$(1150 - 574.08)$$

575.92. ₹ 576./ton.

Abnormal cost = 576 × 125.

72000.

working notes

①. variable cost calculation.

	2021-22	2022-23
cost of production diff.	(2,40,000 - 2,35,980) 4020	42105. (235,980 - 1,93,875)
Production in tons diff.	10.	105.
variable cost = $\frac{\text{Diff in COP}}{\text{Diff in production units}}$	$\frac{4020}{10}$ 402.	$\frac{42105}{105}$ 401.

②. 2020-21 fixed cost. 598.
 production per ton 240.
 capacity 96%.

fixed cost 100% utilisation \rightarrow

$$598 \times 240 = 1,43,520 \rightarrow 96\%$$

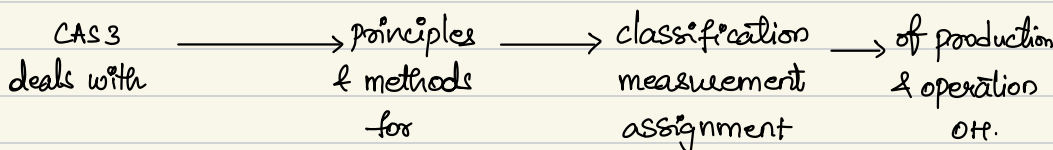
$$\frac{1,43,520}{250} = 574.08.$$

CAS-3 Production and operation overheads. Revised 2015

old CAS 3 (Revised 2011)
CAS on overheads.

new CAS 3 (Revised 2015)
CAS on production & operation overheads.

1. Introduction :



- * To Determine cost of goods produced/ services provided
- * presentation & Disclosure in cost statements.

2. objective

- * uniformity
- * consistency → in
- * principles & method for determining Production & operation OH.
- * To have reasonable accuracy in cost determination.

3. Scope.

Applies to cost statements
↓
classification measurement assignment presentation disclosure } of production & operation OH.

3. Definitions :

- * **Ab normal cost** → unusual / unexpected cost
- * **Administrative OH** → Indirect cost → general management
excludes : production OH, marketing OH & finance

* cost center , cost object , fixed cost , Normal capacity,

Indirect → employee cost , material cost , Expenses, Standard & variable cost.

* **production or operation overhead:**

- Indirect cost related to production of product / providing of service
- Terms production OH, operations OH, factory OH, works OH, manufacturing OH are same
- Includes → Administrative OH relating to production

↓
variable OH

↓
semi-variable OH

↓
Fixed OH

* **Imputed cost:**

Notional cost / estimated cost: not actually incurred

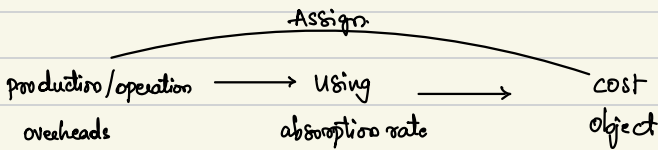
→ But used in decision making / performance evaluation

example → Interest on owners capital
Salary to owner.

* Cost → That are not recorded in books.

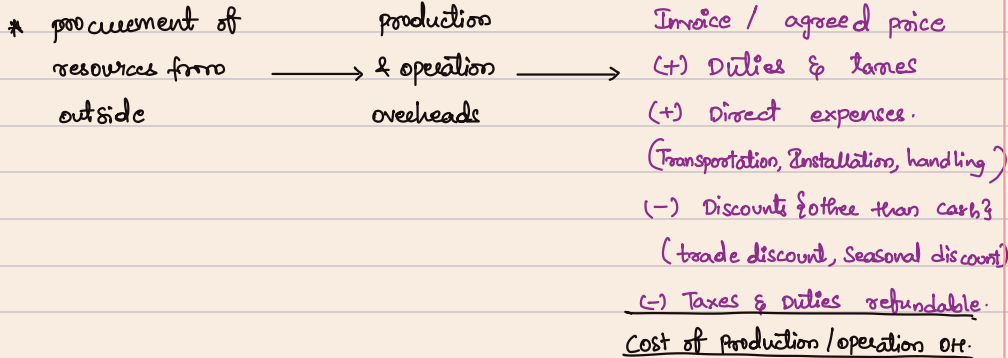
* Used for comparing different decisions / In evaluating profitability accurately.

* **Absorption of Production / operation OH.**



$$\text{Absorption rate} = \frac{\text{Production / operation OH of the Activity}}{\text{Volume of activity}}$$

5. Principle of measurement



* OH → not related to procurement
 Inhouse utilization of resources. → cost incurred in connection

* cost of production & operation overheads

Includes

→ overhead variances due to normal reasons

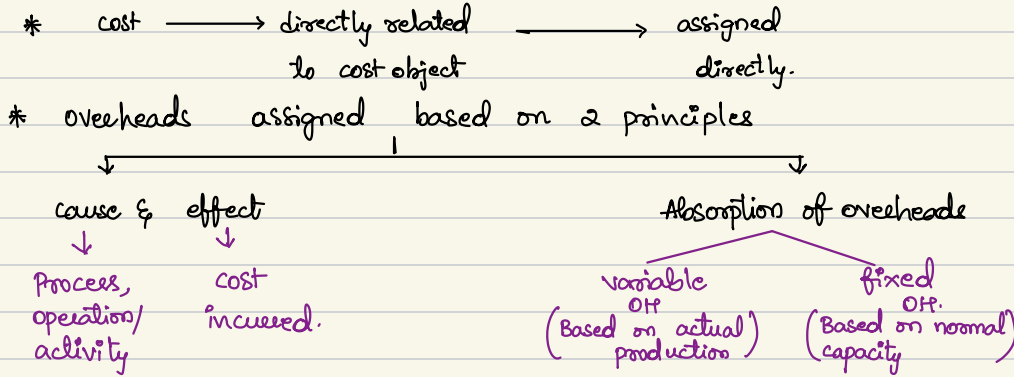
excludes

- Abnormal cost (if material & quantifiable)
- Imputed costs
- variances due to abnormal reasons.
- Subsidy, grant, incentive / any other amount
- fines, penalties, damages & levies paid to authorities / third parties
- Any credits / recoveries that are material & quantifiable
 if recoveries > Total overheads treated as other income.

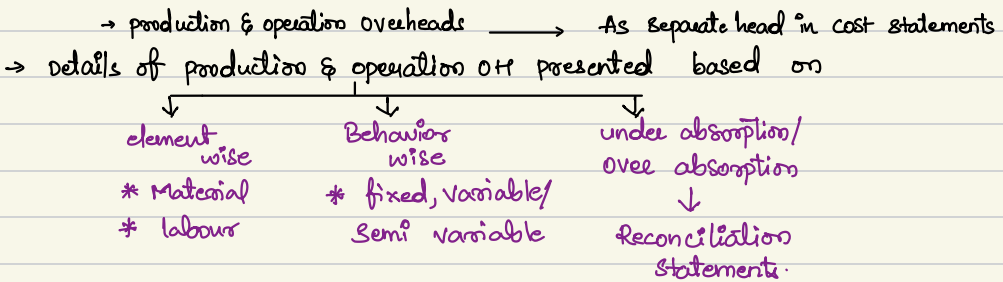
* Any changes in cost accounting principles for measuring production / operation overheads.

- If it is required by law
- to comply with cost accounting standards.
- If changes result in better preparation / presentation of cost statements.

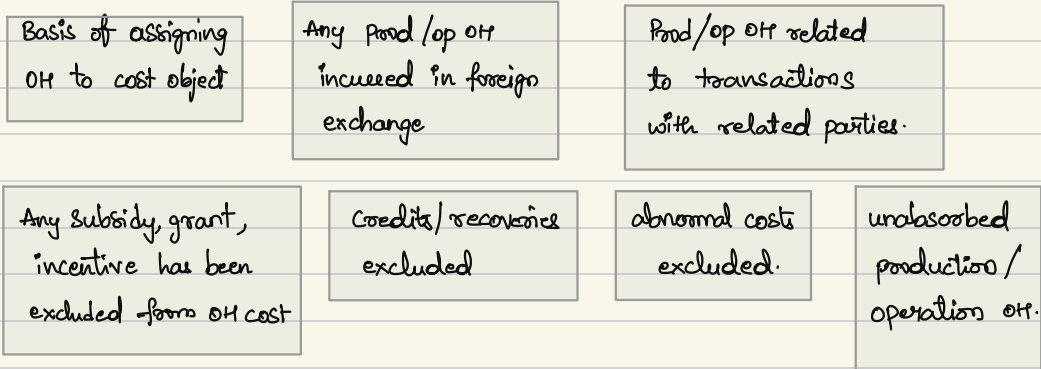
6. Assignment of overheads



7. presentation.



8. disclosures.:



* Disclosures → should be done → only if information is material, significant & quantifiable

* place of disclosures

→ Body of cost statements

→ as a foot note (or)

→ as a separate schedule.

* Any change in cost accounting principles → has material affect → shall be disclosed.
 ↓
 If it is not quantifiable / impact is not determinable → that fact →

9. Effective date : CAS 3 applies to cost statements

↓

Prepared on/ after 1-04-2016

CAS-4 cost of production / Acquisition / Supply of goods / provision of Services

1. Introduction :

old provision
 CAS-4 : cost of production
 for captive consumption
 ↓
 Determination of cost — when goods / services used within the company rather than sold.

new provision
 CAS-4 (Revised 2018)
 cost of production / Acquisition / Supply of goods / provision of Services.
 ↓
 principles & methods of
 - classification } to
 - measurement & } determine
 - assignment } cost.

This concept has become irrelevant after introduction of Goods & Services Tax (GST) on July 1st 2017.

↓
 cost of production / manufacture → major factor in → determining value of supply of goods / services.

CGST Act 2017.

Section 15 (1)
 value of supply = Transaction value
 ↓
 price actually paid / payable where the supplier & recipient are unrelated & where price is sole consideration.

Section 15 (4)
 If transaction value cannot be determined
 ↓
 determined as per Chapter IV of CGST Rules 2017.

- Rule 27: Supplier where consideration is not entirely in money
- Rule 28: Transaction between related persons / distinct persons.
- Rule 29: Supplier b/w principal & agent.

Rule 27 : Supplies where consideration is not entirely in money.

value \longrightarrow open market value

(or)

Total monetary consideration + equivalent value in non monetary terms

(or)

like kind & quality.

Rule 28 : Transaction between related persons / distinct persons.

value \longrightarrow open market value (or)

value of like kind & quality.

* when goods are intended

for sale by recipient \longrightarrow

(unrelated)

value will be 90% of price charged to the recipient's customer.

Rule 29 : Supplies between principal & agent.

value \longrightarrow open market value (or)

90% of resale price charged

by agent to unrelated

customer.

If value of supply cannot be

determined under Rule 27-29.

\downarrow Rule 30

value = 110% of cost of production, acquisition or provision of services.

Rule 31 \downarrow

Residual method: \rightarrow value is determined by reasonable means consistent with section 15

Reasonable means → fair, logical & justifiable method.

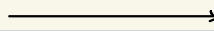
- can use any method that →
- * Reflects the true market value
 - * is consistent with general industry practices
 - * Is transparent & defensible
 - * Compliance with GST principles.

2. objective:

- uniformity
- consistently prepared cost statements for GST purpose.
- Accuracy in calculating Transaction value
- clear disclosure requirements that enhance transparency.

3. Scope :

Standard applies
to cost statements
that involve



- * Cost of production of goods
- * Cost of Acquisition of goods
- * Cost of Supply of goods.
- * Cost of provision/ Supply of Services
- * Determination of value of Supply.

4. Definitions : Refer concept book.

5. Principles of measurement :

- cost of production / acquisition of goods / provision of services
- * measure for each type separately.
- * cost should be aggregate of Direct & indirect costs.

→ **Material cost** : measure separately for each type

i.e; indigenous, material, imported material, bought out components, Process material,
Self manufactured items & accessories.

* Normal scrap / defective materials → Included in material cost.

* abnormal scrap → treated as a loss

* If scrap can be sold, Sale value shall be subtracted from material cost.

→ Employee & utility cost used for production measure separately.

→ packaging cost before sale / dispatch of products → include in total cost of goods.

→ Direct cost measure separately.

→ high value spare parts (Machine parts) → should be treated as assets & depreciated over time.

↓

If used immediately → include in inventory value

→ cost of maintenance

Depreciation &
R&D

} calculate separately for each product /
Service.

→ Joint products cost → measure separately after split off point.
& value of scrap to be excluded.

→ Royalties & fees

a) for use of technology / knowhow → Include in
to produce goods / provide services cost

b) brand usage → not included.

→ overheads & quality control cost: Include in total cost (-) taxes refundable / ITC

→ Abnormal costs, finance costs & losses: not included in cost of production

→ subsidies & incentives : deduct from cost

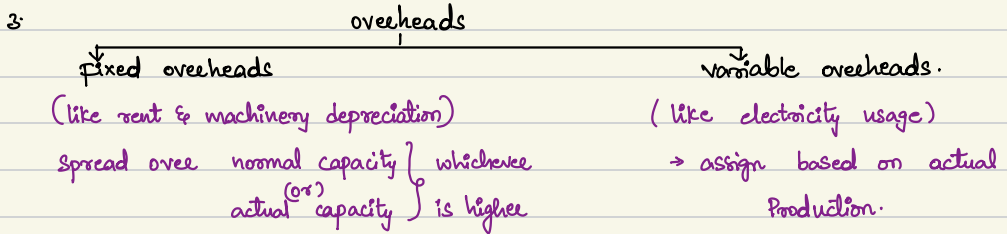
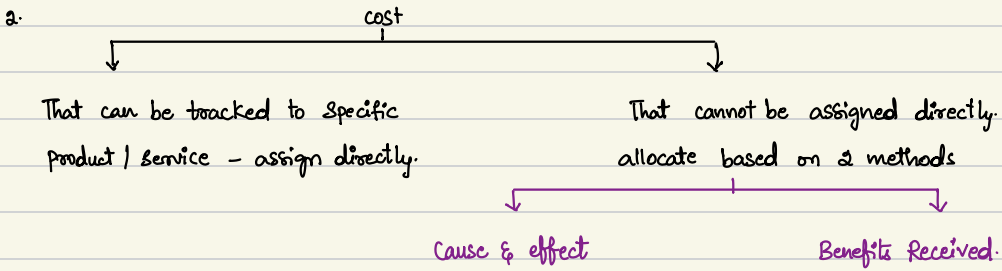
→ Capacity utilization : cost → based on normal capacity / actual capacity
whichever is higher

→ Foreign Exchange & Recoveries : Reduced from cost.

→ work in progress : cost is calculated based on current stage of completion
after adjusting opening & closing stocks.

6. Assignment of cost:

1. cost \rightarrow determined \rightarrow based on normal operations
 ignore abnormal & non recurring costs.



4. Joint Products
 process create more than 1 product
 shared costs \rightarrow allocated based on fair method.
 eg: NO. of units produced (or)
 selling value.

By products
 value of by products should be deducted from cost of main product.

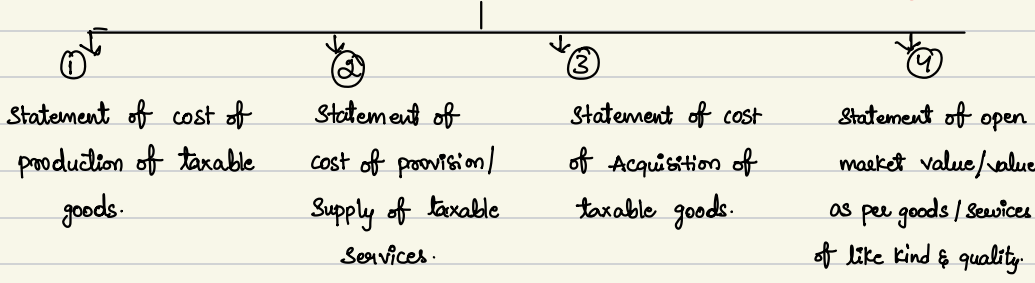
5. Joint Services
 process \rightarrow multiple services
 costs before split \rightarrow fairly divided between services.

6. miscellaneous income
 Income related to production
 like: selling scrap deduct from total cost of production.

7. presentation

* Cost statements \longrightarrow as per applicable format
in appendix.

It is a supplementary material \downarrow \rightarrow Illustrative Examples, flowcharts attached to standard it gives Diagrams, Definitions, forms, Templates, Additional guidance.



* Companies \rightarrow covered in \longrightarrow as per Section 148. shall
 companies cost Records & Audit Rules 2014. of companies \longrightarrow Prepare &
 Act 2013. present
 cost Records &
 * in compliance with Rules, \longleftarrow Cost statements
 Cost Accounting standards & GRAP.

* Companies not covered in Rules 2014. \rightarrow Prepare cost records in compliance with CAS & GRAP

* Cost statements \rightarrow certified by cost Accountants in practice \longrightarrow enable business to determine value of taxable goods.

* If at time of supply then company \rightarrow compute cost on true cost of goods are \rightarrow Budget/standard not determined. \rightarrow basis

\downarrow

Cost Accountant may issue provisional cost certificate

\rightarrow After costs are finalized cost certificate can be issued

\rightarrow variations in cost \rightarrow Supplier

\downarrow

issue Debit or credit note.

* Certified cost statements.

① Registered person \rightarrow as per sec 10(i) of CGST Act (composite scheme)

Aggregate turnover limit < 1.5 crores

certified cost statements \rightarrow issued for 6 month period.

② Aggregate turnover > 1.5 crores \rightarrow Certified cost statements shall be issued on quarterly basis.

&

③ Annual certified cost statement \rightarrow to be issued for financial year

\downarrow

Based on audited accounts

\downarrow

on/ before 31st december of next financial year.

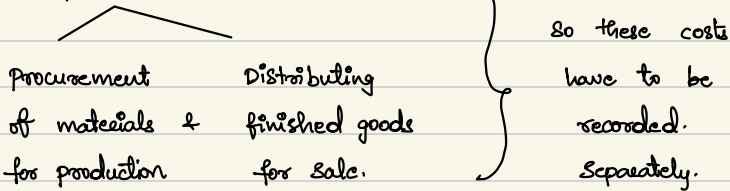
CAS-5 Determination of Average (Equalized) cost of transportation.

1. Introduction :

→ principles of cost accounting → trace, identify, allocate } cost elements → To ensure that all expenses are correctly recorded & apportioned

→ Uniformity → recording transportation expenses & calculating transportation cost.

→ Transportation cost



→ Transportation cost → shown separately in cost accounting records
 ↓
 apart from material procurement / product sales.

→ Finance Act 2003 : when determining assessable value of excisable goods
 ↓
 certificate of transportation cost is mandatory to claim deductions.

2. objective

uniformity	Systematic	Transparency.
in application of	Record Keeping	* in determining
Principles & methods	* Establish system to track	transportation cost.
for determining	all transportation related Expenses	
transportation cost	including: shipping, freight, logistics, fuel & other services cost.	



Should be taken out separately from operating cost to identify them clearly.



* After collecting all costs → Allocate & apportion them → to different } cost centers
} locations /
} Products.



So that entire transportation cost will be distributed fairly

across business

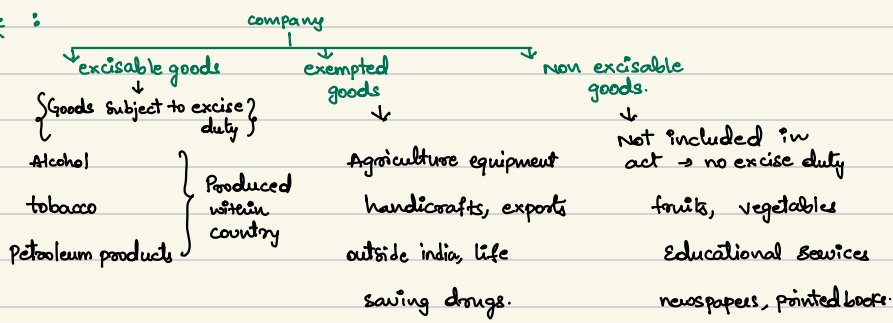


This also helps to understanding costs associated with each Product, location / department.



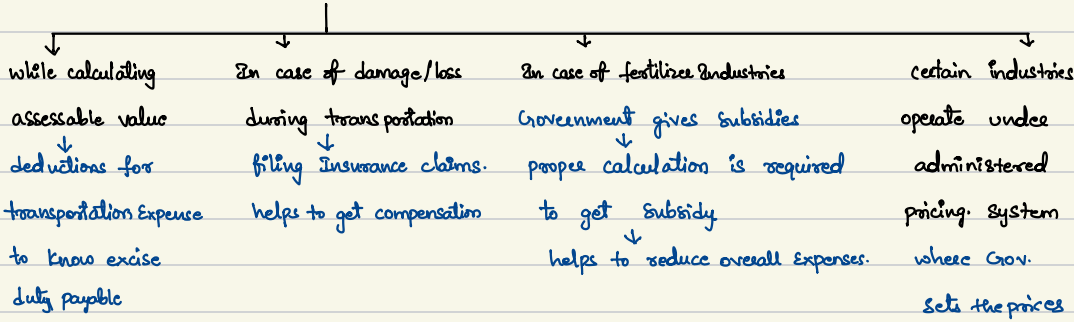
we can ensure precise cost control & analysis.

example :



3. Scope.

Applicable to calculate transportation cost



↓
Inward freight costs are

part of cost of purchase & to be included in acquisition costs of materials
Expense incurred in transporting raw materials / goods to company.

↓
Inventory valuation

→ Transportation cost → including freight charges to be included in cost of goods
↓
It is necessary when using inventory as collateral for loans / advances from banks / financial institutions

4. Definitions :

(i) cost of transportation : Includes

<p><u>freight</u> ↓ Transport goods from 1 place to other like shipping cost through truck, train, ship/plane.</p>	<p>Carriage Moving goods for short distance eg: transporting from warehouse to store.</p>	<p>Transit Insurance money spent to insure goods to protect from damages, loss / theft during journey.</p>	<p>operating fleet costs companies → own trucks/ vehicles for delivery ↓ cost of fuel, maintenance, driver salaries & repairs.</p>
--	---	--	--

Incidental charges

Additional Expenses come up during transportations
eg: tolls pay, loading/unloading fees,
Secondary packaging cost.

excludes →

Detention charges

penalty paid when transport vehicle is delayed beyond schedule time for loading/unloading goods.

Demurrage charges

fees charged when goods stay longer than allowed at terminal
* in port/train station/ causing delays

Transportation cost

Inward transportation cost



Expenses to transport material/goods received at factory/place of use.

Outward transportation cost



Expenses to transport goods from factory, depot

- Raw materials into production facility
- local costs for moving items from port to factory
- loading fees, etc.

- costs to deliver products to customers
- moving from warehouse to store
- Additional charges → freight fees etc.

(ii) depot :

premises for storing materials/goods for dispatch
includes → warehouses, godowns, stockyards.

(iii) Equalised transportation cost

↓
Average cost incurred during specified period.

(iv) Equalised freight

Average freight cost.

5. Maintenance of Records for ascertaining transportation cost

* Keep → detail record of transportation related Expenses

}	eg: freight	→ after adjustments
	Cartage	→ recoveries
	transit insurance	→ abnormal costs

* Company → owns fleet → record all expenses including Salaries for drivers, cleaners, fuel, grease, maintenance, tyres, batteries, trips made, distance covered etc.

* Hired transportation vehicle. → record should contain Date of dispatch, type of transport, description of goods, Destination, challan No., Quantity, Amount paid, distance covered.

* Maintain separate records for

┌	inward transportation cost
	outward transportation cost.

* Separate records

Transportation from factory to depot	Transportation for goods moved to jobworkers & back.
--------------------------------------	--

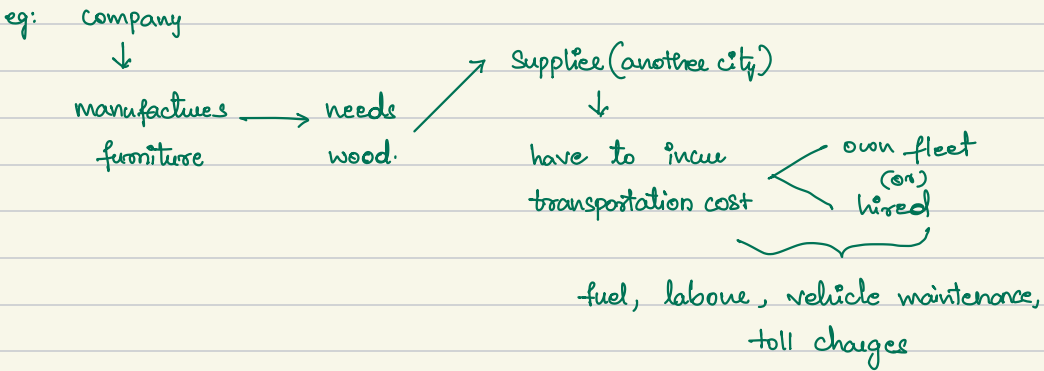
* Maintain distinct records for transportation cost made exclusively for trading activities

↓

cannot claim deduction from excisable goods.

* Separate records \longrightarrow if costs can be directly linked to specific product
 \downarrow
 helps for easier allocation.

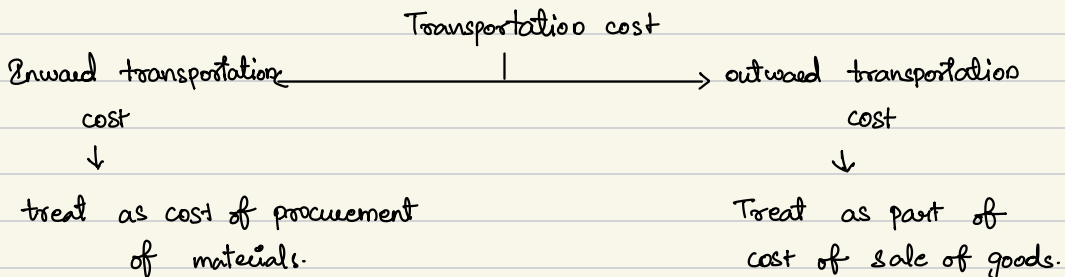
* Records based on apportionment in case of shared transportation cost



* Separate records for exempt & exported goods.

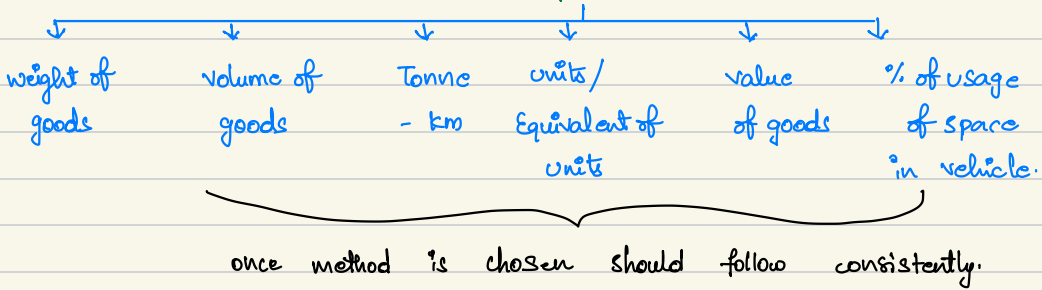
* If goods transported through new road (ship/air)
 \downarrow
 maintain distinct records.

6. Treatment of cost.



* outward transportation cost

Basis of apportionment → depending on nature of product & transportation mode



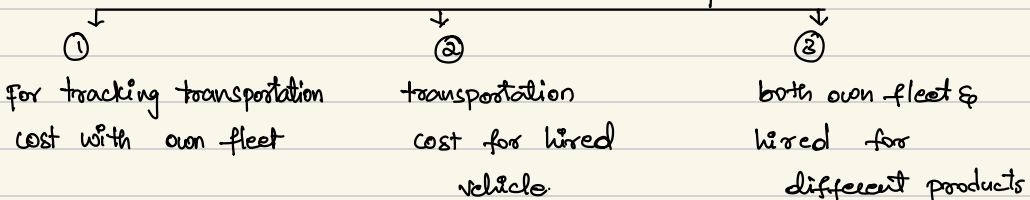
* while determining transportation cost per unit → distance each unit travels can be done by using weighted average cost approach ← to be considered

* Abnormal / Non recurring costs not be included.

* Penalties, detention charges, demurrage charges, abnormal breakdown expense } to be excluded from transportation cost.

7. cost sheet preparation.

* prepare → using format given in Appendix



*

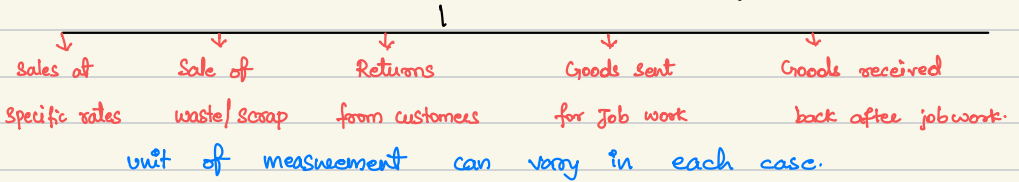


costs → directly allocable to specific product assign that cost to that specific product. as per Appendix 3.

→ common transportation cost ↓
Total should be apportioned to various products as per Appendix 3.
↓

Basis of apportionment have to followed.
(weight, volume, value)

* Additional columns in cost sheet for different type of transactions



* Job work cost → maintain separate records.

* cost Records → allow preparation & verification of transportation cost

Easy apportionment of these costs to various products.

7. Transaction value (Section 8)

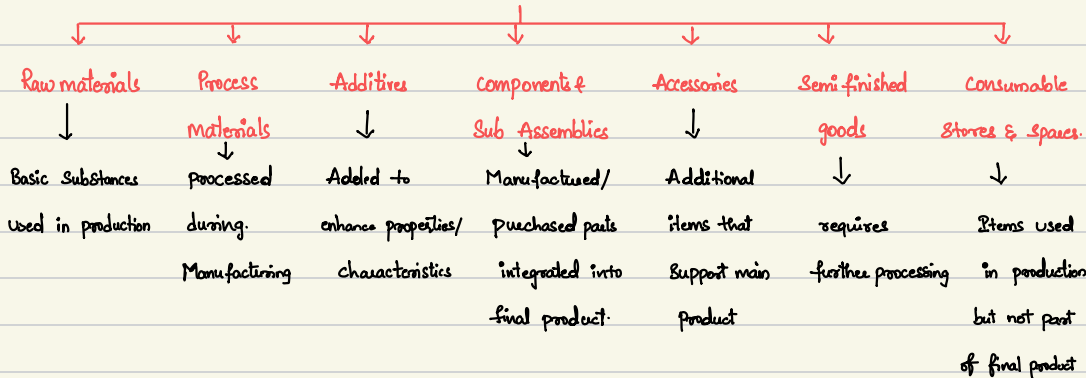
8. effective date → date of issue of this standard.

CAS-6 : Material cost:

* Introduction :

CAS-6 → focuses on → principles & Methods } used to determine Material cost

Material includes



Material excludes → packing materials (CAS-9)

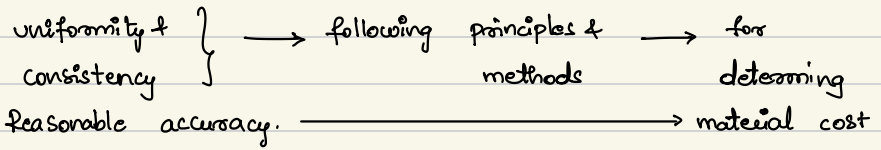
→ CAS 6 outlines Principles & methods for → classification, measurement, Assignment, presentation & disclosure. diff type of materials, value determination, Allocate cost → cost object, cost statements Reporting.

Deals with following issues

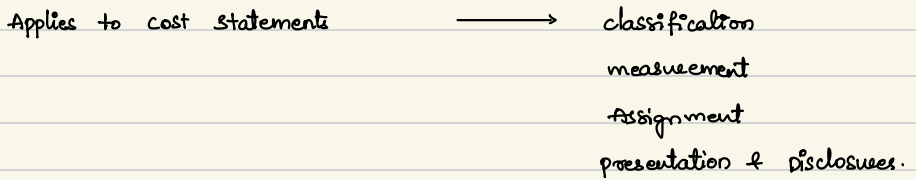
- principle of valuation of materials (value when received)
- principle of valuation of issue of materials (value when issued) for production
- Assignment of material cost to cost object

Methods to allocate cost → Relevant cost object

* objective :



* Scope

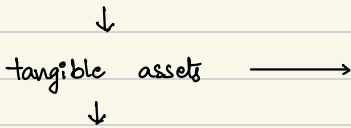


* Definitions :

Abnormal cost, Administrative OH, cost object, Defectives (Rework, Rejects), material (Direct, indirect), material cost, production OH, Scrap, Standard cost, waste & Spoilage.

→ Intermediate product : Requires further processing before sale.

→ Property, plant & equipment



* are used for → production of Goods / supply of services
→ Rental to others,
→ Administrative, Selling & Distribution purposes.

physical items → business owns

seen, touched / measured

Building, machinery,
Equipment, vehicles.

→ Are expected to have useful life beyond one accounting period.

* principles of valuation of receipts of materials

1. valuation of material Receipt

purchase price (+) costs directly linked to procurement
 Duties, taxes, freight inwards, Insurances,
 other expenses.

(-) Trade discounts, rebates
 Refundable taxes / duties (like credits)

2. finance cost related to material acquisition

not included in material cost

3. valuation of self-manufactured materials.

Includes:		excludes
Direct cost ↓ Material	factory OH + Administrative OH-related to production	finance costs, other administrative & marketing OH for captives consumption.
labour, expenses		

→ If spare parts / equipments → property plant & equipment
 recognize & depreciate. Definition.

↓
 If not; classify as inventory
 & include in cost
 when consumed.

→ normal loss / Spoilage before reaching factory

include in cost of remaining materials.

(-) if any recoverable amount from insurance/
 Supplier.

→ loss due to shrinkage / evaporation → if normal
Adjust with cost

→ foreign exchange of imported components → value at rate on date of transaction
late charges do not affect material cost.

→ Demurrage
Detention
penalty } → not to include in material cost.

→ Subsidy
grant
Incentive } related to materials → deduct from material cost

valuation of issue of materials.

→ material issue → valued using → FIFO, LIFO, weighted Average rate
chosen method must be followed consistently.

→ If valued using standard costing → price variances to be treated as part of material cost

→ Abnormal cost to be excluded.

→ material cost include transportation cost



calculate as per CAS-5

valuation of self manufactured components:

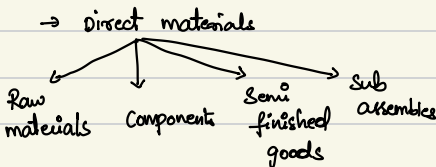
Include	Exclude
Direct material cost	other administrative OT
Direct employee cost	finance cost
Direct expenses	marketing OT
factory overheads } related to	for captive consumption
Administrative OT } production	

Normal scrap) defective → include in material cost
 Abnormal → Exclude & treat as loss after crediting realisable value.

* Assignment of costs:

material	Direct Expenses	Indirect materials.
→ Trace directly → cost object	materials → processed by	→ assign based on actual usage, technical norms/
→ assign based on materials consumed:	Buyer third party → specifications	→ cost of dies, tools, moulds to be amortised
→ If not traceable → estimate.	Processing charges → material cost + treated as Direct expenses	→ materials → useful life > 1 yr include in cost ↓ over useful life.
	↓ Sub contract → material cost	

* Presentation

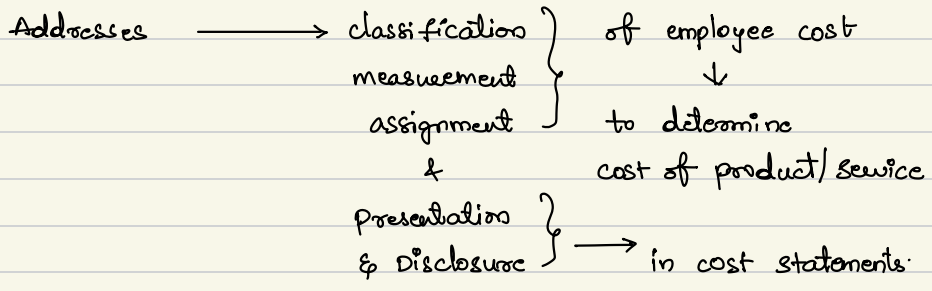
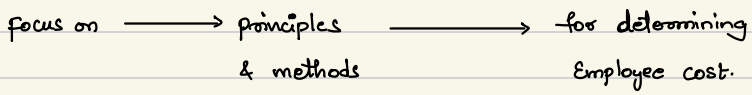


Direct materials
 Purchased
 → indigenous
 → imported
 → self-manufactured

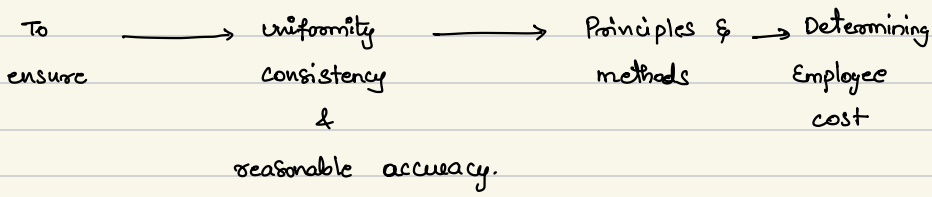
Indirect materials
 ↓
 group → heads
 stores & spares
 consumable stores
 etc..

CAS - 7 Employee cost

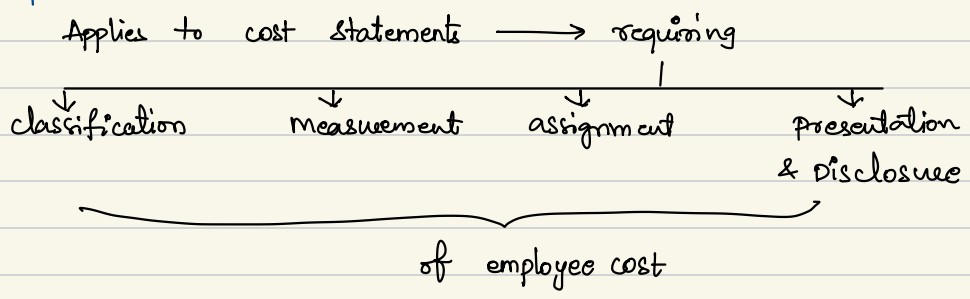
1. Introduction :



2. Objective :

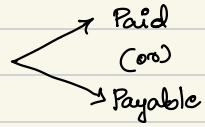


3. Scope :



4. Definition.

1. **Employee cost**: All forms of considerations
 ↓
 for services rendered by employees.
 (Includes) (Excludes)



Temporary part time contract employees
 ↓

Directly engaged by employee on contract basis

Excludes: employees of contractor engaged in organisation.

- * compensation (past periods) due to disputes / court orders.
- * short provisions (prior periods) made up current period.

Forms of payment:

Regular payments



Salaries, wages, allowances
 bonuses, incentives

contributions



contribution to PF, other funds

welfare

Expenses



welfare incentive

other

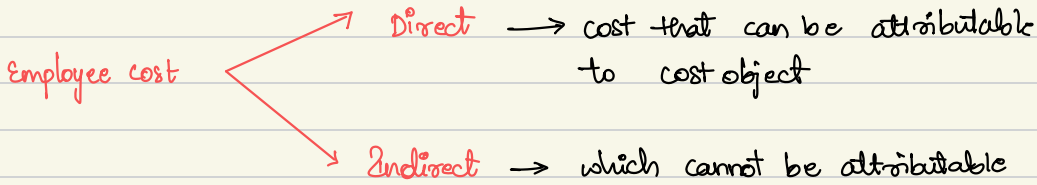
Benefits.

Future employee benefits

Gratuity, leave encashment,
 Retirement Benefits,
 VRs

General Benefits

paid holidays, leave with pay, insurance against accidents, health schemes, workmen's compensation
 free housing,



Idle time → period. → employees are paid but do not work
eg: holidays, lunch breaks.

overtime premium → extra pay → beyond normal wages
↓
for beyond normal working hours.

5. principles of measurement:

Employee cost

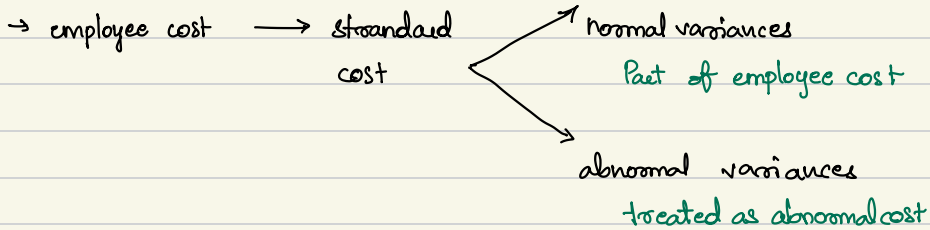
Includes:

Excludes:

- gross pay
- all allowances
- benefits payable by employer
- Bonus (statutory / based on surplus sharing)
- remuneration based on % of profits.
- Remuneration to managerial personnel & executive director, officers.

- Remuneration to non executive directors
↓
Administrative OH
- Imputed cost
- Subsidy, grant, incentives to be deducted.
- Abnormal cost (material, quantifiable)
- penalties, damages → authorities.

- Separation cost (VRs, retrenchment, termination) → amortised over period
- cost of idle time = idle hours × hourly rate of benefits of employees



→ cost of benefits → (eg: free housing / conveyance)

↓

Total cost of resources used to provide that benefit.

→ recovery from employees → towards benefits provided.

↓

deduct from employee cost

6. Assignment of cost

1. cost → traceable → cost object
 assign based on → Time consumed,
 no. of employees engaged.

2. particular employee cost → chargeable to separate cost object

↓

use principle of materiality.

3. employee cost → cannot be traced directly

↓

do by suitable estimates

4. Amortised separation costs → treat as indirect costs

↓

assign to cost object accordingly.

CAS-8 cost of utilities

1. Introduction → * Principles & methods
 * classification, measurement, assignment of cost of utilities
 ↓
 to determine cost of product/service
 * presentation & disclosure → cost statements.

2. objective : uniformity, consistency, reasonable accuracy.

3. scope :

- * apply to cost statements → classification, measurement, assignment, presentation, disclosure of cost of utilities.

* To determine cost of production

↓
 arrive at assessable value of excisable utilities used for captive consumption

* CAS 8 → not applicable → to organisations

↓
 primarily engaged in generation & sale of utilities.

4. Definitions :

* utilities : Inputs → Power, steam, water, compressed air

↓
 which are used for manufacturing process

↓
 but do not form part of final product.

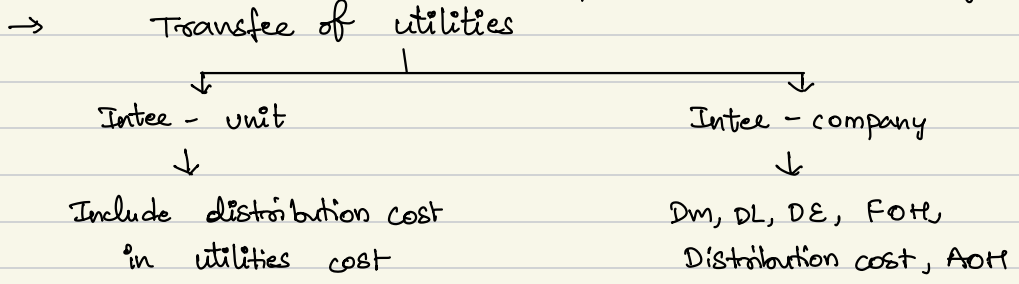
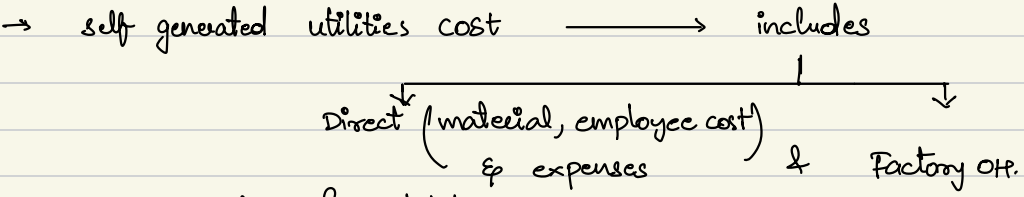
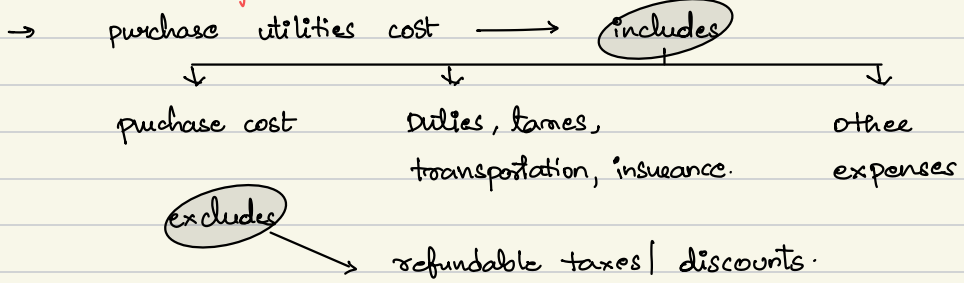
* **stand by utilities** : Backup utility created against failure of main source utilities

* **committed cost** : cost of maintaining stand by utilities.

5. principles of measurement:

→ each type of utility → treat as separate cost object.

(electricity, water)



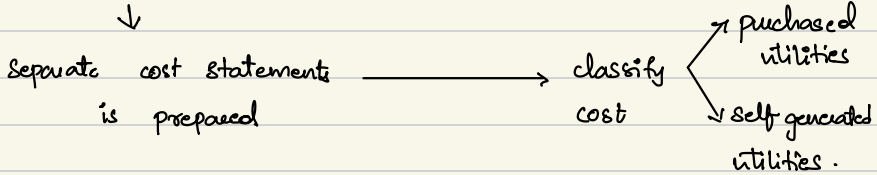
→ utilities sold to outside parties :

Cost → Dm, DL, DE, FOH, AOH, MOH, Distribution cost, sale value including profit margin.

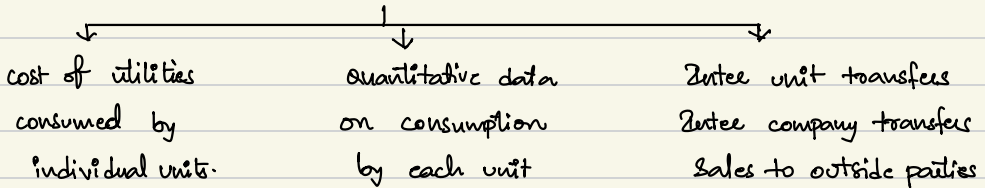
7. presentation :

each type of utility cost. → separate cost head → in cost statements.

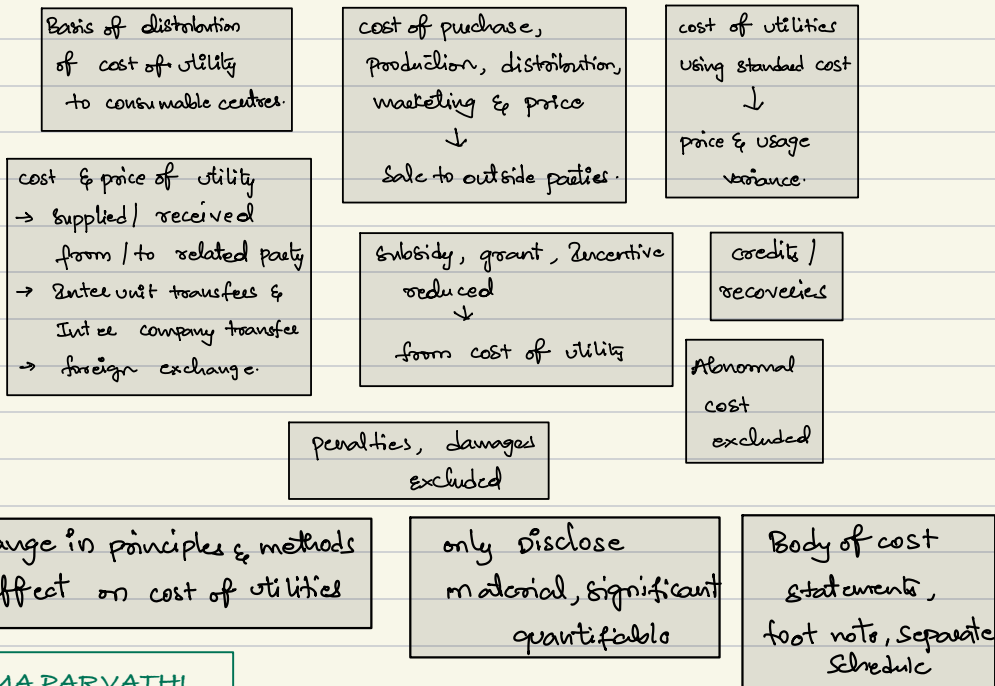
* If for cost of utilities



* Additional details in cost statements



8. Disclosures.



CAS - 9 Packing Material cost (Revised 2017)

Primary packing material



Essential for product preservation & use



considered as part of cost of production

Secondary packing materials



Non essential but aid in transportation & marketing



Included in distribution overheads

Reusable packing materials



Can be Reused for packing products multiple times.



Assign to cost object taking into account the number of times / period over which it is expected to be reused.

CAS 10 Direct Expenses

from purchased resources



Purchase price, taxes, duties, transportation & other procurement costs
(Reduce : discounts/ rebates)

from self manufactured tools/ dies



Include all associated production costs.

lump sum expenses → eg: royalties → Amortise over the period of benefit.
Technical knowhow fee

Direct expenses → Immaterial → Treat as overheads.

CAS 11 Administrative overheads

* Includes All Resources consumed in activities related to general management.



(Employee cost, utilities, office supplies, legal expenses, outside services)

————— Leased Assets —————

↓
operating leases



entire rental
income included

↓
Finance leases



only non finance
cost is included

Software cost —————→ purchased/developed/customized —————→ Amortise over its useful life.

CAS 12 Repairs & Maintenance cost

* Cost —————→ includes both direct & indirect.

In-house maintenance cost



Includes → Material, Spares, manpower, equipment usage, utilities, Resources (Costs)

outsourced maintenance cost



contractor charges, material, utilities, Stores & spares, manpower & Resources (costs)

Repairs by contractors at their premises



Invoiced/agreed prices (+) Duties, taxes & expenses (-) Discounts, taxes refundable & duties.

Repairs by outside contractors.



contractors charges own materials, consumables, spares, manpower, equipment, utilities, resources.

Spares

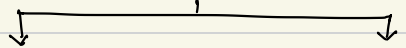


Replacement spares if do not enhance asset's performance consider as Repairs & maintenance cost

high value spare parts



Replaced by new one (&) old spare is Reconditioned



If recognise as property, plant & equipment.



depreciate accordingly.

If does not meet criteria of PPE



classify as inventory & recognise in cost when consumed.

* Major overhaul cost → Amortise over period of benefit.

CAS 13:	cost of service cost centre
CAS 14:	pollution control cost
CAS 15:	Selling & distribution cost
CAS 16:	Depreciation & Amortisation
CAS 17:	Interest on financing charges
CAS 18:	Research & Development cost
CAS 19:	Joint cost
CAS 20:	Royalty & Technical know how fee
CAS 21:	Quality control cost
CAS 22:	Manufacturing cost
CAS 23:	over burden removal cost
CAS 24:	Treatment of Revenue in cost statements.

Refer → Concept Book.

GACAP (Generally Accepted cost Accounting principles)

MCA ministry of corporate affairs



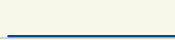
constituted an Expert group



to find out uncodified Accounting practices in Indian Industries.



Recommended a formal codification of GACAP



- * To provide structured framework
- * eliminate needless diversities in practice.
- * To create uniform approach.



following which MCA implemented:



companies (cost Records & Audit Rules) 2014.

↓
objective

↓
Rules mandates



↓
To Streamline Accounting practises Across diverse Sectors.

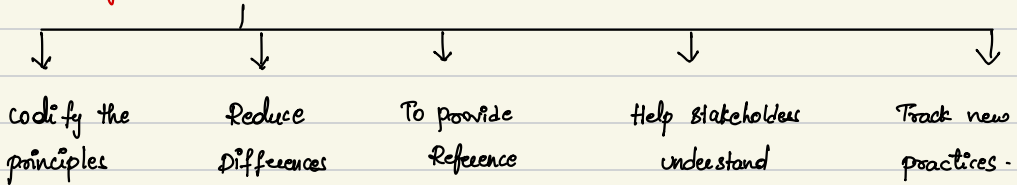
↓
Every company Subject to rules must maintain cost records for all products & activities

Records must be prepared According to GACAP & cost Accounting Standards.

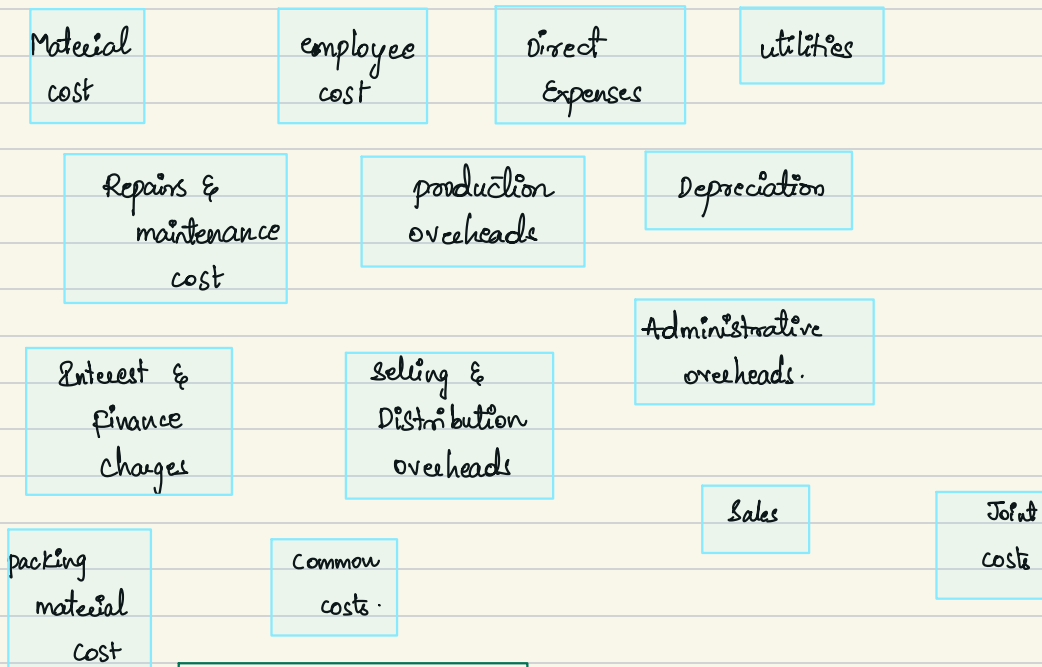
* Benefits of GACAP.



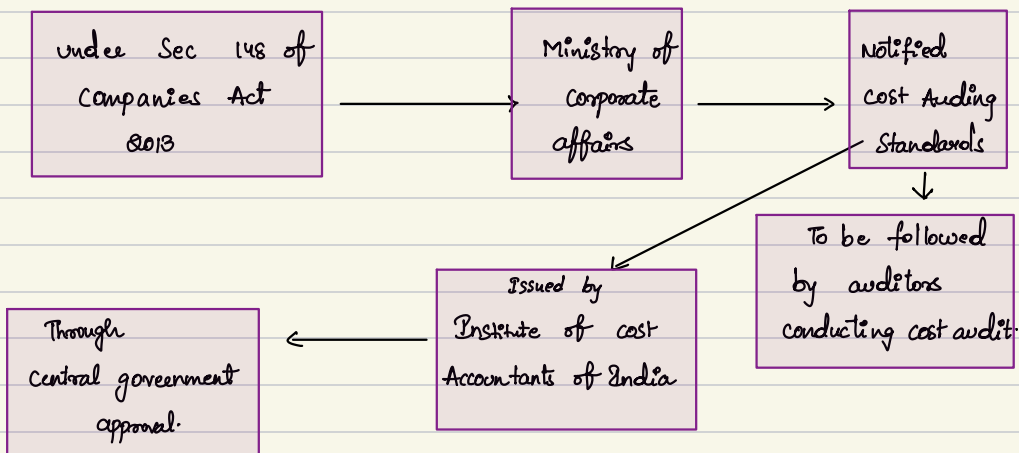
* Objectives of GACAP



* General principles applicable to All elements of cost.



Cost Auditing and Assurance Standards.



Overview

International Federation of Accountants (IFAC)



Issued International standards on Auditing [ISA's]



primarily focused on financial audits.



Institute (ICAI) → member of [IFAC]



with some modifications in framework & content wherever necessary to suit cost audit.



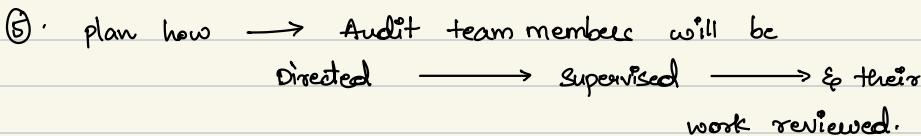
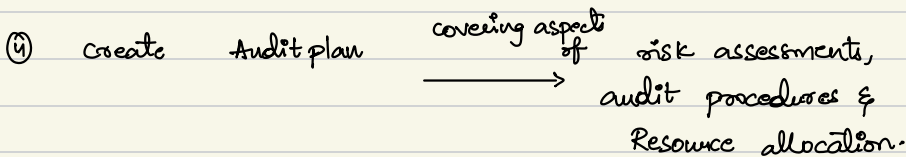
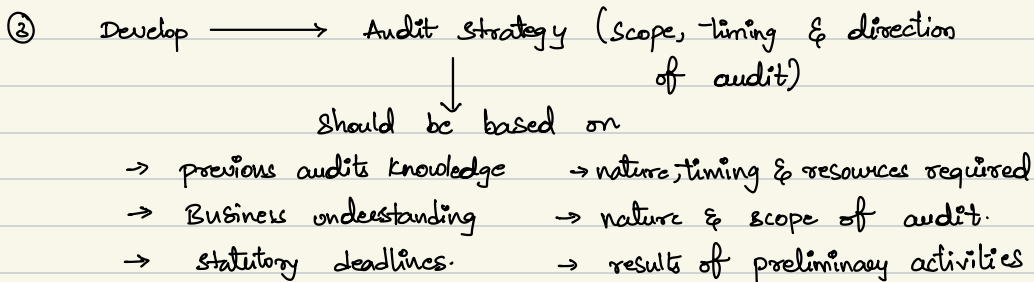
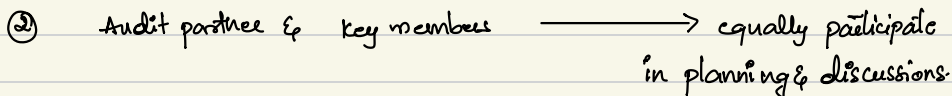
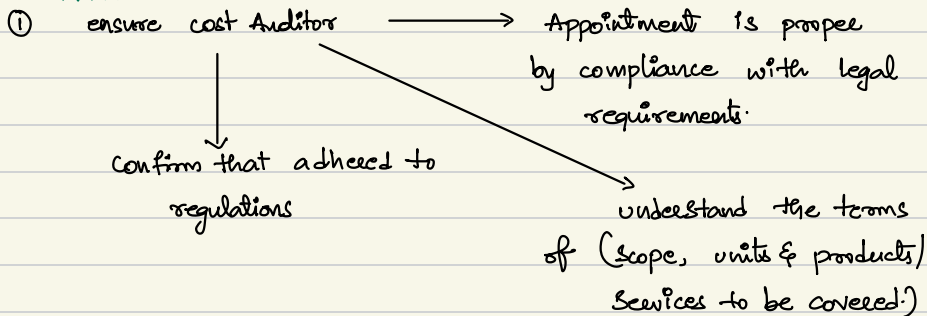
Through approval from government [MCA]



Issued standards on cost auditing.

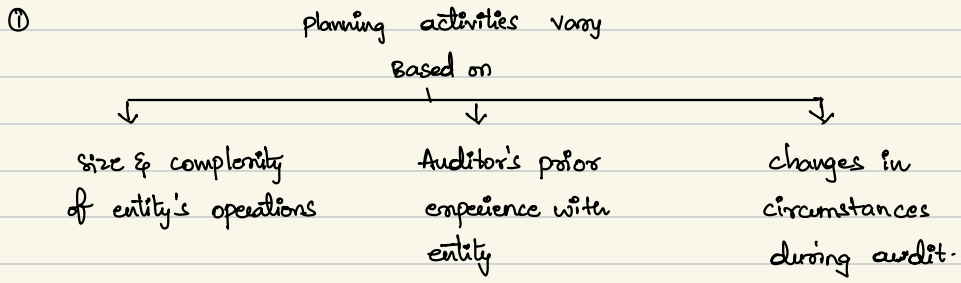
101 - standard on planning an Audit of cost statements.

Requirements



- ⑥ can update audit plan & strategy if needed.
- ⑦ Initial audit procedures → verify client's acceptance
↓
communicate with previous auditor.

Application guidance:



②. planning → ongoing process not one-time phase.
↓
prioritise & sequence audit procedures (early risk assessment)

③ Auditor → ensure *

- * no conflicts of interest / Management integrity issues arise after accepting audit.
- * maintain arm's length relationship with entity

④ Audit partners & team members → give insights → improve audit's efficiency.

⑤ Factors to be considered while formulating audit strategy & plan.

Cost Reporting Framework ↓ Reconcile with finance reports & legal framework	Industry regulations ↓ unique industry features that impact audit.	Reliance on other Auditors ↓ Include Internal & financial auditors	IT System ↓ ERP/ other Systems.	statutory timelines ↓ Reporting deadlines & Board/Audit Committee meetings	Resources. ↓ Available manpower, equipment etc..
--	---	---	--	--	---

⑥ Detailed Audit plan → includes → specific procedures
→ timing
→ risk assessment outcomes

⑦ extent of supervision & review depends on
size & complexity of entity, risk assessment, competence
of audit team

⑧ Adjustments during audit.

⑨ Initial Audit engagements

consult with previous auditor & review past records.	scrutiny of previous yrs transactions & cost related issues.	Procedures to validate opening balances	Additional quality control measures.
---	---	--	---

⑩ For smaller entity → Audit plan need not be
elaborative
↓
but should include all factors.

102 - Standard on Cost Audit Documentation.

→ Purpose of Cost Audit Documentation

- ① Basis for Auditor's conclusions whether overall objectives were achieved.
- ② Serves as proof that cost audit was conducted in line with standard & legal requirements.

→ Functions of Audit Documentation.

helps Audit team to plan & carry out cost audit effectively	Assists Supervisors in guiding & reviewing audit's team work.	ensure audit team is accountable for work performed.	keep records of matters that are relevant for future audit	Internal review by quality control teams as per
External inspections.			↓ Audit quality Guidance manual	↓ Quality review Board.

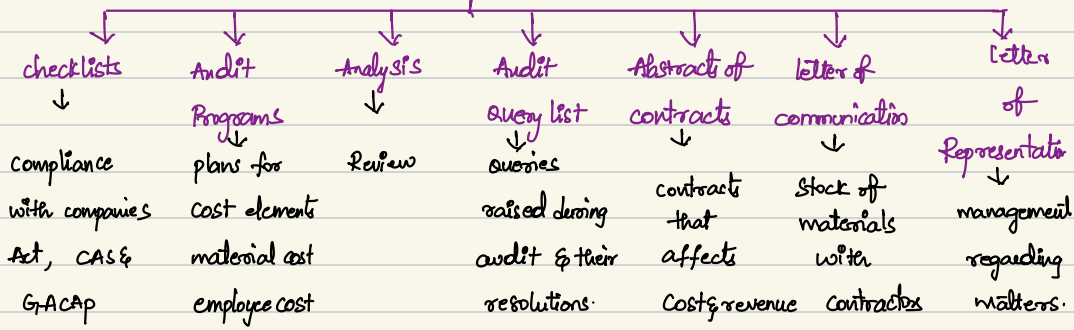
* Requirements of audit Documentation.

- ① Cost Auditor → Record Audit procedures performed
Relevant evidence obtained
conclusions reached.
- ② Documentation → should be clear enough
↓
It should be understandable by another competent person.

- ② Documentation → legal & regulatory requirements:
Adherence to standards
Results of procedures, including
audit evidence & significant
professional judgements made.
- ④ Record → discussions with clients & parties about
significant matters during audit.
- ⑤ Document → If any departures from requirements
from standards.
- ⑥ Include details → Nature, timing, extent of procedures
* what was tested
* who performed & reviewed.
- ⑦ Audit Documentation → prepare on timely basis (to have accuracy
& completeness).
- ⑧ After Audit report is issued → Additional procedures performed
or new conclusions drawn
↓
document along with reasons.
- ⑨ Audit Documentation → should be organized &
assembled into audit file

* Application guidance for cost Audit Documentation.

1: Typical components of cost Audit Documentation



2: form of Documentation Depends on

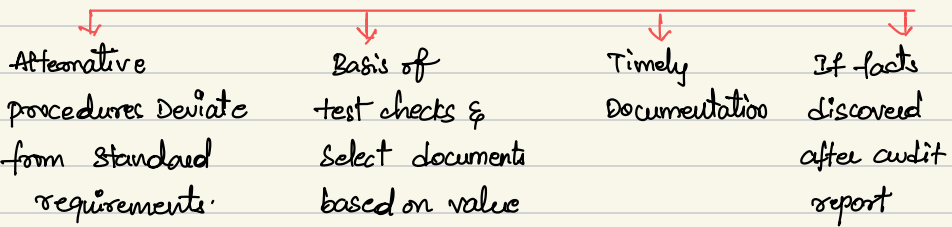
- Size & complexity of entity
- Computerization level of cost records.
- Assessed risk of material misstatements
- Audit methodology tools used.

- ② Document → material consumption norms / related party transactions oral explanations cannot replace Documentation
- ④ Documented → Audit plans, appointment letters & meeting minutes is essential.
- ⑤ Document → Risk of material misstatements & significant judgements.
 ↓
 include minutes of discussions → Management gov bodies third parties

⑥ Small entities documentation

Description of entity & products	organizational chart	manufacturing process flow chart	Internal control risk assessment	significant Audit findings & conclusions
----------------------------------	----------------------	----------------------------------	----------------------------------	--

⑦ Document

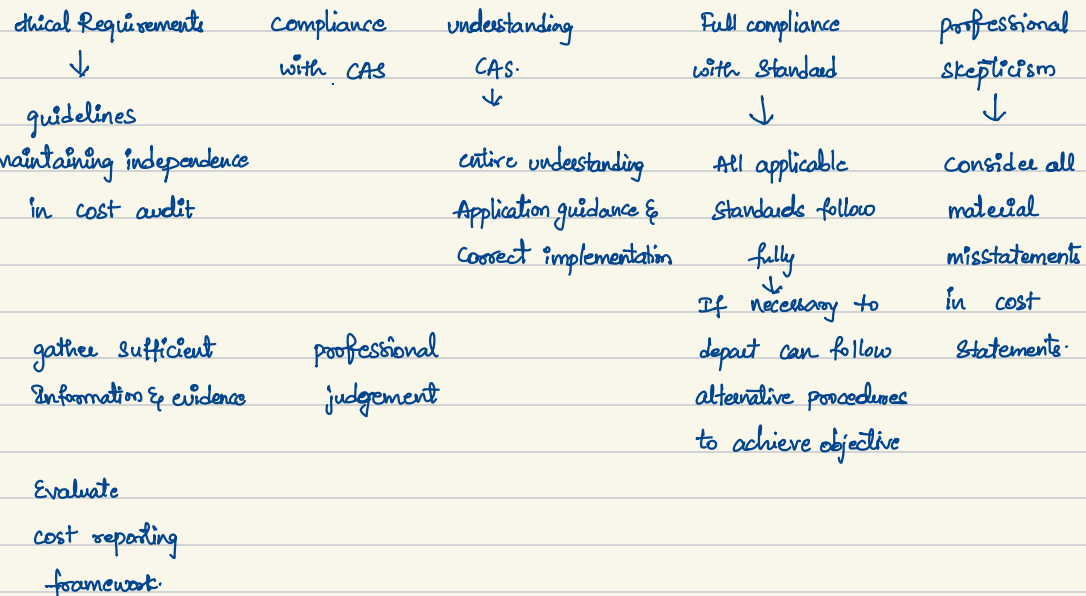


⑧ Document who prepared audit materials & their responsibilities

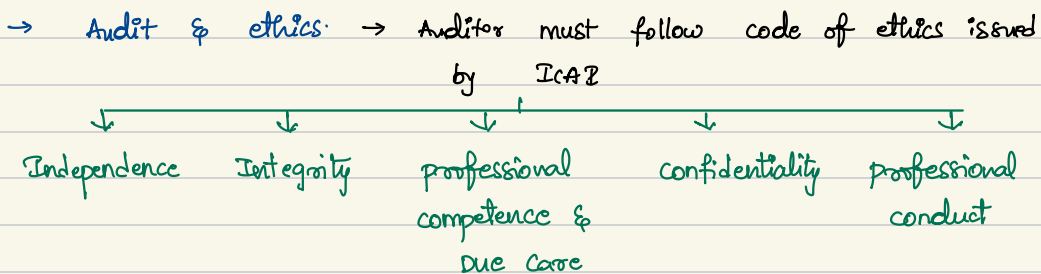
* Documentation is → property of cost auditor
 ↓
 must be retained for atleast 10 years from audit report date.

103 - Standard on overall objectives of Independent cost auditor & conduct of an audit in accordance with standard.

* Requirements:



* Application guidance for cost Audit.



→ conduct of Audit.

Application of Standards	compliance with legal & Regulatory Requirements.	Departure from Standard Requirements.
--------------------------	--	---------------------------------------

→ professional skepticism :

critical Assessment	Reasonable Assurance	Audit limitations	Audit not guarantee.
↓	↓	↓	↓
maintain questioning mind throughout audit, evaluate validity & reliability of audit evidence	obtain sufficient evidence	* profession judgement * Transactions with Related parties.	future viability of entity or efficiency of mgt.

→ Audit Risk & materiality

* Audit risk & Business risks

- ↓
- Auditor focuses only on risk that affect statements
- Audit risk → inappropriate opinion due to material misstatements in cost statements
- The auditor reduces risk by obtaining sufficient evidence & conclusion.

* components of Audit risk

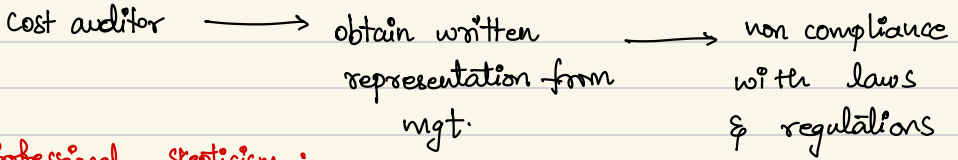
- ↓
- 1) Risk of material misstatement
- 2) Detection Risk (-fails to detect errors/mistake)
- 3) Assertion levels risk evaluates risk at both cost statements & cost heads
- 4) Inherent risk (Complex calculations uncertain estimates)
- 5) control risk. Internal controls will not prevent material misstatements.

* Responsibilities of cost statements

- ↓
- ① Mgt responsibility (Prepare & present cost statements)
- ② cost auditor's responsibility. express opinion on whether cost statements give true & fair view

* non compliance

Mgt representation on non compliance.



Professional skepticism :

* Auditor's mindset → remains alert to possible errors, → During an fraud/ unusual engagement. circumstances

* Professional skepticism is fundamental to successful auditing.

→ allow auditor to discharge responsibilities to stakeholders effectively.

→ critically assessing audit evidence

→ ensuring reliability of documents & responses obtained.

* professional skepticism → helps auditors → identify & respond to fraud risk

where fraud risks are high

→ modify audit procedures & gather evidence

→ seek confirmation from third parties & specialists.

→ Apply forensic audit & techniques.

* elements of professional skepticism

Auditor

Auditor

Auditors

Attributes

mindset

Actions:

Skills & Knowledge that enable thinking

questioning & critical approach to evidence

Appropriate responses to changing audit conditions & pressures.

104- Standard on Knowledge of Business, its processes & Business environment.

* Requirements of cost auditor.

Understanding
Business &
Processes

- nature of entity
- Industry & Regulatory factors
- Cost accounting policies
- performance measurement.

Understanding
entity & its
environment

Understanding
entity's Internal
Control

- control environment
- Risk Assessment process
- Cost Information/MIS
- control Activities
- monitoring controls

IT environment
& control

- IT Architecture Systems & programs
- Access controls
- data change controls
- Information Integrity & Data Security.

* Identifying & Assessing risk of material misstatements.

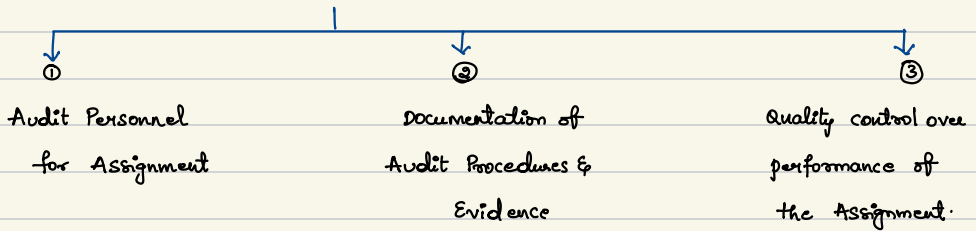
- Identify risk
- Assess Economic & Accounting developments
- Related party transactions
- Subjectivity in measurement
- Revising risk Assessment.

* Documentation

- 1) Identified risk of material misstatement at both cost statements & cost heads level.
- 2) Risk & related controls

Unit 6 : Cost Audit Program

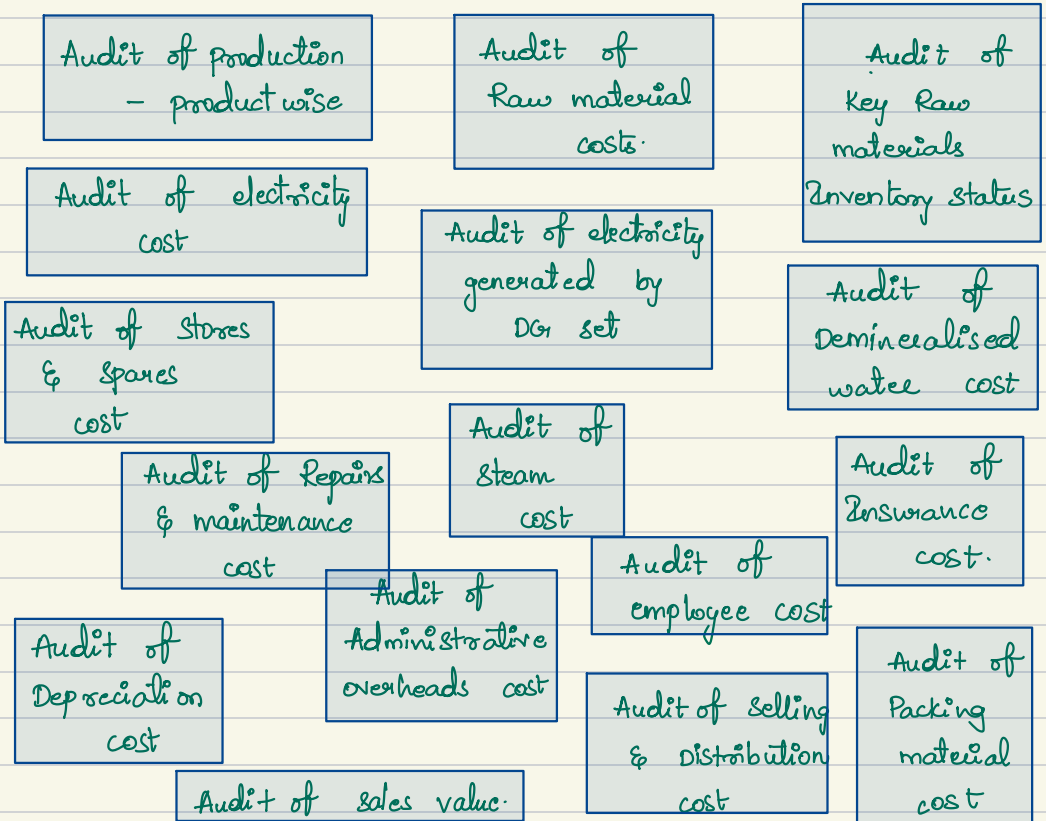
* Factors in planning cost Audit Assignment:



Cost Audit Programme



16 checklists:



Section D

Forensic Audit and Anti-Money Laundering

- Forensic Audit
- Anti-Money Laundering



FORENSIC AUDIT

* Forensic Audit :

→ Analysis & Review

of financial records

of
 → Company
 → Person

 } to extract
 } facts which
 } can be used
 } in court of law

↓
 To detect any illegal action
 Manipulation in Books of Accounts
 Siphoning of funds.

Begins with suspicions & doubts

ends with performance of investigation procedures

* Forensic Audit can be done

financial fraud

↓
 fraud
 embezzlement
 financial crimes

non financial fraud

↓
 bankruptcy
 filing disputes
 closure of business
 divorces

difference

financial audit

↓
 examination for
 statutory compliance

forensic audit

↓
 Investigate financial records
 of entity to derive
 evidence support of fraud
 ↓
 that can be used in court
 of law / legal proceedings

* Common areas of forensic audit:

Asset
Misappropriation

Instances
of corruption

financial
Statement
fraud

- cash theft
- using company's funds for fraudulent payments
- Billing frauds (fictitious Suppliers)
- payroll frauds (fictitious employees)
- theft of Inventory from company.
- misuse of assets.

Conflict
of
Interest

↓
Individuals
Making decisions
that benefits
personal
interest
over company
interest.

Extortion

↓
Demanding
money /
favours
through
coercion/
threats

Bribery

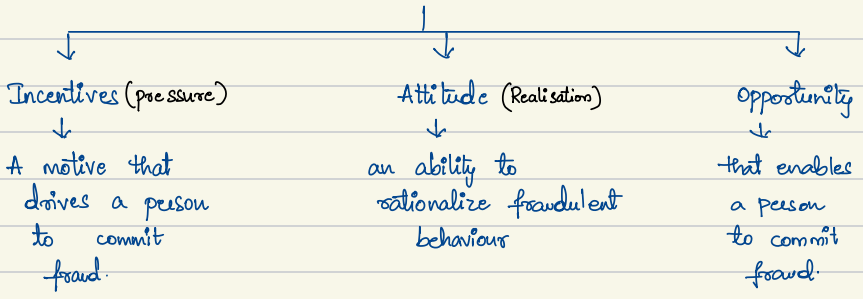
↓
Money /
Something
else of value
is offered
in order to
influence a
situation

- fraudulent financial reporting
- fraud → material misstatements
- deliberate falsification
- (or) omission
- misapplication of standards

Fraud triangle and Fraud risk

* Three elements that are common for any fraud being committed.

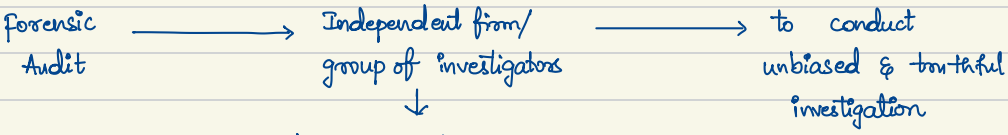
Fraud triangle → Tool used in forensic auditing that explains 3 inter related elements



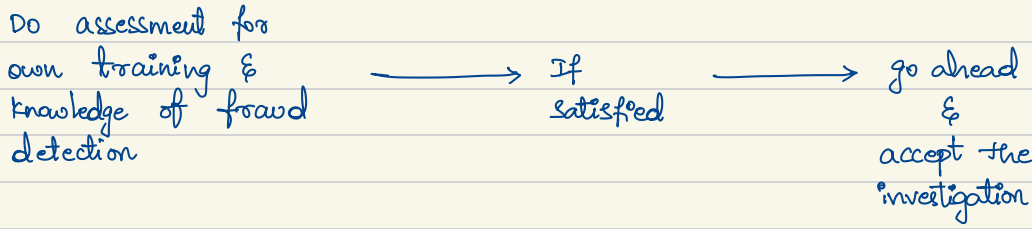
* Investigation Methodology of forensic Audit:

①	②	③	④	⑤
Accepting the Investigation	planning the Investigation	Gathering evidence	Reporting	court proceedings.

1) Accepting the Investigation



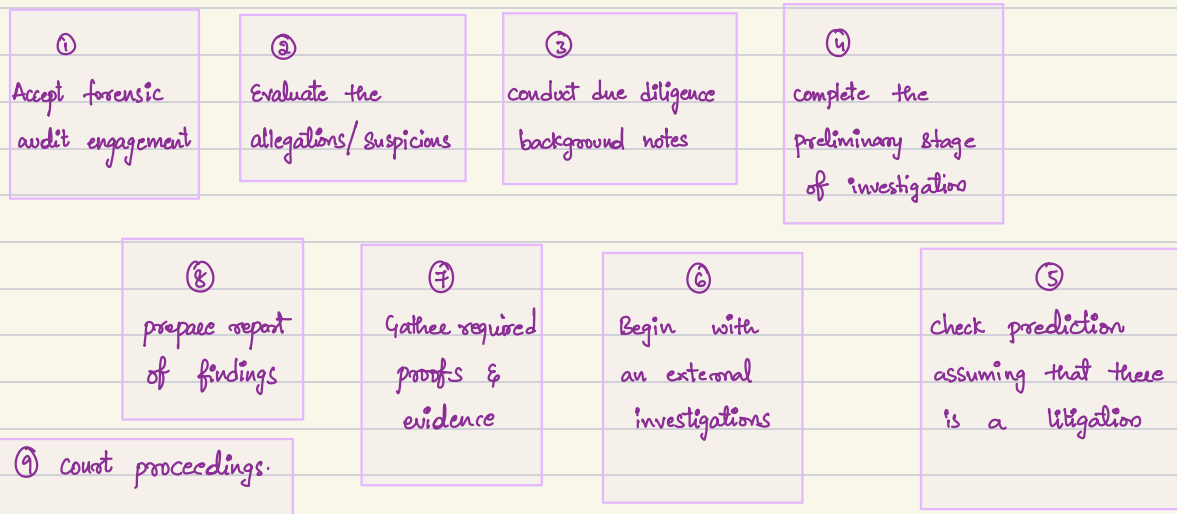
↓
 1st step → Determine wheather they have necessary tools, skills & expertise to go forward with investigation
 ↓



2) planning the Investigation :

Ascertain the goal of audit being conducted
 Determine procedure to achieve it.
 use effective tools & techniques.

* 9 step method for fact findings in case of forensic audit engagement



* Need for forensic Audit

Forensic Auditing → early warning signals of fraud.



is done to detect the fraud & to determine organisation's needs.

Few instances occurrence of which → entity → direct forensic audit.

Theft of business information/ where business systems have been hacked

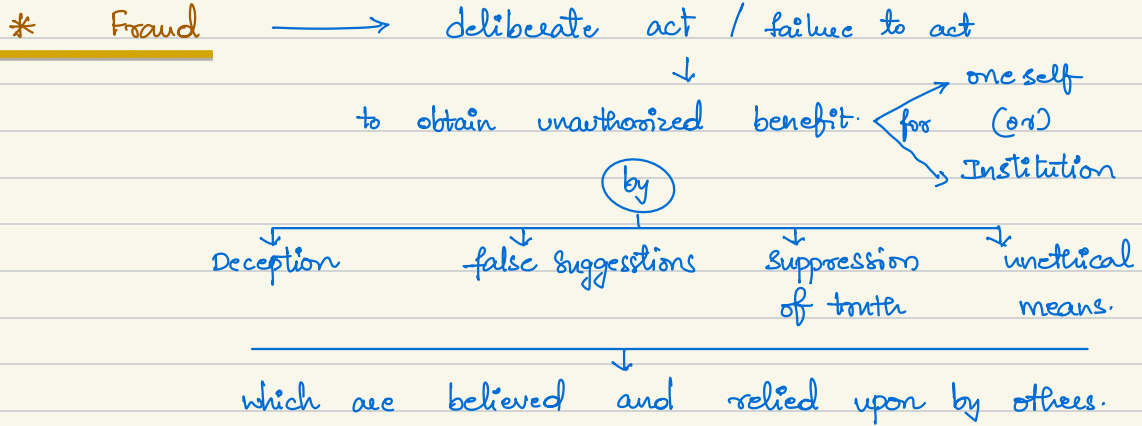
Issues identified by whistle Blowers

Reconciliations. resulted in unidentified material differences

Suspicious of fraud/ illegal activity

Turnover & Balances are showing negative results.

⇒ whistle blower → Individual who provides right information to right people
 that they believe evidences wrongdoing



* Examples of fraudulent acts

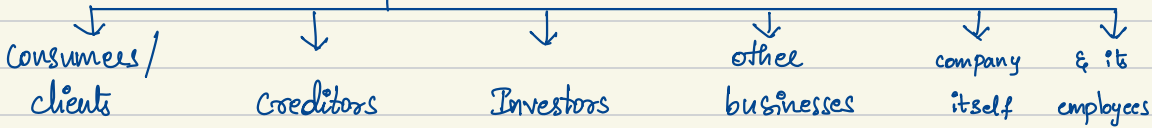
- embezzlement
- Forgery / alteration of documents
- Fraudulent financial reporting
- unauthorized alteration / manipulation of computer files
- misappropriation / misuse of resources
- Authorization / receipt of payment of goods not received / services not performed
- Authorization / receipt of unearned wages / benefits
- Conflict of Interest, violation of ethics.

* Business Fraud / corporate fraud

↓
 Illegal / unethical & deceptive actions
 Committed by company / Individual acting
 in their capacity as employee of company.

→ often extremely complicated
 & difficult to identify
 ↓
 usually takes months to unravel

⇒ victims of corporate fraud



⇒ why corporate fraud happens

①

The Desire / perceived need
 to attract / Retain
 Investors

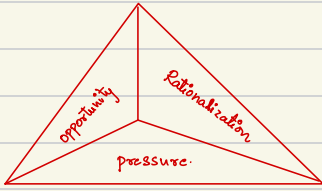
②

problems / defects with
 company's products
 that they want to hide.

⇒ Major corporate fraud cases in the world.



* Fraud triangle



* opportunity → weakness of internal controls
 eg: inadequate → supervision & review
 → separation of duties
 → management approval
 → system control.

* pressure : → motive
 eg: personal financial problems / unforeseen expenses
 personal addictions such as gambling, drugs
 unrealistic deadlines & performance goals.

* Rationalization : → Justification for fraudulent activity
 eg: I need this money & I'll pay it back when I get pay check
 I didn't get raise, The company owes me.

Breaking the fraud triangle → Removing one of the elements to reduce fraudulent activities
 (* opportunity) → coz it provides more actionable route to do fraud.

* Red Flags for fraud:



These are warning signals that fraud risk is higher without any evidence of fraud occurring.

existence of one/two flags are not something to be overly concerned



If multiple flags are present & accounting irregularities/weak controls → then Internal audit department should be contacted

Employee Red flags

1. Sudden lifestyle changes
2. Significant personal debt & credit Problems
3. Behavioural changes (addictions)
4. Fear of losing the job
5. Refusal to take vacation / leave

Management Red flags.

1. overriding of Internal controls
2. decisions are dominated by Individual/group
3. Shows disrespect to regulatory bodies.
4. Policies & Procedures are not documented
5. No monitoring, lack of experience
6. frequent changes in bank accounts
7. excessive & unnecessary year end transactions
8. photo copied / missing documents
9. Reluctant to provide records to auditors
10. Sold company assets below market value.

* Financial Forensics

↓
field that combines Accounting & Investigation

main purpose

→ Discover & gather evidence of criminal activity involving money

⇒ Financial forensic professional

①

Investigate Individuals & organisation finances
↓
Determine how they manage them

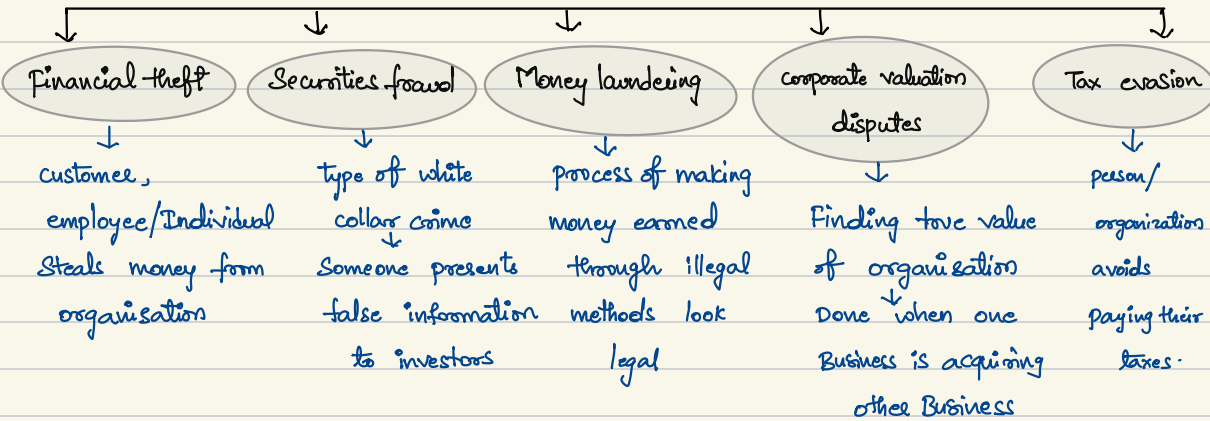
②

help prevent financial crimes & Recover lost assets.

③

Researches other businesses to determine their true value.

Common cases of financial forensics:



Qualities of forensic Accountant / professional

Have a logical mind

Give attention to details

Be Spontaneous

Give value to moral principles

Questions Everything / Inquisitiveness

Good understanding of Accounting transactions & impacts.

* Investigation Techniques for forensic accounting.

- Reviewing public Documents & conducting Background checks
- conducting Detailed Interviews
- Gathering Information from trustworthy Sources
- Analyzing evidence gathered
- conducting Surveillance
- Going undercover
- Analyzing financial Statements.

* Fundamental ethical issues that organisations to maintain integrity.

①

understanding ethical standards



→ Integrity & trust
→ Diversity & Inclusions
→ compliance & Governance.

②

Harassment & Discrimination in workplace



lead to severe financial & Reputational damage
↓
Anti Discrimination laws
Age, Disability, Equal pay, pregnancy, Race & ethnicity, Religion, Sex & Gender identity

③

Health & Safety in workplace



Employee Rights (OSHA)
→ fall protection, hazards communications, Scaffolding (Required Resistance & Max weight), Respiratory protection, Powercled Industrial trucks (fire), ladders, electrical & wiring, machine guarding. General electrical requirements.

④

Psychosocial Risk & mental health



Job insecurity, high job demands, effort - reward imbalance, low autonomy.

⑤

whistle blowing & social media conduct.



Employee → conduct in social media
↓
Influence his Employment status
Disloyalty
Ambiguity

⑥

Ethics in Accounting practices



Accurate Book Keeping
Cooking the Books
Impact on stakeholders

⑦

legislative Response



Stringent financial reporting requirements by Sarbanes Oxley Act

⑧

Non Disclosure & corporate espionage.



theft of confidential info.
↓
Imp of Non Disclosure Agreement
→ protection of sensitive info
→ legal Resources → consequences of unauthorized disclosures
→ Deterrent effect → penalties against potential breaches.

⑨

Technology & privacy practices

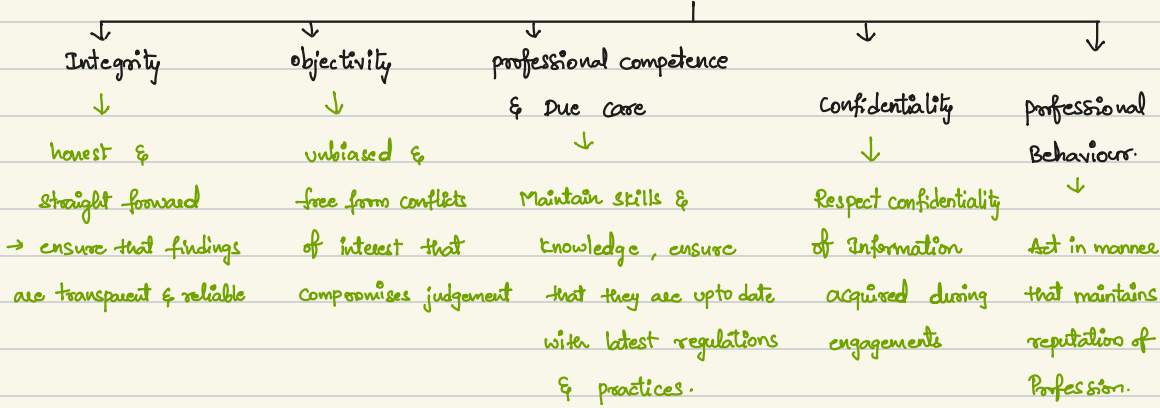


Monitory employee activities with advancement of technology
↓
surveillance
↓
For transparency employee Awareness.

* Ethical Responsibilities of Auditors

To achieve these objectives → auditors must follow certain set of principles

Fundamental ethical principles



* Major Threats in Auditing profession

Self Interest threat	Self Review threat	Advocacy threat	Familiarity threat	Intimidation threat
→ when auditor has financial interest in auditing company	→ when auditor performs non-audit services for a client & audits those same statements.	Auditor promotes/ advocates on behalf of the client which compromise their ability to remain impartial	→ when auditor becomes too close/ familiar with client's mgt/ personnel leading to bias.	→ Auditor is coerced/ threatened by client's mgt, directors & other influential individuals.
→ direct/ indirect financial stake				
→ firm is reliant on client fees → outstanding fees are due.				

* To minimize risk of ethical violation, Auditors & organizations must take proactive steps to uphold those principles

5 Steps

①

Honestly
Assess Needs
& Resources



conduct honest
evaluation of
ethical risks that
organization might face
& ensure that there
are sufficient resources
to address risks.

②

Establish a
Strong
Foundation



→ written standards
of ethical workplace
conduct
→ Training on standards
→ Company Resources
for advise on ethics
→ confidential Reporting
System
→ performance Evaluation
based on ethical conduct
→ Disciplinary systems.

③

Build a culture
of Integrity from
Top down



→ ethical leadership
* Talk about importance
of ethics regularly.
* inform employees about
decisions & actions that
impact them
* uphold promises &
commitments to stakeholders
& employees.
* Acknowledge & reward
ethical conduct.
* hold violators accountable
especially → leadership positions

④

Keep a value
Focus in moments
Big & Small



→ HR Policies: fairness &
Integrity
→ Reward system: Reward
ethical behaviour
→ hiring & Retention:
prioritize candidates with
strong ethical behaviour
→ performance management:
Integrate ethical conduct
into performance evaluations
→ promotion Decisions:
promote individuals who
continuously demonstrate
integrity.

⑤

Re-evaluate &
Revise as
Needed.



→ conduct Risk
Assessment
→ Survey employees
→ hold Focus groups
→ Measure progress.

* characteristics of effective ethics program

- Freedom to question Management without fear
- Rewards for ethical conduct
- NO Rewards for questionable practices.
- positive feed back for ethical Behaviour
- preparedness to address misconduct
- willingness to seek ethics advice.

* challenges in Implementing an effective ethics policy within company.

- ① Resistance from employees.
- ② costs of training & implementation
- ③ Inability to determine RoZ of ethics policy.

* code of conduct in Forensic Audit

Applicability of code

certified fraud examiners Associate Auditors

code of conduct in Forensic Audit

- Integrity
- professionalism
- Responsibility to clients & public
- commitment to excellence.

standards

code of ethics:

Role of certified fraud examiners.

- ① professional conduct → professionalism & due Diligence
- ② Examination → Avoidance of illegal/unethical conduct
- ③ Reporting.
 - Integrity & competence
 - compliance with court orders & Impartial Testimony
 - Evidence Based opinions
 - confidentiality
 - full Disclosure of material matters
 - continual Improvement.

- ↓
- 1. Identifying Evidence of fraud.
 - 2. conducting Interviews & writing Reports.
 - 3. proactively Evaluating fraud Risk.

Anti Money laundering

what is ML & AML

why to understand AML

connection with Terrorism financing
cycle of money laundering.

Sec 2 definitions

Sec 3 Money laundering definition

Sec 4 punishment

Sec 5 Attachment of property.

Sec 6 AA.

Sec 16 power of survey.

Sec 17 power of search & seizure.

Sec 18 power to search a person

Sec 19 Arrest

Sec 21 Retention of Records.

Sec 23 Inter connection transaction.

Sec 24. presumption & onus of proof.

Legal & Regulatory framework

↓
FIU of India

↓
Enforcement
Directorate

↓
RBI

↓
SEBI

↓
Other
Regulatory
Authorities

→ Reporting entity

→ Financial Action task force. Recommendations

Section C

Internal Control, Internal Audit, Operational Audit & Other Related Issues

- Internal Control and Internal Audit | 5%
- Operational Audit & Internal Audit under Companies Act, 2013
- Audit of Different Service Organisations | 5%



Concept 3 : Audit of Hotels

- 1. Internal Control:** Ensure controls are in place to prevent revenue leakage and pilferage.
 - Check effectiveness of cash handling, purchasing, billing, and inventory control for items like food, beverages, and assets (e.g., linens, utensils).
 - Validate compliance with licenses (e.g., bar, health).
- 2. Room Sales & Cash Collections:** Verify room sales, billing for services (e.g., laundry, minibar), and cash collection.
 - Ensure room rates and sales from various points (e.g., restaurant, bar) match the recorded sales.
 - Validate payments by cash, card, and foreign exchange for accuracy.
- 3. Stock Management:** Regularly verify stocks like food, beverages, and hotel supplies.
 - Ensure proper documentation for stock movement, and validate against kitchen orders (KOTs) and guest orders.
 - Physical stock verification with surprise checks is crucial.
- 4. Fixed Assets & Depreciation:** Maintain a proper Fixed Assets Register, noting details like installation date, cost, and depreciation.
 - Ensure depreciation is calculated and recorded accurately.
- 5. Labor Costs & Casual Labor:** Check records and payment accuracy for casual labour and regular staff wages.
 - Ensure proper attendance systems are in place.
- 6. Cost-Revenue Comparison:** Conduct a facility-wise (e.g., swimming pool, spa) comparison of costs versus revenue to monitor performance and suggest improvements.
- 7. Compliance:** Verify compliance with statutory provisions and foreign exchange regulations.
 - Review contracts and payments related to foreign collaborations, agency commissions, and booking arrangements.
- 8. Auditor's Tasks:**
 - Ensure customer bills match consumption records.
 - Review occupancy rates and benchmark them against similar hotels.
 - Validate special receipts for events and facilities (e.g., weddings, banquets).
 - Cross-check wages and salaries with the number of employees.
- 9. Booking & Travel Agent Payments:** Ensure travel agents' commissions are paid as per agreements, and payments from agents are recovered within credit terms.
- 10. Taxes & Charges:** Confirm that all applicable taxes are included in client bills and are paid accurately.