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Subject: Advance Cost Account

Topic: Cost Audit

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M.com. Part I Sem. II

# COST AUDIT

# MEANING

- Cost audit can be defined as verification of correctness of cost accounts and a check on adherence to the cost accounting principles, plans and procedures.
- Cost Audit is an audit of efficiency of minute details of expenditure while the work is in progress, and not a post mortem examination.
- Cost Audit is mainly a preventive measure, a guide for management policy and decisions, in addition to being the barometer of performance.

- According to (CIMA) Chartered Institute of Management Accountants, London, “Cost audit is verification of the correctness of cost accounts and cost accounting plans.”
- According to Institute of Cost Accountants of India cost audit is “ a system of audit introduced by the government of India for the review, examination and appraisal of the cost accounting records and attendant information, required to be maintained by specified industries.”

# OBJECTIVES OF COST AUDIT

## BASIC OBJECTIVES

- To detect errors and to prevent frauds and possible misappropriations.
- To verify through detailed examination that the cost accounts are maintained in accordance with the principles .
- To verify the adequacy of the books of accounts and records related to cost.

# SUBSIDIARY OBJECTIVES

- To control undesirable practices .
- To determine efficiency levels at which an enterprise may operate effectively.
- To see whether the company is adequately managed

# DIFFERENCE BETWEEN COST AUDIT AND FINANCIAL AUDIT

Financial Audit	Cost Audit
It is statutory compulsory under Companies Act	It is not compulsory except in certain cases as provided under section 233B
It covers all the financial transactions recorded in financial books and financial records	It covers only cost records and cost accounts.
It is concerned with the past and historical in nature.	It concerned with forward looking approach.
It aims to examine that the business transactions have been recorded correctly	It aims to verification of cost accounts and ensures the plan prepared in this connection has been duly executed
Reporting the true and fair view of the company's earnings and state of affairs	Cost Auditor is required to report to the management except statutory audit

Financial Audit	Cost Audit
Financial aspect of the accounts is a matter of concern.	Cost aspect of account is of main concern
It is concerned with the scrutiny of reliability or otherwise of transactions	. It is concerned with the propriety and efficiency of the transactions
Financial audit may be needed in both trading or non- trading	Cost audit is needed mainly in trading where cost is involved
Financial audit is based on micro approach	Cost audit follows macro approach
Financial audit examines the accounts of the whole business	Cost audit conducted to examine a product or a factory of the business
Financial auditor is appointed by the members in the general meeting of a company as an ordinary business	Cost auditor is appointed by the board of directors of the company with the previous approval of the Government of India



# ADVANTAGES OF COST AUDIT

## 1. Advantages to the management

- Helps management to regulate production
- Provides reliable cost data for managerial decision
- Check on the role of Uneconomic Unit
- Helps in reducing the price
- Helpful in Budgetary control and Standard Costing
- Proper Valuation of Raw material and WIP
- Assessment of Profitability

## **2. Advantages to the shareholders**

- Guarantee of the proper maintenance of records
- Fair return on Investment
- Timely and proper Information

## **3. Advantages to Customers**

- Helps in Fixation of Fair price
- Increase in the standard of living

## **4. Advantages to the society**

- Tells the true cost of production
- Improves the efficiency of industrial units thereby assists in economic progress of the nation.
- Reduces the price

## 5. Advantages to the Government

- It facilitates settlement of trade disputes of the companies
- Improves working of uneconomic industrial units

# CRITICISM AGAINST COST AUDIT

- Unnecessary interference of government in the working of companies.
- It leads to duplication of work
- Expensive and luxury
- Unrealistic regulations
- Shortage of cost accountants

# PHASES OF COST AUDIT

## EFFICIENCY AUDIT

- Efficiency audit is mainly concerned with evaluation of plans and their results so as to ensure that they have been carried out efficiently.
- Efficiency audit basically starts with the examination of plans or targets and extends to the comparison of actual performance against targets and further investigates the reason for variance
- The aim is to see that the capital invested in the business gives the optimum return and the available resources are allocated among different functions and departments in such a manner so as to give optimum results.
- It also examines the opportunities of a more profitable investment of money in another area

# PHASES OF COST AUDIT

## PROPRIETY AUDIT

- The term propriety means justness or rightness.
- Propriety audit means audit of executive actions and plans which have bearing on finance and profitability of the concerns
- It is an audit of administrative action and plans having financial implications for the enterprise.
- It has been defined as “audit of executive action and plans bearing on the finance and expenditure of the company”.
- It judges the soundness of managerial decisions and suggests the means to avoid the waste in expenditure.
- The audit of PSUs conducted by the Comptroller and Auditor General of India is more of a propriety audit than a financial audit.