

## Quadrant II – Notes

**Paper Code:** COD 122

**Module Name:** Cost Audit as an Aid to Management.

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### Notes:

#### Cost audit as an aid to management

- **System functions effectively:** Cost audit ensures that the cost accounting plan is in accordance with the firm's objectives as well as the system of cost accounting that is adopted functions effectively. It ensures that the cost accounts have been maintained in accordance with the principles of costing.
- **Effective system of management reporting:** By ensuring an effective system of management reporting, cost audit brings to light all forms of waste, idle capacity and profitable and unprofitable lines of activity. Cost audit helps determine efficiency of operations.
- **Enables inter-firm comparison:** Enables inter-firm comparison. It will bring more reliability on the costing data and hence can be more effectively used for inter-firm comparison. Cost audit helps the management in inter-unit comparison which will be helpful in improving the performance of inefficient units.
- **Help in cost determination:** Help management in cost determination, cost reduction and cost control. It provides reliable cost data for managerial decisions. It helps the management in finding out the correct cost of production. It creates cost consciousness, results in improved cost accounting methods and helps to have better internal control.
- **Optimise the use of input resources:** Regular information maintained through cost accounting system and cost audit, is available for management to initiate action to optimise the use of input resources namely human and non-human resources. Wastages will be promptly reported to management so that there may not be recurrence of those wastages.

- **Regulate production:** Helps management to regulate production, exercise production control, choose economical methods of operation and help reduce working cost by pointing out waste, inefficiency, etc. Cost auditor provides the management useful information in regulating production, choosing economical methods of operation, reducing the operation cost and reformulating plans on the basis of findings.
- **Guide future policies:** Guide future policies on the basis of actual cost ascertained, all of which help to improve efficiency in the use of materials, labour and plant, maximise production and realise greater profit. It enables the management to chalk out the future policy based on the report by the cost auditor especially regarding labour, raw material, plant, etc. to maximize production and reduce the cost of the product.
- **Provides necessary information:** As an aid to decision making provides necessary information for prompt decision making. It will help management in taking important decisions because prompt, accurate and reliable information is made available to management with the help of cost audit.
- **Helps various level of management:** Helps the various level of management in arriving at operating and financial decisions. Helps Management to be effective in taking right type of decisions at the right time at different levels of management.
- **Know strength and weaknesses:** By proper appraisal of cost audit report, the management can know its strength and weaknesses. It helps in developing strengths and exercising control over the weaknesses through appropriate measures. It serves as the base for evaluating the internal-divisional performance and thus to identify their strengths and weaknesses for effective control system.
- **Helps in comparing actual results:** It helps in comparing actual results with budgeted results and point out the areas where management action is more needed. It helps in comparing actual results with budgeted by means of various analysis and points out the areas where management action is more essential.
- **Know abnormal costs:** By making comparison of costs, the cost auditor is able to know abnormal costs. Their abnormal costs are brought to the notice of the management for taking remedial measures so that their cost may not arise in the future.

- **Detection of Errors and fraud:** Errors, omission, fraud can be detected and prevented due to the effective auditing of cost accounts. It acts as an effective managerial tool for the detection of errors, frauds, inconsistencies and irregularities so that reliable and smooth functioning of the system is continued.
- **Improve the efficiency of the organisation:** It improves the efficiency of the organisation by achieving the ultimate targets at the lowest possible cost. It is also done by constant review, revision and checking of routine procedure and methods of the cost accounting system.
- **Satisfy management:** Besides, the objective is also to satisfy management whether the accounting records reflect a true and fair view of cost which is so important for price fixation, policy formulation and decision making by management.
- **Increase the productivity:** It can increase the productivity by pin-pointing the weak area of cost of production. Productivity improvement can be done by identifying the reasons for wastages and inefficiencies and overcoming the same through corrective measures.
- **Analyse the cost department efficiency:** The inefficiencies of the personnel's working in the cost department may be revealed. Cost accounting system analysed as part of cost audit also reflects the working efficiency of costing department.
- **Measure the profitability:** It can measure the profitability of the organisation. It reflects the performing ability of the organisation not only in terms of production, cost, productivity, efficiency, etc. but also helps in assessing the profitability level of the organisation over the years. It can ensure accurate determination of profit for tax purposes.
- **Analysis of variances** is facilitated with cost audit because a comparison of actual with standard production and sales is made. Hence, the systems of standard costing and budgetary control will be gainfully applied with cost audit.
- **Improves effectiveness of cost control:** It improves the effectiveness of cost control and cost presentation by introducing efficient routines, reducing expenditure and ensuring promptness. Cost audit will be helpful in implementing the system of budgetary control and standard costing because cost audit lays emphasis on the verification of cost accounts and a check on the adherence to the cost accounting plan.