

An Study Evaluating Cost accounting records and Cost Audit In Engineering companies

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Abstract

Engineering industries plays a vital role in the Indian economy. It has connections with various other sectors of the economy. The revenue generated due to these sectors also contributes to the enhancement of the national economy. In today's economy, these industries are facing the challenge of cost competitiveness. Thus with this perspective it is thoughtful to study the various tools of cost control and cost reduction. And to achieve it, cost audit is important which should be applied to all the manufacturing industries. So with an intention to increase the earning capacity of the industries & cost competitiveness it was felt necessary to study the various provisions applicable to these industries. The study covered the Engineering industries in Pune region, Pimpri-Chinchwad MIDC and also other SMEs from other parts of Pune. The period under the study was of 5 years. The effectiveness of the cost accounting records, its rules & regulations and cost audit in relation to cost competitiveness of the engineering companies was studied. Problems faced in cost audit were also investigated and solutions were suggested to overcome those.

Keywords- Cost Accounting Records, Cost Audit, Engineering Companies

INTRODUCTION

Business sustainability depends greatly on cost and competitiveness. In today's liberalized and growing economy effective use of productive resources such as money labor, machine is the main challenge. With this perspective, the Ministry of corporate affairs in India introduced the tool of maintenance cost accounting records and cost audit for the managers, to help them in better control over the utilization of productive resources and accurate decision making. The cost auditors are so appointed to conduct the Cost audit. Also they are given the responsibility to report about compliance of Cost accounting record rules by the manufacturing organization. But no standard formats are prescribed for the compliance report and Performance appraisal report to be submitted to the authorities after the conducting of the audit.

Engineering industry in India:

The Indian engineering industry accounts for 27 per cent of the total factories in industrial sector and represents 63 per cent of the overall foreign collaborations. The country is increasingly attaining global recognition especially for its low-cost, high-tech frugal innovation technology, according to a World Bank study named 'Unleashing India's Innovations', International companies are outsourcing industrial engineering design tasks to India in sectors like semiconductors, automotive hybrid technologies, next-gen routers in telecom, power generation equipment, aerospace, avionics and consumer electronics, besides setting up research and development (R&D) centres in India. Engineering exports during April-December 2012-13 stood at US\$ 45.33 billion.

STATEMENT OF THE PROBLEM

The maintenance of the cost accounting records is necessary for all the manufacturing industries by the controlling authorities. Various rules & regulations have been laid down for providing information regarding maintenance of cost accounting records. However it is observed that the cost accounting records rules are not followed by all the engineering manufacturing industries.

Also Cost audit is made mandatory for certain class of manufacturing industries. But various problems are faced in conducting the cost audit. It is thought as a time consuming affair in addition to financial audit. . This thinking has made the organizations reluctant to comply with these provisions and are having casual approach towards it. But performance of cost audit will make a positive impact on the earning capacity of an organization.

RESEARCH OBJECTIVES

- To study the present cost audit system in engineering companies.
- To find out the problems of maintaining cost accounting records.
- To study the effect of maintaining cost accounting records to attain cost competitiveness.
- To study the problems faced by the companies in undertaking the cost audit.

- To provide suggestion for efficient cost audit system in the companies.

Survey of literature

1. ICAI, from time to time, releases various standards in order to bring about uniformity in the cost accounting and record keeping. So far it has issued 24 Cost Accounting Standards. Review of these standards show the details that have been prescribed for maintenance of cost accounts and records.

2. Review of Generally Accepted Cost Accounting Principles (GACAP) issued by the ICAI lay down the following framework for the principles –

- a. The principles should focus on value drivers
- b. Costing to be done with a purpose
- c. Cost models must be reality driven
- d. They must be material and cost effective
- e. They should facilitate comparability and consistency
- f. They must be transparent and auditable

3. In the Exposure Draft to Practical Guide to Standards on Cost Auditing issued by the ICAI it has been stated that The Standards on Cost Auditing are required to guide the members in audit of cost statements so that the audit is performed in an efficient and effective manner to ensure achievement of objectives with available resources and securing coordination with the auditee on audit work as mandated under section 148 of the Companies Act, 2013.

The draft has stated 3 phases of a cost audit as under –

Planning

- Understanding the entity and its environment
- Risk identification and Strategy
- Risk and materiality assessment

Performing

- Execution
- Audit Procedures
- Audit Findings

Reporting

- Conclusion
- Reporting

Population, Sample size and technique –

Population -

There are around 4000 engineering companies in Pune. According to another source there are around 1500 engineering companies in Pune. Cost accounting and cost audit is a slightly specialized aspect. Therefore, it was decided to have the population as under – a. 50 top big engineering companies from Pimpri-Chinchwad MIDC and b. 1300 other units.

Sample Selection-

The nature of research being qualitative the demand for accurate quantitative analysis was not there. Following methodology of sample selection was adopted –

1. Choose all the big 50 companies from Pimpri-Chinchwad MIDC
2. Choose randomly another 100 companies from rest of the companies so as to get responses from
3. Fix a sample size of 100 units (50 big companies and 50 small companies from 100 companies chosen)
4. Generate unique 100 random numbers in the range of 1 to 1300
5. Select 100 units based on random numbers generated
6. Send the questionnaire to these 50 + 100 = 150 units
7. Close the survey on receipt of first 100 company responses (total 300 responses – one each from FM, production manager and cost accounting employees)
8. Then send questionnaire to cost auditors of these 100 companies, wherever applicable

Summarized data analysis –

The following table summarizes key parameters and the overall interpretation –

Sr. No.	Parameter	Value(s) –	Interpretation
1	Agreement on effectiveness of existing cost accounting/audit system	12% respondents agreed	Since 88% respondents disagreed it cannot be accepted that current cost accounting/audit systems employed in the engineering industry is effective
2	Agreement on whether proper records are maintained under a system	13% respondents agreed	Since 87% respondents disagreed it cannot be accepted that current cost accounting systems employed in the engineering industry facilitate proper maintenance of cost records
3	Agreement on whether there are no problems in cost audit	12% respondents agreed	Since 88% respondents disagreed it cannot be accepted that current cost audit doesn't have problems
4	Agreement that suggested solutions are effective	86%	Since 86% respondents agreed it can be accepted that suggested solutions can be effective

FINDINGS

1 –Overall responses (400 respondents) -

Qn. No	Question	Max A/DA %	Max A/DA
1.1	Organizations have positive attitude towards costing	92%	Disagree
1.2	Recognition of costing as an independent function	88%	Disagree
1.3	Costing considered more of a compliance	93%	Agree
1.4	Understanding of benefits by management	91%	Disagree
1.5	Benefits not communicated properly	82%	Agree
1.6	Accounting overshadows costing	83%	Agree
1.7	Advanced capabilities of costing	79%	Agree
2.1	Overall resources adequate for costing	87%	Disagree
2.2	Manpower resources adequate for costing	88%	Disagree
2.3	IT resources adequate for costing	85%	Disagree
2.4	Infrastructure adequate for costing	87%	Disagree
2.5	Devotion of time for costing	89%	Disagree
3.1	Costing system - robust & independent	86%	Disagree
3.2	Costing system - neatly designed	85%	Disagree
3.3	Costing system - ability to capture raw-material finer data	87%	Disagree
3.4	Costing system - ability to capture labor finer data	88%	Disagree
3.5	Costing system - ability to capture OHs finer data	87%	Disagree
3.6	Costing system - leveraging IT	89%	Disagree
3.7	Costing system - facilitation of cost control	86%	Disagree
3.8	Costing system - facilitation of cost reduction	85%	Disagree
3.9	Costing system - facilitation of gathering other information	90%	Disagree
3.10	Costing system - generation of costing P & L	88%	Disagree
3.11	Advancement towards models like ABC	90%	Disagree
4.1	Contribution of costing in cost control/reduction	88%	Disagree
4.2	Difficulty in measuring outcomes	83%	Agree
4.3	Unreasonably high expectation from costing	83%	Agree
4.4	Costing information used as secondary	84%	Agree
4.5	Benefits for financial management	88%	Disagree
4.6	Improvement in cost standards	88%	Disagree
4.7	More of MIS than MCS	92%	Agree
5.1	Cost Audit viewed as form-filling	94%	Agree

1. Attitude towards costing system by and large is negative. This can be gauged from the average of responses from the 400 respondents to questions in the 1st section of the questionnaire.

Qn. No	Question	Max A/DA %	Max A/DA
1.1	Organizations have positive attitude towards costing	92%	Disagree
1.2	Recognition of costing as an independent function	88%	Disagree
1.3	Costing considered more of a compliance	93%	Agree
1.4	Understanding of benefits by management	91%	Disagree
1.5	Benefits not communicated properly	82%	Agree
1.6	Accounting overshadows costing	83%	Agree
	Average	88%	

Thus, on an overall basis 88% of the respondents agree that there is a negative attitude towards costing.

2. At the same time 79% of the respondents believe that costing has potential in terms of predictive analysis apart from descriptive analysis

3. In terms of provision of resources for costing in organizations the findings are as under –

Qn. No	Question	Max A/DA %	Max A/DA
2.1	Overall resources adequate for costing	92%	Disagree
2.2	Manpower resources adequate for costing	88%	Disagree
2.3	IT resources adequate for costing	93%	Disagree
2.4	Infrastructure adequate for costing	91%	Disagree
2.5	Devotion of time for costing	82%	Disagree
	Average	87%	

On an average 87% of the respondents have stated that resources for costing are inadequate.

4. On the issue of evaluation of the costing system in place, the findings are –

Qn. No	Question	Max A/DA %	Max A/DA
3.1	Costing system - robust & independent	86%	Disagree
3.2	Costing system - neatly designed	85%	Disagree
3.3	Costing system - ability to capture raw-material finer data	87%	Disagree
3.4	Costing system - ability to capture labor finer data	88%	Disagree
3.5	Costing system - ability to capture OHs finer data	87%	Disagree
3.6	Costing system - leveraging IT	89%	Disagree
3.7	Costing system - facilitation of cost control	86%	Disagree
3.8	Costing system - facilitation of cost reduction	85%	Disagree
3.9	Costing system - facilitation of gathering other information	90%	Disagree
3.10	Costing system - generation of costing P & L	88%	Disagree
3.11	Advancement towards models like ABC	90%	Disagree
	Average	87%	

On an average 87% of the respondents have negated the effectiveness of the costing system in place.

5. Whether it is basic things like ability to capture data related to cost elements to advancement to ABC, respondents have overwhelmingly rejected the effectiveness of the costing systems in place.

6. Findings related to outcome of the systems are as under –

Qn. No	Question	Max A/DA %	Max A/DA
4.1	Contribution of costing in cost control/reduction	88%	Disagree
4.2	Difficulty in measuring outcomes	83%	Agree
4.3	Unreasonably high expectation from costing	83%	Agree
4.4	Costing information used as secondary	84%	Agree
4.5	Benefits for financial management	88%	Disagree
4.6	Improvement in cost standards	88%	Disagree
4.7	More of MIS than MCS	92%	Agree
	Average	87%	

On an average 87% of the respondents have expressed negative views on the outcome of the system.

7. An interesting finding is that most of the respondents have stated that it is difficult to measure the outcome of the costing system.

8. Findings on cost audit problems are as under –

Qn. No	Question	Max A/DA %	Max A/DA
5.1	Cost Audit viewed as form-filling	94%	Agree
5.2	Stakeholders have unnecessarily high expectations	82%	Agree
5.3	Government uses cost audit data	79%	Agree
5.4	Same old format of cost audit report	83%	Agree
5.5	Government changes rules frequently	94%	Agree
5.6	Cost audit a dead exercise	95%	Agree
5.7	Lack of technical knowledge hampers cost audit	94%	Agree
5.8	Lack of trained staff hampers cost audit	84%	Agree
	Average	88%	

On an average 88% of the respondents have agreed that there are various problems in cost audit.

1. Solutions suggested have been responded with lot of positivity as under –

Qn. No	Question	Max A/DA %	Max A/DA
6.1	Combine cost and financial audit	81%	Agree
6.2	Scope for leveraging IT	94%	Agree
6.3	CRA-4 can be simplified	90%	Agree
6.4	Suggestions from company	83%	Agree
6.5	Make things mandatory like S.135	83%	Agree
	Average	86%	

On an average the suggestions have fetched 86% positive response.

CONCLUSION

Overall attitude towards costing is not very positive. This is a major concern. The apathy towards costing, cost records and cost audit has been expressed by all the types of respondents. Respondents have stated they there is a gap in understanding of the benefits of these systems on the part of the management. Better communication in this regard can help. It is quite clear that finance and/or accounts overshadow costing. All the respondents have further stated that their organizations lack adequate resources for costing. One could have digested this fact for organizations that are not required to maintain cost accounting records as per law. However, the same is the case even with those organizations that are required to maintain cost accounting records as per law. This clearly speaks of the stature of costing function in the organizations. The systems in place are operating at a dismal level. They in fact, cannot be called as systems. The fact that even basic things like capturing of elementary costing data related to raw-material, labor and OHs is not satisfactory points out towards the poor level of the systems. Given the sorry state of affairs with the system itself the outcomes are bound to be poor. The system is not producing any worthwhile outcome has been clearly and overwhelmingly stated by all the respondents. The system is a failure in all the 3 areas – cost ascertainment, cost control and cost reduction. It is indeed disheartening to note this. Moving onto cost audit, all the respondents from the organizations to whom cost audit is applicable has stated that there are serious issues with cost audit. It is perceived as a mere form-filling activity. At the same time expectations are very high. But if the inputs to a system and the processing is poor, it is actually futile to expect anything useful in the form of output. The dullness and the deadness with the activity has been clearly highlighted. What is surprising is that the activity per se is actually quite important. Yet the way it is handled, it has lost all its charm and importance. On the other hand, it is considered as a head-ache. Finally the respondents have given highly positive response to the suggestions that have been proposed. Whether it is the idea of combining cost audit with financial audit or making it compulsory, all the suggestions have fetched highly encouraging response.

Suggestions –

A total of 5 suggestions were proposed keeping in mind the problems and practicality of implementation.

These suggestions are listed as under –

- Combine cost and financial audit
- Explore and leverage IT
- Simplification of cost audit reports
- Suggestions from company instead of suggestions from the cost auditor
- Make things mandatory like S.135

Responses were sought from all the respondents to test the acceptability of these. The results of the responses on the 5 solutions proposed were as under –

Qn No.	Suggestion	% agreement
6.1	Combine cost and financial audit	81%
6.2	Scope for leveraging IT	94%
6.3	Simplification of cost audit reports	90%
6.4	Suggestions from company	83%
6.5	Make things mandatory like S.135	83%
	Average	86%

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