

**Guidance Note**  
**on**  
**Cost Accounting Standard**  
**on**  
**Direct Expenses**  
**(CAS-10)**



Issued by

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## FOREWORD



The Council of the Institute of Cost Accountants of India in its meeting held on 21<sup>st</sup> July 2013 has approved the release of the Guidance Note on Cost Accounting Standard on Direct Expenses (CAS 10) as recommended by the Cost Accounting Standards Board.

I am pleased that the Technical Directorate is continuing its efforts to develop and release Guidance Notes on various CAS. This Guidance Note emanated from the pressing need for an appropriate Guidance Note from the Institute on Direct Expenses being one of the important elements of cost of production.

I am confident that this Guidance Note will help the members and other readers to properly understand and apply / implement the various principles of Cost Accounting Standard on Direct Expenses.

I wish to place on record my high appreciation for CMA M.Gopalakrishnan, Chairman and all the members of CASB for 2012-2013.

I am thankful to CMA Rakesh Singh, Chairman CASB for 2013-2014 for bringing out this useful guiding literature for the members.

  
14-8-2013  
(CMA S.C. Mohanty)



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## PREFACE



The Cost Accounting Standards Board is continuing to lead initiatives to fulfill the need for the Guidance Notes on various Cost Accounting Standards developed by the Institute of Cost Accountants of India. I am pleased to present the Guidance Note on Cost Accounting Standard on Direct Expenses (CAS 10). This Guidance Note deals with the Principles and Methods as provided in CAS on Direct Expenses for appropriately determining the cost of production of a product or a service.

I am thankful to the members of the Cost Accounting Standards Board of the Institute for their valuable contribution in finalization of this Guidance Note.

I am also thankful to CMA Suresh Chandra Mohanty, President of the Institute for his guidance and professional support in carrying out activities of the CASB.

I would also like to place on record the efforts put in by the CASB Secretariat, headed by Dr. S K Gupta, Director (Technical) and Shri M L Mehta (Advisor), for all the initiatives and effective co-ordination in compiling this document. I am sure that the Secretariat will come out with more Guidance Notes in the near future.

I am confident that this Guidance Note would be well received by the members.

(CMA RAKESH SINGH)

Chairman, CASB



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**Guidance Note on**

***Cost Accounting Standard on Direct Expenses (CAS-10)***

The Council of the Institute of Cost Accountants of India has issued the Cost Accounting Standard -10 (CAS-10) on Direct Expenses which lays down a set of principles and methods of classification, measurement and assignment of Direct Expenses for determination of the cost of product or service and the presentation and disclosure in the cost statements. The Cost Accounting Standards have been set in bold italic type and reference number of the standard has been retained.

The Guidance Note deals with principles and methods as provided in the CAS-10 and practical aspects in connection with the determination of Direct Expenses for a product or service. In the preparation of cost statement and its attestation, Direct Expenses should be determined with reference to CAS-10.

The Companies (Cost Accounting Records) Rules, 2011 provide that every company, including a foreign company defined under section 591 of the Companies Act, 1956 which is engaged in production, processing, manufacturing or mining activities have to maintain cost accounting records in accordance with the Generally Accepted Cost Accounting Principles (GACAP) and Cost Accounting Standards issued by the Institute, to the extent these are found to be relevant and applicable. The above Rules further provide that these will be applicable to companies wherein:

- (a) aggregate value of net worth as on the last date of the immediately preceding financial year exceeds five crores of rupees; or
- (b) the aggregate value of the turnover made by the company from sale or supply of all products or activities during the immediately preceding financial year exceeds twenty crores of rupees; or
- (c) the company's equity or debt securities are listed or are in the process of listing on any stock exchange whether in India or outside India.

The Companies (Cost Audit Report) Rules 2011 cast a duty on a Cost Auditor appointed under Section 233B of the Companies Act, 1956 to certify inter alia that books and records maintained by the company are in conformity with the Cost Accounting Standards issued by the Institute to the extent these are found to be relevant and applicable.



## Chapter 1

## Introduction

Direct Expenses are the expenses relating to manufacture of a product or rendering of a service which can be identified or linked with the cost object other than those incurred on direct material and direct employee cost.

Examples of Direct Expenses are royalties charged on the basis of production, job charges, hire charges for use of specific equipment for a specific product, cost of special designs or drawings for a product, software services specifically required for a ~~job~~ product, travelling expenses for a specific product. These are dealt below:-

(i) Royalty: Royalty is to be paid to Collaborators or technology suppliers in terms of agreement entered with them. It is payable either in relation to production or sales during the accounting period. If royalty payment is to be computed on the basis of production -the same should be treated as Direct Expenses. Royalty for Upgrading Technology for the product will be included in cost of production, irrespective of whether it is paid on production basis or sales basis. Royalty for Marketing and Distribution, if paid, will be excluded from cost of production.

(ii) Technical Assistance/Know-how fees:

Technical Assistance/know-how fees are paid for acquiring Technical assistance /Know-how. Custom duty paid/payable at the time of import of technical knowhow is treated as part of cost of technical knowhow. This is to be reflected as a line item under paragraph 5 – Abridged Cost Statement of the Companies (Cost Audit Report) Rules, 2011.

(iii) Job/Processing charges for a product: Job Work Charges/Processing Charges which are directly identified or linked with the products will form part of Direct Expenses. Job charges may be for a specific product or for job on contract basis for a product.

(iv) Hire charges for tools etc: Hire charges in respect of tools and equipments which can be directly identified with a particular product will form part of Direct Expenses. Hire charges for



tools for general use is in the nature of indirect Expenses and is to be included in production overheads.

(v) Charges for a particular product designing etc: Product design charges in respect of tools which can be directly identified with a particular product will form part of Direct Expenses. For example, special design was to be developed for a tool as per customer requirements and such expenses incurred in designing of a tool for the product would be treated as Direct Expenses for the product.



## CHAPTER 2

## Definition

### 4. Definitions

**4.1 Abnormal cost:** *An unusual or atypical cost whose occurrence is usually irregular and unexpected and/ or due to some abnormal situation of the production or operation.*<sup>1</sup>

**4.2 Cost Object:** *This includes a product, service, cost centre, activity, sub-activity, project, contract, customer or distribution channel or any other unit in relation to which costs are ascertained.*<sup>2</sup>

**4.3 Direct Employee Cost:** *The cost of employees which can be attributed to a cost object in an economically feasible way.*<sup>3</sup>

**4.4 Direct Expenses:** *Expenses relating to manufacture of a product or rendering a service, which can be identified or linked with the cost object other than direct material cost and direct employee cost.*<sup>4</sup>

**4.5 Direct Material Cost:** *The cost of material which can be attributed to a cost object in an economically feasible way.*<sup>5</sup>

**4.6 Finance Costs:** *Costs incurred by an enterprise in connection with the borrowing of funds.*

**4.7 Imputed Costs:** *Hypothetical or notional costs, not involving cash outlay, computed for any purpose.*<sup>6</sup>

**4.8 Overheads:** *Overheads comprise of indirect materials, indirect employee costs and in Direct Expenses which are not directly identifiable or allocable to a cost object.*<sup>7</sup>

**4.9 Standard Cost:** *A predetermined cost of resource inputs for the cost object computed with reference to set of technical specifications and efficient operating conditions.*

<sup>1</sup> Adapted from CAS 1 paragraph 6.5.19

<sup>2</sup> Adapted from CIMA Terminology

<sup>3</sup> Adapted from CAS 1 paragraph 6.2.4 (Direct labour cost)

<sup>4</sup> Adapted from CAS 1 paragraph 6.2.6

<sup>5</sup> Adapted from CAS 1-6.2.3

<sup>6</sup> Adapted from CAS 1 paragraph 6.5.13

<sup>7</sup> Adapted from CAS 3 paragraph 4.1





**CHAPTER 3**

**Principles of Measurement**

**5. Principles of Measurement:**

**5.1 Identification of Direct Expenses shall be based on traceability in an economically feasible manner.**

Measurement of Direct Expenses depends upon identification and traceability to cost object/product in an economically feasible manner. *The cost object includes a product, service, cost centre, activity, sub-activity, project, contract, customer or distribution channel or any other unit in relation to which costs are ascertained.*<sup>8</sup> It is the logical sub-unit for accumulation of cost. If an expense can be identified with a cost object /product and is sufficient material in amount, it is treated as Direct Expenses. It must also be economically feasible to associate Direct Expenses with units produced. “Economically feasible manner” means cost effectiveness for identification of direct expense and such identification should not be too expensive in relation to expected benefits.

**5.2.1 Direct Expenses incurred for the use of bought out resources shall be determined at invoice or agreed price including duties and taxes, and other expenditure directly attributable thereto net of trade discounts, rebates, taxes and duties refundable or to be credited.**

Direct Expenses are incurred for the use of bought out resources.

These are:

Royalties charged on production, job charges, hire charges for use of specific equipment for a specific product, cost of special designs or drawings/ software services specifically required for a product and the like.

In such case determination of Direct Expenses incurred for a cost object will depend upon the type of Direct Expenses. For Example, royalty payment is to be determined in terms of

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<sup>8</sup> Adapted from CIMA Terminology



collaboration agreement. Job /hire charges will be as per work order and invoice. It shall include duties and taxes and other expenditure (freight/transport). Direct Expenses are to be net of any discount, rebate, taxes and duties (VAT/CENVAT) refundable, if any.

If any design and drawing is imported, custom duty payable/paid, insurance and freight/courier charges if any, will form part of the cost. Supplier will be paid full amount as per invoice. In case Excise Duty/Cess and VAT are refundable, cost of these will be net of these refunds.

***5.2.2 Direct Expenses other than those referred to in paragraph 5.2.1 shall be determined on the basis of amount incurred in connection therewith.***

Dies, tools, scaffolding, and so on are sometime produced internally. Production Cost of these items is to be determined taking into account the direct material cost, direct employee cost, Direct Expenses and production overhead. As and when a decision is taken to produce dies/tools in house, all the above expenses are recorded. Direct material cost is to be measured as per paragraph 5.1 of CAS on Material Cost (CAS-6). The receipt of material shall be valued at purchase price including duties and taxes, freight inwards and other expenditure attributable to procurement. The material cost is to be adjusted for trade discounts, rebates, taxes and duties refundable or to be credited by the taxing authorities.

Similarly benefit of import entitlement is to be credited.

Direct employee cost for internally produced dies, tools etc is to be measured as per paragraph 5.1 of CAS on Employee Cost (CAS-7). It shall take into account the gross pay including all allowances payable along with the cost to the employer of all the benefits. The share of production overhead is to be determined as per CAS-3. Expenses incurred for development and improvement of the process for existing product shall be identified as Direct Expenses.

***5.2.3 Direct Expenses paid or incurred in lump-sum or which are in the nature of 'one – time' payment, shall be amortised on the basis of the estimated output or benefit to be derived from such Direct Expenses.***



In case of lump sum payment or one-time payment, for which benefit is expected in future period, it shall be written off over its useful life. For example Technical know-how fee paid shall be amortized over its useful life.

***5.3 If an item of Direct Expenses does not meet the test of materiality, it can be treated as part of overheads.***

Whether an item of expense is to be treated as Direct expense or indirect expense, is to be determined in terms of materiality of an item. Materiality has not been defined in the standard. Materiality depends on the size and nature of item judged in particular circumstances. An item of expense is considered material if its omission could influence the economic decisions of users of the cost statement. For example Royalty is a material item of cost. It is to be indicated in the cost statement as a separate item under the Companies (Cost Audit Report) Rules, 2011 and not aggregated with production overhead even though it may not be significant in term of the total cost of the product. In another case, job charges can be identified with the cost object but not being material and significant in value, it may be treated as Production overhead.

***5.4 Finance costs incurred in connection with the self generated or procured resources shall not form part of Direct Expenses.***

Finance costs are interest and similar charges payable for borrowed funds. Finance costs are excluded from Direct Expenses.

***5.5 Direct Expenses shall not include imputed costs. In case of goods produced for captive consumption, treatment of imputed cost shall be in accordance with Cost Accounting Standard – 4 (CAS-4).***

Imputed cost does not involve at any time any outright expense or cash outlay. As such it is to be excluded from Direct Expenses. However in case of goods produced for captive consumption, imputed cost is to be considered while determining the cost of goods produced as per Cost Accounting Standard – 4 (CAS-4).

Paragraph 5.14 of CAS-4 provides that In case any input material, whether of direct or indirect nature, including packing material is supplied free of cost by the user of the captive product, the landed cost of such material shall be included in the cost of production. Landed cost of



inputs received free of cost should be calculated as per the guidelines relating to material cost. Paragraph 5.15 of CAS-4 further provides that imputed cost is to be charged for Moulds, Tools, Dies & Patterns etc received free of cost. The amortization cost of such items shall be included in the cost of production. Amortisation should be done on the basis of estimated production that can be achieved during the life of the Mould, Tool, Die or Pattern.

**5.6 Where Direct Expenses are accounted at standard cost, variances due to normal reasons shall be treated as part of the Direct Expenses. Variances due to abnormal reasons shall not form part of the Direct Expenses.**

If standards have been fixed for any Direct Expenses, such as job charges, and the like, variance of Direct Expenses shall be analysed. Variance due to normal reason shall form part of Direct Expenses and any abnormal variance shall be excluded from Direct Expenses. The variance analysis enables management to observe the extent to which actual Direct Expenses are differing from predetermined estimates.

**5.7 Any Subsidy/Grant/Incentive or any such payment received/receivable with respect to any Direct Expenses shall be reduced for ascertainment of the cost of the cost object to which such amounts are related.**

Subsidy and grant received/receivable for Direct Expenses should be deducted therefrom.

**5.8 Any abnormal portion of the Direct Expenses where it is material and quantifiable shall not form part of the Direct Expenses.**

Abnormal cost has been defined under paragraph 4.1 of CAS-10. The rationale of exclusion is that inclusion of such items in the cost will make the cost not comparable with a normal situation. Such an aberration is avoided to understand the cost in a better perspective for any purpose.



**Illustration:**

Certain Direct Expenses were incurred on design and drawing , but due to change in the specification of the product, these drawings were abandoned and were treated as abnormal cost as being material and quantifiable and will not form part of the Direct Expenses.

***5.9 Penalties, damages paid to statutory authorities or other third parties shall not form part of the Direct Expenses.***

Penalties/damages are levied by the statutory authorities for non-compliance with statutory requirements/delay. Penalties/Damages are an abnormal cost and do not form part of the Direct Expenses. It is charged to Profit & Loss account.

***5.10 Credits/ recoveries relating to the Direct Expenses, material and quantifiable, shall be deducted to arrive at the net Direct Expenses.***

If any credit is available relating to Direct Expenses, it is to be deducted from the Direct Expenses for a product.

***5.11 Any change in the cost accounting principles applied for the measurement of the Direct Expenses should be made only if, it is required by law or for compliance with the requirements of a cost accounting standard, or a change would result in a more appropriate preparation or presentation of cost statements of an organisation.***

Principles applied for determining the Direct Expenses be followed consistently. For example profit sharing bonus paid to employees was not to be treated as a part of production cost but of “Total cost of Sales” under previous Cost Audit Report Rules 1996.This principle was being followed consistently but due to change in the principle with the notification of the Companies (Cost Accounting Records) Rules,2011 bonus is now part of the employee cost and forms part of cost production. Thus change in cost accounting principle/law for determining the cost can be made when required by any law as illustrated above or for compliance with cost accounting standards or it results in more appropriate presentation of cost statement.



**CHAPTER 4**

**Assignment of Costs**

**6. Assignment of costs**

**6.1 Direct Expenses that are directly traceable to the cost object shall be assigned to that cost object.**

Assignment of Direct Expenses involves establishing a suitable procedure to identify and record the same by cost object. Invoice/Agreement/Job on contract are the source documents indicating details of Direct Expenses. For internally produced tools, Work Order is the source for assignment of cost. These documents record the cost object /cost centre/product, and items listed are charged at their acquisition cost.



**CHAPTER 5**

**Presentation**

**7. Presentation**

**7.1 Direct Expenses, if material, shall be presented as a separate cost head with suitable classification.** For example

- Subcontract charges
- Royalty on production

Direct Expenses are to be reflected in the cost statement as a separate item of expense if these are material. Materiality has not been defined in the standard. What is considered material or immaterial depends upon the situation.

The following criteria can be applied for determining the materiality. No one criterion is determinative in and of itself.

- The absolute amount – the larger the amount , the more likely that it is material.
- The amount of cost of a product compared to the amount of Direct Expenses under consideration – the greater the proportion of the considered amount of Direct Expenses versus the cost of product, the more likely it is material.
- The relationship of Direct Expenses with product.
- The cumulative impact of individual immaterial items - do they offset one another or do they accumulate in one direction (increase or decrease).
- The cost of determining the Direct Expenses.



**CHAPTER 6**

**Disclosures**

**8. Disclosures**

**8.1 The cost statements shall disclose the following:**

**8.1.1 The basis of distribution of Direct Expenses to the cost objects/ cost units.**

Disclosure is to be made relating to the basis adopted for distribution of direct cost to product/ unit in the cost statement or by way of foot note.

**8.1.2 Quantity and rates of items of Direct Expenses, as applicable.**

Disclosure is to be made in the cost statement both in quantity and rates of items of Direct Expenses. Certain Direct Expenses are paid in lump sum. Details where quantitative information cannot be disclosed, shall be mentioned in the cost statement.

Example:

Royalty of Rs 10.25 lakhs has been determined @ 3% of cost of Production.

**8.1.3 Where Direct Expenses are accounted at standard cost, the price and usage variances**

If the Direct Expenses are accounted at standard cost , the price and usage variances are to be disclosed in the cost statement.

**8.1.4 Direct Expenses representing procurement of resources and expenses incurred in connection with resources generated.**

Disclosure is to be made for Direct Expenses both for procurement of resources and resources generated internally:

Example:





Direct Expenses :

1. Special Design and Drawing procured	<u>Rs 250,000</u>
2. Tools & Dies produced internally:	
Material	Rs 36000
Labour	Rs 12000
Overhead	<u>Rs 6000</u>
Total	<u>Rs 54,000</u>

**8.1.5 Direct Expenses paid/ payable to related parties<sup>9</sup>.**

The related parties have been defined under the Companies (Accounting Standards) Rules, 2006. If Direct Expenses is paid /payable for any supply procured from or supplied to related parties, its relationship, nature of transaction viz quantity, rate, other terms/ conditions of procurement are to be disclosed. The objective of disclosure is to ascertain that the transaction is at arm's length and on purely commercial terms.

**8.1.6 Direct Expenses incurred in foreign exchange.**

Payment made in foreign exchange for the Direct Expenses relating to import of design/drawing, royalty etc shall be indicated in the cost statement as a footnote.

Example: Royalty paid in foreign exchange as per Collaboration Agreement:

Royalty was paid US \$ 5600 on production during the current year (Previous year US \$ 4500).

**8.1.7 Any Subsidy/Grant/Incentive and any such payment reduced from Direct Expenses.**

Any subsidy/grant/incentive received relating to Direct Expenses is to be deducted from the Direct Expenses of the product and disclosure made accordingly by way of a foot note

**8.1.8 Credits/recoveries relating to the Direct Expenses.**

If any credit or recovery is considered while determining the Direct Expenses, the same shall be disclosed in the body of the cost statement.

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<sup>9</sup> Related party as per the applicable legal requirements relating to the cost statement as on the date of the statement



### **8.1.9 Any abnormal portion of the Direct Expenses**

Abnormal portion of Direct Expenses of a product is to be excluded from the cost of the product as the same has not contributed to the product. Disclosure is to be made by way of foot note in the cost statement.

For example : During the year there was a fire resulting in loss of special design and drawings developed for improved process valued at Rs 2.50 lakhs. The same has been excluded from the development cost.

### **8.1.10 Penalties and damages paid etc. excluded from the Direct Expenses.**

Penalties and damages paid are not an item of cost as these are levied for non compliance with regulatory /contractual requirements. These are to be quantified and excluded from cost and disclosure made as a footnote in the cost statement.

### **8.2 Disclosures shall be made only where material, significant and quantifiable.**

Level of materiality and significance has not been stated in the standard. What is considered material or immaterial depends upon the situation. A piece of information is material, if its non disclosure could influence the decision of user.

### **8.3 Disclosures shall be made in the body of the Cost Statement or as a foot note or as a separate schedule.**

Disclosure in the body of cost statement will depend on nature and materiality of Direct Expenses. If it forms material part of the Direct Expenses and can be identified with a product the same shall be disclosed in the cost statement otherwise, disclosures may be by way of foot note.

### **8.4 Any change in the cost accounting principles and methods applied for the measurement and assignment of the Direct Expenses during the period covered by the cost statement which has a material effect on the Direct Expenses. Where the effect of such change is not ascertainable wholly or partly the fact shall be indicated.**



Cost Accounting principles, and methods applied for the measurement and assignment of Direct Expenses are to be applied consistently between one period and another uniformly applied for different Direct Expenses. If any change is made in these principles and methods which results in material impact on the cost of product, the same shall be disclosed in the cost statement or by a foot note. In case the impact of change in principles and methods of cost accounting is not ascertainable, the fact is to be disclosed by a note to the cost statements.



**ANNEXURE I**

**(CAS-10)**

**COST ACCOUNTING STANDARD ON DIRECT EXPENSES**

The following is the COST ACCOUNTING STANDARD – 10 (CAS-10) issued by the Council of The Institute of Cost and Works Accountants of India on “DIRECT EXPENSES”, for comments. In this Standard, the standard portions have been set in ***bold italic*** type. This standard should be read in the context of the background material which has been set in normal type.

**1. Introduction**

**1.1** This standard deals with the principles and methods of determining the Direct Expenses.

**1.2** *This standard deals with the principles and methods of classification, measurement and assignment of Direct Expenses, for determination of the cost of product or service, and the presentation and disclosure in cost statements.*

**2. Objective**

*The objective of this standard is to bring uniformity and consistency in the principles and methods of determining the Direct Expenses with reasonable accuracy.*

**3. Scope**

*This standard should be applied to cost statements, which require classification, measurement, assignment, presentation and disclosure of Direct Expenses including those requiring attestation.*



#### 4. Definitions

The following terms are being used in this standard with the meaning specified.

**4.1 Abnormal cost:** *An unusual or atypical cost whose occurrence is usually irregular and unexpected and/ or due to some abnormal situation of the production or operation.*<sup>10</sup>

**4.2 Cost Object:** *This includes a product, service, cost centre, activity, sub-activity, project, contract, customer or distribution channel or any other unit in relation to which costs are ascertained.*<sup>11</sup>

**4.3 Direct Employee Cost:** *The cost of employees which can be attributed to a cost object in an economically feasible way.*<sup>12</sup>

**4.4 Direct Expenses:** *Expenses relating to manufacture of a product or rendering a service, which can be identified or linked with the cost object other than direct material cost and direct employee cost*<sup>13</sup>. Examples of Direct Expenses are royalties charged on production, job charges, hire charges for use of specific equipment for a specific job, cost of special designs or drawings for a job, software services specifically required for a job, travelling Expenses for a specific job.

**4.5 Direct Material Cost:** *The cost of material which can be attributed to a cost object in an economically feasible way*<sup>14</sup>.

**4.6 Finance Costs:** *Costs incurred by an enterprise in connection with the borrowing of funds.* This will include interest and commitment charges on bank borrowings, other short term and long term borrowings, amortisation of discounts or premium related to borrowings, amortisation of ancillary cost incurred in connection with the arrangements of borrowings, finance charges in respect of finance leases, other similar arrangements and exchange differences arising from foreign currency borrowings to the extent they are

<sup>10</sup> Adapted from CAS 1 paragraph 6.5.19

<sup>11</sup> Adapted from CIMA Terminology

<sup>12</sup> Adapted from CAS 1 paragraph 6.2.4 (Direct labour cost)

<sup>13</sup> Adapted from CAS 1 paragraph 6.2.6

<sup>14</sup> Adapted from CAS 1-6.2.3



regarded as an adjustment to the interest costs<sup>15</sup>. The terms Finance costs and Borrowing costs are used interchangeably.

**4.7 Imputed Costs: *Hypothetical or notional costs, not involving cash outlay, computed for any purpose.***<sup>16</sup>

**4.8 Overheads: *Overheads comprise of indirect materials, indirect employee costs and indirect expenses which are not directly identifiable or allocable to a cost object.***<sup>17</sup>

**4.9 Standard Cost: *A predetermined cost of resource inputs for the cost object computed with reference to set of technical specifications and efficient operating conditions.***

Standard costs are used as scale of reference to compare the actual costs with the standard cost with a view to determine the variances, if any, and analyse the causes of variances and take proper measure to control them. Standard costs are also used for estimation.

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<sup>15</sup> Adapted from CIMA Terminology

<sup>16</sup> Adapted from CAS 1 paragraph 6.5.13

<sup>17</sup> Adapted from CAS 3 paragraph 4.1



## 5. Principles of Measurement:

**5.1 Identification of Direct Expenses shall be based on traceability in an economically feasible manner.**

**5.2.1 Direct expenses incurred for the use of bought out resources shall be determined at invoice or agreed price including duties and taxes, and other expenditure directly attributable thereto net of trade discounts, rebates, taxes and duties refundable or to be credited.**

**5.2.2 Direct expenses other than those referred to in paragraph 5.2.1 shall be determined on the basis of amount incurred in connection therewith.**

Examples: in case of dies and tools produced internally, the cost of such dies and tools will include direct material cost, direct employee cost, direct expenses, factory overheads including share of administrative overheads relating to production comprising factory management and administration.

In the case of research and development cost, the amount traceable to the cost object for development and improvement of the process for the existing product shall be included in Direct Expenses.

**5.2.3 Direct Expenses paid or incurred in lump-sum or which are in the nature of 'one – time' payment, shall be amortised on the basis of the estimated output or benefit to be derived from such direct expenses.**

Examples: Royalty or Technical know-how fees, or drawing designing fees, are paid for which the benefit is ensued in the future period. In such case, the production / service volumes shall be estimated for the effective period and based on volume achieved during the Cost Accounting period, the charge for amortisation be determined.



**5.3 If an item of Direct Expenses does not meet the test of materiality, it can be treated as part of overheads.**

**5.4 Finance costs incurred in connection with the self generated or procured resources shall not form part of Direct Expenses.**

**5.5 Direct Expenses shall not include imputed costs. In case of goods produced for captive consumption, treatment of imputed cost shall be in accordance with Cost Accounting Standard – 4 (CAS-4).**

**5.6 Where direct expenses are accounted at standard cost, variances due to normal reasons shall be treated as part of the Direct Expenses. Variances due to abnormal reasons shall not form part of the Direct Expenses.**

**5.7 Any Subsidy/Grant/Incentive or any such payment received/receivable with respect to any Direct Expenses shall be reduced for ascertainment of the cost of the cost object to which such amounts are related.**

**5.8 Any abnormal portion of the direct expenses where it is material and quantifiable shall not form part of the Direct Expenses.**

**5.9 Penalties, damages paid to statutory authorities or other third parties shall not form part of the Direct Expenses.**

**5.10 Credits/ recoveries relating to the Direct Expenses, material and quantifiable, shall be deducted to arrive at the net Direct Expenses.**

**5.11 Any change in the cost accounting principles applied for the measurement of the Direct Expenses should be made only if, it is required by law or for compliance with the requirements of a cost accounting standard, or a change would result in a more appropriate preparation or presentation of cost statements of an organisation.**





## 6. Assignment of costs

**6.1 Direct Expenses that are directly traceable to the cost object shall be assigned to that cost object.**

## 7. Presentation

**7.1 Direct Expenses, if material, shall be presented as a separate cost head with suitable classification.** e.g.

- Subcontract charges
- Royalty on production

## 8. Disclosures

**8.1 The cost statements shall disclose the following:**

1. **The basis of distribution of Direct Expenses to the cost objects/ cost units.**
2. **Quantity and rates of items of Direct Expenses, as applicable.**
3. **Where Direct Expenses are accounted at standard cost, the price and usage variances.**
4. **Direct expenses representing procurement of resources and expenses incurred in connection with resources generated.**
5. **Direct Expenses paid/ payable to related parties<sup>18</sup>.**
6. **Direct Expenses incurred in foreign exchange.**
7. **Any Subsidy/Grant/Incentive and any such payment reduced from Direct Expenses.**
8. **Credits/recoveries relating to the Direct Expenses.**
9. **Any abnormal portion of the Direct Expenses.**
10. **Penalties and damages excluded from the Direct Expenses**

**8.2 Disclosures shall be made only where material, significant and quantifiable.**

**8.3 Disclosures shall be made in the body of the Cost Statement or as a foot note or as a separate schedule.**

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<sup>18</sup> Related party as per the applicable legal requirements relating to the cost statement as on the date of the statement



***8.4 Any change in the cost accounting principles and methods applied for the measurement and assignment of the Direct Expenses during the period covered by the cost statement which has a material effect on the Direct Expenses. Where the effect of such change is not ascertainable wholly or partly the fact shall be indicated.***

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