



Cost Auditing Standard - 103
Cost Auditing Standard on
Overall Objectives of the Independent Cost Auditor and
the Conduct of an Audit in Accordance with Cost Auditing Standards

The following is the **Cost Auditing Standard** (Cost Auditing Standard - 103) on “**Overall Objectives of the Independent Cost Auditor and the Conduct of an Audit in Accordance with Cost Auditing Standards**”. 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

This Standard on Auditing deals with the overall objectives of the independent cost auditor, the nature and scope of a Cost audit the independent auditor’s overall responsibilities when conducting an audit of cost statements in accordance with Cost Auditing Standards. It also explains the requirements establishing the general responsibilities of the independent auditor applicable in all audits, including the obligation to comply with the Cost Auditing Standards.

The independent Cost Auditor is referred to as “Cost auditor” hereafter.

2. Objectives

The objective of this Standard is to lay down the overall objectives of the Cost Auditor and ensuring the Conduct of the Audit of Cost Statements in accordance with the Cost Auditing Standards.

The Cost auditor’s overall objectives are:

- 2.1. to obtain reasonable assurance about whether the cost statements as a whole are free from material misstatement, whether due to fraud or error, and to enable the auditor to express an opinion whether the Cost Statements are prepared, in all material respects, in accordance with the applicable Cost reporting framework, Cost Accounting Standards(CAS) and Generally Accepted Cost Accounting Principles (GACAP) as issued by the Institute, and give a true and fair view of the Cost of a***



product, activity or service. In the case of a Cost Audit under the Companies Act and Rules prescribed thereunder, the objective is to express an opinion on whether the Cost Statements subject to audit represent a true and fair view of the cost of production, cost of sales and margin of products covered by the Cost Audit.

2.2. to report on the cost statements in the form required by law or by the Cost Auditing Standards in accordance with the auditor's findings.

Where reasonable assurance cannot be obtained, the cost auditor should qualify the opinion and in extreme cases disclaim an opinion.

The Cost Auditors objective may extend to making observations and suggestions where required by applicable regulations.

3. Scope

The scope of this standard is to establish overall objectives of the cost auditor while conducting an audit of cost statements, in accordance with the cost auditing standards.

It also describes management responsibility for the preparation and presentation of the Cost Statement, to identify the Cost Reporting framework and to lay down Cost Accounting policies.

4. Definitions

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

4.1. Audit: *Audit is an independent examination of financial, cost and other related information of an entity whether profit oriented or not, irrespective of its size or legal form, when such an examination is conducted with a view to expressing an opinion thereon.*

4.2. Audit Partner: *Audit partner means the partner in the firm who is a member of the Institute of Cost Accountants of India and is in full time practice and is responsible for the audit and its performance, and for the report that is issued on behalf of the firm,*



and who, where required, has the appropriate authority from a professional, legal or regulatory body.

4.3. Audit Risk: *Audit risk is the risk that the cost auditor expresses an inappropriate audit opinion on the cost statements that are materially misstated. Audit risk is a function of the risk of material misstatement and detection risk.*

(a) The risk of material misstatement has two components viz. Inherent Risk and Control risk.

(1) Inherent risk: the susceptibility of an assertion about the measurement, assignment or disclosure of cost to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.

(2) Control risk: the risk that a misstatement that could occur in an assertion about the measurement, assignment or disclosure of cost and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's internal, operational and management control.

(b) Detection risk: the risk that the procedures followed by the cost auditor to reduce audit risk to an acceptable low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

4.4. Audit Team: *Audit team means all personnel performing an engagement, including any experts contracted by the firm in connection with that engagement.*

4.5. Auditee: *Auditee means a company or any other entity for which cost audit is being carried out.*

4.6. Auditor: *Auditor is used to refer to the person or persons conducting the audit, usually the audit partner or other members of the audit team, or, as applicable the firm. Auditor includes Cost Auditor*



- 4.7. Cost Audit:** *Cost audit is an independent examination of cost statements, cost records and other related information of an entity including a non-profit entity, when such an examination is conducted with a view to expressing an opinion thereon.*
- 4.8. Cost Auditor:** *“Cost Auditor” means an auditor appointed to conduct an audit of cost records and shall be a cost accountant within the meaning of The Cost and Works Accountants Act 1959. “Cost Accountant” is a cost accountant as defined in clause (b) of sub-section (1) of section 2 of The Cost and Works Accountants Act, 1959 (23 of 1959) and who holds a valid certificate of practice under subsection (1) of section 6 and who is deemed to be in practice under subsection (2) of section 2 of that Act and includes a firm of cost accountants.*
- 4.9. Firm:** *Firm means a sole practitioner, partnership including LLP (Limited Liability Partnership) or any other entity of professional cost accountants as may be permitted by law and constituted under The Cost and Works Accountants Act & Regulations.*
- 4.10. Management:** *The person(s) with executive responsibility for the conduct of the entity’s operations. For some entities in some jurisdictions, management includes some or all of those charged with governance.*
- 4.11. Misstatement:** *A difference between the amounts, classification, presentation or disclosure of a reported cost statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable cost reporting framework. Misstatements can arise from error or fraud.*

Where the cost auditor expresses an opinion on whether the cost statements give a true and fair view, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the cost auditor’s judgment, are necessary for the cost statements to be presented fairly, in all material respects, or to give a true and fair view.

- 4.12. Non-compliance:** *Acts of omission or commission by the entity, either intentional or unintentional, which are contrary to the prevailing laws or regulations governing Cost*



Accounting, Cost Records and Cost Audit. Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees. Non-compliance does not include personal misconduct (unrelated to the business activities of the entity) by those charged with governance, management or employees of the entity.

- 4.13. Overall Audit Strategy:** *Overall Audit Strategy sets the scope, timing and direction of the audit, and guides the development of the detailed audit plan.*
- 4.14. Professional Judgment:** The application of relevant training, knowledge and experience, within the context provided by cost auditing standards, cost accounting standards and ethical requirements, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.
- 4.15. Professional Skepticism:** An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatements due to error or fraud, and a critical assessment of audit evidence.
- 4.16. Risk Assessment:** *The audit procedures performed to obtain an understanding of the entity and its environment, including the entity's internal control, to identify and assess the risks of material misstatement, whether due to fraud or error, at the overall cost statement level and at the assertion level including items of cost, cost heads and disclosure thereof.*
- 4.17. Those charged with governance:** The person(s) or organisation(s) (e.g., a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

5. Requirements

- 5.1.** *The cost auditor shall comply with the relevant ethical requirements including those pertaining to independence in respect of cost audit engagements. (refer 6.1)*



- 5.2. While conducting an audit, the cost auditor shall comply with each of the Cost Auditing Standards relevant to the audit. A Cost Auditing Standard is relevant to the audit when the Cost Auditing Standard is in effect and the circumstances addressed by the Cost Auditing Standard exist. (refer 6.2)**
- 5.3. The cost auditor shall have an understanding of the entire text of the Cost Auditing Standard, including its application and other explanatory material, to understand its objectives and to apply its requirements properly.**
- 5.4. The cost auditor shall not represent compliance with the cost auditing standards in the cost auditor's report unless the auditor has complied fully with all of the Cost Auditing Standards relevant to the audit.**
- 5.5. In exceptional circumstances, the cost auditor may judge it necessary to depart from a relevant requirement in a Cost Auditing Standard. In such circumstances, the auditor shall perform alternative audit procedures to achieve the aim of that requirement.{Refer 6.2(c)}**
- 5.6. The cost auditor shall plan and perform an audit with an attitude of professional skepticism recognizing that circumstances may exist that cause the Cost Statements to be materially misstated. (refer 6.3)**
- 5.7. The auditor shall obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor's opinion.(refer 6.4)**
- 5.8. The cost auditor shall exercise professional judgment in planning and performing the audit.**
- 5.9. The cost auditor shall determine whether the Cost Reporting Framework followed by management in preparing cost statements is in line with the Companies Act and the Rules prescribed thereunder. (refer 6.5)**



5.10 *The cost auditor shall not be required to perform audit procedures regarding the entity's compliance with laws and regulations governing cost audit in the absence of identified or suspected non-compliance. (refer 6.6)*

5.11 *If an objective in a relevant Cost Auditing Standard cannot be achieved, the auditor shall evaluate whether this prevents the auditor from achieving the overall objectives of the auditor and thereby requires the auditor, in accordance with the Cost Auditing Standards, to modify the auditor's opinion.*

6 Application Guidance:

6.1 Audit and Ethics: The cost auditor should comply with relevant ethical requirements as per Code of Ethics issued by the Institute of Cost Accountants of India. This code establishes fundamental principles of professional ethics relevant to the auditor while conducting an audit and provides a conceptual framework for applying these principles. The fundamental principles with which the auditor is required to comply are Independence, Integrity, Objectivity, Professional competence and due care, Confidentiality and Professional conduct. In case of an audit engagement, it is in the public interest that the auditor should be independent of the entity subject to the audit. The cost auditor's independence from the entity safeguards the cost auditor's ability to form an opinion without being affected by influences that might compromise that opinion. Independence enhances the auditor's ability to act with integrity to be objective and to maintain an attitude of professional skepticism. (Refer 5.1)

For Example: The provision of services for maintenance of cost records, design and implementation of Cost Systems and internal audit are considered to erode the independence.

6.2 Conduct of audit: (Refer 5.2)

- (a) The Cost Auditing Standards provide the standards for the cost auditor's work in fulfilling the overall objectives of the cost auditor. The Cost Auditing Standards deal with general responsibilities of the cost auditor, as well as cost auditor's further considerations relevant to the application of those responsibilities to specific topics.



- (b) In performing an audit, the cost auditor may be required to comply with legal or regulatory requirements in addition to Cost Auditing Standards. In such cases in addition to complying with each of the Cost Auditing Standard relevant to the cost audit, it may be necessary for the cost auditor to perform additional audit procedures in order to comply with the legislative and regulatory requirements. The Cost Auditing Standards do not override law or regulations that govern audit process.

The form of the cost auditor's opinion will depend upon the applicable cost reporting framework and any applicable laws or regulations such as Companies Act and Rules prescribed thereunder.

- (c) The need for the auditor to depart from a relevant requirement is expected to arise only where the requirement is for a specific procedure to be performed and, in the specific circumstances of the audit, that procedure would be ineffective in achieving the aim of the requirement. (Refer 5.5)

6.3 Professional skepticism: An attitude of professional skepticism means the cost auditor makes a critical assessment, with a questioning mind, of the validity of audit evidence obtained and be alert to audit evidence that contradicts or brings into question the reliability of documents and responses to inquiries and other information obtained from management and those charged with governance. An attitude of professional skepticism is necessary throughout the cost audit process for the auditor to reduce the risk of overlooking unusual circumstances, of over generalizing when drawing conclusions from cost audit observations, and of using faulty assumptions in determining the nature, timing and extent of the cost audit procedures and evaluating the results thereof. When making inquiries and performing other cost audit procedures, the cost auditor should not be satisfied with less-than-persuasive audit evidence based on a belief that management and those charged with governance are honest and have integrity. Accordingly, representations from management are not a substitute for obtaining sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the cost auditor's opinion. (Refer 5.6)

- (a) A cost auditor conducting an audit in accordance with Cost Auditing Standards obtains reasonable assurance that the Cost Statements taken as a whole are free from material misstatement, whether due to fraud or error. Reasonable assurance



is a concept relating to the accumulation of the audit evidence necessary for the auditor to conclude that there are no material misstatements in the Cost Statements taken as a whole. Reasonable assurance relates to the whole audit process.

A cost auditor cannot obtain absolute assurance because there are inherent limitations in an audit that affect the cost auditor's ability to detect material misstatements. These limitations result from factors such as the following:

- (1) The use of sample testing.
- (2) The inherent limitations of internal control (for example, the possibility of management override or collusion).
- (3) The fact that most audit evidence is persuasive rather than conclusive.

Also, the work undertaken by the cost auditor to form an audit opinion is permeated by judgment, in particular regarding:

- (1) The gathering of audit evidence, for example, in deciding the nature, timing and extent of audit procedures; and
 - (2) The drawing of conclusions based on the audit evidence gathered, for example, assessing the reasonableness of the estimates made by management in preparing the Cost Statements.
- (b) Further, other limitations may affect the persuasiveness of audit evidence available to draw conclusions on particular assertions. (For example, transactions between related parties). In these cases certain Cost Auditing Standard identify specified audit procedures which will, because of the nature of the particular assertions, provide sufficient appropriate audit evidence in the absence of:
- (1) Unusual circumstances which increase the risk of material misstatement beyond that which would ordinarily be expected; or
 - (2) Any indication that a material misstatement has occurred.

Accordingly, because of the factors described above, an audit is not a guarantee that the Cost Statements are free from material misstatement, because absolute



assurance is not attainable. Further, an audit opinion does not assure the future viability of the entity nor the efficiency or effectiveness with which management has conducted the affairs of the entity.

6.4 Audit Risk and Materiality: Entities pursue strategies to achieve their objectives, and depending on the nature of their operations and industry, the regulatory environment in which they operate, and their size and complexity, they face a variety of business risks. Management is responsible for identifying such risks and responding to them. However, not all risks relate to the preparation of the Cost Statements. The auditor is ultimately concerned only with risks that may affect the cost statements. (Refer 5.7)

- (a) The cost auditor obtains and evaluates audit evidence to obtain reasonable assurance about whether the Cost Statements give a true and fair view or in accordance with the applicable cost reporting framework. The concept of reasonable assurance acknowledges that there is a risk the audit opinion is inappropriate. The risk that the cost auditor expresses an inappropriate audit opinion when the Cost Statements are materially misstated is known as “audit risk.” The cost auditor reduces audit risk by designing and performing audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base an audit opinion. Reasonable assurance is obtained when the auditor has reduced audit risk to an acceptably low level.
- (b) Audit risk is a function of the risk of material misstatement in the cost statements (or simply, the “risk of material misstatement”) (i.e., the risk that the Cost Statements are materially misstated prior to audit) and the risk that the auditor will not detect such misstatement (“detection risk”). The cost auditor performs audit procedures to assess the risk of material misstatement and seeks to limit detection risk by performing further audit procedures based on that assessment. The audit process involves the exercise of professional judgment in designing the audit approach, through focusing on what can go wrong (i.e., what are the potential misstatements that may arise) at the assertion level and performing audit procedures in response to the assessed risks in order to obtain sufficient appropriate audit evidence.



- (c) The cost auditor is concerned with material misstatements, and is not responsible for the detection of misstatements that are not material to the Cost Statements taken as a whole. The cost auditor considers whether the effect of identified uncorrected misstatements, both individually and in the aggregate, is material to the Cost Statements taken as a whole. Materiality and audit risk are related

In order to design audit procedures to determine whether there are misstatements that are material to the cost statements taken as a whole, the cost auditor considers the risk of material misstatement at two levels:

- (1) the overall cost statement level and
 - (2) In relation to cost heads, items of cost and disclosures and the related assertions.
- (d) The cost auditor considers the risk of material misstatement at the overall cost statement level, which refers to risks of material misstatement that relate pervasively to the Cost Statements as a whole and potentially affect many assertions. Risks of this nature often relate to the entity's control environment (although these risks may also relate to other factors, such as declining economic conditions), and are not necessarily risks identifiable with specific assertions at the cost heads, items of cost or disclosure level. Rather, this overall risk represents circumstances that increase the risk that there could be material misstatements in any number of different assertions, for example, through management override of internal control. Such risks may be especially relevant to the cost auditor's consideration of the risk of material misstatement arising from fraud. The auditor's response to the assessed risk of material misstatement at the overall cost statement level includes consideration of the knowledge, skill, and ability of personnel assigned significant engagement responsibilities, including whether to involve experts; the appropriate levels of supervision;
- (e) The cost auditor also considers the risk of material misstatement at the cost heads, items of cost and disclosure level because such consideration directly assists in determining the nature, timing, and extent of further audit procedures at the assertion level. The cost auditor seeks to obtain sufficient appropriate audit evidence at the cost heads, items of cost, and disclosure level in such a way that



enables the auditor, at the completion of the audit, to express opinion on the Cost Statements taken as a whole at an acceptably low level of cost audit risk. Auditors use various approaches to accomplish that objective. The discussion in the following paragraphs provides an explanation of the components of audit risk.

(f) The risk of material misstatement at the assertion level consists of two components as follows:

(1) “Inherent risk” is the susceptibility of an assertion to a misstatement that could be material, either individually or when aggregated with other misstatements, assuming that there are no related controls. The risk of such misstatement is greater for some assertions and related cost heads, items of cost and disclosures than for others. For example, complex calculations are more likely to be misstated than simple calculations. Cost heads consisting of amounts derived from cost estimates that are subject to significant measurement uncertainty pose greater risks than do cost heads consisting of relatively routine, factual data.

External circumstances giving rise to business risks may also influence inherent risk. For example, technological developments might make a cause changes to a manufacturing process rendering the existing classification of variable and fixed costs inappropriate and cause product contribution to be misstated. In addition to those circumstances that are peculiar to a specific assertion, factors in the entity and its environment that relate to several or all of the classes of cost heads, items of cost, or disclosures may influence the inherent risk related to a specific assertion. These latter factors include, for example, external market constraints may cause normal capacity as an unreliable basis for determining unit costs.

(2) “Control risk” is the risk that a misstatement that could occur in an assertion and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity’s internal control. That risk is a function of the effectiveness of the design and operation of internal control in achieving the entity’s objectives relevant to preparation of the entity’s Cost Statements. Some



control risk will always exist because of the inherent limitations of internal control.

Inherent risk and control risk are the entity's risks; they exist independently of the audit of the Cost Statements. The auditor is required to assess the risk of material misstatement at the assertion level as a basis for further audit procedures, though that assessment is a judgment, rather than a precise measurement of risk. When the auditor's assessment of the risk of material misstatement includes an expectation of the operating effectiveness of controls, the auditor performs tests of controls to support the risk assessment. The Cost Auditing Standard do not ordinarily refer to inherent risk and control risk separately, but rather to a combined assessment of the "risk of material misstatement." Although the Cost Auditing Standard ordinarily describe a combined assessment of the risk of material misstatement, the auditor may make separate or combined assessments of inherent and control risk depending on preferred audit techniques or methodologies and practical considerations. The assessment of the risk of material misstatement may be expressed in quantitative terms, such as in percentages, or in non-quantitative terms. In any case, the need for the auditor to make appropriate risk assessments is more important than the different approaches by which they may be made.

- (g) "Detection risk" is the risk that the cost auditor will not detect a misstatement that exists in an assertion that could be material, either individually or when aggregated with other misstatements. Detection risk is a function of the effectiveness of an audit procedure and of its application by the auditor. Detection risk cannot be reduced to zero because the auditor usually does not examine all of cost heads, items of cost, or disclosure and because of other factors. Such other factors include the possibility that a cost auditor might select an inappropriate audit procedure, misapply an appropriate audit procedure, or misinterpret the audit results. These other factors ordinarily can be addressed through adequate planning, proper assignment of personnel to the audit team, the application of professional skepticism, and supervision and review of the audit work performed.
- Detection risk relates to the nature, timing, and extent of the auditor's procedures that are determined by the auditor to reduce audit risk to an acceptably low level.



For a given level of audit risk, the acceptable level of detection risk bears an inverse relationship to the assessment of the risk of material misstatement at the assertion level. The greater the risk of material misstatement the auditor believes exists, the less the detection risk that can be accepted. Conversely, the less risk of material misstatement the auditor believes exist, the greater the detection risk that can be accepted.

6.5 Responsibility for the Cost Statements: The cost auditor is responsible for forming and expressing an opinion on the Cost Statements. (Refer 5.9)

The term “Cost Statements” refers to a structured representation of the cost information, which ordinarily includes accompanying notes, derived from cost accounting records and intended to communicate an entity’s use of economic resources and the output obtained in accordance with a Cost reporting framework. The term can refer to for example, a cost statement, reconciliation with financial accounts and related explanatory notes.

- (a) The requirements of the Cost reporting framework determine the form and content of the Cost Statements and what constitutes a complete set of Cost Statements. For certain Cost reporting frameworks, a single cost statement as such and the related explanatory notes constitute a complete set of Cost Statements. For example: a Cost Statement under Cost Accounting Standard 4.
- (b) The Cost auditor is not responsible for preparing and presenting the cost statements in accordance with the applicable Cost reporting framework including inter-alia:
 - (1) Designing, implementing and maintaining internal control relevant to the preparation and presentation of Cost Statements that are free from material misstatement, whether due to fraud or error;
 - (2) Selecting and applying appropriate Cost accounting policies; and
 - (3) Making cost estimates that are reasonable in the circumstances.

6.6 Non-compliance: The cost auditor shall request management to provide written representation that all known instances of non-compliance or suspected non-



compliance with laws and regulations governing Cost Accounting, Cost Records and Cost Audit have been disclosed to the cost auditor. The representations provide necessary audit evidence about management knowledge of identified or suspected non-compliance with laws and regulations whose effects may have a material effect on the cost statement however, written representation do not provide sufficient audit evidence on their own, and accordingly do not affect the nature and extent of other audit evidence that is to be obtained by the cost auditor. (Refer 5.10)

7. Effective Date

This Standard is effective for audits on or after September 11, 2015.