



Exposure Draft CAAS - 320
Cost Audit and Assurance Standard on
Planning an Audit of Cost Statements

The following is the exposure draft of **Cost Audit and Assurance Standard** (CAAS 320) on “**Planning an Audit of Cost Statements**”. 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. The need for planning an audit of cost statements and other related information is considered necessary with a view to;
 - a. Acquiring knowledge of the client’s activities, business process, financial and cost accounting policies & systems;
 - b. Establishing the expected degree of reliance to be placed on internal control;
 - c. Determining and programming the nature, timing and extent of the audit procedures to be performed;
 - d. Coordinating with the client with regard to the work to be performed; and
 - e. Ascertaining the nature, timing and extend of manpower required to conduct the audit.

An audit plan shall be revised, as necessary, during the course of the audit.

2. Objective

The objective of this standard is to guide the members in planning for the cost audit so that it is performed in an effective manner. The audit planning shall also include establishing audit strategy for the conduct of the audit.

3. Scope

This Standard deals with the auditor’s responsibility to plan an audit of cost statements and other cost related information. The auditor shall prepare and document the audit plan. While preparing the audit plan, the consideration shall be given to the availability of skilled audit personnel available, time frame for completion of the audit, the nature and the complexities involved, risk assessments and the audit tests to address those risks.

4. Definitions

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

4.1 Audit: *An audit is an independent examination of financial 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 Auditee: *Auditee means a company or any other entity for which audit and or certification is carried out.*

4.3 Audit Risks: *Audit risk is the risk that the auditor expresses an inappropriate audit opinion on cost / financial statements that are materially misstated. Audit risk has three components namely inherent risk, control risk and detection risk.*

- a. Inherent risk – the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.*
- b. Control risk – the risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure 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.*
- c. Detection risk – the risk that the procedures followed by the 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 Assurance engagement – *An engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria. The outcome of the evaluation or measurement of a subject matter is the information that results from applying the criteria.*

There are two types of assurance engagements a practitioner is permitted to perform: a reasonable assurance engagement and a limited assurance engagement.

Reasonable assurance engagement – *The objective of a reasonable assurance engagement is a reduction in assurance engagement risk to an acceptably low level in the*



circumstances of the engagement as the basis for a positive form of expression of the practitioner's conclusion.

Limited assurance engagement – The objective of a limited assurance engagement is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement, but where that risk is greater than for a reasonable assurance engagement, as the basis for a negative form of expression of the practitioner's conclusion.

4.5 Assurance Engagement Risk: *"The risk that the practitioner expresses an inappropriate conclusion when the subject matter information is materially misstated".*

4.6 Audit Strategy: *Audit Strategy sets the scope, timing and direction of the audit, and guides the development of the detailed audit plan.*

4.7 Cost Auditor: *"Cost Auditor" means an auditor appointed to conduct an audit of cost records, under sub-section (2) of section 233B of the Companies Act 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.*

4.8 Engagement Partner: *Engagement partner means the partner or other person 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 engagement 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.*

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

4.10 Experienced Auditor: *An experienced auditor is an individual who has practical audit experience and a reasonable understanding of the audit processes, auditing standards, applicable legal and regulatory requirements, the business environment in which the entity operates and the reporting issues relevant to the entity's industry.*



4.11 Firm: *Firm means a sole practitioner, partnership including LLP or any other entity of professional cost accountants as may be permitted by law and constituted under The Cost and Works Accountants Act & Regulations.*

4.12 Misstatement: *A difference between the amount, 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 auditor expresses an opinion on whether the cost statements are presented fairly, in all material respects, or give a true and fair view, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the 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.

4.13 Risk Assessment: *Risk Assessment is the overall process of risk analysis and risk evaluation.*

5. Requirements

5.1 Elements of an Audit Plan

The audit plan may include the following elements:

- a. The purpose and objectives of the audit
- b. Legal framework under which the audit is being conducted
- c. Significant areas and issues involved
- d. Process and technique to be adopted
- e. Audit Check points, audit activities
- f. Allocation of work contents amongst the audit staff
- g. Time schedules for completion of various tasks/ phases of audit
- h. Determining time lines for submission of Draft Report, discussion thereon with the auditee and submission of final report
- i. Areas to be classified on "Risk" criteria to allocate suitable resources
- j. Determining the extent of detailed examination and coverage in terms of volume
- k. Evaluation of internal controls and professional work carried out by other agencies / experts/ auditors and placing reliance thereon
- l. Materiality considerations and determining the threshold therefore
- m. Structure, contents of the report

5.2 Essentials of Audit Planning



The elements of an audit plan may be similar for different auditee entities. However, the actual contents may differ from auditee to auditee enterprise, and on nature, type & objective of the audit. For a successful audit plan, the following may be adhered to by the firm, its partners and staff:

- a. The audit plan may be reviewed by an experienced auditor, normally not engaged on the assignment. Their experience may be useful to modify the audit plan to meet the audit objectives more vigorously.
- b. The audit plan may be flexible enough to accommodate modifications which may be necessary and should be carried out with the approval of team leader.
- c. Auditing involves the collection and analysis of facts and data sufficient to reach reliable and valid conclusions about the subject of the audit.
- d. The auditing staff should be made familiar of the quality control policies and procedures of the firm. The hierarchy, responsibility & authority for decision making needs to be clearly defined and understood by the audit staff.
- e. The Audit plan includes the nature, timing and extent of audit procedures to be performed by audit teams. Sometimes audit plan requires modification based on revised consideration of assessed risks. e.g.. Auditor gets some information during the course of audit which differs significantly from the information available when the auditor planned the audit procedure.
- f. The expected audit coverage including the number and locations of components.

5.3 Knowledge of the Client's Business;

The auditor needs to obtain a level of knowledge of the client's business particularly relating to the following areas that will enable him to identify the events, transactions and practices that, in his judgment, may have a significant effect on the financial / cost information;

- a. Brief history of the Company and its business activities
- b. Corporate Structure, subsidiaries and other affiliates
- c. Details of key personnel
- d. Details of related parties
- e. Details of any foreign collaboration and agreement
- f. Annual reports and accounts for the last three years
- g. Cost Audit Report of previous three years
- h. Internal control systems and Internal audit reports
- i. Budget of the relevant financial year
- j. Inter unit and inter-company transactions policy
- k. Pricing policies – domestic and exports
- l. Export policy and exporting countries
- m. Product / activity wise market share in domestic and export markets



- n. Products and services – main product lines, by-product and joint products
- o. Manufacturing / production process with flow charts
- p. Plant wise Licensed, Installed and Normal capacity and changes made during last three years
- q. Identification of production cost centres, utilities and service cost centres
- r. Cost accounting policy
- s. Details of cost accounting and related records
- t. Cost accounting manual
- u. Cost Accounting Standards, Generally Accepted Cost Accounting Principles, Cost Audit and Assurance Standards and other relevant publications of the Institute of Cost Accountants of India
- v. Relevant publications of other professional bodies, Industry Associations, trade journals
- w. Visits to the client's premises and plant facilities
- x. Current Government legislation with respect to Cost Accounting Records and Cost Audit
- y. Government rules, regulations and directives affecting the client's business
- z. Current business developments affecting the client
- aa. Existence of parties in whom directors or persons who are substantial owners of the entity are interested and with whom transactions are likely
- bb. Recent or impending changes in technology
- cc. Product selling and distribution methods
- dd. Scope and timing of the examination
- ee. Assistance of client personnel in data preparation.

6. Application and Other Explanatory Material

The elements of an audit plan may be similar for different auditee entities. However, the actual contents may differ from auditee to auditee enterprise, and on nature, type & objective of the audit or authentication assignment.

Obtaining a general understanding of the legal and regulatory framework applicable to the entity and how the entity is complying with the required framework.

The Cost Auditor may discuss elements of planning with the entity's management to facilitate the conduct and management of the audit engagement. Although these discussions often occur, the overall audit strategy and the audit plan remain the Cost Auditor's responsibility.



As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and thereby the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks. This may be the case when information comes to the auditor's attention that differs significantly from the information available when the auditor planned the audit procedures. For example, audit evidence obtained through the performance of substantive procedures may contradict the audit evidence obtained through tests of controls.

If an audit is carried out entirely by the engagement partner, questions of direction and supervision of engagement team members and review of their work do not arise. If particularly complex or unusual issues are involved, and the audit is being performed by an individual Cost Auditor, it may be desirable to consult with other suitably-experienced Cost Auditors or the Institute.