

COST AUDIT AS A GOVERNANCE TOOL: MODERNISING INDIA'S FRAMEWORK FOR EVIDENCE-BASED ECONOMIC POLICY

Abstract

Statutory cost audit under Section 148 of the Companies Act, 2013 has come under periodic pressure from ease-of-doing-business advocates and even from the Industry, even as government bodies continue to draw on the cost data it produces for pricing, anti-dumping and incentive-verification decisions. This article asks a narrower question than critics usually pose - not whether cost audit is flawed, but whether its deficiencies call for reform or removal. The distinction matters because financial and cost accounting answer different questions altogether — one reports what an enterprise earned, the other what a specific product actually cost to make — and regulators such as the NPPA, DGTR and CCI depend on the latter in ways financial statements cannot supply.

The article builds its case partly through comparison, noting that the US, UK, Germany, Japan and South Korea all maintain their own cost-accounting regimes, and partly through history, tracing how the US Cost Accounting Standards Board was defunded in 1980 only to be reconstituted in 1988 once its absence proved costly. A parallel is drawn to India's civil-registration data during the pandemic mortality debate, where contemporaneously recorded figures held up better than retrospective estimates — an argument extended here to cost data generally. Rather than defending the status quo, the article backs the January 2024 Inter-Ministerial Committee's proposals on digital integration, threshold review and data utilisation, and adds its own recommendation to restore item- and activity-wise reporting in place of the current CTA-code format. Its conclusion is that reform, not withdrawal, is the overdue task.



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Introduction

Cost Audit occupies an uneasy position in contemporary policy discourse. While

regulatory authorities rely on correct and standardized cost data to administer large-scale Government schemes—anti-dumping investigations, pharmaceutical pricing, subsidy distribution, production-linked incentives—periodic questions surface about the necessity of mandatory cost records and independent cost audit under Section 148 of the Companies Act, 2013. Rather than viewing cost audit as a legacy mechanism from the administered-pricing era, modern economies recognise it as an essential tool that complements market liberalisation through enhanced transparency and evidence-based policy formulation.

Recent commentary on some social media

platforms has suggested that Government bodies are actively considering curtailment of statutory cost accounting and cost audit requirements as a measure to enhance ease of doing business. While such observations merit respectful consideration—compliance burden is a legitimate policy concern—they deserve examination against the evidence of contemporary regulatory dependence and the international experience. The question is not whether cost audit has deficiencies in implementation or design. The appropriate response to deficiency is modernisation, not dismantling. This distinction between reform and removal is central to the analysis that follows.

This article examines whether and under what conditions, India's statutory cost-audit framework continues to generate sufficient public-policy value to justify the compliance costs it imposes. Using comparative institutional evidence and a functional analysis of India's regulatory ecosystem, it evaluates the framework's present utility, its limitations and the case for proportionate, technology-enabled reform.

Financial Data and Cost Audit Data: Complementary, Not Competing

A foundational confusion underlies much discussion of cost audit: the assumption that cost data and financial data answer the same questions. They do not. Financial accounting aggregates costs by function or nature—cost of goods/services sold, selling and distribution expenses, administrative costs—and reports them at entity level. It answers a single critical question: what did the enterprise earn? By contrast, cost accounting disaggregates these aggregates to product, process or activity level, answering a fundamentally different question: what did each product or service actually cost to produce?

Consider a pharmaceutical company manufacturing twenty products from three manufacturing facilities. Its financial statements will show aggregate cost of goods sold. But a pharmaceutical regulator seeking to determine a ceiling price for one specific drug requires unit-level cost information for that product at that facility—information absent from financial statements. Similarly, a competition regulator investigating

cost-based pricing in a steel plant requires granular data on overhead allocation, capacity utilisation and conversion costs for specific product categories. A trade regulator determining anti-dumping margins requires cost-of-production data disaggregated by product and period. None of this information is produced by financial accounting alone.

Cost audit is the mechanism through which this complementary information is generated and independently verified. It is not a check on financial audit; it is an independent governance function serving regulatory purposes that financial audit cannot address. The two forms of audit are positioned side-by-side in India's statutory framework—Sections 139 and 148 of the Companies Act, 2013—not because cost audit duplicates financial audit, but because it addresses distinct governance needs.

The Case for Structured Cost Information

Cost information matters at the national level not merely for enterprise management but for State action across multiple policy domains. When the Directorate General of Trade Remedies investigates whether imported textiles are being dumped at prices below cost of production, it requires contemporaneously verified cost data from both domestic and foreign producers.

The January 2024 inter-ministerial committee report records the relevance of cost information to trade-remedy administration. Any numerical statement regarding the number of investigations or companies affected should be retained only if the exact figure, period and underlying DGTR submission can be cited by page or paragraph; otherwise, the unverified numbers should be omitted. Without standardised, audited cost data, such investigations would operate under profound information asymmetry—exporters would self-report costs through questionnaire responses, with limited capacity for independent verification.

The National Pharmaceutical Pricing Authority relies on cost structures to determine ceiling prices for scheduled drugs, verify extraordinary profit margins and prevent consumer exploitation of 1.4 billion Indians. The Competition Commission of India used cost data traceable to the statutory framework in its landmark cement-cartelisation

proceedings. The Government's Production-Linked Incentive schemes, committing lakh-crore rupee outlays, depend on cost verification to prevent artificial inflation of claims and misstatement of value addition. Revenue authorities rely on cost information for transfer pricing, indirect tax reconciliation and detection of evasion. While governments track budgeted expenditure and utilization, they lack centralized cost-outcome data, which the statutory cost audit mechanism provides.

These are not peripheral applications. They are central functions of economic governance.

Effect of the Regulatory Gap

Maintaining the statutory cost audit framework ensures continuous generation, standardisation and independent verification of regulatory cost data. The strength of this institutional infrastructure is material. First, uniform cost-recording requirements enable enterprises to maintain comparable records across standardised frameworks, ensuring consistency across companies and periods. Second, independent professional verification provides assurance on cost claims beyond self-certification. Third, when the Government requires reliable cost data for trade investigations, pricing interventions, supply-chain disruptions or policy emergencies, it should be able to access contemporaneously verified information with confidence. The importance of such a mechanism has already been demonstrated in the recent past. During the COVID-19 pandemic, and again during the period of heightened India-China tensions following the Galwan Valley incident, imports of several critical inputs were disrupted, supply chains came under pressure, and the costs of certain raw materials and components increased sharply within a short period. In such situations, the Government needs credible and timely data to assess how external shocks are affecting production costs, prices, industry viability and the broader economy. A rule-based cost accounting and audit framework substantially reduces the information asymmetry that would otherwise arise from post-hoc reconstruction of data. It enables historical cost information to be traced to contemporaneous records, subjected to professional verification and regulatory oversight, thereby providing the Government with a more dependable basis for

timely and evidence-based policy intervention.

Fourth, the loss would not be merely evidentiary but institutional. The Institute of Cost Accountants of India, constituted under parliamentary statute and administered under disciplinary procedures, would lose its primary statutory mandate. The Cost Accounting Standards developed over decades—refined through consultation with industry, academia and regulators—would become advisory guidance rather than binding requirements. The MCA-21 portal, which currently produces a machine-readable national industrial cost dataset, would cease receiving structured data. This is not a marginal regulatory adjustment; it is the dismantling of a governance architecture that regulators have come to depend upon.

Rule-Based Data Governance: A Principle of Public Administration

A fundamental principle of sound public administration deserves emphasis: ****data generated through predefined, uniform and rule-based systems are generally more reliable, comparable and defensible than information reconstructed retrospectively through ad hoc methodologies****.

The importance of this principle became particularly evident during the COVID-19 pandemic, when the reliability of India's reported mortality data was questioned internationally. Certain estimates based on sampling surveys and model-based projections produced mortality figures substantially different from the officially reported numbers, largely because they relied on different methodologies, assumptions and estimation techniques.

India was, however, in a position to respond to such concerns on the strength of its statutory civil-registration framework established under the ****Registration of Births and Deaths Act, 1969****. Deaths were recorded through an institutionalised and legally prescribed system rather than being reconstructed only after the event. The availability of systematically collected official records provided an objective basis for examining the reported mortality figures and demonstrating that divergence between officially recorded deaths and subsequently estimated mortality figures could arise from ****differences in methodology, assumptions,**

coverage and estimation techniques**, and did not, by itself, establish underreporting.

The episode illustrates a broader governance lesson: *when data are generated contemporaneously under a statutory, standardised and auditable framework, their credibility and evidentiary value are inherently stronger than figures reconstructed later through estimation models.*

India's statutory cost accounting framework embodies the same governance principle. Enterprises are required to maintain cost records according to prescribed formats and standards. These records are subject to contemporaneous audit by Cost Accountants bound by professional disciplinary standards. Cost data accumulate continuously in a standardised repository accessible to multiple regulators. When a Government agency requires cost information, it is not retrospectively assembled under pressure from incomplete or biased historical records. It is already in hand—contemporaneously generated, independently verified and comparable across enterprises and periods. This is not a minor administrative efficiency. It is a foundational difference in the quality of evidence available to policymakers.

International Practice: Structured Cost Information Is Globally Valued

The premise that cost audit is uniquely Indian phenomenon does not withstand international examination. Every major economy maintains some framework through which cost information is generated, standardised and made available to regulators. The United States operates a Cost Accounting Standards regime under federal law, requiring contractors under federal negotiated contracts exceeding USD 5 million to maintain cost records and submit to audit by the Defense Contract Audit Agency. The United Kingdom applies Full Economic Costing and Transparent Approach to Costing models to government departments, higher-education institutions and regulated utilities, with penalties for false submissions. Germany mandates cost-plus-basis public procurement with continuous cost monitoring, supported by statutory cost elements defined in its commercial code. Japan's Business Accounting Council has issued ten Cost Accounting Standards applicable

across all business entities. South Korea maintains thirty Cost Accounting Standards for manufacturing and non-manufacturing entities, with mandatory separate schedules of manufacturing costs and cost of sales subject to auditor verification.

What distinguishes jurisdictions is not whether cost-accounting discipline exists but the institutional vehicle through which it operates. India's distinctive contribution has been to combine primary-legislation mandate, professional-body (ICMAI) administration with parliamentary statutory discipline, multi-sector applicability across 39 economically significant sectors, codified standards (25 Cost Accounting Standards), structured digital filing through the MCA-21 portal in XBRL format, and integrated access by multiple regulators. The synthesis of these elements is institutionally unique. It demonstrates that mature, high-capacity economies recognise the policy value of structured cost information and invest in institutional mechanisms to ensure its generation, standardisation and independence.

The USA-India Democratic Precedent: Institutional Resilience and Periodic Renewal

It is interesting to note that the histories of cost accounting governance in India and the United States reveal a striking parallel—and an instructive lesson about democratic governance and evidence-based policymaking. Both nations are major democracies with large, complex economies. Both faced significant concerns from trade and industry sectors during the 1960s regarding profiteering practices and the absence of transparent, verifiable cost data. Both constituted expert committees to examine the problem. Both committees concluded that statutory frameworks for cost accounting and independent cost audit were necessary governance instruments.

India, acting on such recommendations, amended the Companies Act, 1956, to introduce mandatory cost records maintenance and cost audit requirements for specified industries. This framework, refined and updated through successive legislative amendments, persists to the present day as a core governance mechanism.

The United States, through legislative action under 41 U.S.C. 1501 et seq., established the Cost Accounting Standards Board in 1970 to establish

uniformity in cost accounting standards applicable to federal contractors. Like India, the creation reflected democratic deliberation about societal interest in transparent, standardised, independently verified cost information.

Both frameworks faced sustained resistance from trade and industry sectors opposed to compliance requirements. Both governments, at different points, encountered political pressure to curtail or eliminate the frameworks in the name of reducing regulatory burden and easing business operations. The United States experienced the most severe challenge when the original CASB was dissolved on September 30, 1980, due to Congressional defunding. For eight years, from 1980 to 1988, the Board ceased operations entirely. Facing financial starvation and industry pressure, cost accounting standards appeared destined for obsolescence in the United States, just as critics periodically suggest in India today.

The cycle of institutional learning repeated in the United States just as it continues in India. Public and legislative attention to fair trade practices, cost-based pricing integrity, and transparency in government contracting intensified. There was renewed recognition of the value of structured, standardised, independently verified cost information. The United States moved decisively to strengthen cost accounting governance by reestablishing the CASB in 1988. Upon reestablishment, the Board has maintained important activity to address CAS interpretation matters and ensure ongoing consistency in cost accounting practices across government contractors. This demonstrated commitment continues to the present day

India's cost audit framework has evolved through continuous industry engagement and economic calibration. Strategic reviews reflect a commitment to ongoing improvement. Its refinement stems from active reliance by trade remedy - a legal policy tool that governments use to protect local businesses from unfair foreign competition, pricing, competition, and revenue authorities. Unlike the US system, which required reestablishment after restructuring, India maintained institutional continuity by consistently demonstrating its regulatory utility and long-term value.

The USA-India precedent offers a powerful lesson for contemporary policy deliberation. Both major democracies have concluded, through episodic but recurring deliberation spanning decades, that statutory cost accounting and cost audit are governance necessities, not dispensable legacies. Both have experienced sustained resistance from regulated industries and periodic pressure to abandon the frameworks. The United States learned through the painful experience of dissolution and the subsequent need for reestablishment that cost audit frameworks warrant institutional permanence. India has avoided that painful experience through continuous operation and demonstrated utility.

Where deficiencies arise in design, coverage or utilisation, the policy response should be assessed against the relative costs and benefits of modernisation, rationalisation and where justified, discontinuance. On the evidence examined in this article, a modernised framework appears more capable of preserving policy-relevant information while reducing avoidable compliance burden. Contemporaneous, standardised records can materially improve the comparability and auditability of information available to policymakers when compared with data reconstructed after the event.

Reform Agenda for India's Framework - Modernisation

A. Reform direction emerging from the Inter-Ministerial Committee

India's framework has evolved through legislative amendment, stakeholder consultation and periodic review. Its continuing relevance has been assessed by the committee through references to documented use by trade-remedy, pricing, competition and revenue authorities.

The January 2024 inter-ministerial MCA Committee, comprising representatives from the Ministry of Finance, Corporate Affairs, Department of Expenditure, NPPA, CBDT, CBIC, DGTR and sectoral regulators, undertook a comprehensive examination of the statutory cost audit framework. Rather than recommending removal, the Committee recommended rationalisation of sectoral coverage, review of applicability thresholds, integration with GST and PLI dashboards, development of

sectoral cost-intelligence platforms for inter-firm benchmarking, risk-based selection protocols to focus audit efforts on high-policy-impact entities and strengthened utilisation of cost audit data by Government agencies.

The said expert committee has already set a modernisation agenda for cost audit address: (i) Digital integration—real-time, machine-readable filing of cost data with integration into regulatory dashboards, reducing manual compliance burden; (ii) Threshold calibration—periodic review of turnover thresholds and sectoral applicability to ensure compliance cost is proportionate to policy benefit; (iii) Standards refinement—continuous revision of Cost Accounting Standards to reflect technology, sectoral changes and emerging policy priorities; (iv) Utilisation enhancement—establishment of inter-ministerial nodal-officer frameworks and sectoral cost-intelligence platforms to transform raw data into policy-usable intelligence; (v) Confidentiality architecture—robust data-governance safeguards permitting legitimate regulator access while protecting commercially sensitive information; and (vi) Capacity building—investment in the professional competence of Cost Accountants to ensure audit quality and relevance.

B. Further reforms proposed by the author

At this stage, India needs to revisit the existing mechanism, which is opaque to some extent by reporting cost elementwise & grouped cost data under CTA codes and, needs to fall back to original Item-wise and activity wise cost reporting

Conclusion

The case advanced here is not for preserving every feature of the present framework. It is for retaining the public-policy capability to generate reliable, comparable and independently assured cost information, while redesigning coverage, reporting architecture and data use.

Given the **changing contribution and composition of India's industrial and service sectors**, the need has arisen to revisit and expand the coverage of the cost accounting and cost audit framework by bringing appropriate **emerging manufacturing and service activities** within its ambit. Such expansion, based on their economic

significance and policy relevance, is the need of the hour. In this context, **implementation of the recommendations of the January 2024 Inter-Ministerial MCA Committee is now overdue and warrants priority consideration.** MA

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