

# AUDIT AND ASSURANCE

## STUDY TEXT

### Qualifications and Credit Framework

**Q2022**

This Study Text supports study for the following AAT qualifications:

AAT Level 4 Diploma in Professional Accounting

AAT Diploma in Professional Accounting at SCQF Level 8

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## STUDY TEXT

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# INTRODUCTION

## HOW TO USE THESE MATERIALS

These Kaplan Publishing learning materials have been carefully designed to make your learning experience as easy as possible and to give you the best chance of success in your AAT assessments.

They contain a number of features to help you in the study process.

The sections on the Unit Guide, the Assessment and Study Skills should be read before you commence your studies.

They are designed to familiarise you with the nature and content of the assessment and to give you tips on how best to approach your studies.

## STUDY TEXT

This study text has been specially prepared for the revised AAT qualification introduced in February 2022.

It is written in a practical and interactive style:

- key terms and concepts are clearly defined
- all topics are illustrated with practical examples with clearly worked solutions based on sample tasks provided by the AAT in their examining style
- frequent practice activities at the end of the chapters ensure that what you have learnt is regularly reinforced
- 'pitfalls' and 'examination tips' help you avoid commonly made mistakes and help you focus on what is required to perform well in your examination
- 'Test your understanding' activities are included within each chapter to apply your learning and develop your understanding.

## ICONS

The chapters include the following icons throughout.

They are designed to assist you in your studies by identifying key definitions and the points at which you can test yourself on the knowledge gained.



### Definition

These sections explain important areas of Knowledge which must be understood and reproduced in an assessment.



### Example

The illustrative examples can be used to help develop an understanding of topics before attempting the activity exercises.



### Test your understanding

These are exercises which give the opportunity to assess your understanding of all the assessment areas.



### Foundation activities

These are questions to help ground your knowledge and consolidate your understanding on areas you're finding tricky.



### Extension activities

These questions are for if you're feeling confident or wish to develop your higher level skills.

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Our Quality Co-ordinator will work with our technical team to verify the error and take action to ensure it is corrected in future editions.

# Principles of auditing

## Introduction

This chapter demonstrates the features of an audit and introduces the fundamental principles within audit work. This is the basis for the whole Audit and Assurance assessment and introduces some important concepts for the rest of the syllabus.

### ASSESSMENT CRITERIA

The concepts and principles (1.1)  
The regulatory environment (1.2)

### CONTENTS

- 1 What is an audit?
- 2 Important principles in audit work
- 3 Auditing standards
- 4 Features of an audit

# 1 What is an audit?

## 1.1 The purpose of an external audit

The need for an audit arises from the separation between the management and the ownership of companies – directors are responsible for running the company on behalf of the shareholders. Financial statements are prepared by the directors in order to account for their stewardship to the shareholders, and an examination by an independent person (i.e. the external auditor) gives them credibility.

Once the external auditor has conducted their examination, the auditor expresses an opinion in an auditors' report attached to the financial statements.

## 1.2 Definition of Assurance and Audit



### Definition

**Assurance** – an assurance engagement is one 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.



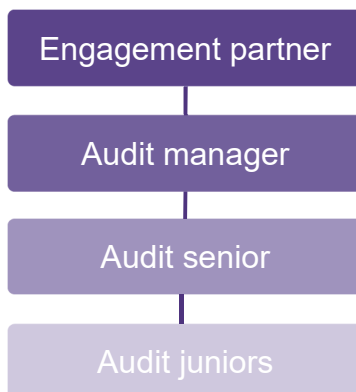
### Definition

**Audit of financial statements** – an audit is a type of assurance engagement and is a process which results in expression of an opinion as to whether the financial statements give a true and fair view of the entity's affairs at the period end, and as to whether they have been properly prepared in accordance with the applicable accounting standards.

The Companies Act 2006 identifies that an external audit is a legal requirement for all UK companies, except those which meet two of the following three criteria: (1) annual turnover not exceeding £10.2m, (2) total assets value not exceeding £5.1m and (3) 50 or fewer employees (this is for companies with an accounting period starting on or after 1 January 2016).

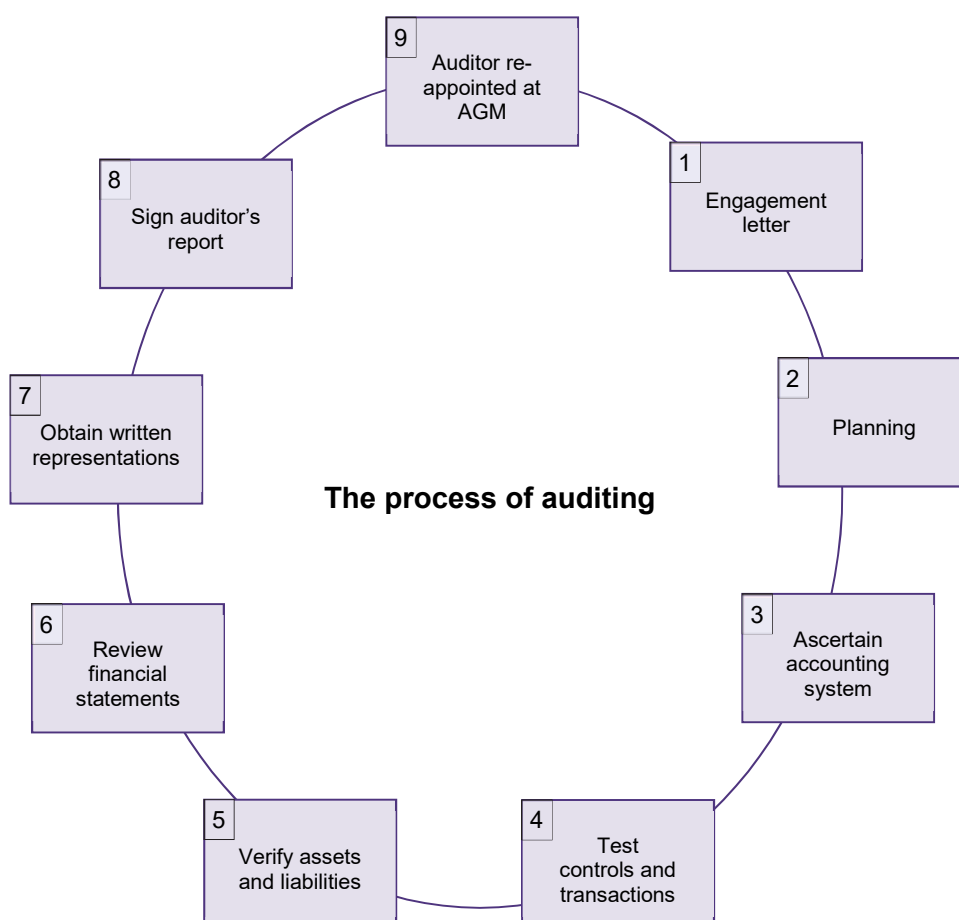
## 4.2 Audit team

A typical audit team for a large company audit might be made up as follows:

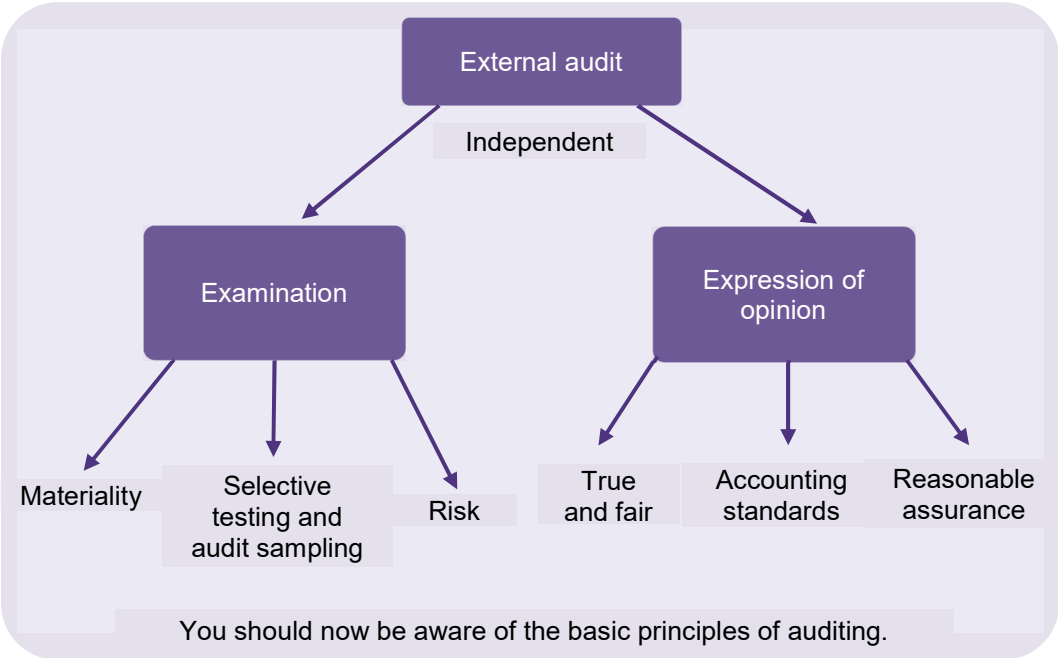


## 4.3 The process of auditing

An audit consists of a cycle of activities which can be broken down into a number of distinct phases as shown below. Review the phases illustrated and discussed below to gain an overview. This will all be developed in later chapters.



# 5 Summary







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