



The Institute of Chartered Accountants of India

Code: IN5AE620536
Subject : 05 Auditing and Ethics

Total Marks: 70
Marks Obtained : 55

Number of Answer Books used : Main + ...2... additional sheets

Date Seal

15 MAY 2021

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620536



ICAI

Paper Code

Z
R
F
1

A B C D E F G H I J K L M N O P Q R S T U V W X Y Z
A B C D E F G H I J K L M N O P Q R S T U V W X Y Z
A B C D E F G H I J K L M N O P Q R S T U V W X Y Z

MCQ Booklet Serial No.

3836626

Paper No. (See Reverse)

5

Level of Exam → Intermediate

Intermediate

Final

Stream → New

Old

1

New

Answers

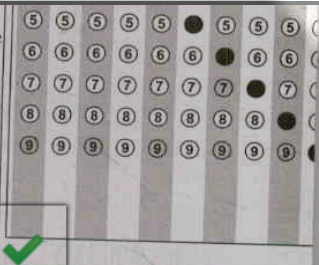
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| 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 2 | 11 | A | B | C | D | 21 | A | B | C | D |
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| 5 | 5 | 5 | 5 | 5 | 5 | 5 | 5 | 8 | 16 | A | B | C | D | 26 | A | B | C | D |
| 6 | 6 | 6 | 6 | 6 | 6 | 6 | 6 | | 17 | A | B | C | D | 27 | A | B | C | D |
| 7 | 7 | 7 | 7 | 7 | 7 | 7 | 7 | | 18 | A | B | C | D | 28 | A | B | C | D |
| 8 | 8 | 8 | 8 | 8 | 8 | 8 | 8 | | 19 | A | B | C | D | 29 | A | B | C | D |
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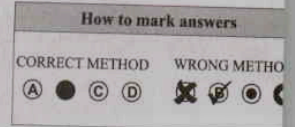
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INSTRUCTIONS TO THE CANDIDATE FOR FILLING THE MCQ ANSWER FIELDS

- 1. Candidate is required to Darken the appropriate Circle.
- 2. Candidate must fill in the correct MCQ Booklet Serial No. as printed on your question booklet which will be taken as final for evaluation.
- 3. If candidate fills in this information wrongly, Institute will not take any responsibility for rectifying the mistake.
- 4. Candidate must Darken the complete circle.
- 5. If candidate wants to change your Answer, erase the all darkened circle completely and make a fresh mark.
- 6. Candidate must NOT make any stray marks on the OMR cover page.
- 7. Rough work must NOT be done on the OMR cover page.
- 7. Mark your answer only in the appropriate space against the number corresponding to the question.



| Q. No. | To be ticked (✓) by the candidate against the Questions answered Descriptive Type | LIST OF EXAM, PAPER NO. AND PAPER NAME (TO BE REFERRED TO FOR FILLING ON THE REVERSE SIDE) | | |
|--------------|---|--|-----------|---|
| | | EXAM | PAPER NO. | PAPER NAME |
| | | Intermediate (IPC) - Old course | | |
| 1 | ✓ | Intermediate (IPC) - (OLD COURSE) | 2 | BUSINESS LAWS, ETHICS AND COMMUNICATION |
| 2 | ✓ | Intermediate (IPC) - (OLD COURSE) | 4 | TAXATION |
| 3 | ✓ | Intermediate (IPC) - (OLD COURSE) | 6 | AUDITING AND ASSURANCE |
| 4 | | Intermediate (IPC) - (OLD COURSE) | 7 | INFORMATION TECHNOLOGY AND STRATEGIC MANAGEMENT |
| | | Intermediate - New | | |
| 5 | ✓ | Intermediate - (NEW COURSE) | 2 | CORPORATE AND OTHER LAWS |
| 6 | ✓ | Intermediate - (NEW COURSE) | 4 | TAXATION |
| 7 | | Intermediate - (NEW COURSE) | 6 | AUDITING AND ASSURANCE |
| 8 | | Intermediate - (NEW COURSE) | 7 | ENTERPRISE INFORMATION SYSTEMS AND STRATEGIC MANAGEMENT |
| | | Final - Old | | |
| 9 | | FINAL - (OLD COURSE) | 3 | ADVANCED AUDITING AND PROFESSIONAL ETHICS |
| 10 | | FINAL - (OLD COURSE) | 4 | CORPORATE AND ALLIED LAWS |
| 11 | | FINAL - (OLD COURSE) | 6 | INFORMATION SYSTEMS CONTROL AND AUDIT |
| 12 | | FINAL - (OLD COURSE) | 7 | DIRECT TAX LAWS |
| 13 | | FINAL - (OLD COURSE) | 8 | INDIRECT TAX LAWS |
| | | Final - NEW | | |
| 14 | | FINAL - (NEW COURSE) | 3 | ADVANCED AUDITING AND PROFESSIONAL ETHICS |
| | | FINAL - (NEW COURSE) | 4 | CORPORATE AND ECONOMIC LAWS |
| | | FINAL - (NEW COURSE) | 7 | DIRECT TAX LAWS AND INTERNATIONAL TAXATION |
| Total | | FINAL - (NEW COURSE) | 8 | INDIRECT TAX LAWS |



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Answer to Question 5(a)

As per Section 53 of the Companies Act, 2013, a company cannot issue shares at a discount (lower than face value) except sweat equity share.



5aStep1



1

Further, a company may issue shares at a price lower than face value under

- Debt Restructuring Scheme
- Statutory Resolution Plan.



A company, if issuing share at discount in any case other than those specified above will be liable for penal action under the Section 53 of the Act.

5aStep2



1

Penalty:- The company shall be liable, in addition to refunding the amount raised, a penalty which shall ~~not~~ be lower of

- a) ₹ 5,00,000
- b) Amount raised through the issue.

along with interest at the rate of 12% per annum.



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Hence, in the case given in the question, PQ & Co. cannot issue shares of face value of ₹100 at ₹95 for the reason to receive more response.

However, if company raises the money through shares issued at a discount, it shall be liable to penal action as specified above.

5a



2

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Answer to Question 5(b)

Any amount shall be included or excluded in the cost of Property, Plant and Equipment (PPE) should comply with Accounting Standard 10 issued by Accounting Standards Board of Institute of Chartered Accountant of India (ICAI).

Examples of costs that should not form part of cost of PPE are :-



- Allocated General overheads



• Cost of inauguration or opening of new facility where PPE is installed.

5b Step 1



2

• Cost of opening of new facility

- Cost of training, hiring of new employees who can run these machines



• Cost of advertisement or marketing expense.

5b



2



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Answer to Question 5(c)

Every professional accountant is expected to comply with the ~~fundable~~ fundamental principle of professional ethics.

Fundamental Principles are:

- Integrity
- Objectivity
- Professional Competence and Due Care
- Confidentiality
- Professional Behaviour.

In the case given,

- (1) A chartered accountant in practice accepted the appointment as auditor of firm in which his sister was partner.

⇒ Violation of principle of Objectivity. Auditor is working in a firm where there is familiarity threat.

- (2) A chartered accountant in practice was approached by his friend to seek some insider information about company, which was his client. He could not refuse his friend's request.

⇒ Violation of principle of Confidentiality.

5cStep1



1



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~~(2)~~ A chartered accountant in practice failed to inform his client

5cStep2



1

Confidentiality principle requires that the professional accountant should not disclose the information obtained by him as a result of his professional status.

He should keep information confidential so that there is a free flow of information between him and client.

(3) A chartered accountant in practice failed to inform his client about the change in laws applicable to his client.

5cStep3



1

Violation of principle of Professional Competence and Due Care.

This ^{principle} requires professional accountant to maintain attain and maintain knowledge & skill so that the client receives services as per the current laws and regulation.

5c



3



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Answer to Question 5(d)

As per clause (xii) of the Paragraph 3 of the Companies Auditor's Report Order, 2020 (CARO), the auditor shall report:

a) whether the Nidhi Company has complied with requirement of Net Owned Funds to Deposits in the ratio of 1:20 to meet its liability



b) whether the Nidhi Company has complied with maintaining 10% unencumbered term deposits as required by Nidhi Rules, 2014 to meet its liability



5dStep1



3

c) whether there has been a default in repayment of deposit or payment of interest, if so disclose the nature during the year and amount.



5d



3



5



10



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Answer to Question 5(a)

SA 220 provides the quality control requirement for an audit engagement.

Responsibilities of an engagement partner for engagement quality control review are :-



Determine whether there is need for quality control review and if so, whether the quality control reviewer has been appointed for such assignment.

6aStep1



2

Ensure that all the matters which are contentious or are difficult or significant are reviewed by the quality control reviewer. The engagement partner ~~shall~~ ^{must} be satisfied with the work of quality control reviewer.



The engagement partner shall not date the auditor's report at a date earlier than the date of completion of quality control review.

6aStep2



1

i.e. The engagement partner shall sign the auditor's report only after the review of quality control reviewer is completed.



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Hence, as in this case, CA M of firm M/s YZ LLP is auditing financial statement of a listed entity ABC Ltd. and the firm has determined that quality control review is required in the engagement.

Hence, a CA M is required to follow the responsibilities stated above to comply with SA-220.

6a



3



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Answer to Question 6(b)

Loans guaranteed by Government.

Central Government :- Where a loan has been secured or guarantee is given by Central Government, and the guarantee is not invoked or repudiated, such loans shall be treated as Standard Asset always but shall be treated as Non-Performing Asset (NPA) for income recognition purpose.

State Government :- Where a loan has been guaranteed by State Government, then if such such loans are overdue they shall be treated as Non-Performing Asset (NPA) for both income recognition purpose and provisioning purpose.

In the case given, MNP Bank has advanced certain loans which are guaranteed by government, ~~the~~

Hence, MNP Bank shall follow the above stated norms for income recognition and classification purpose.



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Answer to Question 6(c)

As per SA 450, the documentation requirements regarding misstatement identified during the audit are :-

Amount below which misstatement would be regarded as trivial.
[misstatement identified as trivial are not communicated to those charged with governance]

6cStep1



3



Misstatement accumulated during the audit and whether they have been corrected by management and those charged with government governance.



The auditor's conclusion as to whether the effect of uncorrected misstatement is material on the financial statement and the auditor's basis for this conclusion.

6c



3





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Answer to Question 6(d)

The lease agreement have been classified into two categories by Accounting Standard 19 which are :-

- a) Operating Lease
- b) Financial Lease.

The AS 19 also lays down the conditions to determine that whether the lease is a financial lease.

One of such condition is :-

If the period of lease substantially covers the whole of the economic life of the asset, such lease shall be finance lease.

In this case given, JK Ltd. entered into lease of plant for 11 years, which is approximately the estimated useful life of economic life of asset

Hence, the lease that JK Ltd. has entered into is finance lease.

6dStep1



3



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14



Accounting Treatment :-



JK Ltd. will record the plant as a asset in its book and the present value of minimum lease payment as the liability in the books,

The lease payment made during the year will have 2 components, one towards the settlement / reduction of lease liability and the other component will represent interest or finance charges

The company can claim depreciation on the asset

Tax Benefits :-



Unlike Operating Lease, the JK Ltd will not record rent expense instead it will claim benefit of depreciation of asset and the interest or finance charge.

6d



3

6



13

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Answer to Question 2(a)

Information that the auditor can get by inquiry of the following personnel :-

i) ~~Internal~~ Internal Audit Personnel :-

The auditor may obtain information related to the ^{internal} controls of the entity and about the operating effectiveness of such control. He may also obtain information related to areas where control are weak or missing which may indicate the auditor the areas which are significant in the audit and requires specific attention.

ii) ~~Internal~~ In-house Legal Counsel :-

The auditor may obtain information about the litigation and claims involving the entity and assessment about their outcome and financial implication, if any.

Such ~~inquiry~~ inquiry is also required as per SA 501.

2aStep1

2aStep2



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iii) Marketing and sales Personnel :-

The auditor may obtain information from such personnel which are :-

- Inquiry about advertisement expense and change in it from previous year



- Inquiry about the free samples distributed

2aStep3



0

- Inquiry about the credit period given by the company to customer

- Inquiry about reasonableness and completeness of sales

iv) Information System Personnel :-

The auditor may obtain information regarding the operations of such system and whether such system is achieving its objective

2aStep4



1



He may also obtain information that whether these ^{has} ~~has~~ been any changes in the system during the year.

2a



3



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Answer to Question 2(b)

The auditor, CA Z may send specific inquiry letter if he considers that entity's external auditor is unlikely to respond to general enquiry letter.

The inclusions in specific enquiry letter are :-

- a) The list of provision litigations and claims involving entity.
- b) Where available, the management's assessment regarding the outcome of such litigation and claims and financial implication, if any, including cost involved.
- c) A request to the external legal counsel to confirm the reasonableness of the list of litigation or claim or provide necessary information if the list is considered to be incomplete.

The auditor may also judge it necessary to meet with the external legal counsel if the matter involves significant risk or the matter is complex or there is disagreement between management and external legal counsel.

2bStep1

2



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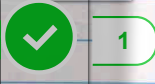
Total Marks: 70
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In case, if the management refuses to give permission to auditor to communicate or meet with the external legal counsel, then the auditor shall express an qualified or disclaimer of opinion in accordance with SA 705.

2bStep2



1

2b



3



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Answer to Question 2(c)

Factors giving rise to inherent limitations due to which auditor cannot provide guarantee that financial statements are free from material misstatement due to fraud or errors are :-

a) Nature of Financial Reporting :-

The auditor cannot give absolute assurance or provide guarantee because the preparation of financial statement by management requires certain judgements or estimates by management. Making of estimates and judgements is a subjective matter and hence auditor cannot obtain absolute assurance.

b) Nature of Audit Procedures :-

The nature of audit procedure are also a factor that restricts the auditor from obtaining absolute assurance. There can be practical or legal implication limitations.

Practical limitation is that auditor makes on



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opinion on the basis of testing of a sample.
Sampling is a example of practical limitation

Legal - The auditor cannot identify related party transactions

• Management may be involved in fraud and can be involved in designing a carefully organised scheme to conceal the fraud.

c) Audit is not an investigation.



An auditor does not have any specific legal powers. He cannot compel the management to provide certain information, he can only request for such information

2cStep1



3

d) Timeliness of financial Reporting and Relevance of Information.

The relevance of information decreases over time.

There has to be maintained a balance between relevance of information and cost of obtaining it.



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e) Future Events :-

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The auditor cannot predict future events. A event may occur in future that may lead to closing down of operations of entity.

2c



3

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Answer to Question 2(d)

Examples of factors that, in auditor's professional judgement, are significant in directing the engagement team efforts, are :-

- a) A significant change in the legal or regulatory environment of the entity, such as change in applicable financial reporting framework.
- b) 3 A recent industry development which is significant, such as change in industry specific reporting requirement.
- c) Other recent significant developments, such as change in the accounting standard (AS).
- d) 2d A change in the nature or size of business, such as entering into new line of business.





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Answer to Question 3(a)

Planning includes the need to consider certain matters, prior to the identification and assessment of the risk of material misstatements. Such matters are :-

- a) Analytical procedures to be applied as risk assessment procedures
- b) Involvement of experts for performing procedures
- c) Determination of materiality for the procedures risk assessment procedures
- d) Other planned procedures to be applied as risk assessment procedures
- e) Obtaining an understanding of the entity's legal and regulatory environment and how the entity complies with the legal and regulatory requirements

3aStep1



4

3a



4



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Answer to Question 3(b)

As per SA 580, 'Written Representation', the period covered by written representation shall be as close as possible to the date of audit report.

3bStep1



1

In case, where there has been a change in the management during the year, the auditor may remind the management of their responsibilities as per the agreement.

In this case, P@ Ltd.'s management changed during the period. The view of management was that they can give representation for the period when they took over and not for prior period when old management were managing the affairs.

3bStep2



1

The auditor shall remind the new management regarding their responsibilities and should obtain written representation from them. The view of new management is not correct as they should take their responsibility as per the terms of engagement even if it is signed by old management.

3b



2



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Answer to Question 3(c)

Circumstances where manual elements in Internal control may be more suitable :-

a) Manual control will be effective in areas involving transaction which are of heterogeneous, heterogeneous ~~transact~~ in nature, the risk involved is significant, the amount involved is charge large.

b) Manual control will be effective in areas where there is difficult to estimate, determine or predict the misstatement, i.e. areas involving different types of misstatements. 3

c) Manual Controls will be effective when the work is to check the operating effectiveness of automated control. 3





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Answer to Question 3(d)

As per SA 610, 'Using the Work of Internal Audit Function', the auditor shall before using the work of internal audit function shall satisfy itself as to the appropriateness of the use of that work.

The coordination between external auditor and internal audit function should take place in order to ensure effectiveness. Such coordination includes communicating:

- a) Nature of such work
- b) Extent of use of work
- c) Materiality determined for the financial statement as a whole
- d) Documentation requirement of the procedures performed
- e) Timing of such work.

3dStep1



1



The auditor shall also read the report submitted by the internal audit function in relation to area in which the auditor intends to use the work of internal audit function.

3d



1

3



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Addl. Book No.1.....

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
ADDL. BOOK

15 MAY 2024

DO NOT WRITE ROLL NUMBER ANYWHERE
ADDITIONAL ANSWER BOOK



Answer to Question 1(a)

Audit Programme is to be prepared for all the audit and should be mandatory in case of large audits.

Audit programme involves a list of procedures to be performed and techniques to be applied to obtain audit evidence.

1aStep1



0

Ans When developing an audit programme, auditor shall consider the



- The size of the entity, the nature of its operation.
- The effectiveness of the internal control.
- The type of service to be rendered by the auditor.
- The risk of material misstatement.
- The desired level of assurance.



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In the case given, APR & Associates, are appointed as auditors of Time Ltd and Bake Ltd. CA R & CA P are engagement partners of Bake Ltd and Time Ltd. respectively. Both the companies are different in terms of volume and nature of business



Opinion of CA R :- Same Audit Programme for audit of both the companies

Opinion of CA P :- Same Audit Programme cannot be used

1aStep2



1



Hence, the opinion of CA P is correct as different audit programme is needed for entities that vary in size, nature, composition, effectiveness of internal control etc.

1a



1



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Answer to Question 1(b)

As per AS 2, the cost of inventory shall not include the abnormal cost of material, labour and overhead. The abnormal cost shall be treated as expense in the period in which they are incurred.

1bStep1

2

Hence, the cost of inventory of ABC & Co. as on 31.03.2024 is :-

Material Purchase Cost 25,05,000

Allocated Transport Cost 18,000

25,23,000

1bStep2

1

∴ Abnormal wastage of ₹2,000 shall be transferred to Profit & Loss Account

Further, as per AS-2, the inventory shall be valued at lower of cost and net realizable value

In the case given, the value of inventory as on 31.03.2024 will be :-



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1bStep3



1

Cost of Inventory 25,23,000

Net Realizable Value 25,24,000

Lower 25,23,000

Hence, the inventory shall be valued at cost
i.e. ₹ 25,23,000 as it is lower than net
realizable value.

1b



4

X

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Answer to Question 1(c)

~~The reporting requirement~~

The responsibility of the persons in relation to internal control and its effectiveness in accordance with the Companies Act, 2013, are :-

a) Section 134(5)(e) requires the Directors to state in the Director's Responsibility Statement that :-

1cStep1



1



The Directors had laid down internal financial controls to be followed by the company and such controls are adequate and operating effectively

b) Section 149(8) requires Independent Directors to make a declaration in relation to internal control, which is :-



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1cStep2 **1** The Internal financial Control to have been designed and such controls are operating effectively and are complied with in practice

1cStep3 **0** Section 177(4)(vii) requires declaration from Audit Committee regarding the operating effectiveness of the internal financial Controls

1c **2**

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Answer to Question 1(d)

⇒ SA 230 puts emphasis ^{on} preparation of document on timely basis during the audit as it will ~~be~~

- enhance the quality of audit
- help in efficient review of audit procedure evidence obtained and conclusions reached before finalisation of audit.

Assembly of audit file is an administrative process ~~of~~ which does not involves performance of new audit procedures or drawing new conclusions.

In this case, CA B is preparing various documents of the client after completion of audit. Hence, the action is not proper as these documents should have been prepared ~~some~~ during the audit.

Audit file contains the record of the audit documentation. It can be in physical or electronic form

Hence, the opinion of CA B that audit file is

1dStep1



1



The Institute of Chartered Accountants of India

Code: IN5AE620536
Subject : 05 Auditing and Ethics

Total Marks: 70
Marks Obtained : 55

4



mandatory in paper form is incorrect.

⇒ SQC 1 requires firm to establish policies & procedures for timely completion of final audit file. Generally, the time ^{allowed} taken for assembly of final audit file is [60 days] from date of audit report.

1dStep2



1

Hence, as in this case, CA B has completed the assembly in [3 months] from date of audit report, the action of CA B is invalid.

⇒ SQC 1 requires to retain a record of audit file. The audit file shall be retained for a period not shorter than (7 years) from date of audit report or if later, date of group auditor's report.

1dStep3



1

Hence, the retention of audit file of clients of for [4 years] is not in accordance with SQC 1.

1d



3

Action of CA B is not proper.

1



10

DO NOT WRITE ANYTHING HERE

DO NOT WRITE ANYTHING HERE

DO NOT WRITE ANYTHING HERE



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Total Marks: 70
Marks Obtained : 55

Result Overview

Awarded Marks: 55

Max Marks:70

NA Not Attempted

O Optional

M Marked

Q1_Compulsory (Score: 10/14)

| Question No | Awarded Marks | Maximum Marks | Status |
|-------------|---------------|---------------|--------|
| 1 | 10 | 14 | M |
| 1a | 1 | 4 | M |
| 1b | 4 | 4 | M |
| 1c | 2 | 3 | M |
| 1d | 3 | 3 | M |

Q2_Q6 (Score: 45/56)

| Question No | Awarded Marks | Maximum Marks | Status |
|-------------|---------------|---------------|--------|
| 2 | 12 | 14 | M |
| 2a | 3 | 4 | M |
| 2b | 3 | 4 | M |
| 2c | 3 | 3 | M |
| 2d | 3 | 3 | M |
| 3 | 10 | 14 | M |
| 3a | 4 | 4 | M |
| 3b | 2 | 4 | M |
| 3c | 3 | 3 | M |
| 3d | 1 | 3 | M |
| 4 | 0 | 14 | O |
| 4a | 0 | 4 | O |
| 4b | 0 | 4 | O |
| 4c | 0 | 3 | O |

| | | | |
|----|----|----|---|
| 4d | 0 | 3 | O |
| 5 | 10 | 14 | M |
| 5a | 2 | 4 | M |
| 5b | 2 | 4 | M |
| 5c | 3 | 3 | M |
| 5d | 3 | 3 | M |
| 6 | 13 | 14 | M |
| 6a | 3 | 4 | M |
| 6b | 4 | 4 | M |
| 6c | 3 | 3 | M |
| 6d | 3 | 3 | M |