



**Royal Mail Group Ltd**

**Regulatory Financial Statements  
2007-08**

**Part 1: Audited financial information**

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## Summary of results

	53 weeks <sup>1</sup>			52 weeks <sup>1</sup>		
	2007-08			2006-07 (restated) <sup>2</sup>		
	USO	Downstream Access	Price Controlled Area	USO	Downstream Access	Price Controlled Area
	£m	£m	£m	£m	£m	£m
Revenue	3,373	571	5,847	3,459	327	5,959
Operating costs	(3,478)	(659)	(6,048)	(3,457)	(375)	(6,028)
Operating (loss)/ profit before exceptional items	(105)	(88)	(201)	2	(48)	(69)
Operating exceptional items	(167)	(37)	(308)	(68)	(9)	(126)
Operating loss	(272)	(125)	(509)	(66)	(57)	(195)
<i>Operating Margin Before Exceptionals</i>	<i>-3.1%</i>	<i>-15.4%</i>	<i>-3.4%</i>	<i>0.1%</i>	<i>-14.7%</i>	<i>-1.2%</i>
<i>Operating Margin</i>	<i>-8.1%</i>	<i>-21.9%</i>	<i>-8.7%</i>	<i>-1.9%</i>	<i>-17.4%</i>	<i>-3.3%</i>
<i>Operational volumes (millions of items excluding Door to Door)</i>	<i>8,699</i>	<i>4,091</i>	<i>19,902</i>	<i>9,341</i>	<i>2,442</i>	<i>20,523</i>

- For the first time the USO is loss-making at an operational level; operating loss before exceptional items being £105m in 2007-08, compared to a profit of £2m in 2006-07.
- The Price Controlled area showed an even larger deterioration in operating loss before exceptional items, from a restated £69m to £201m. Despite a 5% average tariff increase the Price Controlled area revenue decreased by 3.2% on a like-for-like basis.
- Inland addressed mails volumes (working day adjusted) are down 3.2% , combined with significant customer downtrading to cheaper products, against a broadly fixed cost base.
- Downstream Access volumes have increased by 67% in the year to almost 4.1bn.
- In total, stamped mail lost £189m (2006-07: £188m), which was equivalent to 6.1p per item. Profits on business mail (meter and PPI) were insufficient to offset this, a trend worsening from prior years. Overall the first and second class standard products lost £62m (2006-07: £36m loss.)

<sup>1</sup> 2007-08 is a 53 week period compared to 52 weeks in 2006-07. The impact of this on comparative revenue and cost is discussed further in the Financial Summary.

<sup>2</sup> For comparability , the 2006-07 results have been restated to align with the treatment of property now held by Royal Mail Estates Ltd. See page 16 for further details.

## Business review

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### Introduction

As agreed with Postcomm, the Regulatory Financial Statements are held in two documents:

- Part 1: Audited financial information (including the regulatory income statement); and
- Part 2: Unaudited financial information (including a market review and analysis of the results by format).

This review should be read in combination with the market review in Part 2 of the Regulatory Financial Statements. Whilst regulatory requirements specify reporting over the regulatory Services (the "Services"), for business review purposes the Directors believe it is appropriate to focus on the results for the Price Controlled and USO areas.

### Financial Summary

2007-08 is the second year of operating under the amended Licence issued in May 2006 and the new price control within it.

Total Mails revenue declined by 0.6%. 2007-08 was a 53 week period, compared to the normal 52 weeks in 2006-07. In terms of total working days, taking also into account the timing of bank holidays, this amounts to 264.1 days in 2007-08 and 260.5 in 2006-07. Consequently on a working day adjusted basis Total Mails revenue declined by 2.0%.

The decline in revenue is caused by the continuation of negative market trends:-

- declining market volumes;
- losses to Downstream Access ("DSA"); and
- customers downtrading to cheaper products.

Total Mails costs have increased by 1.7%, of which 1.3% (£88m) is estimated to be associated with the additional week of operating in 2007-08.

The largest part of the Letters cost base is the staff costs, where operational staff are paid weekly, and a further 5 days have been paid for in 2007-08. Other costs identified as variable with time include non staff costs such as conveyance and fuel.

### Price Controlled Area Performance

The financial analysis in the remainder of this section focuses on operating profit before exceptional items. A summary of operating profit performance before exceptional items by major product group is shown below:

	2007-08				2006-07 (Restated)			
	Revenue	Profit	Margin	Operational volumes	Revenue	Profit	Margin	Operational volumes
	£m	£m	%	m items	£m	£m	%	m items
1c stamp/ meter/ PPI	1,654	73	4.4	3,885	1,700	109	6.4	4,156
2c stamp/ meter/ PPI	1,019	(141)	(13.8)	4,050	1,055	(151)	(14.3)	4,345
Bulk Mail*	1,235	(114)	(9.2)	6,122	1,472	(83)	(5.6)	7,600
Downstream Access	566	(90)	(15.9)	4,077	325	(49)	(15.1)	2,434
Other	1,373	71	5.2	1,768	1,407	105	7.5	1,988
<b>Total</b>	<b>5,847</b>	<b>(201)</b>	<b>(3.4)</b>	<b>19,902</b>	<b>5,959</b>	<b>(69)</b>	<b>(1.2)</b>	<b>20,523</b>

\*Bulk Mail includes Mailsort, Walksort and Cleanmail

There was an increase in average prices of around 5% for the Price Controlled area. The significant increase in tariff arose because of under-recovery of revenue in previous years.

## Business review

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Notwithstanding this and the impact of the extra working days in 2007-08, Price Controlled area revenues fell by £112m (1.9%). Bulk mail revenues and profit have both been severely affected by the continued transfer of significant volumes to DSA. DSA volumes have increased by 67% to 4.1bn items. In addition, the level of downtrading to cheaper products that first started in 2005-06 has continued to increase, driving revenue dilution relating to changes in both class of service used and in terms of the level of presortation performed by the customer.

Despite a 2p increase in first class tariffs in April 2007 first class Standard Tariff Letter margins fell. The 1p increase in second class tariffs did generate some reduction in losses, particularly in PPI.

### Price Controlled area costs from operations

The following table highlights the breakdown of costs in the Price Controlled area:

	2007-08	2006-07 (Restated)
	£m	£m
People costs	(4,138)	(4,159)
Depreciation, amortisation and impairment	(107)	(88)
Net operating charges	(1,803)	(1,781)
<b>Total</b>	<b>(6,048)</b>	<b>(6,028)</b>

Total costs for the Price Controlled area have risen by only £20m (0.3%). This is considerably lower than the 4.1% average increase in inflation (RPI) year-on-year, and when the additional week's operating costs are taken into account underlying costs have actually reduced.

The majority of front line staff received an increase of 5.4% on basic pay and weekday overtime from 1 October 2007. Despite this people costs actually reduced year on year, which is even more noteworthy given that 2007-08 includes the impact of the additional week of trading. This reflects efficiencies delivered to absorb the impact of the pay award in addition to a slight reduction in pension costs.

The average number of employees within the Letters business has reduced by 2.9% from 170,127 to 165,257. This is broadly in line with the reduction in operational volumes.

People costs represent 68.4% (2006-07: 69.0%) of total costs, which remains an extremely high proportion compared to many other regulated industries.

## Business review

### USO Performance

The table below shows the performance of USO products.

	2007-08				2006-07 (Restated)			
	Revenue	Profit	Margin	Operational volumes	Revenue	Profit	Margin	Operational volumes
	£m	£m	%	m items	£m	£m	%	m items
1c stamp/ meter	1,360	15	1.1	3,117	1,383	58	4.2	3,309
2c stamp/ meter	724	(148)	(20.4)	2,900	733	(138)	(18.8)	3,016
Bulk Mail *	378	16	4.2	1,545	442	28	6.3	1,875
Other	911	12	1.3	1,137	901	54	6.0	1,141
<b>Total</b>	<b>3,373</b>	<b>(105)</b>	<b>(3.1)</b>	<b>8,699</b>	<b>3,459</b>	<b>2</b>	<b>0.1</b>	<b>9,341</b>

\* Bulk Mail includes Mailsort and Cleanmail

In 2006-07 the USO was barely profitable. Due to declining volumes and further downtrading as highlighted in Part 2 of the financial statements, in 2007-08 the USO made a £105m loss. First and second class stamp and meter margins fell despite the April 2007 tariff increases.

The following summary of the income statement for the USO demonstrates that the reason for the poor performance is the significant drop in revenues as a consequence of a 6.9% fall in volume.

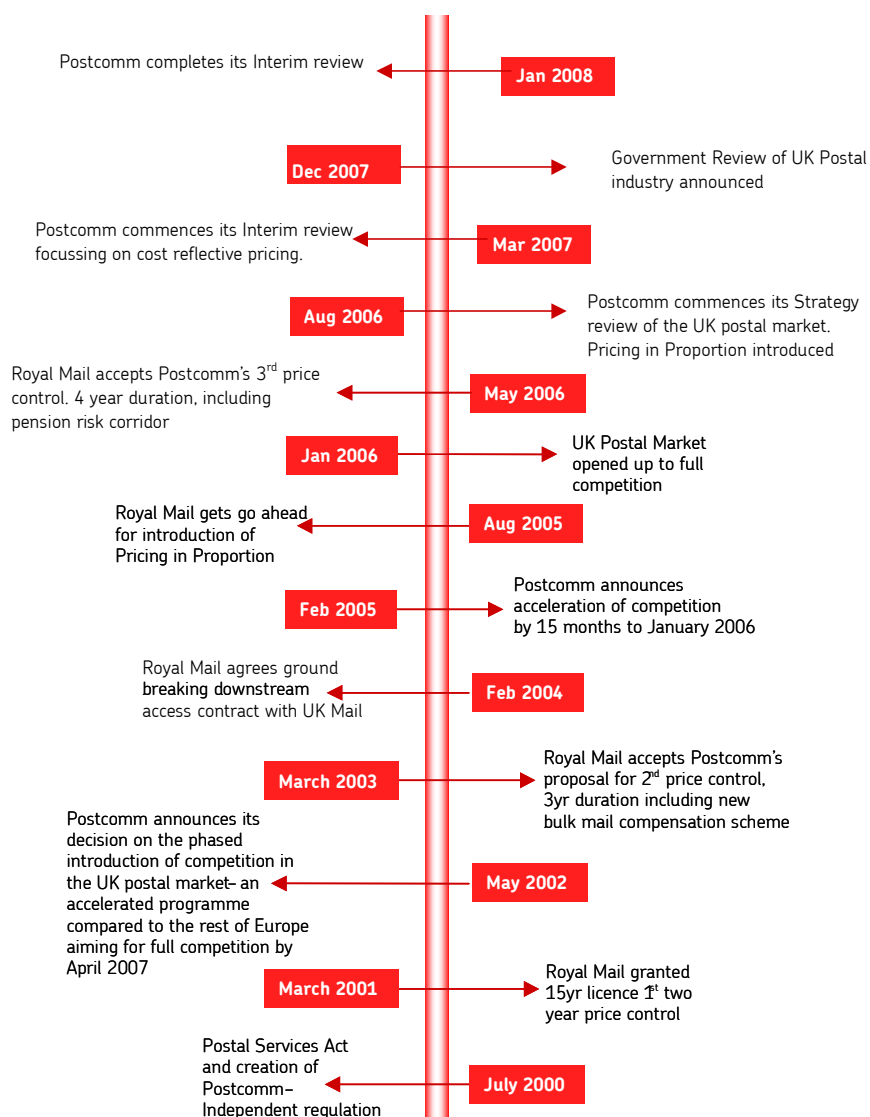
	53 weeks 2007-08 £m	52 weeks 2006-07 £m	Increase/ (decrease) £m	Increase/ (decrease) %
Revenue	3,373	3,459	(86)	(2.5)
Operating costs	<u>3,478</u>	<u>3,457</u>	<u>21</u>	0.6
Operating profit/(loss) before exceptional items	(105)	2	(107)	
Operating exceptional items	<u>167</u>	<u>68</u>	<u>99</u>	145.6
Operating loss	<u>(272)</u>	<u>(66)</u>	<u>(206)</u>	312.1
Volumes	<u>8,699</u>	<u>9,341</u>	<u>(642)</u>	(6.9)

Taking the 53 week year into account costs in the USO actually fell compared to 2006-07.

### Regulatory Review

The Postal Services Commission (Postcomm) was created as the Independent Regulator for the UK postal sector in 2000. Subsequently, Royal Mail Group Ltd (previously Royal Mail Group plc) was granted its first Licence, which required it to provide a universal postal service at affordable prices.

An overview of significant regulatory events since Postcomm was created is highlighted below:



In November 2007 the Group responded to Postcomm's Strategy Review "Emerging Themes" and believes that four key regulatory principles need to be addressed that will result in a truly competitive industry whereby all stakeholders benefit:

- Realign prices to underlying costs - to create transparency for business customers and to ensure that competition is sustainable. Some competitors in the UK are basing their entry strategies on unsustainable business models that target the historical cross-subsidies in Royal Mail's pricing structure, but cross-subsidies are fundamentally incompatible with an effectively functioning competitive market. Postcomm should allow Royal Mail to remove

## Business review

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these cross-subsidies, so that customers face the right pricing signals and competitor models going forward are based on efficiency;

- A narrower range of universal service products - focused on the needs of all social customers and fully funded through stamp prices. Business customers tell us they do not need the protection that the Universal Service Obligation (USO) provides - Postcomm describes many of these customers as "non-captive" and we agree, given the ample choice they have across mail and other communications providers. The USO should therefore be refocused on stamped mail only, and prices should reflect the true costs of this provision;
- Full retail deregulation of business products - the explosion in access competition, representing 40% of bulk mail this year, is encouraging business customers to demand more commercial and innovative responses from Royal Mail. However, Royal Mail is prevented from responding rapidly by regulatory requirements such as an involved process for changing terms and conditions. Royal Mail envisages a near term future in which the intense competition in the business mail market replaces the need for regulation; and
- Continued operational integration of the postal network - we have put in place measures to ensure that competitors and customers have access to our network on fair and reasonable terms. Separation of the postal network would create confusion for customers, introduce complex and costly interfaces, endanger quality of service and put at risk delivery of the transformation programme.

In March 2007, Postcomm commenced an Interim Review of the price control. Royal Mail has asked Postcomm to consider the following pricing proposals in this review, all of which are consistent with realigning prices to costs and entirely driven by the need to react to both the volume erosion and significant downtrading that has been evident for the last eighteen months:

- Reducing the difference between Downstream Access (DSA) and the equivalent retail prices from a high level set to encourage competition, to a level that reflects the underlying upstream costs, because entry has been significantly higher than the Price Control assumptions;
- Allowing Royal Mail's retail business to price its non-USO bulk mail products by zone, thereby making prices of cheap to deliver areas lower by up to 5% and prices of expensive to deliver areas higher by up to 5%. This does not change the price of the "one price goes anywhere" stamp;
- Allowing Royal Mail to further rebalance its prices so that it has the flexibility it needs to keep up with the pace of change in the postal sector; and
- Providing dispensation to Royal Mail with respect to bulk mail compensation and C factor adjustments if they are directly linked to service failures relating to industrial action over Royal Mail's transformation plan

## **Business review**

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In January 2008, Postcomm confirmed the following decisions with respect to its Interim Review:

- Its rejection of a change to the headroom between DSA and equivalent retail prices;
- Its rejection of Royal Mail's retail zonal application; and
- Its agreement to increase the level of rebalancing.

Royal Mail continues to work with Postcomm on industrial action dispensation.

In December 2007, BERR announced a review of the UK postal services market to examine the impacts of liberalisation of UK postal services, trends in the future market development and the likely impact of this on Royal Mail, alternative carriers and consumers. Royal Mail has submitted its first response to this review in March 2008 followed by its second response in May 2008.

## Licence requirements

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Royal Mail Group Ltd is required, originally under Condition 14 of the Licence granted by Postcomm on 23 March 2001, and as amended under Condition 15 of the Licence dated 25 May 2006, to provide regulatory financial statements.

The regulatory financial statements are based on the statutory accounts of Royal Mail Group Ltd for the 53 week period ending 30 March 2008, on which the auditors have expressed an unqualified opinion.

The revenues, costs, assets, liabilities and cash flow effects of non-letter services and subsidiaries, associates and other undertakings (primarily operating outside the UK), have been agreed with Postcomm as being outside of the scope of regulation. Consequently, the main focus in the regulatory financial statements is on the UK operations of the Group mails operations, particularly those that form the USO and Price Control.

The format of the regulatory financial statements is agreed with Postcomm on an annual basis, and where appropriate there are enhancements or exclusions from the Licence requirements to provide readers with information that both Royal Mail and Postcomm believe is more relevant and useful.

The following Services are applicable to the regulatory income statement for 2007-08 and 2006-07:

Service	Service provision
Licensed USO - 0 to 350g <sup>1</sup>	Postal products that form part of the USO, and are below or equal to a 350g weight threshold e.g. first and second class mail below or equal to the weight threshold.
Non-Licensed USO, 350g+ <sup>1</sup>	Postal products that form part of the USO, and are Non-Licensed including those above a weight threshold of 350g.
USO, Non Price Control products	Postal products that form part of the USO, but are not included within the Price Control e.g. Incoming International Mail.
Non USO, Price Control products, excluding Downstream Access <sup>2</sup>	Postal products that do not form part of the USO but are included within the Price Control, excluding Downstream Access.
Downstream Access <sup>2</sup>	Customer and other licensed postal operators' mail, which enters the Royal Mail pipeline after the outward sortation and distribution processes. This is price controlled.
Other letter products	Postal products outside of the USO and the Price Control e.g. Door to Door.

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<sup>1</sup> The split between Licensed and Non-Licensed USO products is shown in Note 2 to these financial statements

<sup>2</sup> Downstream Access and the other non USO price controlled products are also analysed between Licensed and Non-Licensed services in Note 2 to these financial statements

## Licence requirements

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### The USO

The USO is the Universal Service Obligation required under the terms of the Licence granted to Royal Mail Group Ltd as provider of a universal postal service in the UK.

The USO is now formally defined in the Licence by product. The products categorised as USO are set out in Condition 2 (3)(a) of the Licence.

Other specific items, for which the separation across the Service areas is not appropriate, have been excluded but are shown within the adjustments column in the income statement on page 13 in order to reconcile to the result of Royal Mail Letters. Note 1 presents a reconciliation of this result to the audited accounts of Royal Mail Group Ltd. All items below profit before financing and taxation are as stated in the Royal Mail Group Ltd statutory accounts and have not been repeated within the reconciliation.

### The obligation to produce regulatory financial statements

The obligation to prepare regulatory financial statements for Royal Mail Group Ltd is placed on Royal Mail Group Ltd by Condition 15 of the Licence. The principal requirements of the Licence, as agreed with Postcomm, are that regulatory financial statements should:

- provide separate accounts (as if they were separate companies in accordance with the Companies Act 1985) for each of the Services comprising a profit and loss account, Royal Mail Group Ltd balance sheet and cash flow statement, and notes setting out the accounting policies adopted together with a reconciliation to the audited statutory accounts of Royal Mail Group;
- be prepared consistently with appropriate GAAP in so far as those principles may be reasonably applied, or with such other accounting principles as Postcomm may approve in writing. As in 2006-07, Postcomm has agreed that the income statement will be prepared under International Financial Reporting Standards. In so far as they impact upon the Regulatory Financial Statements, the UK GAAP based Accounting Policies used in the audited accounts of Royal Mail Group Ltd are consistent with IFRS;
- be subject to audit;
- be prepared and submitted before 31 July 2008; and
- meet requirements of European Directive 97/67/EC Article 14.

Postcomm has agreed that no balance sheet and cash flow statement should be published in 2007-08.

### Financial statements

This document contains only audited financial information and should be read in conjunction with the unaudited financial information presented and published in Part 2 of the Regulatory Financial Statements.

The basis of preparation of these regulatory financial statements is disclosed in notes A to F on pages 14 to 18.

## Licence requirements

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### Accounting records

The organisation, management and accounting structures of Royal Mail do not align with the Services defined in Condition 15(2)(a) of the Licence as shown on page 10. In addition, an inherent feature of the postal industry is the use of common resources to provide services and products. Royal Mail does not maintain separate ledgers for each of the Services. As a consequence, processes have been developed and estimates have been applied in determining the assignment of costs and revenues to products.

This means that the records are not those that would exist if each of the Services was carried on by a separate business as required by paragraph 2(b) of Condition 15 and accordingly are not such that if each of the separate Services was carried on by a separate company incorporated under the Companies Act 1985 each of those companies would comply with subsections 221(1) and (2) of that Act.

This is consistent with the records supporting the production of previous regulatory financial statements.

### Internal trading eliminations

Royal Mail operates through business units that make use of each other's services in order to take advantage of Group synergies, having regard to the mutual dependencies that exist. Charges for internally provided services have been assigned to products. Adjustments have been made to eliminate internal profits and losses where appropriate, apart from the Post Office Ltd charges that are set using a basis of charges reached through a negotiation between the respective businesses, and Royal Mail Estates Ltd where the charges are set at market rates.

### Methodology

The methodology adopted has been documented in "An overview of the principles and methodologies used in preparing regulatory financial statements for 2008". This methodology was developed following discussions with Postcomm. The methodology and approaches used to create these regulatory financial statements are not intended to establish precedents for future regulatory financial statements.

Royal Mail continues to review and improve its approach and methodologies.

Royal Mail has initiated a review of its costing methodology to incorporate both the requirements of the Third Postal Directive (full market opening by 2010 and the abolition of the reserved area) and the economic cost of providing each of the current services (e.g. first class, second class). This would use an incremental costing approach, which considers what costs could be avoided if Royal Mail were not required to provide that service rather than merely allocating the accounting costs on an operational basis. Royal Mail has shared its initial work on these development areas with Postcomm, and anticipates incorporating the new methodology during 2008-09.

## Income statements

Income Statement 2007-08											
	A	B	C	D=B+C	E	F=A+D-E	G	H	I=F+G+H	J	K=I+J
	Note 2			Note 2	Less	Sub Total	Add back	Add	Sub Total	Note 4	Total
	USO Total	Price Controlled non-USO products excluding Access	Downstream Access <sup>1</sup>	Total Price Controlled non-USO products	USO Non-Price Control products	Total Price Control products	USO Non-Price Control products	Other Letter products	Total Mails	Non-mails activities within RM Letters and other adjustments	Royal Mail Letters total <sup>2</sup>
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Revenue	3,373	2,094	566	2,660	186	5,847	186	711	6,744	192	6,936
Operating costs	(3,478)	(2,148)	(656)	(2,804)	(234)	(6,048)	(234)	(530)	(6,812)	(127)	(6,939)
People costs (Note 3)	(2,243)	(1,570)	(496)	(2,066)	(171)	(4,138)	(171)	(334)	(4,643)	(93)	(4,736)
Depreciation, amortisation and impairment	(75)	(29)	(8)	(37)	(5)	(107)	(5)	(9)	(121)	(45)	(166)
Net operating charges	(1,160)	(549)	(152)	(701)	(58)	(1,803)	(58)	(187)	(2,048)	11	(2,037)
Operating (loss)/profit before exceptional items	(105)	(54)	(90)	(144)	(48)	(201)	(48)	181	(68)	65	(3)
Operating exceptional items:											
ColleagueShare scheme	(115)	(81)	(26)	(107)	(9)	(213)	(9)	(17)	(239)	(5)	(244)
Other	(52)	(36)	(11)	(47)	(4)	(95)	(4)	(8)	(107)	(2)	(109)
Operating (loss)/profit	(272)	(171)	(127)	(298)	(61)	(509)	(61)	156	(414)	58	(356)
<b>Volumes (excluding door to door)</b>	<b>8,699</b>	<b>7,710</b>	<b>4,077</b>	<b>11,787</b>	<b>584</b>	<b>19,902</b>	<b>584</b>	<b>1,007</b>	<b>21,493</b>	<b>-</b>	<b>21,493</b>

### Income Statement 2006-07 (Restated)

					Less	Sub Total	Add back	Add	Sub Total		Total
	USO Total	Price Controlled non-USO products excluding Access	Downstream Access <sup>1</sup>	Total Price Controlled non-USO products	USO Non-Price Control products	Total Price Control products	USO Non-Price Control products	Other Letter products	Total Mails	Non-mails activities within RM Letters and other adjustments	Royal Mail Letters total <sup>2</sup>
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Revenue	3,459	2,366	325	2,691	191	5,959	191	638	6,788	175	6,963
Operating costs	(3,457)	(2,405)	(374)	(2,779)	(208)	(6,028)	(208)	(462)	(6,698)	(129)	(6,827)
People costs	(2,243)	(1,776)	(294)	(2,070)	(154)	(4,159)	(154)	(294)	(4,607)	(95)	(4,702)
Depreciation, amortisation and impairment	(63)	(26)	(4)	(30)	(5)	(88)	(5)	(7)	(100)	(42)	(142)
Net operating charges	(1,151)	(603)	(76)	(679)	(49)	(1,781)	(49)	(161)	(1,991)	8	(1,983)
Operating profit/(loss) before exceptional items	2	(39)	(49)	(88)	(17)	(69)	(17)	176	90	46	136
Operating exceptional items:											
ColleagueShare scheme	-	-	-	-	-	-	-	-	-	-	-
Other	(68)	(54)	(9)	(63)	(5)	(126)	(5)	(9)	(140)	(14)	(154)
Operating (loss)/profit	(66)	(93)	(58)	(151)	(22)	(195)	(22)	167	(50)	32	(18)
<b>Volumes (excluding door to door)</b>	<b>9,341</b>	<b>9,319</b>	<b>2,434</b>	<b>11,753</b>	<b>571</b>	<b>20,523</b>	<b>571</b>	<b>776</b>	<b>21,870</b>	<b>-</b>	<b>21,870</b>

<sup>1</sup> There is a small element of DSA service that is not price controlled, which is included within Other Letter Products above. These DSA services generated £1m profit in the year. The total for all DSA including this is stated in the summary of results on page 3.

<sup>2</sup> The total described above as Royal Mail Letters is reconciled to the Royal Mail Group Ltd statutory accounts in Note 1.

<sup>3</sup> The restatement is discussed further in note (ix) on page 16

## **Regulatory accounting principles and basis of preparation**

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### **A. General**

These regulatory financial statements are based on the financial records of the business and reconciled to operating profit within the Royal Mail Group Ltd statutory accounts on which the auditors have expressed an unqualified opinion. These statements have been prepared in accordance with the accounting policies set out on pages 13 to 18 of the Royal Mail Group Ltd statutory accounts unless otherwise stated.

The financial year ends on the last Sunday in March, and accordingly these accounts cover the 53 week period ended 30 March 2008.

The revenues, costs, assets, liabilities and cash flow effects of non-letter services and subsidiaries, associates and other undertakings (primarily operating outside the UK), have been agreed with Postcomm as being outside the scope of regulation.

Activity and cost driver information is used to assign costs to products; these product costs and revenues are then aggregated into the appropriate Services.

These statements have been prepared adopting the following principles:

- Principles as documented in “An overview of the principles and methodologies used in preparing regulatory financial statements for 2008”; and
- Accounting Policies for the income statement consistent with International Financial Reporting Standards. In so far as they impact upon the Regulatory Financial Statements, the UK GAAP based Accounting Policies used in the audited accounts of Royal Mail Group Ltd are consistent with IFRS.

In cases of conflict the principles as documented in “An overview of the principles and methodologies used in preparing regulatory financial statements for 2008” prevail.

### **B. Income statements**

#### **(i) General principles**

The income statements of the Services have been prepared by applying activity based costing methods and principles to the financial records of the business to assign costs. The resultant statements present the fully allocated costs of products covered by the Licence.

Costs and revenues have been directly allocated to products as far as practicable. Common operational costs that cannot be directly assigned are, using an activity based costing system, attributed to the products equitably. Overhead costs are apportioned to products based on traffic volumes. One off operating costs have been charged to business units where appropriate. In line with activity based costing approaches, estimates and judgements are required and have been applied in order to comply with the requirements of the Licence.

## **Regulatory accounting principles and basis of preparation**

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### **(ii) Revenue**

Revenue is defined as turnover plus internal income for core services. Revenue is assigned directly to the appropriate product, with the exception of stamp and meter revenue. Account traffic revenue is sourced from the billing systems.

Stamp and meter revenue is assigned to Royal Mail products by applying a statistical analysis of mail stream characteristics. Special Delivery stamp and meter revenue is calculated from the volumes recorded by the track and trace system.

### **(iii) Operating costs**

Accommodation and vehicle costs relating to operational postal activities have been included within operating costs in the regulatory financial statements. For the purposes of the regulatory financial statements, depreciation, amortisation and impairment, and people costs have been separately identified.

### **(iv) Operating exceptional items**

The total operating exceptional items (including Colleague Share) relating to the mails operations are allocated across the regulatory Service columns on the face of the regulatory income statement on a basis appropriate and consistent to the type of cost.

### **(v) Share of post tax profit in associates and joint ventures**

The share of the post tax profit of associated undertakings and joint ventures has been assigned to non-letters services (excluded from the Regulatory Financial Statements total) and is included within the adjustments column in the income statement on page 13.

### **(vi) Net profit on disposal of property, plant and equipment**

Profits and losses on sale of properties are held within separate property business units. They are not assigned to the Letters business unit, and consequently do not feature in the income statement on page 13.

### **(vii) Profit / (loss) on disposal of businesses**

Profit / (loss) on disposal of businesses are recorded at Group level and not assigned to the Letters business unit. They do not feature in the income statement on page 13.

### **(viii) Excluded items**

Postcomm has agreed the items below profit before financing and taxation are excluded from the regulatory financial statements.

## Regulatory accounting principles and basis of preparation

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### (ix) Prior year comparatives

In connection with the refinancing package previously agreed with the Shareholder, Royal Mail Group Ltd (i) transferred most of its directly held property assets (excluding building fit-outs) to Royal Mail Estates Limited (RMEsL) on the last day of the 2007 financial year and (ii) entered into leasebacks at market value for the property assets transferred. Accordingly, the 2006-07 result for Royal Mail Letters has been restated to be on a comparable basis as if RMEsL had operated in 2006-07 in the way it has operated in 2007-08.

The prior year regulatory income statement has been restated to reflect the reduction in Royal Mail Letters profit. Royal Mail considers that this will help the reader evaluate year on year movements more transparently.

The impact on operating profit before exceptional items of restating the prior year to reflect the new status of property within RMEsL is shown below.

	USO £m	Price Controlled £m	Royal Mail Letters £m
2006-07 as originally reported	27	(12)	194
Adjustment for RMEsL	(25)	(57)	(58)
2006-07 restated	2	(69)	136

### C. Key drivers

#### (i) Income statement

Revenues are primarily driven directly to products by sales account detail or traffic volumes. Resource costs within the ledgers are driven to activities by activity and utilisation analysis. Appropriate drivers are used to assign activity costs to products. Traffic volumes are used as the primary driver of activity costs to sales products, though weighting factors are also applied to differentiate the cost assignment between product types. Products are then analysed into Services.

#### (ii) Traffic volumes

The activity based costing system makes extensive use of traffic volumes to assign costs to products.

Operational traffic methodology, based on sampling at mail centres, has been used as the basis for measuring inland stamped and metered traffic volumes. This approach involves determining traffic in the workplace by machine counting or by counting numbers of containers and applying statistical techniques.

Royal Mail continues to refine its approach to traffic measurement and statistical procedures for stamp and meter traffic.

Non stamp and meter traffic i.e. "account traffic" volumes are sourced from billing or track and trace systems.

## **Regulatory accounting principles and basis of preparation**

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International traffic volumes are determined by applying a statistically derived “items per kilo” to the weight of mail carried to international destinations.

### **(iii) Activity analysis**

People costs have been assigned to activities based on an analysis of operational hours and samples of the time spent by staff on specific activities. Whilst Royal Mail believes this provides a fair representation of activities in the operation, it has recognised the potential for improvement.

Royal Mail actively reviews the quality of the operationally sourced data that is used to drive costs within its activity based costing system. Continuing activity started in 2006-07, this year attention has been focused on processes surrounding the recording of operational hours worked.

There are inherent limitations in accurately recording staff time by individual activity. Time is recorded in accordance with Authorised Working Duties ('AWDs'), which set out the duties for staff at each operational site against expected traffic volumes. These are amended by 'pressure' (overtime to cover peak workloads) and 'lapsed' (where duties or part of the duties are not undertaken, due to lower workloads) time adjustments each week. An action plan has been deployed to address the recognised inadequacies in the current time recording procedures within mail centres. Royal Mail has rationalised the number of activities to which time can be assigned, and has driven updates in the AWD summaries during 2007-08. This will continue on a rolling basis through 2008-09.

During 2007-08 a process of reapportioning the hours data to reflect the traffic recorded was introduced, which more closely aligns the allocation of hours to activities and traffic profile. This process will be reviewed and enhanced in 2008-09.

A similar approach is intended to be implemented in Delivery offices in 2008-09

Royal Mail has prepared its regulatory financial statements using methodologies that are consistent with previous years.

Other costs have been assigned to activities by the use of appropriate drivers.

### **(iv) Statistical information**

In assigning costs to products and services, Royal Mail makes use of statistically sampled information that is collected from operational sites. This information is used to determine relative weighting factors that allow cost differentials to be generated during the cost assignment process. One of the characteristics sampled is the average size of an item.

Historically, Royal Mail has refreshed this data for the latest sampled information each year, basing measurement on mails characteristic sampling data from the last one to two completed financial years.

In August 2006, Royal Mail introduced Pricing in Proportion. This had an impact on the average size of mail items. Consequently, sampling data preceding this is no longer valid,

## **Regulatory accounting principles and basis of preparation**

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and hence only mails characteristic samples between August 2006 and March 2007 have been used in 2007-08.

### **D. Internal trading and transfer charging**

Royal Mail operates through business units that make use of each other's services in order to take advantage of Group synergies, having regard to the mutual dependencies that exist.

Transfer charges are raised for internal trading and eliminated on consolidation. The elimination is shown in the reconciliation to the Royal Mail Group Ltd results.

Charges made for core services provided by Royal Mail Letters to other business units (i.e. Official Mail) are accounted for within revenue, whilst charges incurred by Royal Mail Letters for other services such as market rental charges for property, are accounted for within other operating charges.

Internal charges used in the production of the regulatory financial statements have been adjusted to reflect actual cost, which ensures that central functions within the Group do not generate a notional profit or loss. The principal exceptions to this are Post Office Ltd charges that are set using a basis of charges reached through a negotiation between the respective businesses, and Royal Mail Estates Ltd charges that are at market rates.

### **E. Balance sheet**

As set out on page 11, Royal Mail has agreed with Postcomm that it is not required to publish a balance sheet for 2007-08.

### **F. Cash flow statement**

As set out on page 11, Royal Mail has agreed with Postcomm that it is not required to publish a cash flow statement for 2007-08.

## Notes to the statements

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The following pages contain note information as follows:-

Note 1 - Reconciliation of the regulatory income statement to the Royal Mail Group Ltd audited operating profit/(loss)

Note 2 - 2007-08 Analysis of the USO and other Price Controlled products between Licensed and Non-Licensed services

Note 3 - 2007-08 People costs analysis

Note 4 - Non-mails activities within Royal Mail Letters and other adjustments

Note 5 - Royal Mail Letters exceptional items included in operating charges

Note 6 - Royal Mail Group Ltd provisions for liabilities and charges

As agreed with Postcomm comparative information is not required for notes 2 and 3.

## Notes to the statements

### 1. Reconciliation of the regulatory income statement to the Royal Mail Group Ltd operating profit/(loss)

2007-08

	Revenue £m	People costs £m	Depreciation and amortisation £m	Other operating charges £m	Operating profit/(loss) before operating exceptional items £m	Operating exceptional items £m	Operating (loss)/profit £m
<b>Royal Mail Letters per Regulatory Income Statement (page 13)</b>	<b>6,936</b>	<b>(4,736)</b>	<b>(166)</b>	<b>(2,037)</b>	<b>(3)</b>	<b>(353)</b>	<b>(356)</b>
Other Units	388	(277)	(16)	(93)	2	(17)	(15)
Inter business eliminations and recharges	(94)	-	-	94	-	-	-
IRED Balance Sheet Support	-	-	-	(9)	(9)	-	(9)
Restatement Adjustment for RMEsL	-	-	-	-	-	-	-
<b>Royal Mail Group Ltd</b>	<b>7,230</b>	<b>(5,013)</b>	<b>(182)</b>	<b>(2,045)</b>	<b>(10)</b>	<b>(370)</b>	<b>(380)</b>

2006-07 (Restated)

	Revenue £m	People costs £m	Depreciation and amortisation £m	Other operating charges £m	Operating profit/(loss) before operating exceptional items £m	Operating exceptional items £m	Operating (loss)/profit £m
<b>Royal Mail Letters per Regulatory Income Statement (page 13)</b>	<b>6,963</b>	<b>(4,702)</b>	<b>(142)</b>	<b>(1,983)</b>	<b>136</b>	<b>(154)</b>	<b>(18)</b>
Other Units	344	(288)	(29)	(23)	4	(1)	3
Inter business eliminations and recharges	(92)	-	-	92	-	-	-
Removal of impairment of investment in Spring (not in RMG Ltd)	-	-	-	-	-	10	10
IRED Balance Sheet Support	-	-	-	-	-	-	-
Restatement Adjustment for RMEsL	-	-	-	58	58	-	58
<b>Royal Mail Group Ltd</b>	<b>7,215</b>	<b>(4,990)</b>	<b>(171)</b>	<b>(1,856)</b>	<b>198</b>	<b>(145)</b>	<b>53</b>

## Notes to the statements

### 2. 2007-08 Analysis of the USO and other Price Controlled products between Licensed and Non-Licensed services

<b>USO Products</b>			
	Licensed 0 - 350g £m	Non Licensed £m	Total £m
Revenue	2,261	1,112	3,373
Operating Costs	(2,494)	(984)	(3,478)
People costs (analysed below)	(1,756)	(487)	(2,243)
Depreciation, amortisation and impairment	(50)	(25)	(75)
Net operating charges	(688)	(472)	(1,160)
Operating profit/(loss) before exceptional items	(233)	128	(105)
Operating exceptional items			(167)
Operating profit/(loss)			(272)
Volumes (excluding door to door)	7,952	747	8,699

<b>Non-USO Price controlled Products, Including Access</b>		
Licensed 0 - 350g £m	Non Licensed £m	Total £m
2,228	432	2,660
(2,378)	(426)	(2,804)
(1,748)	(318)	(2,066)
(33)	(4)	(37)
(597)	(104)	(701)
(150)	6	(144)
		(154)
		(298)
10,999	788	11,787

#### People costs analysis

<b>USO Products</b>			
	Licensed 0 - 350g £m	Non Licensed £m	Total £m
Wages, salaries and social security	(1,528)	(424)	(1,952)
Pensions	(228)	(63)	(291)
People costs total as above	(1,756)	(487)	(2,243)

<b>Non-USO Price controlled Products, Including Access</b>		
Licensed 0 - 350g £m	Non Licensed £m	Total £m
(1,521)	(277)	(1,798)
(227)	(41)	(268)
(1,748)	(318)	(2,066)

## Notes to the statements

### 3. 2007-08 People costs analysis

	USO Total £m	Price Controlled non-USO Products excluding Access £m	Downstream Access £m	Total Price Controlled non-USO Products £m	USO Non Price Control Products £m	Total Price Control Products £m	USO Non Price Control Products £m	Other Letter Products £m	Total Mails £m	Non-mails activities within RM Letters and other adjustments £m	RM Letters Total £m
Wages, salaries and social security	(1,952)	(1,366)	(432)	(1,798)	(149)	(3,601)	(149)	(291)	(4,041)	(81)	(4,122)
Pensions	(291)	(204)	(64)	(268)	(22)	(537)	(22)	(43)	(602)	(12)	(614)
Total People costs	(2,243)	(1,570)	(496)	(2,066)	(171)	(4,138)	(171)	(334)	(4,643)	(93)	(4,736)

## Notes to the statements

### 4. Non-mails activities within RM Letters and other adjustments

Non-mails activities include the Address Management Centre, Customer Management, Logistics and Stamps & Collectables. Other adjustments relate to the elimination of inter-business activities and reclassifications, where there is different treatment of costs between the statutory accounts and the regulatory financial statements. Centrally held costs are those which relate to regulated activities but are held within the holding company.

2007-08				
	Revenue £m	People costs £m	Depreciation, amortisation and impairment £m	Net operating charges £m
Non-mails activities	129	(52)	-	(46)
Interbusiness / Other adjustments	63	(41)	(45)	57
<b>Total</b>	<b>192</b>	<b>(93)</b>	<b>(45)</b>	<b>11</b>

2006-07 (Restated)				
	Revenue £m	People costs £m	Depreciation, amortisation and impairment £m	Net operating charges £m
Non-mails activities	120	(54)	-	(42)
Interbusiness / Other adjustments	55	(41)	(42)	50
<b>Total</b>	<b>175</b>	<b>(95)</b>	<b>(42)</b>	<b>8</b>

### 5. Royal Mail Letters exceptional items included in operating charges

	2007-08 £m	2006-07 (Restated) £m
Provision for restructuring	(109)	(140)
ColleagueShare scheme	(244)	-
Impairment of intangible assets	-	(4)
Impairment of goodwill relating to associates	-	(10)
	<b>(353)</b>	<b>(154)</b>

The £109m restructuring charge is all in respect of employee related costs (2006-07 £140m).

## Notes to the statements

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### 6. Royal Mail Group Ltd provisions for liabilities and charges

	2007-08 £m	2006-07 (Restated) £m
Total provisions for liabilities and charges	226	114

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The provision includes amounts relating to ColleagueShare £105m (2007 £Nil), onerous property contracts £23m (2007 £35m) and decommissioning costs, £7m (2007 £9m) with the balance of £91m (2007 £70m) principally relating to redundancy.

During the year £219m (2007 £141m) was charged to operating exceptional items and £3m released (2007 charged £20m) to other operating costs.

The provision is in the main expected to be utilised in 2008-09 with the remaining amounts expected to be utilised over the next two to three years, except for £105m (2007 £Nil) relating to ColleagueShare expected to be utilised within 5 years and £2m relating to onerous property contracts expected to be utilised over a period longer than 3 years. The timing of cash flows for such provisions are by their nature uncertain and dependent upon the outcome of related events.

The change in the carrying value of the discounted element of the provision due to the passage of time is not material.

## Statement of responsibilities

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Royal Mail Group Ltd is required, as agreed with Postcomm and under Condition 15 of the Licence, to provide regulatory financial statements in respect of each regulatory Service.

Royal Mail Group Ltd confirms that the regulatory financial statements have been prepared, after agreeing formats with Postcomm, in accordance with the above requirement and:

1. The statements have been prepared using accounting systems operating on the basis of objectively justifiable cost accounting principles that assign cost and revenue data to the Services;
2. Costs and revenues have been directly allocated to products as far as practicable. Common operational costs that cannot be directly assigned are, using an activity based costing system, attributed to the products equitably. Overhead costs are apportioned to products based on traffic volumes. In line with activity based costing approaches, estimates are required and have been applied in order to comply with the requirements of the Licence. Where there is no obvious driver to assign overhead costs to products, judgements are applied to ensure such costs are reasonably assigned;
3. The regulatory financial statements have been prepared adopting the following principles:
  - Principles as documented in “An overview of the principles and methodologies used in preparing regulatory financial statements for 2008; and
  - Accounting Policies for the income statement consistent with International Financial Reporting Standards. In so far as they impact the income statement, the UK GAAP based Accounting Policies used in the audited accounts of Royal Mail Group Ltd for the year ended 30 March 2008 are consistent with IFRS. In cases of conflict the principles as documented in “An overview of the principles and methodologies used in preparing regulatory financial statements for 2008” prevail; and
4. The regulatory financial statements are based on the financial records of the business and have been reconciled to the operating profit within the audited Royal Mail Group Ltd statutory accounts.

The methodology adopted to produce the regulatory financial statements has been documented in “An overview of the principles and methodologies used in preparing regulatory financial statements for 2008” and in notes A to F on pages 14 to 18. The methodology and approaches used to create these financial statements are not intended to establish precedents for future regulatory financial statements.

Signed on behalf of the Board of Royal Mail Group Ltd.

Adam Crozier  
16 July 2008

Ian Duncan  
16 July 2008

## **Independent auditors' report**

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Independent auditors' report to the Directors of Royal Mail Group Ltd ("the Company") issued as required by Condition 15 of the Licence dated 25 May 2006 granted by the Postal Services Commission ("Postcomm").

We have audited Part 1 of the Regulatory Financial Statements on pages 3 to 24. Part 1 of the Regulatory Financial Statements, which have been prepared by the Company, comprises separate statements for the year ended 30 March 2008 for each of the services described on page 10 ("the Services").

This report is made solely to the Company's directors, as a body, in accordance with the requirements of Condition 15 of the Licence and the terms of our engagement. Our audit work has been undertaken so that we might state to the Company those matters we are required to state to them in a report of the independent auditors and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's directors as a body, for our audit work, for this report, or for the opinions we have formed.

### **Basis of Preparation**

Part 1 of the Regulatory Financial Statements has been prepared using the "Regulatory accounting principles and basis of preparation" set out on pages 14 to 18, as agreed with Postcomm to meet Condition 15 of the Licence.

Part 1 of the Regulatory Financial Statements is separate from the Statutory Financial Statements of the Company and has not been prepared on the basis of the presentation and disclosure requirements of International Financial Reporting Standards ("IFRS"). Financial information other than that prepared on the basis of IFRS does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 1985.

As explained in the "Regulatory accounting principles and basis of preparation" on pages 14 to 18, as agreed with Postcomm to meet the requirements of paragraph 2 of Condition 15 to the Licence, Part 1 of the Regulatory Financial Statements is prepared by disaggregating balances recorded in the general ledgers and other accounting records of the Company maintained in accordance with the Companies Act 1985 and used, in accordance with that Act, for the preparation of the statutory financial statements of the Company for the years ended 30 March 2008 and 25 March 2007 ("the Statutory Financial Statements").

As explained on pages 14 to 18 in the "Regulatory accounting principles and basis of preparation", in selecting appropriate attribution methods and appropriate non-financial data for use within the attribution models employed in the production of Part 1 of the Regulatory Financial Statements, the Company has had to make certain estimates and exercise its judgement, having regard to the terms of Condition 15 to the Licence, including cost causality and objectivity. The Company has informed Postcomm that attribution methods and non-financial data sources will be subject to ongoing review and, where deemed appropriate, improvement. Some changes have been made in the current year to certain attribution methods and these are described in the "Regulatory accounting principles and basis of preparation" and notes to Part 1 of the Regulatory Financial Statements.

### **Respective responsibilities of the Directors and independent auditors**

The Company's responsibilities for preparing Part 1 of the Regulatory Financial Statements as agreed with Postcomm to meet the requirements of Condition 15 of the Licence are set out in the Statement of responsibilities on page 25.

Our responsibilities, as independent auditors, are established in the United Kingdom by the Licence, and by professional guidance.

We report our opinion as to whether Part 1 of the Regulatory Financial Statements for the year ended 30 March 2008 has been properly prepared, in all material respects, in accordance with the "Regulatory accounting principles and basis of preparation" on pages 14 to 18 and with the requirements of paragraph 4(a) of Condition 15 of the Licence.

We also report our opinion as to whether the records maintained pursuant to paragraph 1 of Condition 15 to the Licence comply with the requirements of paragraph 2 of Condition 15 to the Licence, amended as agreed with Postcomm.

We also read the Business review and Licence requirements in Part 1 and the Review of the year section of Part 2 of the Regulatory Financial Statements and consider the implications for our report if we become aware of any apparent misstatements within them.

### **Basis of audit opinion**

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board except as noted below. This includes examination, on a test basis, of evidence relevant to the amounts and disclosures in Part 1 of the Regulatory Financial Statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the Part 1 of Regulatory Financial Statements, and of whether the accounting policies are consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that Part 1 of the Regulatory Financial Statements is free from material misstatement, whether caused by fraud or other irregularity or error. However, as the nature, form and content of Part 1 of the Regulatory Financial Statements is determined by the Regulator, we did not evaluate the overall adequacy of the presentation of the information, which would have been required if we were to express an audit opinion under International Standards on Auditing (UK and Ireland).

Our opinion on Part 1 of the Regulatory Financial Statements is separate from our opinion on the statutory accounts of the Company on which we expressed an unqualified audit opinion on 4 July 2008, which are prepared for a different purpose. Our audit report in relation to the statutory accounts of the Company (our "statutory" audit) was made solely to the members of the Company, as a body, in accordance with section 235 of the Companies Act 1985. Our statutory audit work was undertaken so that we might state to the members of the Company those matters we are required to state to them in a statutory auditor's report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume any responsibility to anyone other than the Company and the members of the Company as a body, for our statutory audit work, for our statutory audit report, or for the opinions we have informed in respect of that statutory audit.

### Opinion

Although the Company maintains records for each service, many of the group's revenues and costs are not directly identifiable with individual services because of the extent of common assets and services. Therefore the preparation of the Regulatory Financial Statements requires a significant number of apportionments. This means that the records are not those that would exist if each of the Services were to be carried on by separate businesses in accordance with paragraph 2(b) of Condition 15 and accordingly are not such that if each of the separate Services was carried on by a separate company incorporated under the Companies Act 1985 each of those companies would comply with subsections 221(1) and (2) of that Act. Except as indicated above in our opinion the above records have been maintained to comply with the requirements of paragraph 2 of Condition 15 to the Licence, amended as agreed with Postcomm; and

In our opinion, Part 1 of the Regulatory Financial Statements of the Services for the year ended 30 March 2008, have been properly prepared, in all material respects, in accordance with the "Regulatory accounting principles and basis of preparation" on pages 14 to 18 and with the requirements of paragraph 4(a) of Condition 15 of the Licence.

Ernst & Young LLP

London

16 July 2007

## **Glossary and explanation of terms**

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### **£m**

Million pounds sterling.

### **2007-08**

53 week period ending 30 March 2008.

### **2006-07**

52 week period ending 25 March 2007.

### **Account traffic**

Account traffic is the volume of mail associated with customers who pay for postal services on account.

### **Activity based costing (“ABC”)**

Activity based costing is a widely used and accepted method of costing products, services, customers and sales channels based upon the cost of the activities required to produce these outputs. The method identifies the resource consumed by activities and assigns a cost to the resource utilised by each activity. These are aggregated to derive activity costs.

Activity costs are then assigned to outputs, based upon pre defined cost drivers. These cost-drivers provide a measure of the intensity or frequency of an activity demanded by a product or service and reflect a cause and effect relationship.

### **Bulk Mail**

The Bulk Mail definition includes Mailsort, Walksort and Cleanmail products.

### **Business units**

Business units are the separate divisions that make up Royal Mail Group Ltd.

### **Downstream Access**

Customer and other licensed postal operators’ mail, which enters the Royal Mail pipeline after the outward sortation and distribution processes.

### **EC Directive**

A requirement placed upon the postal administrations of all EU member states to produce accounts in accordance with a prescribed specification.

### **Fully allocated cost (“FAC”)**

The summation of direct and assigned costs for products or services such that no common costs are left unassigned.

### **Group**

The business units that together make up Royal Mail Group Ltd, including Royal Mail Letters, Parcelforce Worldwide, and Post Office Ltd in the UK.

### **IFRS**

International Financial Reporting Standards.

### **Long run marginal costs (“LRMC”)**

## **Glossary and explanation of terms**

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The cost incurred in processing additional volumes of mail, assuming that levels of efficiency and service are maintained and that changes are made to all resources that need to be changed in order to achieve this. The assessment is typically made over a 3 to 5 year time horizon.

### **Mail stream characteristics**

The payment method, class and format of mail items.

### **Pipeline**

The sequence of operational processes that is followed by an item of mail. The full pipeline includes collection, sortation/ processing, distribution and delivery.

### **Postal services**

A collective term for the Licensed USO, Non Licensed USO and Other letter products.

### **Postal Services Commission (“Postcomm”)**

The body created under the Postal Services Act 2000 to regulate postal services in the UK.

### **Products**

Products and services offered to customers.

*For a full list of products refer to [www.royalmail.com](http://www.royalmail.com) and select Product A-Z.*

### **PSA**

Postal Services Act 2000.

### **Regulatory financial statements (“Regulatory accounts”)**

The statements, accounts and reports as expressed in the terms of the Licence which specifically refer to the year ended 30 March 2008 and comparative information for the previous year.

### **Revenue derived traffic**

Volumes where the stamped and metered elements are derived from ledgered revenue using average unit revenues and the Mail Characteristics Survey – a survey of mail types (product stream and content) and volume which is used to derive payment method and class of mail items.

### **Royal Mail**

The business units that collectively deliver the regulatory Services.

### **Royal Mail Estates Ltd**

A wholly owned subsidiary of Royal Mail Group Ltd. RMEsL leases its property fixed assets to Royal Mail Group Ltd under operating leases.

## **Glossary and explanation of terms**

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### **Royal Mail Group Ltd**

A wholly owned subsidiary of Royal Mail Holdings plc and immediate parent undertaking of Post Office Ltd, General Logistics Systems International Holdings B.V. and Royal Mail Estates Ltd, for which company statutory accounts are prepared.

### **Royal Mail Holdings**

Royal Mail Holdings plc.

### **Royal Mail Letters**

The principal business unit within Royal Mail.

### **The Licence**

The Licence granted to Royal Mail Group Limited, by the Postal Services Commission on 23 March 2001, as amended up to 25 May 2006.

### **The Services**

The regulatory Services as defined by Postcomm.

### **UK**

United Kingdom.

### **UK GAAP**

UK Generally Accepted Accounting Practice.

### **Underlying growth**

Volume growth based on revenue derived traffic volumes adjusted for the number of working days in each accounting year.

### **USO**

Universal Service Obligation.