

Post Office Limited

**POST OFFICE LIMITED**  
**(Company Number 2154540)****Meeting of the AUDIT, RISK AND COMPLIANCE SUB-COMMITTEE**  
**to be held at 08.30 on Tuesday 21 May 2013**  
**at 148 Old Street, London, EC1V 9HQ in the Board Room**

			<b>Action Requested</b>
08.30	1	Presentation of draft Annual Report and Financial Statements for the 53 weeks ended 31 March 2013	
		• Draft Annual Report and Financial Statements	Chris Day
		• Briefing Book	Annex A Annex B
08.55	2	Audit results report	E&Y report
09.10	3	Any other business (a) Update on various Financial Services matters, including Bank of Ireland (UK) plc capital & liquidity	Nick Kennett
<b>POL executives will then leave the meeting</b>			
09.15	4	Opportunity for auditor comments	
09.25	5	Date of Next Meeting	Wednesday 5 June 2013 14.00-16.00

PRESENT: Alasdair Marnoch (Chairman)  
Susannah Storey (Non-executive director)  
Neil McCausland (Non-executive director)  
Tim Franklin (Non-executive director)

SECRETARY: Alwen Lyons (Company Secretary)

IN ATTENDANCE: Alice Perkins (Company Chairman)  
Chris Day (CFO)  
Sarah Hall (Head of Financial Control and Compliance)  
Malcolm Zack (Head of Internal Audit)  
Angus Grant (Ernst & Young)  
Jeremy Midkiff (Ernst & Young)

APOLOGIES FOR ABSENCE: Susan Crichton (HR & Corporate Services Director)

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**POST OFFICE LIMITED AUDIT, RISK & COMPLIANCE SUB-COMMITTEE**

**Annual Report and Financial Statements for 2012-13**

**1. Purpose**

The purpose of this paper is to:

- 1.1 Invite the Post Office Limited Board Audit Risk and Compliance Sub-Committee to review the Post Office Limited Annual Report and Financial statements for the 2012-13 financial year and to recommend their approval to the Post Office Limited Board.

**2. Background**

- 2.1 The ARC agreed a number of changes to the process for the production of the Post Office Limited Annual Report and Financial Statements at its meeting in November 2012. For the first time the Post Office has opted not take advantage of exemptions available to it as a wholly owned subsidiary of Royal Mail Holdings plc. The Annual Report and Financial Statements have been produced as if Post Office Limited was a standalone group and follow the content and style of a listed plc where that approach can be taken.
- 2.2 The following documents are attached to this paper:
  - Plan of the Annual Report contents;
  - Draft Annual Report;
  - Draft Financial Statements;
  - Initial design concepts;
  - ARC briefing book to aid understanding of the financial statements.

**3. Annual Report and Financial Statements approach and plan**

- 3.1 The Annual Report and Financial Statements are planned for publication in the first week of July against the backdrop of tight budgetary control within the company, a difficult external economic environment which is putting pressure on margins and discussions with Government around future strategy and post-2015 funding positions.
- 3.2 We have developed the messages and content by working very closely with a comprehensive range of stakeholders and contributors from across the business to ensure it accurately reflects the progress we have made. ExCo directors and their teams have been closely involved in the process. Please note that the report will be copy edited for style and consistency.
- 3.3 The approach follows the overall positioning set out to the ARC in February:
  - solid progress on fundamentals creating confidence for the journey ahead (with a sense that in key areas, such as Network and Crown Transformation, *the turnaround has started*, albeit in difficult circumstances);
  - excitement at the innovation and change capabilities of this newly independent company to deliver commercial and social value: *the spirit of a start-up*;

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- realism as to the task ahead, and empathy with subpostmasters and colleagues as we *work together* in challenging circumstances.
- 3.4 The Financial Statements have been prepared by Finance and the Ernst & Young audit work is largely complete. The Annual Report is still subject to audit review. For the first time the Post Office has prepared consolidated Financial Statements under International Financial Reporting Standards (IFRS), which is in line with a majority of listed plcs. Post Office Limited still has a statutory obligation to produce company accounts and these have been prepared in accordance with the Companies Act 2006 and UK Generally Accepted Accounting Practice (UK GAAP), consistent with prior years. A full ARC briefing book is attached. This provides a more detailed analysis of the results to aid understanding of the financial statements.
- 3.5 We have a project plan which is being led by the Communications team working closely with Finance. The current timeline is:
- 15 May – ARC and Board receive report in Word format
  - 20 May – Initial feedback from Board
  - 21 May – ARC meeting reviews Annual Report together with the Financial Statements and will be asked to recommend that the Board approves the Annual Report and Financial Statements.
  - 21 May – Board reviews the Annual Report together with the Financial Statements and will be asked to approve it and delegate authority to a Sub-Committee to approve final changes and sign on a later date
  - 22 May – Further amendments made following Board feedback
  - 21-29 May – share draft of Annual Report and Financial Statements with Royal Mail and Shareholder Executive for review and comment
  - 6 June – PDFs of designed pages for proofing and sign off
  - June – date to be confirmed – Board Sub-Committee approves final version and signs. Ernst & Young sign the audit report.
  - 7 June to beginning of July – building online version and printing hard copy
  - w/c 1 July – launch

**4. Proposal**

- 4.1 We have appointed Merchant Cantos, an agency which specialises in producing annual reports for leading public and private organisations. They have been working closely with the Communications team to produce the report.
- 4.2 Traditional paper copies of the report will be produced alongside an interactive digital version which will be accessible via [postoffice.co.uk](http://postoffice.co.uk). This will feature a fresh and modern look and feel, including video interviews from the Chairman, Chief Executive, members of staff, customers and subpostmasters.
- 4.3 The content includes an introduction from the Chairman and an executive summary from the Chief Executive. In order to ensure that the Post Office surprises with its approach, space has also been set aside for comments and reflections from members of staff, customers and subpostmasters. A full

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Corporate Governance section, Financial Review and Directors' Remuneration Report are all included for the first time.

- 4.4 We are commissioning new photography and video content for the report and have engaged an agency to support this. The project is funded from the communications budget.
- 4.5 A full PR, stakeholder and colleague engagement plan, including defensive Q&A is being developed around the report, including a launch event which includes key stakeholders, suppliers, journalists and colleagues/subpostmasters.
- 4.6 A number of options are being considered for using the Annual Report as a platform for positive PR. These include our commitments to support digital inclusion, our role in High Street renewal and the "public purpose" engagement campaign, which is due to start in July. We propose taking a tactical approach to this element of the report, making a final decision closer to publication.
- 4.7 The structure of the report is designed to flow from the headline statements from the Chairman and CEO through operational reviews and on to the financial report, led by the CFO's review.
- 4.8 The design of the report will be such that the operational section will be introduced with a "business at a glance" section which gives an overview of each business area before going into more detail. This is important to consider when reading the document. There may be elements which feel repetitive but this will be considered in the layout and designs.
- 4.9 The design process will also allow opportunities for use of graphics such as pie charts.

**5. Recommendation**

- 5.1 The Post Office Limited Board Audit Risk and Compliance Sub-Committee is asked to:
  - Review the Annual Report and Financial Statements and provide individual comments to Chris Day and Mark R Davies by 9am on Monday 20 May;
  - Recommend to the Post Office Board
    - i. That the Annual Report and Financial Statements should be approved; and
    - ii. That authority is delegated for reviewing final amendments and completing the Annual Report and Financial Statements on behalf of Post Office Limited to a Sub-Committee, the quorum for which to comprise any three of Alice Perkins, Paula Vennells, Chris Day and Alasdair Marnoch.
  - Note that the Chairman of the Audit Risk and Compliance Sub-Committee will be asked to provide a verbal update of this meeting to the Board.

Post Office Limited Annual Report and Financial Statements 2012-13

## Section: Overview

Title: Who we are

At the Post Office our aim is to provide customers with the things that are important to them – from mail to their broadband package, car insurance to their savings account. Whether customers come into branch, are on the move, or shop online, we will ensure they can trust us to always deliver a great experience. That's the Post Office promise.

Heading: The Post Office in numbers

- The largest retail network in the UK
- 11,780 branches
- 99.7% of the population within three miles of a branch
- Number one travel money provider
- Fast-growing UK financial services provider
- Biggest acceptor of contactless payments in Europe
- 18 million customers a week, including half of the UK's small businesses
- 15 billion inland addressed items handled every year
- 95% of all UK debit card accounts accessible through our branches
- The sixth largest telecoms provider in the UK
- 87% customer satisfaction across our branches
- One of the most trusted brands in the UK

## Section: Overview

### Chairman's foreword

It is with great pleasure and pride that I write the foreword to the first Annual Report and Financial Statements for the Post Office as an independent business.

The Report describes the way in which the Post Office has embarked on a remarkable turnaround to reverse the trend of years of declining revenues, sustained branch closures and a reputation for inconvenience and queues.

Thanks to our Shareholder, the government, we are investing millions of pounds into our network over the three years up to April 2015. There is no longer a programme of Post Office branch closures. Instead, we are modernising the network, increasing our opening hours, offering new services, developing new methods of interacting with our customers, working with our key partners in new ways, cutting costs and increasing our revenues.

All of this puts the Post Office on the path to securing financial sustainability for the long term, reducing our dependence on the taxpayer to the minimum, and changing our culture so that we are always on the front foot, responding to changes in the world around us in partnership with the key people on whom we depend for the delivery of our services. If we are successful in achieving these changes, in particular financial sustainability, the conditions for the successful mutualisation of the Post Office could be in place - a prospect which could help to secure the kind of self-sustaining Post Office we all want to see in the future.

A series of important changes has already happened and many more are in the pipeline.

We ceased to be a subsidiary of Royal Mail Group Limited in April 2012 and began operating independently. Since then, I have completed the formation of my Board and we are now operating Board governance in keeping with best practice in the corporate world. Full details of the Board members and our Board committees are on pxx. I am delighted to have been able to appoint such able people with varied backgrounds who are all committed to supporting and challenging the Post Office as it pursues the changes which must be made if we are to secure its future.

We achieved a number of notable successes last year. For the second year running, our revenues are up on the previous year despite the difficult economic environment. We are on the road to reducing our reliance on the Network Subsidy Payment received from the government. We have made great headway in our plan to modernise the network of branches run by our agents. 1,450 have signed up to be converted into new operating models which give much better service to customers, resulting in higher footfall and turnover. And we have made real improvements to the running of our Crown branches where the operating loss has reduced this year from £xx million to £37 million.

We have won a number of new government contracts under which we are providing some completely new services and enabling central and local government to realise significant administrative savings. We are also offering new financial services, maintaining our appeal to customers who come to us for the reliability and transparency of our financial offers. Our mails business, meanwhile, remains the market leader and is increasingly innovative.

We are clear about the way forward for the Post Office and about the changes which need to take place to build on the successes set out in this Report. We are equally clear, that there are

significant challenges ahead; the going is not easy. This turnaround, like any other, requires people throughout the organisation and their partners to work in new ways. We need to win new business on proper commercial terms - something which is difficult in current economic circumstances. And we need to reduce our high fixed costs while at the same time finding the resources to operate on our own two feet and to modernise and innovate - catching up after years of under-investment.

I would like to thank the Post Office Chief Executive, Paula Vennells, her team and all the people who work to support the Post Office business, and have brought about the remarkable changes we have already seen and will see in the coming months and years. I would like also to thank all those stakeholders and partners with whom we work so closely.

The Post Office has a long and honourable 370-year history. We need to retain the essence of what has made it great and made it loved, while at the same time making it fit for the future. It is in that context that this Annual Report and Financial Statements should be seen. They report on the first steps of progress into the future - a future which blends the trust, integrity and accessibility, for which the Post Office is renowned, with the contemporary relevance, innovation and professionalism of a financially sound 21st century business.

Alice Perkins

Chairman

## Section: Overview

### Title: Chief Executive's review

The Post Office is committed to a strategy which will grow and modernise our business business and customer excellence is always at its core. It is heartening, therefore, to be able to report good progress in these endeavours during the 2012-13 financial year. In essence, the evidence on the pages which follow shows that we have started to turn the business around, remaining at the heart of communities while becoming increasingly commercial and entrepreneurial.

In a challenging economic climate, and with particular pressures on the high street, we can report strong progress in attracting the revenue so important to underpinning the business and sustaining the network. Revenue has grown in three of our four pillars during 2012-13, with turnover increasing by £44 million to £1.02 billion. Mails and Retail revenue has grown by 4.3%, Financial Services by 6.4%, and Telecoms by 7.5%, while Government Services revenue remained flat in the context of the very tight fiscal environment resulting in reducing volumes and margins.

This is an encouraging performance. It demonstrates our increasing appetite for innovation, the power of the Post Office brand and the continued attractiveness to customers of accessibility through a branch network of 11,780 outlets, and our inherent principles of trust, transparency and fairness.

This solid progress means we are able to report an increase of £33 million to £94 million in operating profit before exceptional items. This includes £210 million received from the government in 2012-13 as a subsidy to support the branch network. This enabled the provision of key general and economic services to citizens nationwide, including the most remote as well as the most deprived areas of the country. We are proud as a commercial business with a public purpose to fulfill this critically important task, and we are committed to maintaining the network.

The subsidy payment constituted 17 % of revenue in 2012-13 and will decline by £10 million in the coming year and by a further £40 million in 2014-15. Future extension of this payment will depend on government-spending decisions beyond 2015. To achieve our ambition of reducing dependency on the subsidy and achieving commercial sustainability, it is critical to continue modernising and innovating, growing revenue and continuing to focus on our customers while keeping a strong control on costs.

The significant practical progress which has been made in strategy implementation is therefore very welcome. In 2010 the government pledged £1.34 billion of funding for the Post Office up to 2015. While half of this related to the network subsidy the remainder was pledged to support the modernisation of the Post Office.

The activity undertaken in 2012/13, in pursuit of this goal, has been unprecedented in our history. A major transformation programme to modernise the branch network began, with hundreds of branches converting to new, more customer-friendly, formats and building the momentum to convert many more.

There is no more visible indicator of a Post Office that is changing for the better than the changes customers see in their cities, towns and villages. And the evidence is that these changes are meeting with approval: customer satisfaction with the new 'main' and 'local' branch models runs at 95%<sup>[6]</sup>, while queue times in the 'local' model have fallen below a minute and customers are using new opening hours stretching from early morning to late evening. Subpostmasters switching to the

new models, meanwhile, are able to increase their retail businesses. Moreover, the physical network that is so central to our business is now being complemented by online and telephone channels, further enhancing the convenience of our service to customers.

Naturally, a programme such as this involves challenge. The Post Office has made significant progress, for instance, in reducing the losses in the network of Crown branches directly managed by the business. There remains a long way to go to reach the point where this part of the network breaks even, and that is why we are holding firm in relation to our position on pay and franchising in the Crown network. There will be other challenges ahead, but as our Chairman has noted in her foreword, we are determined to complete a transformation which underpins the future of the Post Office and brings more benefits to our millions of customers.

If our financial and practical progress has been encouraging in 2012-13, so has our pursuit of new ways of running the business. In 2012 we set up a stakeholder forum to begin a process which is a key step in our journey toward potential future mutualisation, that of defining the public purpose of the Post Office. In 2013-14 we will complete this work and over the summer ahead we will engage the public on this work, with a view to embedding this public purpose in our business planning and processes.

It is a process in tune with our ambitions to be more proactive in delivering our public purpose. The Post Office is a long-standing part of UK high streets and will work hard to support their revival in challenging economic times, joining with others to lead and develop solutions which help high streets and other communities to survive and thrive. We will step up our work in supporting the growth of small business by ensuring that we develop more of the products and services they need to grow. We are also working with the Business in the Community high street task force, supporting the work of 'town teams' in Sydenham, Stockton-on-Tees and Brighton, work which complements our membership of the High Street Forum co-chaired by the Department for Communities and Local Government and Alliance Boots.

The Post Office will also work ever more closely with those seeking to close the digital skills gap, work which is so important to a thriving economy. As a founder member of Go On UK, the charity set up to make the UK the most digitally skilled nation in the world, the business will focus on building the online skills of our people. We will also work with our partners to develop solutions which will enable the 16 million people in the UK, who still do not have basic online skills, to access and enjoy the benefits of being online.

As Chief Executive of this great business, I would like to thank all those who have worked so hard for it over the past year, whether they are members of our staff or those whose businesses deliver our services.

I am particularly grateful to Alice Perkins and to the Board for their guidance throughout the year. They have strengthened our strategic oversight in relation to the markets in which we operate – Mails and Retail, Financial Services, Government Services and Telecoms – and brought a level of focus and challenge to decision making at the Post Office which has helped both revitalise the company and energise its commercial focus.

The Post Office changed significantly over the course of 2013-13, and for the better. We have no illusions about the hard work ahead, but our determination to deliver the business transformation of the decade remains undimmed.

Paula Vennells Chief Executive

## Section: Overview

### Title: Strategy

Boxout: [THE STRATEGY WILL BE DEPICTED THROUGH GRAPHICS SETTING OUT OVERALL OBJECTIVES AND EVIDENCE OF PROGRES DURING THE FINANCIAL YEAR 12/13]

#### Key objectives

The Post Office strategy is based on being commercially successful and growing as a business, while maintaining the key role that Post Office branches play in supporting communities across the UK.\* Our people are fundamental to the way we do business; they are at the core of everything we do and are therefore critical to the success of the Post Office strategy.

#### Growth

Objective: A key part of our strategy to 2015 is to grow income by introducing new products and services across our portfolio to offset declining income from traditional product areas.

Evidence from 2012-13: Introduced new products such as Post Office mortgages while also attracting and retaining clients – RBS and HSBC signed up to partner banking – and winning new contracts such as the DVLA licensing contract.

#### Modernisation

Objective: To modernise the Post Office and the network through the Network Transformation programme, Crown Transformation programme (to break even by 2015) and investment in technology to improve customer-facing systems.

Evidence from 2012-13: To date, a total of 1,450 branches have either been converted or subpostmasters have signed contracts to have their branches modernised in 2012-13. 507 local and main branch conversions have resulted in 17,500 additional opening hours. Crown transformation: progress to reduce losses – financial performance improved by £9 million; successfully introduced new ways of working including increased automation and longer opening hours in pilot branches.

This year has seen the completion of the rollout of new PIN Pad payment devices, making the Post Office the largest contactless payment network in Europe.

#### Customer excellence

Objective: To put customers at the heart of everything we do, transform our technology to offer more responsive and customer-focused systems.

Evidence from 2012-13: Improvement in online capabilities, including a full website redesign. Our website now receives four million customer views per month, with unique visitors 30% up year on year. In 2012-13, overall customer satisfaction across 1,000 of our largest branches was 87%<sup>[1]</sup>.

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<sup>[1]</sup> Quadrangle Brand and Customer Insight Programme 2011-12 & 2012-13 (1,000 largest branches)

\* This strategic approach is fully consistent with the government's policy document on the Post Office Network 'Securing the future of the Post Office Network in the Digital Age'.<sup>1</sup>

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Section: Operational review

Title: Branch network

Modernising the Post Office branch network

The Post Office has an unrivalled network, with a branch within three miles of 99% of the population. No other retailer can match the reach which puts the Post Office at the heart of communities across the UK.

The business is committed to maintaining its branch network of more than 11,700 outlets, ensuring services are readily accessible to communities across the UK. The physical network, increasingly enhanced by digital and telephone services, lies at the core of the business. 97% of the Post Office branches in the network are run in conjunction with retail partners on an agency and franchise basis.

Underpinning the commitment to the network is an unprecedented branch modernisation programme – the largest investment in the history of the Post Office – which is creating modern, commercially sustainable branches that are improving customer experience.

This modernisation programme involves transforming those branches that are operated by other businesses or independent subpostmasters on behalf of the Post Office, and the 370 (offering public access) Crown branches directly owned and managed by the Post Office.

Network Transformation programme

Dependent on size, independent operators of Post Office branches are able to convert to one of two new models – a main branch or a local branch.

Main branches, of which there are now 178, continue to offer a dedicated Post Office counter, often open plan, in a brighter more modern environment. In addition, the majority of services will continue to be available outside traditional hours – for as long as the host business is open – from the retail counter.

The local model, for smaller branches (329 (NB need to use the figures as of March 31)), fully integrates the Post Office with the host business, offering services from the retail position rather than a dedicated Post Office counter. This often means services are available for much longer than before – in many cases from early morning until late at night, seven days a week.

With more than 507 new-style main and local Post Office branches already established during 2012-13, subpostmasters and customers across the UK are benefiting from a new modern approach to offering Post Office services. Customers are responding positively to longer opening hours, brighter environments and open plan counters. Independent research shows customer satisfaction scores at both these modernised main and local branches are consistently around 95%.

Subpostmasters are also benefiting from more efficient ways of working as well as increases in both their Post Office revenue and accompanying retail business.

Interest in the new models remains strong, with subpostmasters at a further 943 branches already signed up to convert during 2013-14.

Box out

Postal Affairs Minister, Jo Swinson, joined us at the Bishop's Hull local Post Office in Somerset to celebrate the opening of more than 500 new model branches in the network. She said: "The Post Office is the cornerstone of many residents and businesses. With more than 11,700 branches, it provides unparalleled reach into communities up and down the country. The government recognises this value which is why we have made a clear commitment to its future."

Graphic: insert px of Jo Swinson

Boxout: Breakdown of the Post Office network to be inserted on these pages once numbers have been cross-referenced with other figures

Section: Operational review

Title: Network transformation case studies

Greenwich main Post Office, London

Sandeep and Damandeep Sandhu have enjoyed a smooth transition of their branch. They believe the modernisation programme will give the Post Office a much more competitive edge on the high street.

Sandeep said: "The refurbishment of branches is essential. It means our branches are improving the aesthetics such as flooring and lighting to really compete and look professional. The Post Office has sustained its trusted status and now looks modern as well."

Note to design: px available

Dingwall main Post Office, The Highlands

Alicen Lawrie's branch is open from 7am to 9pm on weekdays allowing many customers working in nearby Inverness to visit at either end of the day. She said: "The new open plan counters fit very well in the surroundings of my convenience store. It helps our staff have more comfortable conversations with our customers."

Note to design: px available

Steve Roper, Sowerby Bridge main Post Office, West Yorkshire

"Staff prefer the open plan counters. The branch is a much friendlier environment and it's easier to have quality conversations with customers. We also have a private conversation area at the other side of the branch where we can speak to customers about financial services, telecoms products, savings and life insurance offers because people feel more at ease in privacy."

Note to design: px available

Drumaness local Post Office, County Down

Johnny Kimber and his customers have welcomed the new open-plan format and longer opening hours in the busy branch. He said: "Our Post Office services are now available an extra 69 hours every week, and this has already brought in new customers. We're a much more realistic option for everyone now and the Post Office is a far more convenient high street proposition."

Note to design: px available

Medway Parade local Post Office, West London

Chitty Thavachelvam is winning new business every day after converting to a local model. She said "I've been able to extend my retail counter, and have noticed new customers coming through the door, who are now able to take advantage of Post Office services until 10.30pm on Sunday nights."

Note to design: px available

Section: Operational review  
Title: Network transformation in numbers

507

New branches

We now have 507 new main and local branches open across the UK

1450

Contracts signed

507 branches have already been converted while a further 943 subpostmasters are already signed up to be converted to the new models in 2012-13, making a total of 1,450

87%

Increase in opening hours

Across our main and local estate there has been an average increase in opening hours of 87% following conversion to the new model (34% increase for mains and 117% increase for locals on average)

71%

Subpostmaster satisfaction

Subpostmaster satisfaction in transformed branches is also high with an average score of 71%

10% Increase in retail sales

An average retail sales increase of 10% is being reported across mains and locals

Customer reaction

95%

Satisfied customers

Customers are continuing to demonstrate high levels of satisfaction with the models, with satisfaction levels at 95% for both mains and locals

55

Seconds

Average waiting times in branches are 55 seconds in local branches two minutes in main branches  
20% (locals) and 8% (mains)

Visiting branches outside traditional opening hours

Customers are delighted with the extension of opening hours and the added convenience. On  
average, 20% of customers are visiting local branches outside of core hours and 8% in mains

## Section: Operational review

### Crown Transformation programme

At a time when other high street brands are disappearing, the Post Office is investing in 294 of our Crown branches. These are usually larger branches in towns or city centres, are those directly managed by the Post Office.

Crown branches are fundamental to the future of the Post Office, and real progress has been made towards the target of turning around the current losses to achieve breakeven by March 2015. Over the last year, the losses for this part of the network have reduced from £46 million to £37 million. The on-going transformation builds upon this progress and is based on increasing income, improving the customer experience and controlling costs.

Customers will benefit from brighter, more modern branches with improved layouts. Many will give customers the option to use self-serve Post & Go machines, private consultation areas for financial services, and the benefit of longer opening hours. More open plan counters will be introduced and we will have more team members on the shop floor greeting and guiding customers. This new approach has been trialled with notable success across both customer and financial measures at a range of branches.

In six locations we will take the opportunity of merging branches in close proximity to create larger branches with improved facilities for customers. For a further 70 we are looking for retail partners to operate branches on our behalf. This approach will ensure we maintain a high standard of service in an area while putting the branch on a stronger commercial footing for the future.

Case study: Nottingham Post Office transformed November 2012  
(images available of this branch)

#### What changed?

- Redesign of the branch with new customer zones
- New ways of working with more colleagues on the shop floor
- Financial Services consultation area with two private rooms
- Earlier opening on Mondays and Tuesdays
- New signage throughout the branch
- Four extra Post & Go machines with staff on hand to offer help

#### What's the feedback?

- Waiting times have reduced, with 63% of customers being served within five minutes compared with 49% before transformation and 36% during the same period in the previous year
- Increase in income by 9% year on year
- Twice as many customers choosing to use the self-serve Post & Go

Case study: New Malden Post Office transformed February 2013  
(images available of this branch)

What changed?

- Redesign of the branch to improve customer flow
- Retail area repositioned to drive income
- New mails zone with one extra Post & Go and staff on hand to offer help
- Private consultation room for Financial Services

What's the feedback?

- Waiting times have almost halved to an average of 2.37mins
- Increase in revenue by 6% year on year
- Three times as many customers choosing to use the self-serve Post & Go machines

Case study: Birmingham Post Office transformed November 2011  
(images available of this branch)

What changed?

- Redesign of the branch to improve customer flow
- Extra Post & Go machines with staff on hand to offer help
- Extended opening hours
- Added two internal ATM machines

What's the feedback?

- Increase in income by 44% year on year
- Government Services revenue has risen by 43% year on year
- Mails and Retail sales are up 7% year on year

Case study: Derby

(image available of this branch)

A brand new centrally located Post Office branch opened in Derby city centre in May 2013. The new branch, offering longer opening hours, 10 counter positions, self-serve mails zone and private consultation areas, replaces two branches that were located on the fringes of the city. The move to the newly refurbished premises will secure the long-term future of the Post Office in Derby city centre and follows a 12-week public consultation.

Operational review: Branch network

Title: Supporting our network

Boxout: Technology (to be checked by IT)

The Post Office is continuing to invest in technology to ensure the continued provision of high-quality, reliable services which improve customer service. There has been significant investment in the key systems that underpin our service to customers.

Drop & Go

Launch of Drop & Go self-service machines for small businesses – A pre-paid card lets business customers drop off their mail and parcels and pay quickly and have them processed without waiting

Post & Go

Rolled out Post & Go self-service machines – These enable customers to save time by posting mail and parcels without the need for a branch colleague

Pin Pad payment devices

- Completion of the rollout of 30,000 new Pin Pad payment devices, making the Post Office the largest contactless payment network in Europe. Contactless payments allow customers to make purchases of £20 or less simply by tapping their contactless enabled card or mobile over electronic readers, saving time and improving the overall customer experience in branch.

Horizon point-of-sale system

- Provides a secure and reliable service to 33,000 counter positions. At peak times, it handles around 1,000 transactions per second. (INCLUDE ANY ENHACEMENTS MADE TO HORIZON IN 2012-13?)

Extending helpdesk availability

- IT has extended the helpdesk opening hours to support the increase in opening hours in branches. With longer opening hours, customers can access postal services at a time convenient to them while branch colleagues can use the helpdesk for longer so that they can respond to customer queries quickly.

New customer relationship management system

Copy to be added

Boxout: Supply chain

The Post Office customer base contains some of the most financially dependent members of the UK population. Therefore, a key driver for the business is providing reliable access to cash.

- The Supply Chain, part of the business, collected and delivered more than £42 billion of cash, coin, foreign exchange, secure stock, (stamps, postal orders etc.) and transactional stock, (government forms and leaflets). Included 754,000 Cash and Valuables in Transit (CViT) visits to and from these branches
- £3 billion of customers monies are processed and banked on the day after collection
- CViT operation is the third largest in the UK after G4S and Loomis

Section: Operational review

Title: Business at a glance

## Mails and Retail

Mails and Retail is the largest product area in the Post Office, generating up to 40% of the business' total turnover. Our long-term partnership with Royal Mail Group and diverse customer base is central to retaining our position as the UK's number one mails and parcels retailer.

The Post Office offers an unparalleled range of Royal Mail Group mails and parcels products and services. These include everything from next-day guaranteed courier services to home shopping returns and collections.

In the Post Office mails and parcels business, small businesses are critical and account for up to one third of our income and include many online sellers and small local enterprises.

The business' relationship with Camelot means that the Post Office is one of the main lottery distributors in the UK, offering a range of Camelot national lottery products including scratch cards and EuroMillions in more than 6,000 outlets. The Post Office also works with Vow Retail Ltd to offer customers high-quality stationery, office supplies and collectible product ranges through selected branches and online.

Boxout: Mails and Retail revenue grew from £392 million in 2011-12 to £409 million in 2012-13, an increase of 4.3%

## Financial Services

Our Financial Services business is a fast-growing UK financial services provider, aiming to challenge the traditional banks by offering simple, transparent and value-for-money products, supported by an unrivalled network.

The portfolio includes a broad range of products to meet the needs of a large and diverse customer base, which we offer through strong partnerships with third-party providers, of which Bank of Ireland (UK) plc is one. The Post Office and Bank of Ireland (UK) plc have built a successful business since 2003, providing financial services across the Post Office network in the UK.

The Financial Services business includes the Post Office-branded personal financial services products, foreign currency, payments services (such as bill payment), personal and business partner banking and ATMs.

Our personal Financial Services products include a comprehensive range of insurance products such as car, home and travel; savings products such as Growth Bond, Online Saver, and Cash ISA; and lending products such as mortgages and credit cards.

The Financial Services business is a key focus for the Post Office as the organisation continues to build a commercially sustainable business.

Boxout: Financial Services revenue grew from £264 million in 2011-12 to £281 million in 2012-13, an increase of 6.4%

## Government Services

The Government Services business offers a range of essential services in our branches on behalf of a number of government departments. These services are used by a variety of customers including pensioners collecting their state pension, customers who want to renew their passport, drivers buying their car tax or renewing their driving licence using state-of-the-art technology.

The Post Office partners with the Department for Work and Pensions for the Post Office card account, which allows customers to collect their state pension or benefits in cash, either in a Post Office branch or from a Post Office ATM. We also issue car tax discs on behalf of the DVLA and capture digital photographs for the renewal of driving licence photo counterparts. The Post Office uses ground-breaking Application Enrolment and Identity technology which offers a paperless process for our customers in 754 Post Office branches nationwide. One example is our contract with UK Border Agency where foreign nationals can enrol for an identity card. In addition, the Passport Check & Send service for customers applying for a passport, helps ensure their applications are error free and processed quickly.

Boxout: Government Services revenue remained flat year on year at £164 million

## Telecoms

The Telecoms business incorporates three main product areas: HomePhone and Broadband, Mobile Top-up and International Phone cards.

HomePhone and Broadband offers a competitive fixed line phone and broadband services to just under 500,000 residential customers, making us the sixth largest telecoms provider in the UK. Customers are attracted by our low-cost services, UK-based call centre and ability to pay bills in cash at any of our branches. This service will be migrating to a managed service provided by Fujitsu in the summer of 2013.

Mobile Top-up allows customers to top-up their pre-pay mobile phone for all the main UK mobile networks at any of our branches. The Post Office has the UK's largest estate of top-up enabled terminals in the UK. This is run through an agreement with E-Pay.

International Phonecards, a service run through an agreement with Econet Mobile, are pre-paid products enabling customers to make low-cost international phone calls so that they can stay in touch with friends and family overseas.

Box-out: Telecoms revenue grew from £120 million in 2011-12 to £129 million in 2012-13, an increase of 7.5%

## Section: Operational Review

### Title: Mails and Retail

Mails and Retail is core to the Post Office's offering to individual customers and small businesses in the UK. The Mails and Retail business generated revenue of £409 million in 2012-13, representing growth of £17 million compared to the previous year.

Extremely strong commercial performance across the product portfolio, activity relating to the Olympics and Paralympics and our best Christmas mails and parcels sales ever has made this the single most successful year for the Mails and Retail part of the business.

The Post Office gives customers access to an unrivalled mails and retail product range combined with unparalleled expertise and professionalism from its frontline teams. Revenue grew across all four main categories of the product portfolio (Mails, Parcels, Retail and Lottery) in 2012-13. This was delivered by:

#### Creating and enhancing Royal Mail services

The Post Office Mails team enhanced services with Royal Mail to maximise opportunities from online shopping collection and returns. The launch of our new Drop & Go priority service for small business customers has helped us retain and grow our Mails business. Small businesses and eBay customers can sign up for a pre-paid card to enable them to drop off their mail and have it processed in their absence. The Post Office now has more than 2,300 small businesses signed up to the service with further enhancements planned for the year ahead.

#### General parcels market growth

We have achieved an 8% growth in parcels revenue through a combination of a boom in online shopping and eBay customers and continued improvements in frontline training and sales capability.

#### Launching online retail shop

The new online shop was launched in July 2012 and has seen steady growth ever since. The shop offers an extensive range of mailing solutions, collectibles and office supplies.

#### Expanding our network of Lottery terminals

The rollout of an additional 1,850 Camelot Lottery terminals has helped the Post Office deliver a 5.2% growth in Lottery sales over the course of 2012-13; this has been further facilitated by strong Lottery marketing.

Overall, the Post Office consolidated its position as the number one distributor of mails and parcel products in the UK. The strength, quality and convenience of the Lottery and retail product ranges added further value to Post Office customers.

Looking ahead, the Post Office will continue to develop small business propositions to increase value and convenience for this critical customer group. We will maximise opportunities to grow the services we provide in this sector, in partnership with Royal Mail, particularly in the fast-growing online shopping market.

Boxout: Key highlights

- 30% growth in Retail revenue
- 8% increase in Parcels revenue
- 5.2% growth in Lottery sales
- 3.5% growth in Mails revenue

Boxout: Key launches

- Drop & Go launch - A prepaid card lets small businesses drop off parcels and pay quickly without queuing - by the end of 2012-13, 2,300 small business customers had signed up
- New online retail shop offering mailing solutions, collectibles and office supplies

Section: Operational Review

Title: Financial Services

The Financial Services business is placing the Post Office as a challenger in the sector and giving customers a real mainstream alternative. The Post Office aims to offer simple, relevant and value-for-money products, supported by excellent customer service and an unrivalled network.

The comprehensive range of financial products and services covers savings, credit cards, mortgages insurance, foreign currency, payments services (such as bill payments), personal and business partner banking and ATMs.

In 2012-13 we continued to build an award-winning financial services business\*, challenging the market with simple, value-for-money and transparent products. In achieving this, the Post Office delivered £281 million in revenue - an increase of 6.5% on last year - which was driven predominantly by growth in savings and lending.

Financial Services works with a range of partners and suppliers and a key development in the last year has been the renegotiation and reconfirmation of the arrangements with Bank of Ireland (UK) plc. The strong partnership with Bank of Ireland (UK) plc, which dates back to 2003, delivered significant growth in 2012-13, particularly in the Personal Financial Services area - Growth Bonds, Online Saver and Reward Saver. We also extended our award-winning mortgage range, offering competitive rates that featured regularly in Best Buy tables. The Financial Services business continues to improve accessibility of its products to customers, including making mortgages available in branch.

The Post Office maintained its position as the market leader in foreign exchange against a backdrop of a challenging travel market. The public also voted the Post Office the Best Foreign Exchange retailer and Best Travel Insurance Provider at the 2012 British Travel Awards, for the sixth and seventh year respectively.

Our Financial Services team won and retained key contracts in the bill payment market, ensuring that customers can continue to use their local, convenient Post Office branches throughout the UK to pay bills.

Contactless payment terminals were installed across 30,000 counter positions in our extensive network across the UK. This move makes the Post Office the biggest user of contactless acceptance technology in Europe, allowing customers to pay for transactions of up to £20 using contactless cards and Near Field Communication (NFC) enabled mobile phones.

We continued to work on our personal banking offering, and increased access of UK bank accounts in our network by signing new agreements with HSBC and First Direct. 95% of all UK debit card holders can now access their accounts from a Post Office branch.

The Financial Services business is a key focus for the Post Office as the organisation continues to build a commercially sustainable business. In 2013-14 the Post Office is announcing a current account, the next step in our strategy of growing an already well-established financial services portfolio.

Extensive research into the current account market tells us that customers want simplicity, transparency and good value for money. With more branches than all the UK banks combined, the Post Office is very excited at the prospect of offering a current account through the most accessible retail network in the UK. The current account has already launched in a small number of Post Office branches during spring 2013 with a wider rollout planned for later in the financial year.

Growth will help the Post Office achieve the goals of providing customers with the option to service all their financial needs under one roof and allowing the Post Office to become the leading financial services challenger brand in the UK.

#### Boxout: Highlights

- Best Travel Insurance Provider at the 2012 British Travel Awards, as voted by the public, for the seventh successive year
- Best Foreign Exchange / Travel Money Retailer at the 2012 British Travel Awards, as voted by the public, for the sixth successive year
- Agreement with HSBC and First Direct for their customers to have free access to their accounts at all of our Post Office branches from spring 2013
- The Post Office became the biggest acceptor of contactless payments in Europe
- What Mortgage Awards 2012: Best Online Lender, Best Fixed Rate Mortgage Provider

## Section: Operational Review

### Title: Government Services

The Post Office is, and will remain, the front office for government delivering services on behalf of government departments through the Post Office branch network and online channels. In 2012-13 we grew our passport Check & Send business by 12.5% and increased our revenue from capturing customers' biometrics on behalf of the United Kingdom Border Agency (UKBA) by 284%.

The main priority in 2012-13 was to retain the contract for Front Office Counter Services provided on behalf of the Driver Vehicle Licensing Agency (DVLA). This framework contract will allow other government departments to contract with the Post Office without having to run a further procurement process. The contract is for seven years with an option to renew for a further three years.

In November the Post Office was successful in retaining the DVLA framework contract for Front Office Counter Services. In addition, the Post Office also won a place on the Department for Work and Pensions (DWP) Identity Assurance Framework contract which is now being managed by the Cabinet Office, Government Procurement Service. It was particularly pleasing to be awarded a place on the Identity Assurance Framework and to retain the DVLA Front Office Counter Services contract against strong competition.

As well as these significant contract wins, our new world-leading Application Enrolment and Identity business generated more than £12 million of revenue and now accounts for more than 9% of our total Government Services revenue. This service, available in 104 Post Office branches, captures digital finger prints, photographs and electronic signatures for the UKBA and photographs for customers renewing their driving licences. It also allows the Post Office to extend the services offered and includes increased security features such as the ability to record transactions in branch.

Nearly 90% of Government Services revenue is still generated by the traditional motoring, benefits and passport services. We saw significant growth in our passport and existing Identity business, which helped to offset the decline in benefits payment. Income from the Post Office card account declined as customers continue to migrate to bank accounts. Income from motoring, primarily the issuing of tax discs in our branches, was broadly flat compared to 2011-12.

In 2013-14 the Post Office expects to complete the rollout of new services with the DVLA and continue to grow the passport business. The year will also see the Post Office laying the foundations for future growth in the Government Services market as we seek to support the rollout of Universal Credit and the government's Digital by Default agenda.

#### Boxout: Key highlights

- Won the DVLA framework contract for the provision of Front Office Counter Services
- Growth in the Passport Check & Send service with an increased market share
- Awarded a place on the DWP Identity Assurance framework contract

Section: Operational review

Title: Telecoms

The Post Office Telecoms business consists of HomePhone and Broadband, Mobile Top-up and International Phonecards. 2012-13 was a very positive year for the business as it achieved an 8% increase in revenue from £120 million to £129 million. The HomePhone and Broadband business performed particularly well, offsetting weakening performance in our Mobile Top-up business. The Post Office was also able to increase profitability of the portfolio.

At the beginning of the year, the Post Office signed an agreement with Fujitsu Services to provide the HomePhone and Broadband services from the summer of 2013. This is a strategically important agreement as it provides us with a platform from which we will be able to develop and grow our business in an agile and cost-effective way. The new platform will make it easier for customers to sign up to our services through branches and online. It will also reduce our cost base and provide improved and flexible back office IT systems. The customer experience will be enhanced with improved online account management tools and access to higher speed broadband services over the TalkTalk network. The agreement with Fujitsu Services will also enable the development of bespoke services for the SME market.

Over the course of the year, the Post Office boosted revenue generated by the HomePhone and Broadband business increasing from £112 million to £122 million, an increase of just under 10%. This achievement has been driven by two key factors: first, the customer base is very stable, driven by solid customer acquisition across all channels, and a reduction in customer churn, particularly in high-value segments. Second, a number of changes to our service offering were implemented which has made it more attractive to higher value customers, while improving customer retention.

The Post Office has seen a reduction in the volume of mobile top-up transactions in our branches as mobile networks actively look to migrate customers from post-pay to pre-pay packages and customers top-up less frequently. However, we still achieved 15 million transactions and remain the largest estate of top-up enabled retail outlets in the UK.

The International Phonecard business has been in decline for a number of years and continues to be impacted as customers move to solutions such as Skype.

The Post Office will continue to grow the Telecoms business in 2013-14, both in terms of revenue and customers, but it will be a transitional year as we migrate our services to our new supplier. This transition will provide the platform to enable our Telecoms business to grow rapidly in the future. The Post Office is also looking at opportunities to enter the mobile market during the coming financial year so that we are able to offer our customers the full suite of telecoms products.

Boxout: Highlights

- £9 million increase in revenue
- New contract signed with Fujitsu Services
- Mobile launch planned for 2013-14

## Section: Performance Review

### Title: Our people

The Post Office is proud of its heritage and equally proud of the unique role our colleagues play at the heart of communities, serving a public purpose, while becoming increasingly commercial and entrepreneurial. The Post Office also recognises the important role our support teams play in delivering the business strategy. We strive to nurture our people, ensuring they feel valued, trusted and committed to putting the customer first. The Post Office is ambitious about the future and confident of the key role our people will play in achieving that vision.

This year saw the introduction of our core values – Care, Challenge and Commit. These three values sit at the centre of everything we do and are intrinsic to how the Post Office interacts with customers and colleagues. Our values underpin our employee proposition and help to deliver the best possible customer experience, while at the same time giving everyone within the business the chance to fulfil their potential.

The Post Office is particularly proud of the progress made in relation to talent, diversity, people development and engagement.

### Engaging with our people

We value the opinions and ideas of our colleagues. Our employee engagement survey, which was conducted in 2012, is managed by independent research company Ipsos MORI. The survey helps the Post Office understand how colleagues are feeling about the business, what is going well and where we can improve.

The survey saw many positive results, especially compared to similar companies:

- An impressive response rate of 76%
- An increase in the Engagement Index score from 62% to 68% from the previous year
- 84% of employees would recommend Post Office services to friends and family (retail norm 71%)
- 76% of employees feel proud to work for the Post Office (retail norm 49%)

While the survey demonstrated a number of positive results, we are keen to continue with this progress and ensure we listen to our colleagues and build on this success for next year and beyond.

### Learning and development

The Post Office continues to support the development of people right across the organisation.

Our people have undertaken a broad range of development activities this year including:

- Introduction of 'Discovery Days' for new managers, ensuring they have the tools to succeed in their new roles

- Supporting the development of a Post Office procurement function, utilising internal expertise, external training and professional qualifications
- Introduction of the Certificate of Professional Business Practice in the Information Services team in partnership with Sheffield Hallam University – sharing skills, knowledge and best practice across the organisation
- Building the capability and commercial skills of our managers through the development of the Crown Leadership Excellence programme which will launch in spring 2013.

### Talent and diversity

Becoming an organisation working independently of Royal Mail Group has required an increase in capability and expertise across a range of areas. New-found corporate responsibilities have been taken on across the breadth of the professional functions. Coupled with the goal of ensuring a high-performing sustainable business, we have put in place a robust assessment and development approach, looking at both performance and future potential of our senior leaders with the overall aim of raising the capability of our people.

Raising our leadership capability and performance standards will continue to be an important focus which the Post Office will deliver through its Leadership Development programme.

At this stage of our development, building talent and diversity merits special attention. The Board has, therefore, delegated authority to the Nominations Committee to monitor the development of a talent management programme for senior levels of the organisation.

As part of this, we have introduced a range of initiatives to promote an inclusive workforce. These include establishing a diversity forum; recruiting young people under 24 on the Paid Work Experience programme and launching our Trainee Manager scheme.

The Post Office is also proud of the progress made in gender equality. Our Chairman and CEO are women. The Board has equal numbers of male and female directors and women make up half of the Executive Committee. To ensure we maintain this focus, we have pledged our support to the government's Think, Act, Report initiative which is aimed at improving gender equality in the workplace.

Our general policy will be to recruit for talent, using a range of tools, including encouraging open applications through our attraction website, engaging specialist recruitment consultancies and operating specific talent attraction campaigns.

Challenges remain, but we are confident our commitment to building a culture of inclusion will continue to make the Post Office relevant to its increasingly diverse customer base.

We view our approach to diversity as an integral part of talent management. This year we have developed two programmes, taking positive action on both fronts.

#### Paid Work Experience programme

Over the last 12 months, the government and media have both highlighted the problem with high unemployment in inner city areas, especially among young people. The Paid Work Experience

programme aims to provide a period of paid employment during the Christmas period for young people and those furthest from the labour market. The Post Office employed 61 individuals in the lead up to Christmas in some of the busiest Crown branches across London and Greater Manchester. The initiative led to 39 individuals being offered further employment. Due to the success of the scheme, in 2013-14 the Post Office intends to extend the programme within the branch network.

#### Trainee Manager scheme

The scheme was designed to take positive action to attract young people to consider a career with the Post Office, working with our colleagues and customers in our Crown branches. We employed eight individuals under the age of 24 to work in the London area. The trainees have subsequently undertaken a development programme including a foundation degree, senior manager mentoring and regular learning sessions. The scheme has already seen positive results with three progressing to other managerial roles in the business. The trainees continue to progress and have provided a welcome injection of new ideas and enthusiasm.

#### Accelerated development scheme for senior leaders

We have started to inject talent into different levels of the organisation and are currently piloting a high-potential development programme for new entrants at the senior leadership level. This focuses on accelerated career progression across a range of roles within the business, alongside targeted personal development in which individuals draw upon a range of available activity including coaching, mentoring and behavioural workshops.

#### Safety, health and wellbeing

The safety and wellbeing of our people is of paramount importance to the Post Office. This year we have embarked on an extensive programme of health checks that will allow all our employees to understand how healthy they are, and learn about what they can do to reduce the risk of illness and improve their wellbeing.

The Post Office aims to fulfil its business mission without compromising the safety of customers, employees, suppliers and all those affected by our activities. We want to make healthy and safe working a way of life.

To this end, the business ensures:

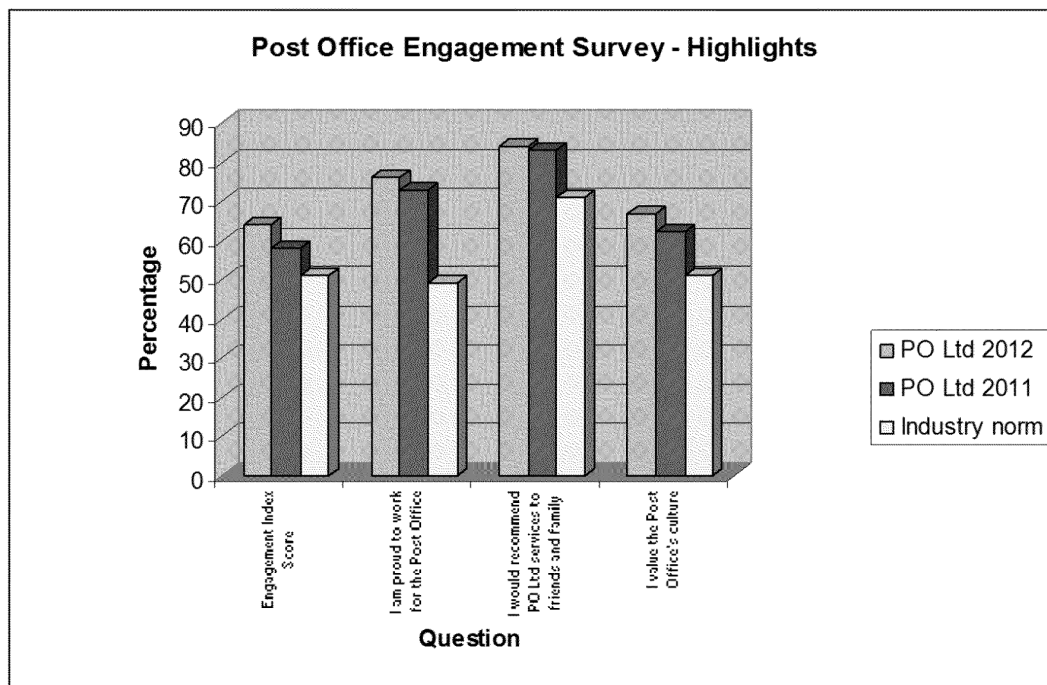
- we comply fully with the relevant legislation
- that the health and safety responsibilities of our employees are clearly defined, allocated and understood
- we encourage and help all our people to carry out their responsibilities through effective health and safety management systems, with safe premises, equipment and processes
- we improve our employees' capability to manage and work safely, through instruction and training
- we support and encourage our people to get involved in the health and safety performance of our business and pursue a healthy and safe lifestyle and

- we monitor and review how well we put our health and safety policies into practice.

Looking ahead

The Post Office wants people who are capable of delivering a turnaround strategy. Therefore, we aim to continue building people capability; to foster a culture of continuous learning; to increase our people’s understanding of our business in a commercial context along with our social purpose; to develop a proactive talent and career management process that recognises the value in diversity; and to continue to nurture a culture where people are actively encouraged and valued as role models of Care, Challenge and Commit.

Boxout 1



Boxout 2

Our people vision

Great performance through great leadership

The Post Office will attract and develop great people who have pride in and a passion for delivering value for customers and reflect the diverse communities we serve. Everyone will have a strong sense of ownership for their work, demonstrating initiative and flexibility, working well together to adapt to the rapidly changing needs of our markets. We will have an environment where our people work in partnership with all those who contribute to the success of our business. The Post Office will be a place where people are valued and respected, are encouraged and supported to fulfil their potential and rise to the commercial challenge.

Section: Performance review

Title: Our people

Case studies

James Reid – Property Lead, Network Transformation programme

Picture required

James joined the Post Office from Royal Mail a year ago on the Network Transformation programme as a Field Change Advisor in South Wales.

James saw the role as a great opportunity to develop and support the change across the network. “The role was really rewarding and I really enjoyed working with the subpostmasters.

“I then saw the Property Lead role advertised and went for it. It did mean moving down to London, but I have been made to feel really welcome. I feel really proud that my managers saw potential in me and have helped me settle in to a new role and a new city.

“I think I have achieved a lot this year and feel I am making a real difference. Seeing converted branches opening and knowing you have helped to do that, feels great. I am here for a career and see my long-term future with the Post Office.”

Ashley Hall – Change Analyst, Finance

Picture required

Ashley joined the Post Office 13 years ago. A year ago, Ashley was an administrator in the Information Services team when he became one of the successful applicants for the Certificate in Professional Business Practice introduced by the Post Office with Sheffield Hallam University.

“The course was a great opportunity to develop in my current role. I couldn’t have imagined the difference it has made to me in just 12 months. I’ve been actively encouraged by my managers to improve my skills and make a positive contribution to the business.”

Ashley has since moved to his new role in the Finance team.

“I’ve now had the opportunity to work in another part of the business and continue with my qualification. It’s really broadened my horizons. Personally, I feel more valued and understand the contribution I make to the wider business.”

Bushra Ali – Trainee Manager, Network

Picture required

Bushra joined the Post Office a year ago through the Trainee Manager scheme.

"I hadn't ever considered a career with the Post Office, but after meeting the people at the interview and seeing their passion, I couldn't wait to join."

In the last 12 months, Bushra has worked in five different branches and was part of the Post Office team working in the Olympic village during London 2012. She is also undertaking a foundation degree in Retail Management.

"It's challenging doing my degree alongside work, but it's given me so many practical skills I can apply to work. I've gained confidence and learned so much about our products and services, as well as developing my leadership skills. I'm really grateful for the support I've received from my managers and mentor. I'm still really enjoying myself and I'm really keen to become a Branch Manager."

#### Shahidul Islam – Paid Work Experience

Picture required

Shahidul joined the business in November, through the Paid Work Experience scheme. He was our youngest candidate at 16. He currently works in Houndsditch.

"I left school in the summer and started looking for work. I had tried a number of companies but with no luck. I was really pleased when I got my role with the Post Office.

"Everyone has been really supportive and my managers have helped me a lot and are always there for me. I learnt a lot of new skills and met different people from different walks of life. I think my main achievement has been developing my communication skills.

"I've changed a lot in the time I have been here, I've started to really believe in myself and feel like I have a future here."

## Section: Performance Review

### Title: Our customers

It is essential to our growth strategy that our customers feel they get a first-class experience every time. So, we are rigorously focused on putting them at the heart of the business. In 2012-13 we carried out extensive research to better understand our diverse customer base and their needs.

Research has shown what we do well and where we need to improve. Customers value the Post Office and rate our customer service highly, but tell us they want the Post Office to be easier to do business with and that we should offer them a greater choice of ways to interact with the Post Office.

Using this feedback will help shape the ongoing development of a multi-channel strategy for the future that optimises convenience, choice and relevance for Post Office customers.

### Customer satisfaction

The Post Office has made some significant progress over the past year with the relationships we have with our many customers. 18 million customers visit our branches every week, half the small businesses (SMEs) in the UK use our services each week, 34 million visit our website each year and nearly eight million customers talk to our 34 UK and Republic of Ireland contact centres each year.

In 2012-13 the Post Office experienced impressive customer satisfaction rates with 87% of customers saying they were happy with the service they received, consistent with 2011-12<sup>[1]</sup>.

Underlying these high customer satisfaction ratings, there has been a reduction in wait times. The average wait time in 2012-13 was three minutes, which is 12 seconds quicker than 2011-12 and one minute and eight seconds quicker than 2010-11<sup>[2]</sup>.

Our research also told us that we needed to re-engage customers with the overall Post Office brand in order to achieve future growth. We, therefore, launched a brand campaign in October inviting customers to consider the Post Office in a different way.

The Post Office understands how important customer service is during the lead up to Christmas. As a result, we put extra effort into making Christmas easier for our customers. This formed a business-wide project during November and December which contributed to improved sales performance and customer perception. Christmas Makers (Post Office management and support staff working in branches), longer opening hours, online help, pop-up Post Office branches and discounted stamp arrangements were highlighted to customers by press, outdoor and digital advertising and PR. This helped to demonstrate how we were making strides to be easier to deal with. All of this delivered our best ever Christmas performance, with our core Mails product range exceeding last year by 3.8%, with 86% of customers saying they were satisfied with their experience in branch<sup>[3]</sup>.

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<sup>[1]</sup> Quadrangle Brand and Customer Insight Programme 2011-12 & 2012-13 (1,000 largest branches)

<sup>[3]</sup> Empathica Voice of Customer Programme: December 2012

There was also a positive impact on wait times in December with an average wait time of three minutes and 47 seconds - 80 seconds quicker than last year and three minutes and 27 seconds quicker than 2011<sup>[2]</sup>.

#### Voice of Customer programme

The Post Office is constantly looking at ways to improve customer satisfaction and offer more convenient channels for customers to provide feedback. Our new Voice of Customer programme to 'tell us - how we did today' was piloted in 150 branches this year. It uses pre-printed till receipts, cards and a QR code to invite customers to give feedback online, via mobile or by telephone.

At the end of March 2013, we had feedback from 36,500 customer visits. This feedback helps the Post Office address customer issues at branch level quickly (such as plans for dealing with busy times and reducing queue times), as well as helping to develop an overall strategy to address common themes across the network.

Customers also have the opportunity to praise service where it is 'above and beyond' and more than 700 individual 'wows' are received weekly<sup>[4]</sup>.

Voice of Customer is in place in more than 2,000 of our largest branches and will be rolled out to all newly transformed branches in 2013-14.

A key focus in 2013-14 will be to make the Post Office an easier organisation to do business with. The modernisation of the network and Crown branches, coupled with our multi-channel strategy, and offering more transparent and relevant products and services will be essential in ensuring this happens and that the customer view remains at the heart of the Post Office's strategy.

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<sup>[2]</sup> ABa Mystery Shopping Programme 2012-13

<sup>[4]</sup> Empathica Voice of Customer Programme 2012-13

Section: Performance review

Title: Our customers

Boxout

Transformed branches

Customers in transformed network branches are already enjoying even higher levels of satisfaction than the rest of the network:

- In both main and local branches, 95% of customers were satisfied<sup>[5]</sup>
- Average wait time in transformed network branches was one minute and one second<sup>[5]</sup>
- 71% of subpostmasters were satisfied with their new Post Office branch<sup>[5]</sup>

Case study:

In line with the high street, the Post Office has introduced automated self-service kiosks which help customers save time. The Post & Go kiosks help customers post letters and parcels and buy stamps and packaging. One customer commented: "Michael (Post Office) was very welcoming when I came into branch. He asked if I needed help with anything while I was posting a parcel. He asked if there was anything important inside and if I needed to get it there for the next day which neither applied to me. Michael then helped me to process it through the Post & Go machines near the door; it was so easy."

Durham Crown branch<sup>[6]</sup>

Case study: Small businesses

It is estimated that up to half of the UK's small businesses will visit a Post Office at least once a week. This is often for mail services – with Post Office branches providing a convenient access point to the onward postal distribution system. In an increasingly digital age, this means that these businesses are able to transact beyond their immediate geographical environment, taking orders by post, phone and internet and being able to fulfil them throughout the country and the world. The Post Office network acts as a critical part of the infrastructure supporting the growth of small businesses throughout the UK.

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<sup>[5]</sup> Brass Network Transformation Programme research: August 2012-March 2013

<sup>[5]</sup> Brass Network Transformation Programme research: August 2012-March 2013

<sup>[5]</sup> Brass Network Transformation Programme research: August 2012-March 2013

<sup>[6]</sup> Empathica Voice of Customer Programme 2012/13

This Post Office infrastructure also provides a wider suite of services that can conveniently meet the needs of local small businesses – including banking and cash services as well as insurance, travel and Government services. The strong local relationships with small businesses are strengthened by the empathy and understanding of their needs from subpostmasters who are typically running the Post Office in a small business themselves.

This is an area of development for Post Office. Service enhancements have been developed to meet small business needs, such as 'Drop and Go' whereby local businesses can drop off packages at their local office and the Post Office will apply the postage and billing afterwards. This is an approach that will continue to develop strongly over the next few years as the Post Office plays its role in promoting growth in a sector that is so critical for growth and employment prospects across the UK.

Section: Performance Review

Title: Corporate responsibility

Environment

The Post Office recognises its environmental responsibilities and is committed to minimising our adverse environmental impact by means of a continuous improvement process.

We embrace environmental considerations in the business management process and decision making throughout the organisation.

We set ourselves some challenging goals for 2012-13:

- 5% reduction in building energy use
- 5% reduction in CO2 from vehicle fuel
- 5% reduction in water use
- 55% of all waste generated to be recycled.

Year-end performance against these goals was encouraging in that we achieved or exceeded three out of four goals. Our performance in reducing building energy use was significantly affected by the unusually severe weather conditions during the winter of 2012-13.

Activities

Change control

All business projects and supplier contracts are reviewed for environmental impacts and recommendations made to positively influence them so that they make use, whenever possible, of sustainable raw materials and examine responsible end-of-life considerations.

Buildings

A large percentage of Post Office buildings now have low-energy lighting, low-water usage utilities, and all fixtures and fittings are now obtained, wherever possible, from sustainable sources or from materials that can easily be reused or recycled.

Vehicles

The Post Office is continually looking at technological advances and new materials to reduce the weight of our vehicles so they use less fuel. A new concept vehicle will go on trial in the second financial quarter of 2013-14. This vehicle will also utilise telemetry systems, which will enable us to improve overall fuel efficiency. Our aim is that this vehicle will become our flagship for the future, further supporting our environmental aspirations.

By autumn 2013 three quarters of our operational fleet of 420 vehicles will also meet the current Euro 5 emissions standard, and 50% of the fleet will have been adapted to accommodate exhaust gas reduction systems and deliver improved performance.

Waste

Most of our buildings are now participating in the Dry Mixed Recycling scheme where everything that can be recycled is now segregated into separate bins or bags. This is a key initiative to reduce dependence of the Post Office on sending waste to landfill, something that is both expensive and environmentally unsustainable. In addition to this, 100% of all our confidential waste is now shredded, pulped and sent to manufacture recycled paper.

The Post Office measures and looks to reduce the amount of packaging that is produced and the quantity of electrical and electronic equipment that will end up in waste streams once they have reached the end of their useful life. To assist the Post Office in meeting these obligations, we have arrangements with Biffa, our prime waste contractor and Valpak, who specialise in the treatment of electrical waste.

#### Sustainable operations

We actively look for opportunities to ensure that all of the paper we use is from sources accredited by the Forest Stewardship Council and aim to advertise this fact by including the FSC logo on all of our point-of-sale literature. Currently, some 90% of all the paper we buy is from FSC accredited "mixed" sources. This means that the pulp used has come from either well managed forests, controlled sources or from recycled wood or fibres. In addition, we have also reduced the amount of packaging associated with our retail sales by some 44%.

#### Disability and accessibility

The Post Office strives to be one of the most accessible organisations in the UK by ensuring colleagues with disability needs are provided with all of the support they need and disabled customers receive an excellent customer experience.

In 2012-13 the Post Office achieved the following:

- Following separation from Royal Mail, the Post Office Disability Helpline was launched to provide solutions and specialist equipment to help employees with disability or accessibility issues
- Provided grants to agent branches to upgrade their outlets to make them more accessible
- Ensured accessibility was an integral part of the Network Transformation programme. We also developed a new Post Office Accessibility Guide and incorporated disability training as a core part of Network Transformation training
- The Post Office created and meet a panel of accessibility experts from disability organisations on a regular basis. Their role is to advise on accessibility issues facing disabled people, new and best industry practise, and changes and developments within the Post Office that may impact on disabled customers and our people.

Section: Performance review

Title: Corporate responsibility

#### Charity Giving

The Post Office has a rich history of charity giving with our people and customers supporting a wide variety of causes. We have been major supporters of BBC Children in Need for several years. In 2012, the branch network increased its impact by playing a leading role in Children in Need's BearFaced initiative. This gave extra impetus to our fundraising, helping engage customers and branches to have fun and get involved. Our fund raising activities helped raise more than £1m for Children in Need, a record amount for the Post Office.

We have also developed Your Charity this year, an exciting new approach to our fundraising activity. Your Charity empowers branches and teams to choose their own charity to support. The rollout has already started and will continue throughout 2013.

#### Digital inclusion

As a founder partner of Go ON UK, the Post Office is committed to helping the 16 million people in the UK who have either never used, or rarely use the internet develop the necessary digital skills to enjoy the benefits of being online.

The internet has become an integral part of everyday life so we want to ensure our own people have the necessary digital skills to get the most out of being online.

We are committed to providing the basic digital skills training and support to all our permanent Post Office colleagues and we will be progressing this initiative during the next financial year.

To help customers become digitally literate, we plan to launch the Online Centre Locator in all of our 11,780 branches in June 2013, which for the first time will signpost customers across the UK to their nearest digital training location. We are working with a number of partners to deliver this database which covers 1000s of learning centres across the UK.

We also participated in a number of digital inclusion campaigns in 2012-13, including Go on Give an Hour which encouraged those online to help a friend, family member or neighbour to get online.

#### Business in the community scheme

In 2012/13 the Post Office became a standalone member of the Business in the Community (BITC) scheme, working to develop our support for both BITC and a wider community role in line with our public purpose.

Our work with the BITC-led high street task force is offering the Post Office an opportunity to work with three of the 27 government-backed Town Teams to help redefine and regenerate their high streets. The Post Office is now working with the Sydenham, Stockton on Tees and Brighton teams and the local communities to help regenerate interest, activity and ultimately provide a long-term future for these areas so that they can survive and thrive. As a part of every community across the UK, the Post Office is proud to be playing its part in this pilot work protecting the sustainability of these local amenities and retail hubs.

The Post Office also supports the BITC Rural Action Group in its work to help communities in villages and rural areas across the UK where often the Post Office plays an important social and economic role providing services to those who otherwise may feel isolated.

The Post Office takes pride in being a responsible business and looks forward to developing its relationship and support further in the coming year.

Section: Performance review

Title: Financial review

Chris Day [Insert picture]  
Chief Financial Officer

#### Summary results

The Post Office has delivered a sound performance in its first year operating as an independent business. Turnover has increased by 4.5% with strong performance in three of the four core product pillars. This has enabled investment in building the Post Office brand and driving future revenue growth. Whilst the scale of transformational change required to reach the goal of commercial sustainability remains significant our performance in 2012-13 was a significant step in the right direction.

#### Key Financial Performance Indicators

	2013 £m	2012 £m	Variance £m	Variance %
Turnover	1,024	980	44	4.5
Operating profit before exceptional items	94	61	33	54.1
Operating loss before exceptional items and Network Subsidy Payment	(116)	(119)	3	2.5
Operating cashflow	151	38	113	>100%

Operating profit before exceptional items was £94 million (2012 - £61 million), and there was a cash inflow of £151 million (2012 - £38 million).

#### Profit and Loss Summary

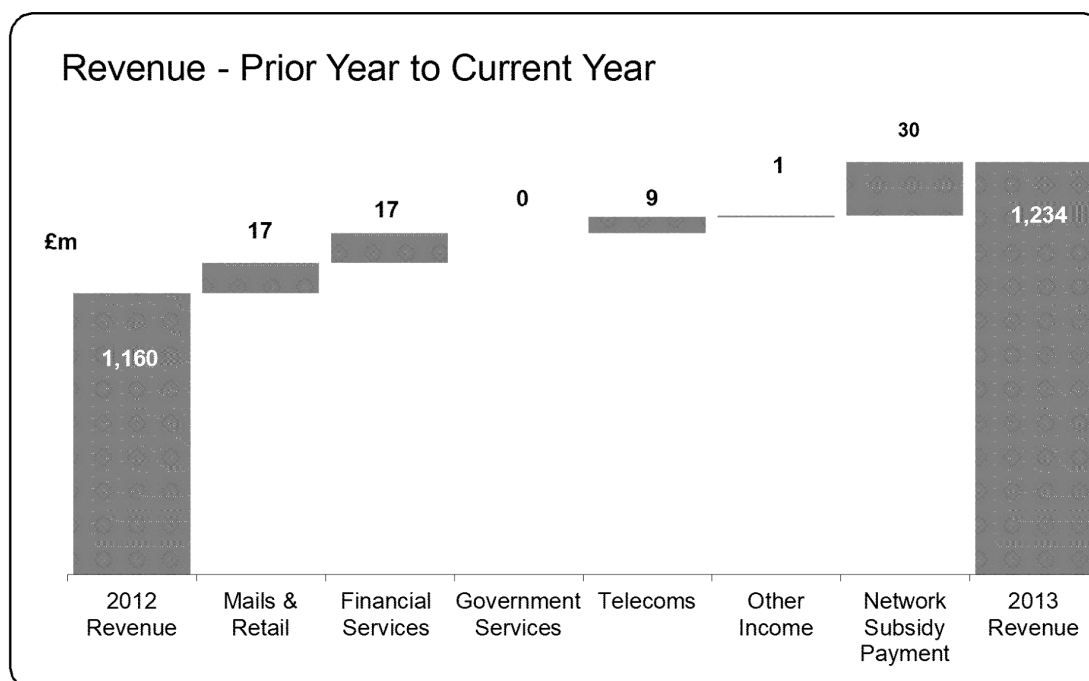
	2013 £m	2012* £m	Variance £m	Variance %
Turnover	1,024	980	44	4.5
Network Subsidy Payment	210	180	30	16.7
Revenue	1,234	1,160	74	6.4
People costs	(259)	(254)	(5)	(2.0)
Subpostmasters' costs	(478)	(483)	5	1.0
Other operating costs	(435)	(393)	(42)	(10.7)
Share of profit from joint ventures and associates	32	31	1	3.2
Operating profit before exceptional items	94	61	33	54.1

\* Note that Royal Mail Holdings plc Annual Report and Financial Statements 2011-12 reported operating profit after modernisation costs but before other exceptional items of £59 million. The prior year result has been presented to exclude modernisation costs consistent with 2013 where results are reported before all exceptional items.

## Revenue

The Post Office's revenue increased by £74 million (6.4%) to £1,234 million including an increase of £30 million in the Network Subsidy Payment from the government. The Post Office segments income into four pillars; Mails & Retail, Financial Services, Government Services and Telecoms. The pillars and their performance are analysed below.

	2013	2012	Variance	Variance
	£m	£m	£m	%
Mails & Retail	409	392	17	4.3
Financial Services	281	264	17	6.4
Government Services	164	164	0	-
Telecoms	129	120	9	7.5
Other income	41	40	1	2.5
Turnover	1,024	980	44	4.5
Network Subsidy Payment	210	180	30	16.7
Revenue	1,234	1,160	74	6.4



## Mails & Retail

The Mails and Retail pillar includes all the services provided for Royal Mail and Parcelforce. It also includes Lottery and retail services such as sales of collectibles as well as packaging and stationery.

Mails and Retail revenue of £409 million increased by £17 million (2012: £392 million). Of this, turnover in relation to Royal Mail products increased by £13 million, driven primarily by strong parcel and premium product volumes and the impact of the stamp price rise introduced on 30 April 2012. In addition, retail turnover increased by £2 million due to the collectibles relating to the Diamond Jubilee and the Olympics memorabilia. The rollout of 1,850 additional terminals contributed to an increase of £2 million in income from sales of lottery tickets.

## Financial Services

The Financial Services pillar includes Post Office branded personal financial services products, ATMs and travel services as well as traditional services such as bill payment and over-the-counter banking transactions.

Financial Services revenue in 2013 increased by £17 million to £281 million (2012: £264 million).

During the year the Post Office sold its 49.9% share in its financial services associate, Midasgrange Limited, to the majority shareholder and long-term banking partner, Bank of Ireland (UK) plc. This was part of a wider agreement to restructure this long-term relationship, aligning the partners to build a significant long-term financial services business. Through this agreement, the Post Office will offer an increasing range of transparent and value-for-money financial products and services, providing value to customers, subpostmasters and the Post Office.

Personal Finance Services income rose by £24 million driven by strong growth in savings products (particularly Growth Bonds, Online Saver and Reward Saver) and the introduction of new mortgage products. The value of savings held in Post Office branded accounts increased by £2 billion to almost £18 billion. Revenue from traditional financial services products including bill payment services and Postal Orders declined. This was due to the increasing provision of electronic alternatives to paper-based products and the increasing use of alternative payment methods. Revenues were impacted by the wind down of the Department of Work and Pensions contract for Cash Cheques (Green Giro) and the decision by NS&I to provide most of their products through their own direct channel.

## Government Services

The Government Services pillar covers services provided under contract to government departments. This includes services in relation to the work of the Department for Work and Pensions (DWP), the Driver and Vehicle Licensing Agency (DVLA) and the Identity and Passport Service (IPS).

Government Services revenue of £164 million remained flat (2012 - £164 million), though income from the Passport Check & Send service increased by £3 million due to higher volumes from growth in both our market share and the overall market. Conversely, the anticipated growth in income from identity-related services has been disappointing. Revenue from the payment of benefits through the Post Office Card Account was £4 million lower impacted by customers continuing to migrate to receiving benefits through bank accounts.

## Telecoms

The Telecoms pillar includes the Post Office HomePhone and Broadband services as well as e-top up services and phonecards.

Telecoms revenue of £129 million (2012 - £120 million) increased by £9 million. Income from HomePhone and Broadband rose by £10 million primarily due to increased customer numbers following the introduction in May 2012 of more competitive service packages. Income from e-top ups was £1 million below prior year as more customers migrated away from pre-pay and mobile networks reduced their transaction fees. Despite this reduction in income, the Post Office is still a significant provider in the top-up market and its share of the retail market has been maintained at approximately 5%.

## Other income

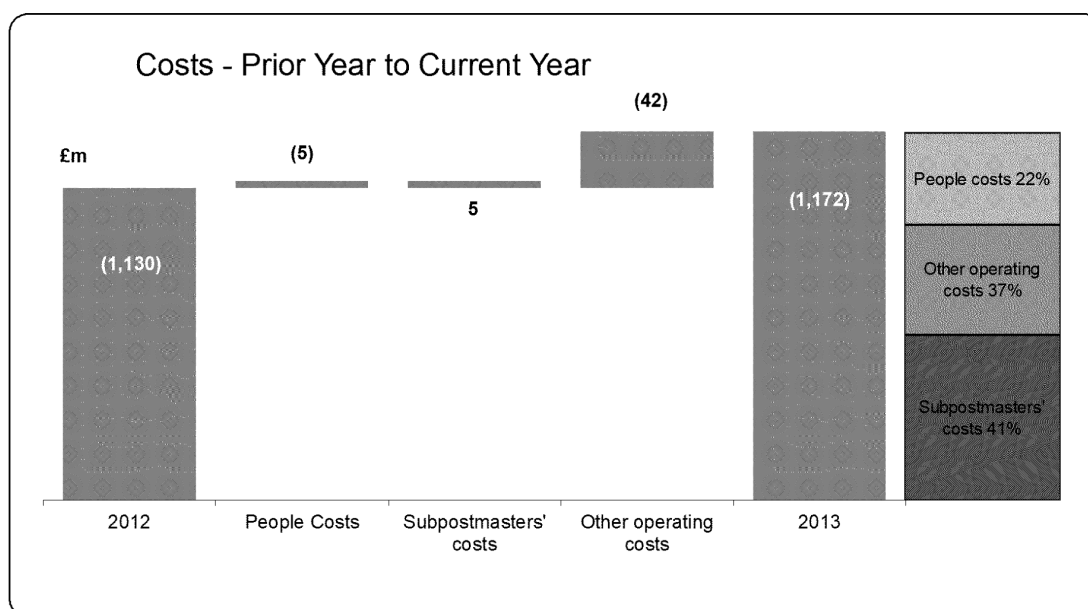
Other income is generated primarily from the Supply Chain business which manages and distributes cash for Post Offices and for third parties. It also offers warehousing services, mainly to Royal Mail. Other income increased marginally to £41 million (2012: £40 million) reflecting the growth in cash in transit income from third parties.

## Network Subsidy Payment

The Network Subsidy Payment is government grant revenue towards the costs of maintaining the Post Office network. The payment increased by £30 million in the year to £210 million; this will begin to reduce with effect from 2013-14 as set out in the current funding agreement with the government.

## Costs

Total costs rose by £42 million to £1,172 million (2012: £1,130 million).



#### People costs

People costs of £259 million (2012 - £254 million) have increased by £5 million reflecting the associated costs of bringing a number of functions in-house, following separation from Royal Mail, and historical pay agreements. These are partially offset by efficiency savings in the Crown network.

#### Subpostmasters' costs

Subpostmasters' costs of £478 million are £5 million lower than last year (2012 - £483 million). This includes decreases in fixed costs arising from the introduction of the new network models.

#### Other operating costs

Other operating costs have increased by £42 million to £435 million (2012- £393 million), driven largely by additional programmed investment spend. This one-off investment spend was £50 million (2012 - £26 million) and included an increase in media spend to raise customer awareness of Post Office services in addition to focused campaigns on travel-related services and mortgages together with development of new and improved services. There were also increases in the cost of sales, reflecting greater sales volumes, and in property related costs.

#### Joint venture and associate

Share of operating profit from the joint ventures (First Rate Exchange Services Limited) and associate (Midasgrange Ltd until its sale on 1 September 2012) was £32 million (2012 - £31 million). First Rate Exchange Services Limited results improved despite lower retail sales due to market conditions. This has been achieved mainly through driving efficiencies in operating costs. Post Office Limited's interest in the associate company, Midasgrange Ltd was sold during the year and made a loss on disposal of £30 million.

## Exceptional Items

	2013	2012
	£m	£m
Exceptional items		
Operating exceptional items:		
Restructuring costs including subpostmasters' compensation	(79)	(2)
Impairment of investment, property, plant and equipment	(66)	(36)
Government grant	98	
Subtotal operating exceptional items	(47)	(38)
Non-operating exceptional items:		
Profit on disposal of property, plant and equipment	2	1
Loss on sale of associate	(30)	
Net exceptional items	(75)	(37)

## Restructuring costs

Restructuring costs include the costs of delivery of major change. Network transformation resulted in costs of £12 million for subpostmasters' compensation and £40 million programme costs. Costs of £10 million relate to IT transformation which will create the IT infrastructure appropriate for a business with ambitious growth plans. Redundancy costs of £11 million were incurred during the year and mainly related to the Crown network. Business transformation payments of £4 million (2012 - £3 million) are payments that are sometimes made to staff as an incentive in order to secure agreement for significant changes in working practices to improve business efficiency.

## Government Grant

In addition to the Network Subsidy Payment to support the network, the Post Office also receives government grant funding towards the transformation programme. Government grant funding of £200 million was received in the year. The additional government grant funding is included within operating exceptional items to match the associated costs. £98 million of this government grant funding has been allocated in accordance with the designation letter, dated 2 April 2012, from the Department of Business, Innovation and Skills, to cover £66 million capital expenditure, £12 million network transformation related subpostmasters' compensation and £20 million network transformation programme costs.

## Treasury

Following the transfer of Post Office Limited from the ownership of Royal Mail Group Ltd to Royal Mail Holdings plc on 1 April 2012, Post Office Limited has operated an independent Treasury function and manages its own financial assets (including network cash) and financial liabilities (mainly government loans).

The Treasury function derives its authority from the Board and provides regular reports for Board review. It has the authority to undertake financial transactions relating to the management of the underlying business risks, however, it does not engage in speculative transactions and does not operate as a profit centre. The principal financial instruments utilised are deposits and borrowings.

The cash position of the business remains strong with cash and cash equivalents of £971 million (2012 £820 million) and a net cash inflow during the year of £151 million.

Net debt (excluding cash in the Post Office network) decreased by £119 million year on year as shown in the table below:

	2013 £m
Net debt brought forward at 25 March 2012	(325)
Net cash inflow before financing activities (see page XX)	244
Deduct: Increase in cash in the network included in net cash inflow	(121)
Finance costs paid	(4)
Total net debt carried forward at 31 March 2013	(206)

Post Office Limited's borrowing facility from the government and the associated Framework Agreement imposes constraints on the purposes for which the facility can be used and the availability of external borrowing. Post Office Limited's treasury policy is to minimise the amount drawn down on the loan in order to reduce the interest charge. The facility is limited to a maximum of £1.15 billion or the amount of security available (mainly network cash), whichever is the lower. The maximum drawn down under the facility during the year was £499 million on 30 March 2012. The facility is available at two days' notice.

At 31 March 2013 the company was financed as follows:

Borrower: Post Office Limited	Interest	Facility	Facility	Utilised	Average
Purpose	rate*	end date	£m	£m	Loan
	%				maturity
					date
Network Cash	1.0	2016	1,150	291	2013

\* Average interest rate of loan drawn down

#### Pensions

Post Office Limited is a participating employer within the Post Office Section of the Royal Mail Pension Plan (RMPP) and is a participating employer within the Royal Mail Defined Contribution Plan (RMDCP). Royal Mail Group Ltd is the principal employer of the Royal Mail Senior Executives' Pension Plan (RMSEPP) and Post Office Limited is a participating employer within RMSEPP. RMPP and RMSEPP are both defined benefit plans on a career average basis.

On 1 April 2012 – after the granting of state aid by the European Commission on 21 March 2012 – almost all of the pension liabilities and pension assets of the Royal Mail Pension Plan (RMPP), built up until 31 March 2012, were transferred to HM Government. On this date, the RMPP was also sectionalised, with Royal Mail Group Ltd and Post Office Limited each responsible for their own sections in future. This arrangement left the RMPP fully funded on an actuarial basis in respect of historic liabilities at this date.

The balance sheet pension position moved from a deficit of £206 million at March 2012 to an asset of £97 million at March 2013. The improvement in position is primarily due to the transfer to government noted above.

Both defined benefit plans are now closed to new members. RMSEPP closed on 31 December 2012 and has no active members. New employees are offered membership of the defined contribution plan.

#### Pension cash payments for all plans

The future funding of ongoing pension contributions into RMPP and deficit payments into RMSEPP is being discussed with the respective pension trustees. The payments for 2013 disclosed in the table below were based on the arrangements that were in place for the 2012 financial year.

	2013	2012
	£m	£m
Regular pension contributions	(24)	(24)
Funding of the pension deficit - RMSEPP	(2)	-
Payments relating to redundancy	(2)	(3)
Net cash payments	(28)	(27)

The regular future service contributions cash rate for RMPP expressed as a percentage of pensionable pay remained at 17.1% (2012 - 17.1%). The regular rate of employee contributions for the RMPP remains unchanged at 6%.

#### Events after the reporting period

In accordance with the funding agreement with government announced on 27 October 2010, for which state aid approval was received on 28 March 2012, Post Office Limited received £415 million of funding on 2 April 2013.

.....  
Chris Day  
Chief Financial Officer  
Post Office Limited  
XX June 2013

Section: Performance review

Title: Business Risk

Ref required to Corporate Governance section

The information below details the key business risks, their impact and how the Post Office manages these risks.

Key Risk	Impact	Mitigation
<p>1. Changes in customer preferences</p> <p>There is decline in the traditional Post Office income streams as customer preferences change.</p> <p>The revenue growth plans in personal financial services, mails, government and telecoms are ambitious. New income streams may fail to grow sufficiently to exceed the losses from traditional products in decline.</p>	<p>Projected reduction in government subsidy is not delivered.</p>	<p>We have introduced new services in growth areas and continue to refine and develop these product offerings. There are detailed plans in place to deliver the growth trajectory and progress against these plans is monitored rigorously.</p>
<p>2. Funding</p> <p>As set out in note xx, Post Office Limited has a funding agreement with government until 31 March 2015 with a working capital facility until 31 March 2016. There is a risk that funding beyond these dates cannot be negotiated or that state aid approval is not granted in time.</p>	<p>Funding is required beyond 2015 in order to complete the business modernisation and sustain the non-profitable elements of the network. The working capital facility is required to fund the cash in the network.</p>	<p>Planning is well underway for the future period beyond 2015 and discussions will commence shortly with Government.</p>
<p>3. Business transformation programmes</p> <p>We are managing a significant number of change programmes</p>	<p>Failure to implement the</p>	

<p>to modernise the Post Office and enable its processes to operate independently from those of Royal Mail Group. These include the network, Crown and IT transformation programmes. The success of the Post Office strategic plan depends upon the successful realisation of the benefits from these programmes.</p>	<p>modernisation will leave the Post Office with an unsustainable cost base and a continued reliance on significant government subsidy.</p>	<p>We have detailed plans in place to manage the transformation and ensure it is delivered within budget and on time. Delivery is tracked monthly by a Transformation Board made up of Executive Committee members which provides direction and oversight over the programmes' delivery.</p>
<p>4.Engagement risk</p> <p>The support and active engagement with our people and subpostmasters during this significant time of change is key to the successful delivery of our strategy. Withdrawal or lack of support from our employees or subpostmasters in the network could cause delays in the Post Office transformation programmes and limit our ability to meet business objectives.</p>	<p>Lack of support from our people and subpostmasters will jeopardise our ability to meet our strategic goals of growth, profitability and reduced reliance on government subsidy.</p>	<p>We maintain a fluid and comprehensive engagement programme with unions, staff and subpostmasters. These include regular meetings with the National Federation of subpostmasters (NFSP), Communication Workers Union (CWU) and Unite, senior management briefings to staff and subpostmasters, as well as events to engage our people in our vision and strategy.</p> <p>We have a people plan aimed at addressing staff motivation and skill needs. This includes development of new leadership and reward frameworks and increased focus on recruitment and training.</p>

<p>5. Regulatory &amp; compliance</p> <p>There is a risk of non-compliance with the changing regulatory environment. We operate under an extensive regulatory environment including areas such as financial and postal services, procurement, competition law and data security regulations.</p>	<p>Failure to meet regulatory requirements could result in fines, negative impacts on our reputation, as well as costs of investigation and resolution.</p>	<p>Our legal and compliance team works closely with the relevant business owners in identifying new requirements and monitoring compliance against existing ones.</p> <p>The Risk and Compliance Committee monitors key risks and actions to mitigate them.</p>
<p>6. Business continuity</p> <p>The Post office has particular operational risks around disruption of its services.</p> <p>This includes adverse weather conditions, industrial action, systems breakdown or failure of a critical supplier.</p>	<p>Breakdowns in the network would reduce quality of service, increase costs and/or damage our reputation.</p>	<p>Disaster recovery and business continuity plans are under continuous development and review in line with business change. This includes contingency planning and training in the event of disruption such as industrial action or IT failure.</p> <p>Key suppliers' ability to continue to meet Post Office's requirements is closely monitored.</p>

## Section: Governance

### Board biographies

#### Board:

Post Office Limited's Board of Directors is chaired by Alice Perkins CB. As Non-Executive Chairman she is independent both of the executive management of Post Office Limited and of its special shareholder. The Board comprises the Chairman, five other Non-Executive Directors and two Executive Directors.

#### Board responsibilities

The responsibilities of the Board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to the shareholder.

There are a number of Board committees which deal with specific topics requiring independent oversight including audit, risk and compliance, nominations of the Board, pensions and senior remuneration.

Each committee is chaired by a Non-Executive Director and operates within its own agreed, documented Terms of Reference.

#### Alice Perkins CB – Post Office Limited Chairman (Chairman of Nominations Sub-Committee)

Alice had a wide-ranging career in the civil service, which included policy and operational roles in health, social security and public spending in the HM Treasury. Alice was also the Civil Service's Group HR Director in the Cabinet Office between 2001 and 2005. Before joining the Post Office as Chairman in September 2011, she served as Non-Executive Director on the boards of Littlewoods, BAA and TNS, where she also chaired the Remuneration Committee. Alice is an external member of the Oxford University Council, a business coach at the JCA Group, and a member of the faculty at Meyler Campbell where she teaches senior executives how to coach.

#### Neil McCausland – Senior Independent Director (Chairman of Remuneration Sub-Committee)

Neil has had a portfolio of non-executive roles over the last 10 years. He is currently Chairman of three companies. Snow and Rock, a retail chain selling skiing and outdoor brands, bikes and running gear; Dwell, a multi-channel contemporary furniture retailer; and Skin, a chain of skin treatment clinics specialising in laser hair removal. Until recently he was Chairman of footwear company Kurt Geiger, and a Governor of Nuffield Health, which operates hospitals and health clubs. Neil began his career at Marks & Spencer, before becoming Managing Director of C&A and Chief Executive of NAAFI (an MOD agency).

#### Alasdair Marnoch – Non-Executive Director (Chairman of Audit, Risk and Compliance Sub-Committee) – being updated

Alasdair Marnoch joined the Board of the Post Office as a Non-Executive Director on 23 May 2012. A Chartered Accountant, he chairs the Board's Audit, Risk and Compliance Sub-Committee which reviews the statutory accounts and financial controls. Alasdair has had wide experience as Finance Director of a number of FMCG and service businesses, including listed companies. Most

recently, he served as CFO of the Equiniti Group, a leading provider of complex administration and processing services to the public and private sectors.

#### Tim Franklin - Non-Executive Director

Tim Franklin joined the Board as a Non-Executive Director on 19 September 2012. Tim was Chief Operating Officer of the Co-operative Banking Group until the end of 2011, having previously served as Managing Director of the Britannia Building Society. Prior to that, he was Director of Customer Programmes and Loyalty and Managing Director of Savings at Barclays. Tim's experience extends across the private and public sectors. He is also a Non-Executive Director of HM Land Registry and was previously on the Boards of Reclaim Fund Limited, Mutual Plus Limited and the Link Cash Machines Network.

#### Virginia Holmes - Non-Executive Director (Chairman of Pensions Sub-Committee)

Virginia brings to the Board extensive knowledge of the financial services industry including both investment management and banking. Her experience includes serving as Chief Executive of AXA Investment Managers UK and more than a decade with the Barclays Bank Group where she ultimately served as Managing Director of Barclays Bank Trust Company. Virginia currently serves on the boards and chairs the investment committees of both the Alberta Investment Management Corporation in Canada and the Universities Superannuation Scheme in the UK. She also serves on the boards of Standard Life Investments Ltd and JPMorgan Claverhouse Investment Trust plc.

#### Susannah Storey - Non-Executive Director

Susannah Storey is the representative of the Department for Business, Innovation and Skills on the Post Office Board. She has recently been appointed as Director of Corporate Strategy and Change at the Department of Energy and Climate Change. Susannah has been a civil servant since 2006, working at the Shareholder Executive until 2013 in a number of roles including Head of the Royal Mail and Postal Services team and Chief Operating Officer. Prior to the Shareholder Executive, Susannah worked in investment banking at Citigroup and Schroders, specialising in UK Corporate Finance.

#### Paula Vennells - Chief Executive

Paula has worked for the Post Office since 2007 in a number of senior roles including Managing Director. She became Chief Executive on 1 April 2012. Previously, Paula spent five years with Whitbread plc as Group Commercial Director. She began her career with Unilever and L'Oreal and held directorships in sales and marketing with a number of major retailers including Dixons Stores Group and Argos. She is currently a Non-Executive Director and Trustee for Hymns Ancient and Modern Group.

#### Chris Day - Chief Financial Officer

Chris joined the Post Office in August 2011 from the BBC where he had been Group Financial Controller since 2005. Prior to that, Chris spent 14 years in FMCG with Grand Metropolitan/Diageo in a succession of Treasury/Corporate Finance roles in the UK, and as Finance Director in the Netherlands and subsequently Germany/Austria. Earlier in his career Chris worked as a financial management consultant at KPMG having started his career with Beecham Group.

#### Alwen Lyons - Company Secretary

Alwen Lyons joined the Post Office in 1984 as a graduate and has worked at a senior level in several directorates including network, finance and marketing. She became the Company Secretary in July 2011, after leading the project to separate Post Office Limited from Royal Mail Group.

Section: Governance

Title: Corporate governance

Corporate governance statement

The shares in Post Office Limited (the "Post Office") were transferred from Royal Mail Group Ltd to Royal Mail Holdings plc on 1 April 2012 and the Post Office has operated independently since that date.

Corporate governance principles

As the Post Office is not a company whose shares are listed and traded on a public exchange, it is not formally required to report on its compliance with the UK Corporate Governance Code (the "Code"). Nonetheless, the Board of the Post Office believes this is an appropriate benchmark for reporting on corporate governance.

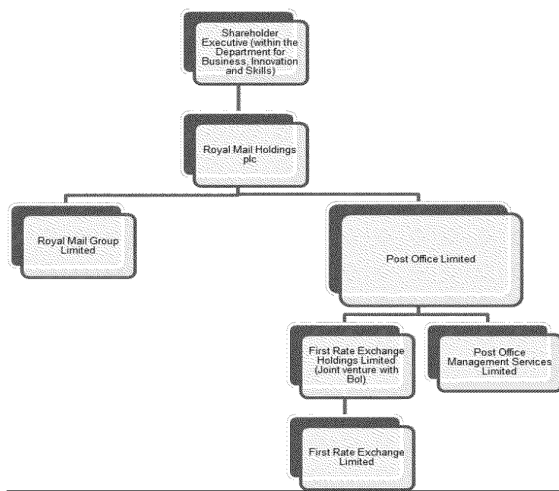
During the year, the Post Office has further established a full Board and Committee structure and has set principles for good governance which follow the provisions of the Code, so far as they can apply to a Government-owned entity which has no private or institutional external shareholders.

Legal ownership structure

The Post Office is a wholly owned subsidiary of Royal Mail Holdings plc. The Secretary of State for Business, Innovation and Skills (BIS) holds a special share in Post Office Limited. The Special Shareholder's rights are set out in the Post Office Limited Articles of the Association. These include a requirement for Post Office Limited to obtain the Special Shareholder's consent for Directors' remuneration arrangements.

A strong link remains between Royal Mail and the Post Office – the Post Office has a long-term agreement in place to continue to supply Royal Mail products and services through its network. That link is currently reinforced in the corporate structure by a common group holding company (Royal Mail Holdings plc) which holds shares in both Post Office Limited and Royal Mail Group Ltd.

Neither Royal Mail Holdings plc nor BIS, through its Shareholder Executive (ShEx), have any day-to-day involvement in the operations of the Post Office or the management of its branch network and staff.



## The Board

Alice Perkins was appointed as Chairman of the Board in July 2011, marking the first step on the road to building an independent Board for the Post Office. Neil McCausland joined in September 2011 as the Senior Independent Director and, in the year under review, a further four Non-Executive directors have been appointed, each bringing particular skills and experience relevant to the business targets of growth, modernisation, customer focus and business efficiency.

The Board is unusual in having a female Chairman and Chief Executive and being equally balanced between men and women. The Board, comprises two Executive Directors and six independent Non-Executive Directors, including the Chairman. This provides a strong level of independent challenge to decision-making and enables the Post Office to call upon a wide range of experience and opinion. Short biographies of all members of the Board appear on page X of this Annual Report.

The Remuneration Committee liaises with ShEx in BIS to obtain Special Shareholder's consent for all Directors' appointments and the terms under which they serve, including Non-Executive Directors' fees and any changes in the total remuneration for each Executive Director. The Executive Directors' contracts provide for six months' notice of termination to be given by the director and 12 months' notice to be given by the organisation.

Non-Executive Directors are not employees of the Post Office but provide services under the terms of an individual Letter of Appointment, signed at the commencement of their directorship. All Non-Executive Directors are entirely independent of the Post Office, having no other connection or financial interest, other than as customers and taxpayers.

## Non-Executive Directors' Terms of Office

Director	Date of appointment	Term of office	Unexpired term at 31 March 2013	Committee memberships
Alice Perkins	21 July 2011	Rolling 12 month contract	N/A	Nominations (Chair) Remuneration
Tim Franklin	19 September 2012	4 years	3 years 172 days	ARC
Virginia Holmes	4 April 2012	3 years	2 years 4 days	Pensions (Chair) Nominations Remuneration
Neil McCausland	22 September 2011	4 years	2 years 175 days	Remuneration (Chair)

				ARC Nominations
Alasdair Marnoch	18 May 2012	3 years	2 years 48 days	ARC (Chair)
Susannah Storey	18 April 2012	3 years	2 years 18 days	ARC Pensions

### Board meetings

The Board meets at least eight times a year, with an additional strategy away day, and has a formal schedule of matters reserved to it.

The Board's responsibilities include setting the Post Office's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to the shareholder. During the year to 31 March 2013 the Board has focused on financial performance, network transformation, and the people and capability of the business. Over the last six months the Board's primary focus was on setting the strategic direction for the business, in preparation for completion during 2013-14 of the Strategic Plan and Funding Agreement with Government for the period 2015-20.

During the year under review, the Board established sub-committees which met regularly to undertake more detailed reviews in specialist areas, as recommended by the Code. Such focus areas included accounting policy and practices, risk and controls, pensions, executive remuneration, the processes for evaluation of performance, and the nomination and appointment of new directors or the removal of directors from the Board.

The full Terms of References for the Board sub-committees can be found on the Post Office website.

The following shows the attendance of the directors at meetings of the Board and its principle committees during the year:

	Board	ARC	Mutualisation Committee	Nominations Committee	Pension Committee	Remuneration Committee
Alice Perkins	8/8	3/4 <sup>†</sup>	3/3	2/2	-	4/4
Chris Day	8/8	4/4 <sup>†</sup>	3/3	-	7/7	-
Tim Franklin*	5/5	2/3	2/2	-	-	-
Virginia Holmes	8/8	-	2/3	2/2	7/7	4/4

Neil McCausland	8/8	4/4	3/3	2/2	-	4/4
Alasdair Marnoch*	7/7	4/4	3/3	-	-	-
Susannah Storey*	8/8	3/3	2/3	-	6/6	-
Paula Vennells	8/8	-	3/3	-	-	2/2 <sup>†</sup>

\*from date of appointment

<sup>†</sup> in attendance, by invitation

#### Board sub-committees

##### Audit, Risk and Compliance Committee

The Audit, Risk and Compliance Committee (“ARC”) is made up of five Non-Executive Directors and is chaired by Alasdair Marnoch. The ARC considers Post Office Limited’s financial reporting, including accounting policies and internal financial controls. It looks at the levels of risk which exist within the Post Office and the steps taken to mitigate those risks.

During the year the Post Office has been building its own risk management, internal control and internal audit procedures and this will be an area for further development during the coming year.

One of the ARC’s primary responsibilities during the period was to review both the half-year trading statement and the full-year accounts, to assess the validity of assumptions made and the accounting policies used and to consider the ways in which the Post Office should present its financial performance.

A second major responsibility has been to promote the development of a risk management framework suited to the complex nature of the Post Office business. This will take some time and is a key focus area for the coming year. The development of risk management and control procedures and the establishment of a full internal audit programme are areas of high priority.

In this period, a new Head of Internal Audit was appointed and the transition from using the Royal Mail internal audit function to building a new internal team had begun.

The ARC works with both the internal audit team and Ernst & Young, the external auditor.

##### Remuneration Committee

The Remuneration Committee is made up of three Non-Executive Directors and is chaired by Neil McCausland, the Senior Independent Director. The committee is responsible for making recommendations to the shareholder on the remuneration of the Executive Directors in accordance with the articles of association. In doing so, it also reviews the remuneration policy and packages of the most senior leadership team, being the roles which report directly to the Chief Executive. It also obtains information on salary levels across the business and within external organisations of comparable size in order to set remuneration levels within an appropriate context.

The Chief Executive may attend meetings, at the invitation of the Chairman, to discuss matters relating to the remuneration of the Chief Financial Officer and members of the Executive Committee, but the committee upholds the principle that no individual may be involved in discussions concerning their own remuneration.

The committee is able to consult on remuneration matters with the Human Resources & Corporate Services Director, other members of the Human Resources team and with external consultants. In the year under review, advice was primarily obtained from New Bridge Street on market practice and benchmark development. New Bridge Street consultants have no other links with the Post Office which could compromise their independence.

No material changes can be made to directors' base salaries, benefits or incentives without Special Shareholder consent. Further details of the schemes now in place, and a table setting out the remuneration paid to all directors in the year to 31 March 2013, are provided in the Directors' Remuneration Report on page X.

#### Nominations Committee

The Nominations Committee is made up of three Non-Executive Directors and is chaired by Alice Perkins, the Chairman. It met for the first time in December 2012, with director appointments up to that time having been made according to specific criteria, following discussions with the shareholder.

The primary role of this committee is to recommend to the Board any changes in Board membership and manage the process for recruiting and replacing directors. The Board is complete and no immediate changes are expected. The committee will keep under review the balance of skills, experience and diversity available within the Board and each of the Board sub-committees.

The Nominations Committee will also oversee the process for Board and committee performance evaluation, and monitor talent and diversity (see pxx). The Chief Executive may attend meetings, at the invitation of the Chairman, to discuss matters relating to the talent and diversity policies.

#### Pension Committee

The Pensions Committee is made up of two Non-Executive Directors and one Executive Director and is chaired by Virginia Holmes.

The Pensions Solution, adopted in April 2012, saw a substantial transfer of assets from the Royal Mail Pension Plan (RMPP) to the government, in return for the government assuming the obligations for past service liabilities. The transfer was made possible following European Union approval for UK government state aid.

As part of the solution, the pension fund was sectionalised, with the Post Office assuming responsibility for that part of the pension fund that relates to Post Office employees and pensioners.

The Board has delegated authority to the Pension Sub-Committee to appoint professional advisers, to enter into negotiations with the trustees of the RMPP on the forthcoming valuation of the funds, to agree the investment strategy for the Post Office sections and to monitor funding levels and investment performance. The committee reports back to the full Board so that its work can dovetail with executive recommendations and union negotiations on pay and benefits.

In August 2012 the committee recommended to the Board the appointment of AON Hewitt as its investment advisers. Working with AON Hewitt and with Towers Watson, its Actuarial advisers, the committee has satisfied itself as to the fair value of assets transferred into the Post Office section at 1 April 2012 and agreed a revised investment strategy with the trustees of the RMPP with the aim of maintaining the long term sustainability of the Scheme and protecting against an unmanageable increase in liabilities for the Post Office in the future.

#### Mutualisation Sub-Committee

The Mutualisation Sub-Committee is chaired by Alice Perkins, the Chairman of the Post Office and its membership is the same as that of the full Board. It met for the first time on 4 July 2012, the week in which the government published the response to its consultation 'Building a Mutual Post Office'. The committee is responsible for ensuring that the work to develop proposals for the mutualisation of Post Office Limited is provided with strategic direction, involves the appropriate level of stakeholder involvement and has adequate support.

The focus of the committee has been to consider the financial, cultural and business implications of mutualisation to ensure that progress on mutualisation supports and enables the successful delivery of the Post Office's transformation programme and the delivery of its future commercial strategy, which is an essential prerequisite of any change in governance.

#### Performance evaluation

The Board intends to carry out an annual evaluation of the effectiveness of the Board and of the Board sub-committees. The initial performance evaluation will take the form of an assessment by the Chairman. Following this internal review, external evaluations will be completed every three years.

#### Executive Committee

Below main Board level, the Executive Committee (ExCo) is the most senior management body and is made up of the Chief Executive and each of her direct reports, supported by some business unit heads who report to members of the Executive Committee. The committee works within the delegated authorities established by the Board.

The ExCo implements the strategy agreed by the Board and monitors business performance and development at a day-to-day level. It meets formally at least once a month to discuss proposals for new business development, receive financial and other performance reports, and address urgent issues which have arisen within the business requiring senior level resolution. Twice yearly, it reviews the results of personal performance assessments undertaken throughout the organisation.

The Chief Executive, Chief Financial Officer and the Company Secretary attend both Board and ExCo meetings which facilitates and strengthens the communication channels between the senior leadership team and the Board and its committees.

The Terms of Reference of the ExCo have been set out in writing and are available to download from the Post Office website.

#### Risk management

The Post Office has adopted the requirements of the FRC Guide to Corporate Governance and established an approach to the management of risk, tailored to meet the demands of a new business with ambitious plans for expansion in its chosen markets.

The Board takes ownership of risk management through its Audit, Risk and Compliance Committee (ARC). The Business' Risk & Compliance Committee reports into the ARC and is responsible for:

The Board takes ownership of risk management and has asked its Audit and Risk Committee to co-ordinate a proposed approach in this area for:

- review and challenge of risk management
- approval and endorsement of policies to mitigate risk and
- development of the risk management framework.

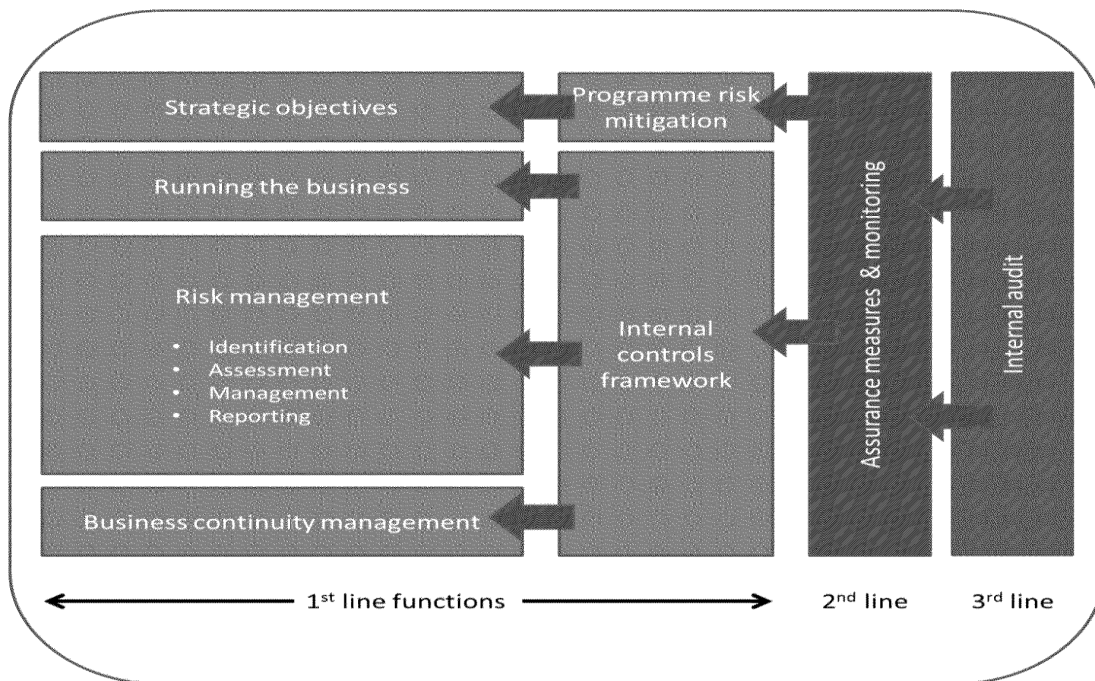
This committee is chaired by the Director of HR & Corporate Services and reports to the Post Office Executive Committee. The committee comprises members of the executive committee and other senior managers.

During the year the Post Office set up its own Internal Audit department as part of the 'three lines of defence' model (see below). Internal Audit provides independent assurance and advice on the risk management framework, its future strategy and evolution, and reports directly to the ARC.

The business also governs financial and related regulatory risk with its partner, the Bank of Ireland (UK) plc through established joint regulatory risk committees.

#### Risk management framework

The Post Office has set out the components of risk management in its risk framework. This framework is described at high level in the diagram below.



The framework utilises a 'three lines of defence' model to establish accountability and responsibility for the effective operation of this framework.

1 <sup>st</sup> Line of Defence	• Day-to-day risk management in business operations
2 <sup>nd</sup> Line of Defence	• Risk management oversight and challenge
3 <sup>rd</sup> Line of Defence	• Independent assurance

1<sup>st</sup> line of defence – is responsible for managing risk in day-to-day business operations

2<sup>nd</sup> line of defence – comprises central functions which oversee regulatory compliance and provide advice on the operation of the framework

3<sup>rd</sup> line of defence – provides independent assurance in respect of the Post Office's regulatory risk management

The risk framework is supported by the Risk & Compliance team, with dedicated resource in place to administer the tools and committees in use to manage risk.

## Progress

Over the past 12 months, each directorate has gone through a process of identifying and assessing the risks associated with achievement of its respective objectives. These risks are recorded on a software tool to enable aggregation, comparison and risk reporting. In addition, the key strategic programmes of the business capture their own risks.

The top 12 risks from each of these sources, together with the respective mitigation plans, are reviewed by the Risk & Compliance Committee to assess the robustness of risk assessment and management.

The above assessment will be supplemented in the first quarter of the new financial year with a top down assessment of the company's risks by the Post Office Executive Committee.

## Risk appetite

Over the next 12 months the Post Office will be fully developing its risk appetite statements for each of the key risks, with a view to establishing where additional risk may be taken to generate new opportunities and/or where further treatment of existing risks is required.

## Business continuity

As part of the development of risk management, the Post Office is bringing together a wide range of business continuity arrangements throughout the business under one central policy and governance framework to ensure that the Post Office is capable of withstanding any significant threat to its ongoing operations.

## Directors' report

The directors present the Group Annual Report and Financial Statements for Post Office Limited. These financial statements relate to the 53 weeks ended 31 March 2013.

## Principal activities

The Group's principal activities are the provision of access to a wide range of mails, government, financial, travel and retail services through its network of Post Office branches and other channels across the United Kingdom (UK).

## Review of the business and expected future developments

Information contained within the Chief Executive's Review (pxx) and the Financial Review (pxx) constitutes the business review required by the Companies Act 2006 and is incorporated into this directors' report by reference.

## Results and dividends

The profit after taxation for the year was £38 million (2012 - £30 million). The directors do not recommend the payment of a dividend (2012 £nil dividend).

## Pensions

As explained in note 19 on 1 April 2012, almost all of the pension assets and liabilities of the Royal Mail Pension Plan were transferred to HM Government. On this date the Royal Mail Pension Plan was also sectionalised with Royal Mail Group Ltd and Post Office Limited responsible for their own sections. All employees were transferred to be directly employed by Post Office Limited on the same date.

Royal Mail Group Ltd is the principal employer in the Royal Mail Senior Executive Pension Plan and for the Royal Mail Defined Contribution Plan. Post Office Limited became a participating employer for both of these plans with effect from 1 April 2012. Post Office Limited continues to account for approximately 7% of the Royal Mail Senior Executive Pension Plan scheme as it has done previously. Both defined benefit schemes were closed to new members in 2008 and the Royal Mail Senior Executive Plan closed on 31 December 2012. New employees are offered membership of the Royal Mail Defined Contribution Plan.

The balance sheet pension surplus of £97m (2012 - £206m deficit) has arisen principally due to the transfer of pension assets and liabilities to HM Government.

Prior to 1 April 2012, Royal Mail Group Ltd had the legal relationship with the trustees of both defined benefit plans and, as such, the trustees held Royal Mail Group liable for the actuarial deficit in the scheme. All employees were employed by Royal Mail Group Ltd and seconded to Post Office Limited under an agreement between Post Office Limited and Royal Mail Group Ltd. Post Office Limited met the full costs of employment and was responsible for the funding of the pension deficit attributable to these employees. Consequently, Post Office Limited recognised a balance sheet deficit based on employee numbers over 12 years and represented approximately 7% of the total balance sheet deficit at that time. The net pension interest, deficit recovery payments and actuarial gains or losses were also allocated on this basis, giving Post Office Limited approximately 7% of the total balance sheet deficit at the balance sheet date. The current service cost, regular future service contributions and curtailments were computed separately for Royal Mail Group Ltd and Post Office Limited based on common factors/rates.

#### Political and charitable contributions

During the year charitable contributions of £989,702 (2012 - £320,108) were made. No political contributions were made in the year (2012 £nil).

#### Research and development

Research and development expenditure during the year amounted to £nil (2011 £nil).

#### Policy on the payment of suppliers

The Post Office policy is to use its purchasing power fairly. Payment terms are agreed in advance for all major contracts. For lower value transactions, the standard payment terms printed on the purchase order apply. It is policy to abide by the agreed terms. The business has sought to comply with the Department for Business, Innovation and Skills (BIS) Better Practice Code. The number of days' purchases in creditors at the balance sheet date was 24 days (2012 - 33 days).

#### Land and buildings

The net book value of land and buildings, based upon a historic cost accounting policy and excluding fit-out, is £11 million (2012 - £11 million). In the opinion of the Directors, the aggregate market value of Post Office's land and buildings at the year end exceeded their net book value by £73 million (2012 - £45 million).

#### Directors and their interests

The following served as directors of Post Office Limited during the year ended 31 March 2013 and remain in post as at the date of approval of these financial statements.

A Perkins CB

N W McCausland

V A Holmes (appointed 4 April 2012)

S J Storey (appointed 18 April 2012)

A Marnoch (appointed 23 May 2012)

T A Franklin (appointed 19 September 2012)

P A Vennells \*

C M Day \*

\*Executive Directors

No director has a beneficial interest in the share capital of Post Office Limited. All the Non-Executive Directors are considered to be independent, having no financial connection with Post Office Limited other than by virtue of the fees paid for their services as a director. The emoluments of directors are set out in the Directors' Remuneration Report (pxx).

## Insurance and qualifying third-party indemnity provisions for directors

Post Office Limited maintains directors' and officers' liability insurance for the benefit of all directors and officers of Post Office Limited.

A partial qualifying third-party indemnity provision (as defined in section 234 of the Companies Act 2006) was and remains in force for the benefit of all the directors of Post Office Limited and former directors who held office during the year. The indemnity is granted under article 129 of Articles of Association or Royal Mail Holdings plc, the ultimate parent company. The indemnity is partial in that it does not allow Post Office Limited to cover the costs of an unsuccessful defence of a third-party claim.

## People

Our goal is to ensure that all employees are engaged and involved in the business and are aligned and equipped to meet business objectives. As part of our commitment to drive better service for customers we continue to focus on improving the quality of our leadership, professionalising key roles, recognise the importance of diversity and achieving greater employee involvement in decision making.

Training and development programmes have been put in place to support our ambition to create a high-performance customer-oriented sales culture. This ambition is further supported by a range of bonus schemes which are based on the achievement of business targets.

Underpinning all of this is a need for dignity at work, where everybody feels valued, is treated fairly and equally with everyone playing a full part in helping the business to achieve its goals.

Regular employee engagement surveys are conducted to allow employees an opportunity to express their views and opinions on important issues. This two-way communication encourages all employees to contribute towards making business improvements.

## Corporate responsibility

Post Office Limited is committed to carrying out its activities in a socially responsible manner in respect of the environment, employees, customers and local communities. Further information can be found in on page X.

## Disabled employees

The Post Office's policy is to give full consideration to applications for employment from disabled people. Employees who become disabled while employed receive full support through the provision of training and special equipment to facilitate continued employment where practicable. The business provides training, career development and promotion to disabled employees wherever appropriate.

## Post balance sheet events

[To be confirmed post year end.]

## Going concern

After analysis of the financial resources available and cash flow projections for Post Office Limited, the directors have concluded it is appropriate to prepare the financial statements on a going concern basis. Further details are provided in accordance with the fundamental accounting concept in note 1 of the financial statements.

Audit information

The directors confirm that, so far as they are aware, there is no relevant audit information of which the auditor is unaware and that each director has taken all reasonable steps to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

Auditor

The auditor, Ernst & Young LLP, is deemed to be reappointed under section 487(2) of the Companies Act 2006.

By order of the Board

Alwen Lyons

Secretary

Post Office Limited (company number 2154540)

148 Old Street, London EC1V 9HQ

XX June 2013

Section: Governance

Title: Directors' remuneration report

Statement by the Chair of the Remuneration Committee

I welcome this opportunity to outline our progress on executive remuneration during the year. Remuneration is a highly sensitive issue in the challenging economic environment in which we operate and, as a publicly funded business with a commercial and public purpose, we embrace the transparency and accountability required to establish a responsible approach to remuneration.

Once the Post Office Board appointment process was complete in September 2012, a Remuneration Committee was set up to take responsibility for executive remuneration. The members of the committee are independent Non-Executive Directors (NEDs) and no individual participates in discussions about their own remuneration. We have used the recommended governance principles and proposed legislative changes on the disclosure of executive remuneration to prepare this report and to aid the development of the remuneration strategy.

The committee recommends the strategy and policy for Executive Directors' remuneration to the Post Office Board for their approval taking into account their potential impact across the organisation. Prior written consent of the Special Shareholder is required in respect of any variation or amendment to the remuneration of the Executive Directors. During this first year I have held regular dialogues with officials and ministers in the Department for Business Innovation & Skills to build working relationships and a common understanding of the issues.

The Post Office has begun the journey to turnaround the business to become a sustainable organisation, characterised by sound cost control in a performance culture and active stakeholder participation and engagement. We are planning the future of the business for the next 10 years so the longer term remuneration policy becomes very important. We have deliberately made no changes to the remuneration policy for the Executive Directors during this first year as we build a track record of solid achievements against challenging targets.

The framework for the Executive Directors' remuneration was inherited, with neither the Board nor the Remuneration Committee involved in its creation. The Remuneration Committee faces a difficult situation in which it needs to incentivise senior leaders during the transition to turn the business around while working within a constrained framework and challenging circumstances. There is limited scope to flex the remuneration framework and reward mechanism to suit the circumstances and reward appropriately.

The Chief Executive, Paula Vennells, and the Chief Financial Officer, Chris Day, were appointed to their roles prior to 1 April 2012, the date the Post Office commenced operating independently from Royal Mail Group. While the responsibilities of the Chief Executive and Chief Financial Officer have increased significantly, their remuneration remains unchanged.

An extensive remuneration benchmarking exercise was undertaken during the year and data from similar-sized organisations from three distinct sectors was considered. The organisations used for the benchmarking activity came from the mutual, government owned and PLC sectors. The results of the benchmarking showed the levels of Post Office executive reward for both fixed and total remuneration are substantially below the market median. The Remuneration Committee agreed that whilst it would not recommend any immediate remedial action, the relative market position of

the Executive Directors would be kept under review. Any recommended future change in remuneration for Executive Directors would be subject to Special Shareholder approval.

For the financial year ended 31 March 2013, the committee was satisfied that there had been a clear link between performance of the business and payments under the two incentive plans, the Short Term Incentive Plan (STIP) and the Long Term Incentive Plan (LTIP). Details of STIP and LTIP targets and the results achieved are shown in the Implementation section of the Remuneration Report.

The remuneration policy will remain largely unaltered for 2013-14 and the Remuneration Committee is in discussion with the Special Shareholder on the future remuneration framework for Executive Directors. The Post Office is undergoing a fundamental transformation and we anticipate that each year progressively more demanding targets will be set for the STIP and LTIP in order to achieve our goal of financial sustainability.

The Remuneration Committee is comfortable that the current policy provides a strong link between reward and performance and I commend this report to our stakeholders.

Neil McCausland

Chair, Remuneration Committee

## The remuneration report

This report has been prepared in accordance with the provisions of the Companies Act 2006 to the extent that they are applicable for an unlisted company. The committee has also, where practicable, adopted early the proposed legislative requirements for disclosure of directors' pay being put forward for UK listed companies. Accordingly, the remuneration report has been split into two sections: a policy report and an implementation report. The policy report sets out the policy for the remuneration of directors and its link to the business strategy. The implementation report sets out how this policy was applied during the year under review and the remuneration received by directors. Both sections of the report have been approved by the Remuneration Committee and the Board.

### Remuneration policy report

The committee is responsible for setting the remuneration packages for the Chief Executive and Chief Financial Officer and determining the overall remuneration policy for the Chief Executive's direct reports and the Company Secretary.

The committee's intention is that the remuneration policy should align with the business strategy and risk profile so that individuals are motivated to deliver the Post Office's objectives and protect its brand value. The Post Office remuneration strategy is based on the following:

- Attracting and retaining the right people within an agreed policy to lead and deliver the strategic plan
- Using incentives appropriately to reward the achievement of the turnaround strategy and promote the long-term viability of the organisation
- Reinforcing an emerging culture of co-ownership and partnership
- Providing a transparent approach to the disclosure of pay

### Remuneration policy summary

The table [overleaf] describes the remuneration policy for the year ended 30 March 2014 and the breakdown of the packages for the Executive Directors, which comprise of fixed pay (base salary, benefits and cash in lieu of pension contributions) and pay at risk (STIP and LTIP).

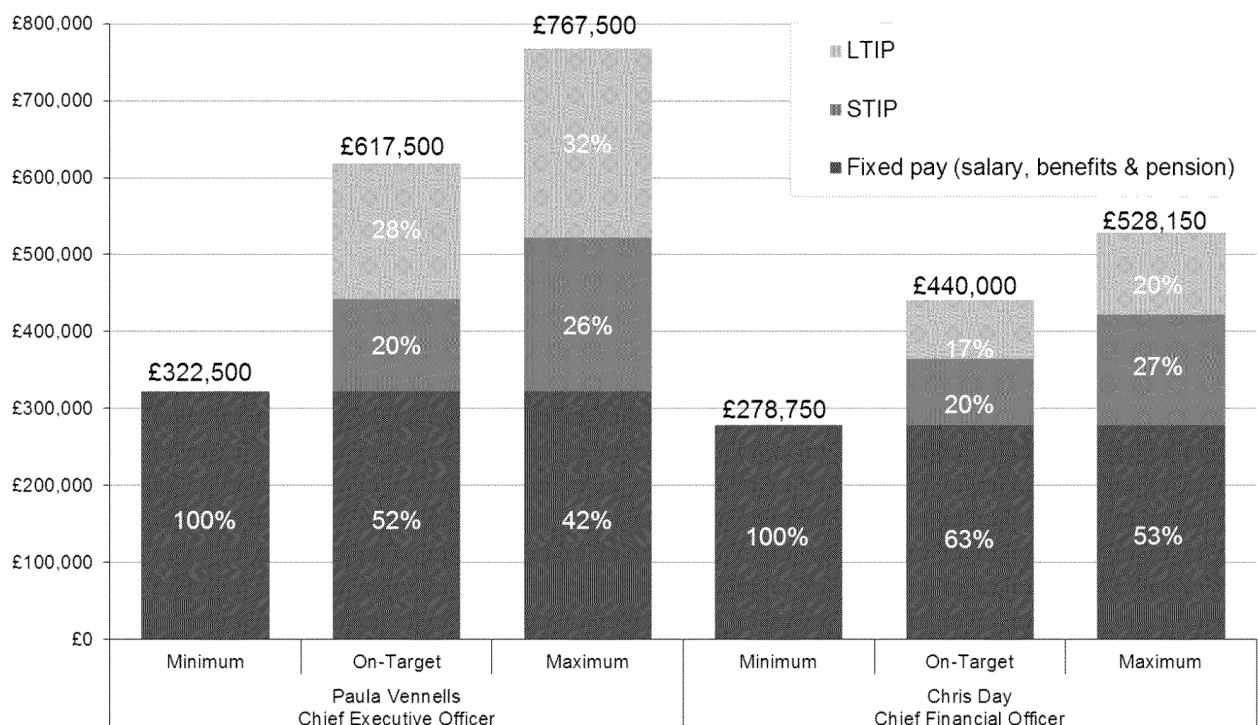
Remuneration policy table

Element	Link to strategy	Operation	Performance period	Maximum values
Base salary	<p>Determined by reference to the skills and responsibilities of the individual.</p> <p>Consideration is given to pay and employment conditions elsewhere in the Post Office when determining base salary increases and to market data on comparable roles.</p>	<p>Directors' salaries are reviewed annually. The next review is scheduled for July 2014.</p>	-	<p>The current salaries for the Executive Directors, as at 1 April 2013, are:</p> <p>Chief Executive: £250,000</p> <p>Chief Financial Officer: £215,000</p>
Benefits	<p>Participation in life and health assurance schemes, company car and private medical schemes are part of Post Office-wide benefit programmes to retain talented staff and encourage greater health and wellbeing.</p>	<p>The value of the benefits package is monitored by the Remuneration Committee and benchmarked against comparator organisations.</p>	-	<p>Car allowance of £7,700 per annum plus value of other benefits as appropriate.</p>
Pension	<p>Pension provision is provided by the Post Office and is available to all employees to help them meet their retirement needs and provide a competitive remuneration package. Executive Directors receive a salary supplement in lieu of pension scheme membership.</p>	<p>A salary contribution in lieu of pension is paid as a cash supplement to the Chief Executive and Chief Financial Officer.</p>	-	<p>25% of salary</p>
Short-term Incentive Plan (STIP)	<p>The STIP drives and rewards performance against a set of key financial and operational targets taken from the balanced scorecard, set each year according to the current priorities for the business.</p> <p>STIP awards are also linked to the achievement of personal performance</p>	<p>The metrics and target ranges are agreed annually with the Board and the Special Shareholder as part of the annual business and budget planning cycle.</p> <p>The STIP metrics are a mixture of financial (45%), customer (20%) modernisation (25%), employee engagement (10%) measures which link directly to the overall strategy.</p> <p>80% of the STIP award is based on the balanced scorecard and</p>	One year	<p>The maximum STIP opportunity is 80% of salary (with 48% of salary being payable for on-target performance).</p> <p>The maximum STIP opportunity for the Chief Financial Officer is 67% if salary (40% of salary for on-target performance)</p>

	objectives.	20% is based on individual performance objectives which are agreed with the Board and will require approval by the Special Shareholder.		
Long-Term Incentive Plan (LTIP)	<p>The LTIP is designed to reward and retain key executives and senior managers and to incentivise the achievement of longer term performance goals.</p> <p>The payout of the award is based on the achievement of strategic targets linked to the longer term development growth of a sustainable business.</p>	<p>Performance measures for the LTIP are drawn from the Post Office Funding Agreement agreed with the Special Shareholder.</p> <p>The intention is to award an LTIP subject to Special Shareholder agreement. The proposed awards follow a three-year cycle. Awards for 2013 will be based on access criteria and EBITDAS targets.</p>	Three financial years	<p>70% of salary for the Chief Executive and 35% of salary for the Chief Financial Officer is payable at target performance.</p> <p>Up to 98% of salary for the Chief Executive and up to 49% of salary for the Chief Financial Officer is payable at maximum performance.</p>

Performance scenarios 2013/2014

The charts below show the quantum and composition of the current remuneration policy for the Executive Directors under three performance scenarios. These are scenarios showing potential remuneration assuming there is no STIP or LTIP payout, (i.e. fixed pay only), on-target performance (i.e. STIP and LTIP paying out at a target level) and maximum performance (full payout of STIP and LTIP).



On-target performance assumes an award of 48% of salary under the STIP and 70% of salary under the LTIP for the Chief Executive (40%\* and 35% of salary respectively for the Chief Financial Officer).

Maximum performance assumes an award of 80% of salary under the STIP and 98% of salary under the LTIP for the Chief Executive (67%\* and 49% of salary respectively for the Chief Financial Officer).

\*subject to Special Shareholder approval

Statement of pay considerations elsewhere in the Post Office

The committee takes into account the pay and employment conditions of employees elsewhere in the Post Office when setting the remuneration policy for the Executive Directors. For

example, when determining salary increases for the Executive Directors, consideration is given to the policy and budget applied elsewhere to other employees. The balanced scorecard used for the STIP for Executive Directors is also used to assess performance in the STIP for Post Office managers, providing alignment between performance reward for all employees at manager level and above.

#### Contracts and loss of office payment policy

Each of the Executive Directors has a signed contract with the Post Office.

#### Key terms of the contract

Notice period	12 months to be given by the Post Office and six months by the director.
Remuneration-related provisions	Salary and benefits including health cover, a company car or car allowance, life and health insurance and cash allowance in lieu of pension equivalent to 25% of base salary.

#### Clawback provision

Executive Directors have clawback clauses in their contracts, as well as the STIP and LTIP rules, which provide for the return of any over-payments in the event of mis-statement of the accounts, error or gross misconduct on the part of an executive.

#### Non-Executive Directors

The fees paid to the Chairman are approved by the Special Shareholder. Fees for the Non-Executive Directors are determined by the Executive Directors and are submitted to the Special Shareholder for approval taking into account time commitment and responsibilities.

The fees paid to the Chairman and Non-Executive Directors are not pensionable and they receive no other benefits.

Non-Executive Directors' Letters of Appointment are described in the Corporate Governance statement (pxx).

#### Statement of consideration of shareholder's views

The Chairman of the Committee communicates regularly with the Shareholder Executive on behalf of the Special Shareholder on all matters concerning executive remuneration and the Special Shareholder approves all aspects of Executive Director Remuneration.

## Implementation report

## Remuneration for each director (audited)

Name	Annual fees	Actual salary/ fees 2012-2013	Benefits	Cash in lieu of pension	STIP	LTIP	Total
Non-Executive Directors							
Tim Franklin	£35,000	£18,603	-	-	-	-	£18,603
Virginia Holmes	£35,000	£34,712	-	-	-	-	£34,712
Alasdair Marnoch	£45,000	£38,589	-	-	-	-	£38,589
Neil McCausland	£50,000	£50,000	-	-	-	-	£50,000
Alice Perkins	£100,000	£100,000	-	-	-	-	£100,000
Susannah Storey (Note 1)		£0	-	-	-	-	£0
Executive Directors (Note 2)							
Paula Vennells	£250,000	£250,000	£9,779	£62,500	£157,936	£217,508	£697,723
Chris Day	£215,000	£215,000	£9,779	£53,750	£129,053	-	£407,582
		£706,904	£19,558	£116,250	£286,989	£217,508	£1,347,208

Note 1: Susannah Storey is an employee of the Shareholder Executive of the Department for Business, Innovation and Skills and therefore receives no director's fee.

Note 2: The salaries for Paula Vennells and Chris Day remain unchanged. There is no planned increase for the review in July 2013.

[Benefits comprise a company car (or cash equivalent), participation in life and health assurance schemes and private medical provision.]

## Pay at risk paid to Executive Directors in 2012-13 (audited)

## a) Short Term Incentive Plan 2012-13

The Short Term Incentive Plan is based on the Post Office balance scorecard for 2012-13. Six measures from the scorecard were identified for use in the STIP. These relate to financial performance (50%), the customer experience (25%) and achievement of specific objectives related

to the modernisation program (25%). Financial performance was assessed through the use of stretching revenue and operating profit targets. Strong growth in the business during the year delivered revenue of [(£1.02bn)] which was between target and stretch performance. Tight cost control meant that operating profit [(£94.2m)] was in excess of the stretch hurdle. Significant improvements were made in our interaction with customers, with reductions in queue times and call centre targets being achieved. Overall, performance exceeded the on-target level across all the six measures and was in excess of the stretch hurdle for two measures.

#### Chief Executive

The STIP payable to the Chief Executive is based on the balanced scorecard (80%) and personal performance (20%). The balanced scorecard element paid out at 144.2% leading to a bonus of 55.5% of salary. For the personal element, following a review of the achievements of the personal objectives by the Chairman, the Remuneration Committee judged that the Chief Executive had achieved 80% of her individual objectives, leading to a bonus of 7.7% of salary.

Taking account of both the financial and personal elements the total STIP for 2012-13 of 63% of salary was awarded.

#### Chief Financial Officer

The STIP payable to the Chief Financial for 2012-13 was based on the balanced scorecard with a multiplier applied based on personal performance with the plan year. His bonus based on the balanced scorecard was 40% of salary. The multiplier applied resulted in an increase by a factor of 1.5.

Taking account of both financial and personal elements, the total STIP awarded to the Chief Financial Officer for 2012-13 was 60% of salary.

As shown in the policy section the STIP structure for 2013/14 the intention is to harmonise the STIP design for the Chief Financial Officer with that of the Chief Executive and lose the multiplier. These changes will be subject to Special Shareholder approval.

#### b) Long Term Incentive Plan awards 2010-2013

The LTIP award to pay out this year is based on the three-year performance period ended 31 March 2013. The award value for the Chief Executive was 70% of salary with a maximum stretch value of 1.4 times the target award (98% of salary). There was no award made to the Chief Financial Officer as he had not commenced employment with the Post Office on the award date. The primary performance condition for the 2010 award was operating profit (sliding scale of targets).

Operating profit for the year-ended 31 March 2013 (£94.2 million) was between the target and stretch level. The resulting payout under the 2010 LTIP was 124.3% of the maximum (87% of salary for the Chief Executive). Other Post Office employees also participated in this scheme, receiving awards of between 25% and 43% of salary.

#### Outstanding Long-Term Incentive awards

Under the remuneration policy, LTIP awards are granted annually. The Chief Executive Officer and Chief Financial Officer have the following outstanding awards:

	Target award	Stretch award	Performance period
Paula Vennells – Chief Executive Officer			
2011 LTIP	£175,000	£245,000	Three years to 31 March 2014
2012 LTIP	£175,000	£245,000	Three years to 31 March 2015
Chris Day – Chief Financial Officer			
2011 LTIP	£50,167*	£70,234	Three years to 31 March 2014
2012 LTIP	£73,500	£102,900	Three years to 31 March 2015

\*LTIP award pro-rated as commenced employment 1 August 2011

Both the 2011 and 2012 LTIP awards are subject to challenging financial and strategic performance conditions.

Total pension entitlements (audited)

Paula Vennells and Chris Day each receive a cash supplement of 25% base pay in lieu of pension scheme membership.

Paula Vennells accrued benefits under the Royal Mail Senior Executives Pension Plan (an HMRC approved defined benefit occupational pension scheme) until 5 April 2012 when she left the scheme.

Age at Year end	Accrued benefit at 25 March 2012 or date of appointment to the Board if later	Accrued benefit at 31 March 2013 or date of leaving if earlier	Increase in accrued benefits during the period (net of inflation)	Transfer value of increase before inflation less Directors' contributions
	£ pa	£ pa	£ pa	£ pa
54				
Paula Vennells	14,721	15,225	180	3,340

Age at Year end	Transfer value at 25 March 2012 or at date of appointment to Board if later	Transfer value at 31 March 2013	Transfers in received during the period	Member's contributions in the period	Movements in the period less Directors' contributions
	£		£	£	£
54					

£

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Paula Vennells	283,759	314,926	204	30,963
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Relative importance of the spend on pay (audited)

Total people costs at Post Office Limited (excluding exceptionals) for the year ended 31 March 2013 were £259 million, of which £1.4 million related to Directors' pay. This compares to total revenues of £1.02 billion.

Outside directorships

Subject to Board approval, the Executive Directors are permitted to take on Non-Executive positions with other companies and are allowed to retain the fees received in respect of such positions. Paula Vennells is a Director of Hymns Ancient and Modern and a fee of £xx in respect of the year ended 31 March 2013.

**Post Office Limited**

Registered Number 2154540

**Post Office Limited**  
**Financial Statements**  
**2012-2013**  
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Note: Disclosures highlighted are to be confirmed.

## Post Office Limited

### Statement of directors' responsibilities

The Directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the financial position of the Group and of the Company and the financial performance and cash flows of the Group and of the Company for that period. Under that law the Directors have elected to prepare the Group consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and have elected to prepare the Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law.) In preparing those financial statements, the Directors are required to:

- Select suitable accounting policies and apply them consistently;
- Present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's financial position and financial performance;
- State that applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records, which disclose, with reasonable accuracy at any time, the financial position of the Group and of the Company to enable them to ensure that the Group consolidated financial statements comply with the Companies Act 2006 and Article 4 of the IAS Regulation and the Company financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Group and Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors confirm that to the best of their knowledge:

- The Group consolidated financial statements, prepared in accordance with IFRS as adopted by the EU and in accordance with the provisions of the Companies Act 2006 give a true and fair view of the assets, liabilities, financial position and profit of the Group;
- The Company financial statements prepared in accordance with United Kingdom Generally Accepted Accounting Practice, give a true and fair view of the assets, liabilities, financial position and profit of the Company; and
- The management report contained in this report includes a fair view of the development and performance of the business and the position of the Group as a whole and of the Company, together with a description of the principal risks and uncertainties they face.

## Post Office Limited

### Independent auditor's report to the members of Post Office Limited

We have audited the consolidated financial statements of Post Office Limited for the 53-week period ended 31 March 2013 which comprise the Consolidated income statement, the Consolidated statement of comprehensive income, the Consolidated statement of cash flows, the Consolidated balance sheet, the Consolidated statement of changes in equity and the related notes 1 to 25. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report 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 members as a body, for our audit work, for this report, or for the opinions we have formed.

#### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page X, the directors are responsible for the preparation of the group financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the group financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

#### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### Opinion on financial statements

In our opinion the group financial statements:

- give a true and fair view of the state of the group's affairs as at 31 March 2013 and of its profit for the 53-week period then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

#### Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the group financial statements are prepared is consistent with the group financial statements.

#### Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

#### Other matter

We have reported separately on the parent company financial statements of Post Office Limited for the 53 week period ended 31 March 2013.

#### Ernst & Young LLP

Angus Grant (Senior statutory auditor)  
for and on behalf of Ernst & Young LLP, Statutory Auditor  
London

[Date]

Notes:

1. The maintenance and integrity of the Post Office Limited's web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.
2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## Post Office Limited

## Consolidated income statement

for the 53 weeks ended 31 March 2013 and the 52 weeks ended 25 March 2012

	Notes	2013 £m	2012 £m
<b>Continuing operations</b>			
Turnover		1,024	980
Network Subsidy Payment		210	180
<b>Revenue</b>		<b>1,234</b>	<b>1,160</b>
People costs excluding restructuring costs	3	(259)	(254)
Subpostmasters costs		(478)	(483)
Other operating costs		(435)	(393)
Share of post tax profit from joint ventures and associates	11	32	31
<b>Operating profit before exceptional items</b>	4	<b>94</b>	61
Operating exceptional items	5	(47)	(38)
- government grant		98	-
- restructuring costs		(79)	(2)
- other		(66)	(36)
<b>Operating profit</b>		<b>47</b>	23
Profit on disposal of property, plant and equipment		2	1
Loss on sale of associate		(30)	-
<b>Profit before financing and taxation</b>		<b>19</b>	24
Finance costs	7	(4)	(7)
Finance income	7	1	1
Net pensions interest	19	2	2
<b>Profit before taxation</b>		<b>18</b>	20
Taxation credit	8	31	10
<b>Profit for the financial year from continuing operations</b>		<b>49</b>	30

Note that the Royal Mail Holdings plc financial statements for the year ended 25 March 2012 reported operating profit after modernisation costs but before other exceptional items of £59m for Post Office Limited. In the income statement above the prior year result has been presented to exclude modernisation costs consistent with 2013 where results are reported before all exceptional items.

## Post Office Limited

**Consolidated statement of comprehensive income**  
for the 53 weeks ended 31 March 2013 and the 52 weeks ended 25 March 2012

	Notes	2013 £m	2012 £m
<b>Profit for the financial year from continuing operations</b>		<b>49</b>	30
<b>Other comprehensive income:</b>			
Actuarial gains on defined benefit pension schemes	19	<b>14</b>	108
Taxation on items taken directly to equity	8	<b>(21)</b>	-
<b>Total comprehensive income for the year</b>		<b>42</b>	138

## Post Office Limited

Consolidated statement of cash flows  
for the 53 weeks ended 31 March 2013 and the 52 weeks ended 25 March 2012

	Notes	2013 £m	2012 £m
<b>Cash flows from operating activities</b>			
Operating profit before exceptional items		94	61
Adjustment for:			
Depreciation and amortisation	4	-	1
Share of profit from joint ventures and associates	11	(32)	(31)
Pension operating costs		25	24
Working capital movements:		71	24
(Increase)/Decrease in trade and other receivables		(138)	11
Increase in trade and other payables		207	15
(Increase) in inventories		(2)	-
Increase/(Decrease) in non-exceptional provisions		4	(2)
Pension operating costs paid		(26)	(27)
Cash payments in respect of operating exceptional items:		133	(27)
Business transformation		(41)	(12)
Government grant		200	-
Restructuring costs		(11)	(15)
Other		(15)	-
Net cash inflow from operating activities		265	25
Income tax recovered		11	12
<b>Cash flows from investing activities</b>			
Investment in associate		(11)	-
Dividends received from joint ventures and associates	11	40	38
Finance income received		1	-
Proceeds from sale of property, plant and equipment		2	2
Proceeds from disposal of associate		2	-
Purchase of property, plant and equipment		(66)	(33)
<b>Net cash (outflow)/inflow from investing activities</b>		<b>(32)</b>	<b>7</b>
<b>Net cash inflow before financing activities</b>		<b>244</b>	<b>44</b>
<b>Cash flows from financing activities</b>			
Finance costs paid		(3)	(4)
Payments to finance lease creditors		(3)	(3)
(Repayment)/proceeds from bank borrowings		(86)	2
<b>Net cash (outflow) from financing activities</b>		<b>(92)</b>	<b>(5)</b>
<b>Net increase in cash and cash equivalents</b>		<b>152</b>	<b>39</b>
Effect of exchange rates on cash and cash equivalents		(1)	(1)
Cash and cash equivalents at the beginning of the year	13	820	782
<b>Cash and cash equivalents at the end of the year</b>	13	<b>971</b>	<b>820</b>

## Post Office Limited

Consolidated balance sheet  
at 31 March 2013, 25 March 2012 and 28 March 2011

	Notes	2013 £m	2012 £m	2011 £m
<b>Non-current assets</b>				
Intangible assets	9	-	-	-
Property, plant and equipment	10	11	11	12
Investments in joint ventures and associates	11	60	89	96
Retirement benefit surplus	19	97	-	-
<b>Total non-current assets</b>		<b>168</b>	100	108
<b>Current assets</b>				
Inventories		8	6	5
Trade and other receivables	12	362	226	241
Cash and cash equivalents	13	971	820	782
Financial assets – derivatives	17/18	1	-	-
<b>Total current assets</b>		<b>1,342</b>	1,052	1,028
<b>Total assets</b>		<b>1,510</b>	1,152	1,136
<b>Current liabilities</b>				
Trade and other payables	14	(898)	(583)	(579)
Financial liabilities – interest bearing loans and borrowings	15	(291)	(377)	(375)
– obligations under finance leases	22	(3)	(4)	(4)
Provisions	16	(19)	-	-
<b>Total current liabilities</b>		<b>(1,211)</b>	(964)	(958)
<b>Non-current liabilities</b>				
Financial liabilities – obligations under finance leases	22	(4)	(6)	(9)
Other payables	14	-	(2)	(5)
Provisions	16	(7)	(14)	(26)
Retirement benefit obligation	19	-	(206)	(316)
<b>Total non-current liabilities</b>		<b>(11)</b>	(228)	(356)
<b>Net assets/(liabilities)</b>		<b>288</b>	(40)	(178)
<b>Equity</b>				
Share capital	20	-	-	-
Share premium		465	465	465
Retained earnings		(179)	(552)	(690)
Other Reserves		2	47	47
<b>Total equity/(deficit)</b>		<b>288</b>	(40)	(178)

The financial statements on pages XX to XX were approved by the Board of Directors on XXX 2013 and signed on its behalf by:

**P A Vennells**  
Chief Executive

**C M Day**  
Chief Financial Officer

## Post Office Limited

### Consolidated statement of changes in equity for the 53 weeks ended 31 March 2013 and the 52 weeks ended 25 March 2012

	Notes	Share premium £m	Retained earnings £m	Other reserves £m	Total equity £m
<b>At 26 March 2012</b>		465	(552)	47	(40)
Profit for the year		-	49	-	49
Actuarial gain on defined benefit schemes	19	-	14	-	14
Transfer of pension deficit to government	19	-	286	-	286
Sale of interest in associate		-	45	(45)	-
Taxation of items taken directly to equity	8	-	(21)	-	(21)
<b>At 31 March 2013</b>		<b>465</b>	<b>(179)</b>	<b>2</b>	<b>288</b>

Opening other reserves of £47m comprised £2m relating to First Rate Exchange Services Holding Limited, the joint venture entity, and £45m that was recognised on the formation of Midasgrange Limited, the associate entity. In September 2012 the Group disposed of its interest in the associate and therefore £45m included in other reserves relating to Midasgrange Limited was transferred to retained earnings.

	Notes	Share premium £m	Retained earnings £m	Other reserves £m	Total equity £m
<b>At 28 March 2011</b>		465	(690)	47	(178)
Profit for the year		-	30	-	30
Actuarial gain on defined benefit pension schemes	19	-	108	-	108
<b>At 25 March 2012</b>		465	(552)	47	(40)

## Post Office Limited

### Notes to the financial statements

#### 1. Accounting Policies

##### Financial year

The financial year ends on the last Sunday in March and for this reason these financial statements are made up to the 53 weeks ended 31 March 2013 (2012 – 52 weeks ended 25 March 2012).

##### Basis of preparation

The financial statements on pages ~~xx~~ to ~~xx~~ have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. Unless otherwise stated in the accounting policies below, the financial statements have been prepared under the historic cost accounting convention.

For all periods up to and including the year ended 25 March 2012, the Group (comprising the Company and its subsidiary undertaking) prepared its financial statements in accordance with United Kingdom Generally Accepted Accounting Practice. These financial statements for the year ended 31 March 2013 are the first the Group has prepared in accordance with IFRS as adopted by the European Union.

Accordingly the Group has prepared financial statements which comply with IFRS as adopted by the European Union applicable for periods ending on or after 31 March 2013, together with comparative period data as at and for the year ended 25 March 2012. In preparing these financial statements, the Group's opening statement of financial position was prepared as at 28 March 2011, the Group's date of transition to IFRS as adopted by the European Union.

The Company is incorporated and domiciled in the United Kingdom. The Group consolidated financial statements are presented in Sterling and all values are rounded to the nearest £m except where otherwise indicated.

##### Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiary undertaking. Subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date when such control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. All intra-group balances, transactions, unrealised gains and losses resulting from intra-group transactions are eliminated in full.

##### Changes in accounting policy and disclosures

The changes to accounting policies and disclosures which have been necessary as part of the transition to reporting under IFRS as adopted by the European Union have had no effect on the income statement or net asset position.

##### Accounting standards issued but not yet applied

The following new and revised accounting standards are relevant to the Group and are in issue but were not effective (and in some instances have not yet been adopted by the EU) at the balance sheet date:

- Annual improvements to IFRS 2009-2011 Cycle
- IFRS 9 Financial Instruments: Classification and Measurement
- IFRS 10 Consolidated Financial Statements
- IFRS 11 Joint Arrangements
- IFRS 12 Disclosures of Interests in Other Entities
- IFRS 13 Fair Value Measurement [impact on derivative assets]
- IAS 1 (amended) Presentation of Items of Other Comprehensive Income
- IAS 12 –(amended) Deferred Taxation: Recovery of Underlying Assets [impact being assessed by Group Tax]
- IAS 19 (revised) Employee Benefits
- IAS 27 (revised) Separate Financial Statements
- IAS 28 (revised) Investments in Associates and Joint Ventures
- IAS 32 (amended) Offsetting Financial Assets and Liabilities [impact being assessed by Group Treasury]

The Directors do not expect that the adoption of the standards listed above will have a material impact on the financial statements of the Group in future periods.

## Post Office Limited

### Fundamental accounting concept – going concern

The Group has net assets at 31 March 2013 and has operated at a profit before exceptional items during 2012-13 for the fifth year running.

A funding agreement with Government was announced on 27 October 2010 which provided for:

- Funding of £410m for 2012-13
- Funding of £415m for 2013-14
- Funding of £330m for 2014-15
- Extension of the existing working capital facility with the Department for Business, Innovation & Skills (BIS) of £1.15bn up to 31 March 2016

State Aid approval for the funding for 2012-13 to 2014-15 was received on 28 March 2012 and it was also recognised that the working capital facility was no longer deemed State Aid. £410m was received on 2 April 2012.

This investment will take the form of a Government Grant and enable the Group to modernise the branch network and the continuation of the Network Subsidy Payment recognises the major social value that Post Offices provide to communities. New main and local branches are currently being rolled out across the United Kingdom. Customers are beginning to benefit from a much better retail experience including extended opening hours. This programme is designed to make the Post Office network more self-sustaining and, over time, less dependant on direct subsidy. This programme will not involve branch closures.

The Directors are satisfied with the progress made towards modernisation during 2012-13 and that the plans in place and the substantial investment secured will enable the Group to continue to modernise and to secure its future. However, they note that the scale of change required remains significant so not without risk.

After careful consideration of the plans for the coming years, the Directors continue to believe that Post Office Limited will be able to meet its liabilities as they fall due in the foreseeable future. Accordingly, on that basis, the Directors consider that it is appropriate that these financial statements have been prepared on a going concern basis.

### Critical accounting estimates and judgements in applying accounting policies

The Group makes certain estimates and assumptions regarding the future. Estimates and assumptions are continually evaluated based on historical experience and other factors. In the future, actual experience may differ from these estimates and assumptions. In addition the Group has to make judgements in applying its accounting policies which affect the amounts recognised in the accounts. The most significant areas where judgements and estimates are made are discussed below:

#### Pension assumptions

The costs, assets and liabilities of the pensions operated by the Group are determined using methods relying on actuarial estimates and assumptions. These pension figures are particularly sensitive to changes in assumptions for discount rates, mortality and inflation rates. Details of the key assumptions are set out in Note 19.

Pension liabilities are measured on an actuarial basis using the projected unit credit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term. Judgement has been applied in determining that for these purposes a high quality corporate bond constitutes AA rated or equivalent status bonds.

#### Provisions

The Group has recognised provisions where a present legal or constructive obligation exists as a result of a past event, where it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate of the amount can be made. Provisions are detailed in Note 16. Due to the nature of provisions the future amount settled may be different from the amount that has been provided.

#### Revenue

Turnover from Government, financial, mails and telephony services comprises the value of services provided. Turnover from all other products comprises the commission received excluding VAT, from the Group's principal activities in providing access to a wide range of financial and retail services through its network of post office branches across the UK and other channels. Turnover relating to line rental for telephony services is recognised evenly over the period to which the charges relate and revenue from calls is recognised at the time the call is made. Turnover from all other transactions is recognised when the transaction is completed. All turnover is derived wholly from within the United Kingdom.

The Network Subsidy Payment is Government grant revenue recognised to match the related costs of making available the network of public Post Offices that the Secretary of State for Business, Innovation and Skills considers appropriate.

#### Net revenue

Net revenue is calculated using revenue less cost of sales, which consists of directly attributable costs of delivering the service or product.

## Post Office Limited

### Operating exceptional items

Operating exceptional items are items of income and expenditure arising from the operations of the business which, due to the nature of the events giving rise to them, require separate presentation on the face of the income statement to allow a better understanding of financial performance in the year, in comparison to prior years.

### Intangible assets

Intangible assets acquired separately or generated internally are initially recognised at cost and are reviewed for impairment. An impairment loss is recognised in the income statement for the amount by which the carrying value of the asset exceeds its recoverable amount, which is the higher of an asset's net realisable value and its value in use.

Amortisation of intangible assets with finite lives is charged annually to the income statement on a straight-line basis as follows.

Software	1 to 6 years
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### Property, plant and equipment

Property, plant and equipment is recognised at cost, including attributable costs in bringing the asset into working condition for its intended use.

Depreciation of tangible fixed assets is provided on a straight-line basis by reference to cost and to the remaining useful economic lives of assets and their estimated residual values. The lives assigned to major categories of tangible fixed assets are:

	Range of asset lives
Land and buildings:	
Freehold land	Not depreciated
Freehold buildings	Up to 50 years
Leasehold buildings	The shorter of the period of the lease, 50 years or the estimated remaining useful life
Plant and Machinery	3 – 15 years
Motor vehicles and trailers	2 – 12 years
Fixtures and equipment	2 – 15 years

### Impairment reviews

Unless otherwise disclosed in these accounting policies, assets are reviewed for impairment if events or changes in circumstances indicate that the carrying value may be impaired. The Group assesses at each reporting date whether such indications exist. Where appropriate, an impairment loss is recognised in the income statement for the amount by which the carrying value of the asset (or cash generating unit) exceeds its recoverable amount, which is the higher of an asset's net realisable value and its value in use.

### Leases

Finance leases, where substantially all the risks and rewards incidental to ownership of the leased item have passed to the Group are capitalised at the inception of the lease with a corresponding liability recognised for the fair value of the leased item or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability.

Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term.

Leases where substantially all the risks and rewards of ownership of the asset are retained by the lessor, are classified as operating leases and rentals are charged to the income statement over the lease term. The aggregate benefit of incentives are recognised as a reduction of rental expenses over the lease term on a straight-line basis.

### Investments in joint ventures and associates

Investments in joint ventures and associates within the Group's financial statements are accounted for under the equity method of accounting. Under this method the investment is carried in the balance sheet at cost plus post-acquisition changes in the Group's share of the net assets of the joint venture/associates less any impairment in value. The income statement reflects the Group's share of post tax profits from the joint venture/associates.

### Inventories

Inventories include printing and stationery, retail and lottery products, is carried at the lower of cost and net realisable value after adjusting for obsolete or slow-moving stock.

## Post Office Limited

### Taxation

The charge for current income tax is based on the results for the year as adjusted for items which are not taxed or are disallowed. It is calculated using tax rates in legislation that has been enacted or substantively enacted by the balance sheet date.

Deferred income tax assets and liabilities are recognised for all taxable and deductible temporary differences and unused tax assets and losses except:

- initial recognition of goodwill
- the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit and loss.
- taxable temporary differences associated with investments in subsidiaries, associates and interest in joint ventures, where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future and
- deferred tax assets are recognised only to the extent that it is probable that taxable profit will be available against which they can be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the tax asset is realised or the liability is settled, based on tax rates that have been substantively enacted at the balance sheet date. Deferred tax balances are not discounted.

Current and deferred tax is recognised in the income statements, except to the extent that it relates to items recognised in other comprehensive income or directly to equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively. Further details on deferred tax can be found in note 8 to the financial statements.

### Pensions and other post-retirement benefits

People working for the Company were employed by Royal Mail Group Limited and seconded to the Company until 31 March 2012. On 1 April 2012 they were transferred to be directly employed by the Company. Membership of occupational pension schemes is open to most permanent UK employees of the Company. All members of defined benefit schemes are contracted out of the earnings-related part of the State pension scheme.

The pension assets of the defined benefit schemes are measured at fair value. Liabilities are measured on an actuarial basis using the projected unit credit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term. The resulting defined benefit asset or liability is presented separately on the face of the balance sheet. Full actuarial funding valuations are carried out at intervals not normally exceeding three years as determined by the Trustees and, actuarial valuations are carried out at each balance sheet date and form the basis of the surplus or deficit disclosed.

For defined benefit schemes, the amounts charged to operating profit, as part of staff costs, are the current service costs and any gains and losses arising from settlements, curtailments and past service costs. The net difference between the interest costs and the expected return on plan assets is recognised as net pensions interest in the income statement. Actuarial gains and losses are recognised immediately in the statement of comprehensive income. Any deferred tax movement associated with the actuarial gains and losses is also recognised in the statement of comprehensive income.

For defined contribution schemes, the Group's contributions are charged to operating profit, as part of staff costs, in the period to which the contributions relate.

### Foreign currencies

The functional and presentational currency of the Group is sterling (£).

Transactions in foreign currencies are recorded at the spot exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional rate of exchange ruling at the balance sheet date. Currently hedge accounting is not applied to any monetary assets and liabilities. All differences are therefore taken to the income statement.

### Trade receivables

Trade receivables are recognised and carried at original invoice amount less an allowance for any non-collectable amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

### Borrowing costs

Borrowing costs in relation to the working capital loan facility are recognised as an expense when incurred unless they are directly attributable to the construction or development of a qualifying asset, in which case they are capitalised using the weighted average cost of borrowing for the period of construction/development.

### Government grants

Government grants are shown separately in the income statement to match the expenditure to which they relate.

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### Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probably that an outflow of resources will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at an appropriate pre-tax rate.

### Financial instruments

The classification of financial instruments included on the balance sheet is set out below:

#### Financial assets

Financial assets are classified into the following categories: at fair value through the income statement, loans and receivables, and available for sale as appropriate based on the purpose for which they were required. Financial liabilities are classified as either fair value through the income statement or as financial liabilities measured at amortised cost.

#### Financial liabilities – interest-bearing loans and borrowings

All loans and borrowings are classified as financial liabilities measured at amortised cost.

#### Financial liabilities – obligations under finance leases

All obligations under finance lease and hire purchase contracts are classified as financial liabilities measured at amortised cost.

#### Derivative financial instruments

The Group uses derivative financial instruments to manage its exposure to fluctuations in foreign exchange rates. Such derivative financial instruments are initially stated at fair value. Hedge accounting has not been claimed for foreign exchange derivative instruments.

#### Fair value measurement of financial instruments

The fair value of quoted investments is determined by reference to bid prices at the close of business on the balance sheet date.

Where there is no active market, fair value is determined using valuation techniques. These include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; and discounted cash flow analysis and pricing models. Specifically, in the absence of quoted market prices, derivatives are valued by using quoted forward prices for the underlying currency and discounted using quoted interest rates. Hence derivative assets and liabilities are within Level 2 of the fair value hierarchy as defined within IFRS 7.

For the purposes of disclosing the fair value of investments held at amortised cost in the balance sheet, in the absence of quoted market prices, fair values are calculated by discounting the future cash flows of the financial instrument using quoted equivalent interest rates as at close of business on the balance sheet date.

#### Derecognition of financial instruments

A financial asset or liability is derecognised when the contract that gives rise to it is settled, sold, cancelled or expires.

### Cash and cash equivalents

Cash and cash equivalents in the balance sheet comprise cash at bank and in hand and short-term deposits (cash equivalents) with an original maturity date of three months or less. In addition the Group uses Money Market funds as a readily available source of cash, and these funds are also categorised as cash equivalents.

For the purpose of the statement of cash flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of bank overdrafts. Cash equivalents are classified as loans and receivables financial instruments.

## Post Office Limited

### 2. Segmental reporting

In accordance with IFRS 8 'Operating segments,' an operating segment is defined as a business activity whose operating results are reviewed by the chief operating decision maker ('CODM') and for which discrete information is available. The Group's CODM is the Executive Committee as defined in the [Directors' Report](#) on Page XX.

The CODM has determined the operating segments based in the information reviewed by them for the purposes of allocating resources and assessing performance. Operating segments have not been aggregated in order to present reportable segments. All segmental activities are located wholly within the United Kingdom.

The CODM assesses the performance of the operating segments based on net revenue. This is calculated using segmental revenue less segmental cost of sales, which consists of directly attributable costs of delivering the service or product. The net revenue measure excludes the effect of indirect costs and the effects of non-recurring expenditure such as redundancy costs and asset impairment. Interest income and expenditure is not allocated to segments as this type of activity is driven by the central treasury function.

Assets and liabilities as recognised on the Group balance sheet are not considered to be segmental assets or liabilities but rather are managed by the Group's central functions. The information reviewed by the CODM does not include assets or liabilities split by segment. A description of the activities of the business segments is included on Page XX within the financial commentary to the financial statements.

Revenue from a major customer represents approximately 27% of the Group's total revenue in 2013. This revenue was reported within the Mails & Retail segment.

2013			
	Revenue £m	Cost of Sales £m	Net Revenue £m
Mails & Retail	409	(5)	404
Financial Services	281	(1)	280
Government Services	164	(30)	134
Telephony	129	(85)	44
Other	41	-	41
Sub total	1,024	(121)	903
Network Subsidy Payment	210	-	210
<b>Total</b>	<b>1,234</b>	<b>(121)</b>	<b>1,113</b>

2012			
	Revenue £m	Cost of Sales £m	Net Revenue £m
Mails & Retail	392	(4)	388
Financial Services	264	(3)	261
Government Services	164	(28)	136
Telephony	120	(79)	41
Other	40	-	40
Sub- total	980	(114)	866
Network Subsidy Payment	180	-	180
<b>Total</b>	<b>1,160</b>	<b>(114)</b>	<b>1,046</b>

A reconciliation between underlying segment net revenue and profit before taxation is provided below:

## Post Office Limited

	2013 £m	2012 £m
Underlying segment net revenue	1,113	1,046
Indirect costs	(1,051)	(1,016)
Share of post tax profit from joint ventures and associates	32	31
<b>Operating profit before exceptional items</b>	<b>94</b>	<b>61</b>
Operating exceptional items	(58)	(38)
<b>Operating profit</b>	<b>36</b>	<b>23</b>
Profit on disposal of property, plant and equipment	2	1
Loss on sale of associate	(30)	-
<b>Profit before financing and taxation</b>	<b>8</b>	<b>24</b>
Finance costs	(4)	(7)
Finance income	1	1
Net pensions interest	2	2
<b>Profit before taxation</b>	<b>7</b>	<b>20</b>

**3. Staff costs and numbers**

Employment and related costs were as follows:

	2013 £m	2012 £m
<b>People costs excluding restructuring costs:</b>		
Wages and salaries	215	213
Social security costs	19	17
Pension costs (note 19)	25	24
Total	259	254

	Period end employees		Average employees	
	2013	2012	2013	2012
Total employees	7,886	7,798	7,842	7,734

## Post Office Limited

### 4. Operating profit from continuing operations before exceptional items

Operating profit from continuing operations before exceptional items is stated after charging:

	2013 £m	2012 £m
Bureau de Change foreign currency exchange losses	1	1
Depreciation	-	1
Operating lease charges – Land and buildings	20	25
– Vehicles and equipment	62	62
Fees payable to the group's auditors for audit and other services:	£000	£000
– parent company and group audit	331	195
–taxation services	-	-
–other non-audit services	105	108

### 5. Operating exceptional items

	2013 £m	2012 £m
Government grant	98	-
Business transformation	(4)	(3)
Network transformation including subpostmasters compensation	(52)	-
Restructuring – severance	(11)	1
– other	(12)	-
Impairment of intangible assets (note 9)	(25)	(17)
Impairment of property, plant and equipment (note 10)	(41)	(19)
<b>Total operating exceptional items</b>	<b>(47)</b>	<b>(38)</b>

The £4m charge in respect of business transformation represents a provision for staff payments linked to changed working practices (2012 £3m).

Due to ongoing operational losses (excluding Network Subsidy Payment) the carrying value of all property plant and equipment other than freehold and long leasehold property has been impaired to the recoverable amount.

### 6. Directors' emoluments

The Directors received the following emoluments:

	2013 £000	2012 £000
Emoluments, excluding pension contributions and LTIP*	1,129	904
Contributions to pension schemes	1	58
Amounts receivable under Long-Term Incentive Plans	218	-

\*Figures include any cash supplements received in lieu of pension.

Directors accruing pension entitlements during the period under:	2013 Number	2012 Number
Defined benefit schemes	0	2
Defined contribution schemes	-	-

## Post Office Limited

The highest paid Director received the following emoluments:

	2013 £000	2012 £000
Emoluments and LTIP, excluding pension contributions*	698	463
Company contributions to pension schemes	1	47
Transfer value of accrued pension benefits	315	284

\* Figures include any cash supplements received in lieu of pensions.

### 7. Net finance costs

	2013 £m	2012 £m
Interest receivable	1	1
Interest charge, unwinding discount on provisions.	(1)	(1)
Interest payable on loans	(3)	(6)
Total	(3)	(6)

### 8. Taxation

#### (a) Taxation gains recognised in the year

	2013 £m	2012 £m
Corporation tax credit for year	(10)	(11)
Tax under provided in previous years	-	1
Current tax	(10)	(10)
Deferred tax relating to pension surplus taken to equity	(21)	-
<b>Income tax credit reported in the consolidated income statement</b>	<b>(31)</b>	<b>(10)</b>

#### (b) Factors affecting current tax credit on loss on ordinary activities

The tax assessed for the year differs from the standard rate of corporation tax in the UK of 24% (2012 26%). The differences are explained below:

	2013 £m	2012 £m
Profit on ordinary activities before tax	18	20
Profit on ordinary activities multiplied by the standard rate of corporation tax in the UK of 24% (2012 26%)	4	5
Net decrease in tax charge resulting from recognition of deferred tax assets	(35)	(15)
Expenditure disallowable for tax	1	2
Adjustment in respect of prior period	-	1
Losses from disposals ineligible for relief	7	-
Effect of group relief surrenders to other companies	-	5
Associates/joint venture profit after tax included in Group pre-tax profit	(8)	(8)
Total current tax (see above)	(31)	(10)

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### (c) Factors that may affect future tax charges

The Group has unrecognised deferred tax assets of £190m (2012 £337m), comprising £0m (2012 £52m) relating to the retirement benefit obligation, £133m (2012 £157m) relating mainly to fixed asset timing differences, and £57m (2012 £128m) relating to tax losses that are available to offset against future taxable profits. The Group has rolled over capital gains of £3m (2012 £3m); no tax liability would be expected to crystallise should the assets into which the gains have been rolled be sold at their residual value, as it is anticipated that a capital loss would arise.

Finance Act 2012 reduced the main rate of corporation tax to 23% with effect from 1 April 2013. The effect of this change on deferred tax balances is included in these financial statements and is detailed above. In the 2012 Autumn Statement, the Chancellor of the Exchequer announced that the main rate of corporation tax will be 21% for the year commencing 1 April 2014 and in the March 2013 Budget he announced that the rate will be further reduced to 20% with effect from 1 April 2015. In accordance with accounting standards the effect of these rate reductions on deferred tax balances has not been reflected in these accounts due to the relevant legislation not having been substantively enacted at the balance sheet date. A reduction to 20% would, based on losses and temporary differences at 31 March 2013, reduce the Group's unrecognised deferred tax assets by £25m.

Under the Postal Services Act 2011, trading losses which arose due to pension contributions and which are unused at 31 March 2013 will be extinguished. The estimated gross value of the losses extinguished is £175m. The unrecognised losses carried forward disclosed above are stated net of this amount.

### (d) Tax effect of exceptional items

There is a tax credit on exceptional items of £nil (2012 £nil). This is calculated on a "with and without" basis assuming that losses are surrendered firstly to joint ventures and secondarily to companies in the Royal Mail Group.

## 9. Intangible assets

Cost	2013 £m	2012 £m	2011 £m
At 26 March 2012, 28 March 2011, 29 March 2010	183	166	155
Additions	25	17	12
Disposals	-	-	(1)
<b>At 31 March 2013, 25 March 2012, 27 March 2011</b>	<b>208</b>	<b>183</b>	<b>166</b>
<b>Amortisation and impairment</b>			
At 26 March 2012, 28 March 2011, 29 March 2010	183	166	155
Impairment (see note 5)	25	17	11
<b>At 31 March 2013, 25 March 2012, 27 March 2011</b>	<b>208</b>	<b>183</b>	<b>166</b>
<b>Net book value</b>			
<b>At 31 March 2013, 25 March 2012, 27 March 2011</b>	<b>-</b>	<b>-</b>	<b>-</b>

The above intangible assets relate to software.

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## 10. Property, plant and equipment

	Land and Buildings				Plant and machinery £m	Fixtures and equipment £m	Total £m
	Freehold £m	Long leasehold £m	Short leasehold £m	Motor vehicles £m			
<b>Cost</b>							
At 28 March 2011	78	17	113	34	1	696	939
Additions	4	-	-	1	-	13	18
Disposals - external	(4)	-	-	(1)	-	-	(5)
Transfers from Royal Mail Group Ltd	1	-	1	-	-	-	2
<b>At 25 March 2012</b>	<b>79</b>	<b>17</b>	<b>114</b>	<b>34</b>	<b>1</b>	<b>709</b>	<b>954</b>
Reclassification	-	1	(1)	-	-	-	-
Additions	9	-	1	9	-	22	41
Disposals - external	(1)	-	-	(1)	-	(12)	(14)
<b>At 31 March 2013</b>	<b>87</b>	<b>18</b>	<b>114</b>	<b>42</b>	<b>1</b>	<b>719</b>	<b>981</b>
<b>Depreciation</b>							
At 28 March 2011	67	16	113	34	1	696	927
Depreciation	1	-	-	-	-	-	1
Impairment (see note 5)	4	-	1	1	-	13	19
Disposals - external	(3)	-	-	(1)	-	-	(4)
<b>At 25 March 2012</b>	<b>69</b>	<b>16</b>	<b>114</b>	<b>34</b>	<b>1</b>	<b>709</b>	<b>943</b>
Depreciation	-	-	-	-	-	-	-
Impairment (see note 5)	9	1	-	9	-	22	41
Disposals - external	(1)	-	-	(1)	-	(12)	(14)
<b>At 31 March 2013</b>	<b>77</b>	<b>17</b>	<b>114</b>	<b>42</b>	<b>1</b>	<b>719</b>	<b>970</b>
<b>Net book value</b>							
<b>At 31 March 2013</b>	<b>10</b>	<b>1</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>11</b>
At 25 March 2012	10	1	-	-	-	-	11
At 28 March 2011	11	1	-	-	-	-	12

Depreciation rates are disclosed within accounting policies (note 1). No depreciation is provided on freehold land, which represents £3m (2012 £3m) of the total cost of properties.

During the year the legal ownership of a number of properties were transferred from Royal Mail Group Limited to Post Office Limited for no consideration.

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### 11. Investments in joint ventures and associates

The following entities have been included in the consolidated financial statements using the equity method:

#### Joint ventures

During 2012-13 and 2011-12, the Group's only joint venture investment was a 50% interest (1,000 £1 ordinary A shares) in First Rate Exchange Services Holdings Limited, whose principal activity is the provision of Bureau de Change. First Rate Exchange Services Holdings Limited is a company registered in the United Kingdom.

#### Associates

During 2011-12, the Group's only associate investment was a 49.99% interest (4,999 £0.01 ordinary A shares) in Midasgrange Limited, whose principal activity is the provision of personal financial products. This investment was disposed of during the year ended 31 March 2013. At the date of disposal the carrying value of the Group's investment was £32m. Proceeds of £2m were received giving a loss on disposal of £30m which has been recognised in the consolidated income statement.

	Joint venture £m	Associate £m	Total £m
Share of net assets			
Total net investment at 26 March 2012	67	22	89
Share of post tax pre dividend profit/(loss)	33	(1)	32
Investment in associate	-	11	11
Disposal	-	(32)	(32)
Dividend	(40)	-	(40)
<b>Total net investment at 31 March 2013</b>	<b>60</b>	<b>-</b>	<b>60</b>

	Joint venture £m	Associate £m	Total £m
Share of net assets			
Total net investment at 28 March 2011	73	23	96
Share of post tax pre dividend profit/ (loss)	32	(1)	31
Dividend	(38)	-	(38)
Total net investment at 25 March 2012	67	22	89

	2013		2012			2011		
	Joint venture £m	Total £m	Joint venture £m	Associate £m	Total £m	Joint venture £m	Associate £m	Total £m
<b>Share of assets and liabilities:</b>								
Current assets	184	<b>184</b>	180	38	218	151	25	176
Non-current assets	3	<b>3</b>	3	18	21	2	17	19
Share of gross assets	187	<b>187</b>	183	56	239	153	42	195
Current liabilities	(127)	<b>(127)</b>	(116)	(34)	(150)	(80)	(19)	(99)
Share of net assets	60	<b>60</b>	67	22	89	73	23	96
<b>Share of revenue and profit:</b>								
Revenue	75	<b>75</b>	75	49	124	74	39	113
Profit after tax	32	<b>32</b>	32	(1)	31	29	(4)	25

## Post Office Limited

**12. Trade and other receivables**

<b>Current:</b>	<b>2013 £m</b>	2012 £m	2011 £m
Trade receivables	<b>32</b>	39	45
Prepayments and accrued income	<b>81</b>	39	27
Client receivables	<b>240</b>	138	158
Other receivables	<b>9</b>	10	11
Total	<b>362</b>	226	241

The Group receives and disburses cash on behalf of Government agencies and other clients to customers through its branch network. Amounts owed from/to Government agencies and other clients are disclosed separately as client receivables (as above) and client payables (see note 14.)

As at 31 March 2013 trade and other receivables of £1m (2012 £1m) were impaired and fully provided for. All movements on the provision during the year have been less than £1m. Trade and other receivables of £8m (2012 £7m) were past due but not impaired. The aging analysis of the past due amounts are as follows:

	<b>2013 £m</b>	2012 £m
Provided for or not yet overdue	<b>24</b>	32
Past due not more than one month	<b>7</b>	3
Past due more than one month and not more than two months	<b>1</b>	3
Past due more than two months	<b>-</b>	1
Total	<b>32</b>	39

The fair value of trade and other receivables is not materially different from the carrying value.

**13. Cash and cash equivalents**

	<b>2013 £m</b>	2012 £m	2011 £m
Cash in the Post Office Limited network	<b>879</b>	758	704
Short-term bank deposits	<b>6</b>	19	34
Money market fund investments	<b>86</b>	43	44
<b>Total cash and cash equivalents</b>	<b>971</b>	820	782

Cash and cash equivalents comprise amounts held physically in cash, cash deposits available on demand or for three months or less. Where interest is earned it is at a floating or short term fixed rate. The fair value of cash and cash equivalents is not materially different from the carrying value.

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**14. Trade and other payables**

	2013 £m	2012 £m	2011 £m
<b>Current:</b>			
Trade payables	43	32	36
Accruals and deferred income	134	140	121
Advance customer payments	50	48	67
Social security	10	9	10
Client payables	528	332	314
Amounts due to pension schemes relating to redundancies	-	-	3
Amount due to other companies within the Royal Mail Holdings Group	6	9	12
Capital payables	18	10	6
Business transformation	7	3	10
Government Grant deferred income	102	-	-
<b>Total</b>	<b>898</b>	583	579
<b>Non-current:</b>			
Other payables	-	2	5
<b>Total</b>	<b>898</b>	585	584

Of the £200m Government Grant received £98m has been allocated against income statement expenditure in accordance with the terms and conditions of the Grant. The remaining £102m has been deferred into the balance sheet as disclosed above. The fair value of trade and other payables is not materially different from the carrying value.

**15. Borrowings**

	2013 £m	2012 £m	2011 £m
BIS loans drawn down	291	377	375

The loans under the facility are short dated on a programme of liquidity management and mature on average 1 day after the year end (2012 1 day). The fair value of borrowings is not materially different from the carrying value. On maturity it is expected that further loans will be drawn down under this facility, which expires in 2016. The undrawn committed facility, in respect of which all conditions precedent had been met at the balance sheet date is £859m (2012 £773m.) The average interest rate on the drawn down loans is 1.0% (2012 0.8%).

The facility is currently restricted to funding the cash and near cash items held within the Post Office Limited network.

The facility (including drawn down loans) is secured by a floating charge over all assets of Post Office Limited and a negative pledge over cash and near cash items. The negative pledge is an agreement not to grant security over the assets or to set up a vehicle that has the same effect.

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## 16. Provisions

	Crown Conversions Project £m	Network Transformation £m	Other £m	Total £m
At 26 March 2012	9	-	5	<b>14</b>
Charged in operating exceptional items	-	10	12	<b>22</b>
Charged in operating costs	-	-	6	<b>6</b>
Charged in financing costs	1	-	-	<b>1</b>
Utilisation	(3)	-	(14)	<b>(17)</b>
At 31 March 2013	7	10	9	<b>26</b>
Disclosed as:				
Current	4	8	7	<b>19</b>
Non - current	3	2	2	<b>7</b>
	7	10	9	<b>26</b>

Other provisions of £9m (2012 £5m) include property contracts, comprising amounts from onerous lease obligations and personal injury claims.

Amounts charged in financing costs relate to the unwinding of discounted long-term provisions.

The Crown Conversions project relates to past franchising of Crown offices and onerous property lease provisions are expected to be utilised within 5 years.

## 17. Financial assets and liabilities

The Group's financial assets and liabilities are shown in the table below:

	2013			2012			2011		
	Current	Non current	Total	Current	Non current	Total	Current	Non current	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Cash and cash equivalents	<b>971</b>	-	<b>971</b>	820	-	820	782	-	782
Derivative assets	<b>1</b>	-	<b>1</b>	-	-	-	-	-	-
BIS loan	<b>(291)</b>	-	<b>(291)</b>	(377)	-	(377)	(375)	-	(375)
Finance leases obligations	<b>(3)</b>	<b>(4)</b>	<b>(7)</b>	(4)	(6)	(10)	(4)	(9)	(13)
<b>Total financial assets/ (liabilities)</b>	<b>678</b>	<b>(4)</b>	<b>674</b>	439	(6)	433	403	(9)	394

The Group's principal financial assets and liabilities comprise cash, money market liquidity investments, loans and finance leases. The Group has various other financial instruments such as trade receivables and trade payables, which arise directly from operations are disclosed further in Notes 12 and 14.

The Group enters into derivative transactions, which create derivative assets and liabilities, principally forward currency contracts. The purpose is to manage the commodity and currency risks arising from the Group's operations.

The main risks arising from the Group's financial assets and liabilities are interest rate risk, liquidity risk, foreign currency risk and credit risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below:

## Post Office Limited

### Interest rate risk

The Group's exposure to market risk for changes in interest rates relates to the Group's debt obligations and interest bearing financial assets. The BIS loans to Post Office Limited of £291m (2012 £377m) are at short-dated fixed interest rates – average maturity 1 day (2012 average 1 day). On maturity it is expected that further loans will be drawn down under this facility which expires in 2 016. The total interest bearing financial assets of the Group of £92m (2012 £62m) are at short-dated fixed or variable interest rates.

The table below sets out the carrying amount by maturity of the Group's financial instruments that are exposed to interest rate risk.

### Financial year ended 31 March 2013

	Average Effective interest rate	Within one year £m	1-2 years £m	2-5 years £m	More than 5 years £m	Total £m
<b>Fixed rate</b>						
Short-term bank deposits	0.5	6	-	-	-	6
BIS loan	1.0	(291)	-	-	-	(291)
Obligations under finance leases	9.0	(3)	(4)	-	-	(7)
Total		(288)	(4)	-	-	(292)
<b>Floating rate</b>						
Money market fund investments	0.5	86	-	-	-	86
<b>Non-interest bearing</b>						
Cash in Post Office network	-	879	-	-	-	879
Derivative assets	-	1	-	-	-	1
Total		880	-	-	-	880
Net total financial assets/(liabilities)		678	(4)	-	-	674

### Financial year ended 25 March 2012

	Average Effective interest rate	Within one year £m	1-2 years £m	2-5 years £m	More than 5 years £m	Total £m
<b>Fixed rate</b>						
Short-term bank deposits	0.7	19	-	-	-	19
BIS loan	0.8	(377)	-	-	-	(377)
Obligations under finance leases	9.0	(4)	(3)	(3)	-	(10)
<b>Floating rate</b>						
Money market fund investments	0.8	43	-	-	-	43
<b>Non-interest bearing</b>						
Cash in Post Office network	-	758	-	-	-	758
Net total financial assets/(liabilities)		439	(3)	(3)	-	433

## Post Office Limited

### Foreign currency risk

The Group is exposed to foreign currency risk resulting from balances held to operate Bureau de Change services. The Group's foreign currency risk management objective is to minimise the impact on the Income Statement of fluctuations in the exchange rates. The Group aims to hedge 90% of significant forecast future currency balances (principally but not restricted to US dollar and Euro) to match the anticipated holding period of the currency. The Group hedges its foreign currency risk principally through external forward foreign currency contracts with First Rate Exchange Services Holdings Limited.

### Credit risk

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. Financial credit risk arises from cash balances (including bank deposits and cash and cash equivalents) held by the Group and business credit risk arises from exposures to customers. Business risk includes commissions receivable and client related settlements for amounts paid out of the Post Office network on their behalf.

The Group aims to minimise its financial credit risk through the application of risk management policies approved by the Board. Counterparties are limited to major banks and financial institutions. The policy restricts the exposure to any one counterparty by setting appropriate credit limits.

Business credit risk is monitored centrally. The individual relationships and the contracts attached to them are managed by dedicated teams and procedures are place to monitor any concentrations of credit risk. The level of bad debt incurred for the Group is less than 1% (2012 less than 1%) of turnover.

### Capital management

The Group's objectives when managing capital (defined as the net of borrowings and amounts due under finance leases and cash and cash equivalents excluding cash in the Post Office Network) are to safeguard its ability to continue as a going concern and to maintain an optimal capital structure in order to support the business and maximise stakeholder value. In managing the Groups capital levels the Board and the Executive Committee regularly monitor the level of debt in the Group, the working capital requirements and the forecast cash flows. The Board and Executive Committee plan accordingly following this review process in order to meet the Groups capital management objectives.

### Liquidity risk

The Group's primary objective is to ensure that the Group has sufficient funds available to meet its financial obligations as they fall due. This is achieved by aligning short-term investments and borrowing facilities with forecast cash flows. Typical short-term investments include money market funds and short term bank deposits with approved counterparties. Borrowing facilities are regularly reviewed to ensure continuity of funding. The unused facility for the Group of £859m (2012 £773m) expires in 2016.

### Sensitivity

As a result of the mix of fixed and variable rate financial instruments and the currency hedge programmes in place, the group has no material exposure to risk from interest rate or exchange rate prices.

## Post Office Limited

The tables below set out the gross (undiscounted) contractual cash flows of the Group's financial liabilities. For loans and finance leases, these cash flows represent the undiscounted total amounts payable including interest.

	2013		
	BIS Loan	Finance Lease	Total
<b>Amounts falling due in:</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
One year or less	291	3	294
More than 1 year but not more than 2 years	-	4	4
More than 2 years but not more than 5 years	-	-	-
More than 5 years	-	-	-
<b>Total</b>	<b>291</b>	<b>7</b>	<b>298</b>

	2012		
	BIS Loan	Finance Lease	Total
<b>Amounts falling due in:</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
One year or less	377	4	381
More than 1 year but not more than 2 years	-	4	4
More than 2 years but not more than 5 years	-	4	4
More than 5 years	-	-	-
<b>Total</b>	<b>377</b>	<b>12</b>	<b>389</b>

	2011		
	BIS Loan	Finance Lease	Total
<b>Amounts falling due in:</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
One year or less	375	4	379
More than 1 year but not more than 2 years	-	4	4
More than 2 years but not more than 5 years	-	8	8
More than 5 years	-	-	-
<b>Total</b>	<b>375</b>	<b>16</b>	<b>391</b>

### 18. Hedging programmes

Details of the Group's derivative financial instruments, used to manage the risks identified above are as follows:

	2013	2012
	Assets	Assets
<b>Fair value of derivative financial instruments:</b>	<b>£m</b>	<b>£m</b>
Currency hedges	1	-
<b>Total</b>	<b>1</b>	<b>-</b>

#### Currency hedges

The Group mitigates its foreign currency risk exposure principally through external foreign currency forward contracts with First Rate Exchange Services Holdings Limited. At the year end the gain on unmatured currency hedges was £1m and taken to the income statement as hedge accounting is not claimed. The hedges mature in April 2013.

#### Derivative values

At any point in time, the derivative in programmes above are either 'in the money' which means the hedged rates are better than the current market rates or 'out of the money' which means that the hedged rates are worse than the current market rates. The resulting gains and losses as at the balance sheet date are recognised in the income statement. An associated financial asset or liability is created in the balance sheet (as detailed above.) The financial asset or liability is released when the derivative matures. The Groups hedging transactions are settled net.

## Post Office Limited

### 19. Pensions

On 1 April 2012, almost all of the pension assets and liabilities of the Royal Mail Pension Plan (RMPP) were transferred to HM Government. On this date the RMPP was also sectionalised with Royal Mail Group Limited and Post Office Limited responsible for their own sections. All employees were transferred to be directly employed by Post Office Limited on the same date.

Royal Mail Group Limited is the principal employer in Royal Mail Senior Executive Pension Plan (RMSEPP) and Post Office Limited became a participating employer with effect from 1 April 2012. Post Office Limited continues to account for approximately 7% of the RMSEPP scheme as it has done previously.

Prior to 1 April 2012, Royal Mail Group Limited had the legal relationship with the Trustees of both RMPP and RMSEPP and, as such, the Trustees held Royal Mail Group liable for the actuarial deficit in the scheme. All employees were employed by Royal Mail Group Limited and seconded to Post Office Limited under an agreement between Post Office Limited and Royal Mail Group Limited. Post Office Limited met the full costs of employment and was responsible for the funding of the pension deficit attributable to these employees. Consequently Post Office Limited recognised a balance sheet deficit based on employee numbers over 12 years and represented approximately 7% of the total balance sheet deficit at that time. The net pensions interest, deficit recovery payments and actuarial gains or losses were also allocated on this basis, giving the Post Office Limited approximately 7% of the total balance sheet deficit at the balance sheet date. The current service cost, regular future service contributions and curtailments were computed separately for Royal Mail Group Limited and Post Office Limited based on common factors/rates.

The disclosures in this note relating to the year ended 31 March 2013 reflect the Post Office Limited sectionalised RMPP scheme which is independently operated by the Group and the approximate 7% share of the RMSEPP scheme. The comparative figures for the year ended 25 March 2012 and the opening position at 28 March 2011 represent approximately 7% of the previous combined RMPP and RMSEPP plans.

The disclosures in this note relate to the year ending 31 March 2013 and show how the value of the assets and liabilities have been calculated at the balance sheet date.

The Group participates in pension schemes as detailed below.

Name	Eligibility	
Royal Mail Pension Plan (RMPP)	UK employees	Defined benefit
Royal Mail Senior Executive Pension Plan (RMSEPP)	UK senior executives	Defined benefit
Royal Mail Defined Contribution Plan (RMDCP)	UK employees	Defined contribution

#### Defined Contribution

The charge in the profit and loss account for the defined contribution schemes and the Group contributions to these schemes was £1m (2012 £1m) during the year. A new defined contribution plan (RMDCP) was launched in April 2009. New recruits joining from 31 March 2008 are able to begin paying contributions to the new plan after they have worked for the Group for a year.

#### Defined Benefit

Both RMPP and RMSEPP are funded by the payment of contributions to separate trustee administered funds. The latest full actuarial funding valuation of both schemes was carried out as at 31 March 2009 using the projected unit method. For RMPP, this valuation was concluded at £10.3bn deficit. For RMSEPP, the valuation was concluded at £100m deficit. RMPP includes sections A, B and C each with different terms and conditions:

- Section A is for members (or beneficiaries of members) who joined before 1 December 1971;
- Section B is for members (or beneficiaries of members) who joined after 1 December 1971 and before 1 April 1987 or to members of Section A who chose to receive Section B benefits;
- Section C is for members (or beneficiaries of members) who joined after 1 April 1987 and before 1 April 2008.

A series of changes to RMPP and RMSEPP began to take effect on 1 April 2008.

The changes encompass:

- the Plans closed to new members from 31 March 2008;
- all pensions and benefits earned before 1 April 2008 are still linked to final salary at the time of retirement;
- from 1 April 2008, defined benefits building up for employee members of the Plan are earned on a career salary basis;
- employees can continue to take their pension on reaching 60 but the normal retirement age increased to 65 for benefits earned from 1 April 2010; and
- from 1 April 2010 it is possible to draw pension earned before the change to normal retirement age at 55, and continue working while still contributing to the Pension Plan until the maximum level of benefits has been reached.
- on 31 December 2012 RMSEPP was closed.

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Payment of £24m (2012 £23m) was made by the Group during the year in respect of regular future service contributions, nearly all relating to RMPP. The regular future service contributions for RMPP, expressed as a percentage of pensionable pay, has remained at 17.1% (2012 17.1%), effective from April 2010. This rate is not expected to change materially during 2013-14. For RMSEPP, these contributions have remained at 35.9% (2012 35.9%) until its closure.

The Group pays 7% of the total deficit payment required to fund the deficit in RMSEPP and a payment of £2m (2012 less than £1m) was made by the Group during the year. Following the State Aid clearance granted on 21 March 2012 and the subsequent transfer of the historical pension deficit to HM Government on 1 April 2012 no RMPP deficit payment was made during 2011-12 or 2012-13. For RMSEPP, deficit recovery payments will be £1m per annum, from 1 April 2010 to 31 January 2024.

A current liability of £nil (2012 £nil) has been recognised for payments to the pension schemes relating to redundancy. During the year, payments of £2m (2012 £3m) relating to redundancy were made.

The following disclosures relate to the gains/losses and surplus/deficit in the scheme recognised for RMPP and RMSEPP defined benefit plans in the financial statements of the Group:

### a) Major long-term assumptions

The size of the RMPP pension surplus, which is large in the context of the Group and its finances, is materially sensitive to the assumptions adopted. Small changes in these assumptions could have a significant impact on the surplus and overall income statement charge. The major long-term assumptions were:

	At 31 March 2013 % pa	At 25 March 2012 % pa	At 28 March 2011 % pa
Rate of increase in salaries	4.3	4.3	4.5
Rate of pension increases – RMPP sections A/B	2.3	2.3	2.8
Rate of pension increases – RMPP section C	3.2	3.3	3.5
Rate of pension increases – RMSEPP all members	3.3	3.3	3.5
Rate of increase for deferred pensions – RMSEPP members transferred from Section A or B of RMPP	3.3	3.3	3.5
Rate of increase for deferred pensions	2.3	2.3	2.8
Discount rate	4.8	5.1	5.5
Inflation assumption (RPI)	3.3	3.3	3.5
Inflation assumption (CPI)	2.3	2.3	2.8
Expected average rate of return on assets	n/a	5.9	6.5

In June 2010, the Government announced that it was intending to change the inflation measure used to determine statutory minimum indexation in deferment and in payment from RPI to CPI from April 2011. Where relevant, the inflation assumption has changed from RPI to CPI.

The above assumptions relate to both defined benefit plans with the exception of the expected average rate of return on assets which was computed for the combined assets of the plans. The expected average rate of return on assets was a weighted average of the long-term expected rate of return of each principal asset class (see section b). The expected average rate of return was computed at each balance sheet date based on the market values and long-term rate of return of each principal asset class as at that date. The change in IAS 19 that will be implemented with effect from 1 April 2013 means that the expected average rate of return on assets is no longer required.

The following table shows the potential impact on the RMPP assets and pension surplus of changes in key assumptions:

	£m
Changes in RPI and CPI inflation of +0.1% pa	(4)
Changes in discount rate of +0.1%pa	4
Changes in real salary growth of +0.1% pa	(6)
Changes in CPI assumptions of +0.1% pa	(1)
An additional 1 year life expectancy	(4)

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### Mortality

The mortality assumptions for the RMPP sectionalised scheme are based on the latest self administered pension scheme (SAPS) mortality tables with appropriate scaling factors (106% for male pensioners and 101% for female pensioners). For future improvements the assumptions allow for 'medium cohort' projections with a 1.25% floor. These are detailed below:

Average expected life expectancy from age 60:	2013	2012	2011
For a current 60 year old male RMPP member	26 years	26 years	26 years
For a current 60 year old female RMPP member	29 years	29 years	29 years
For a current 40 year old male RMPP member	29 years	29 years	29 years
For a current 40 year old female RMPP member	32 years	32 years	32 years

### b) Plans' assets and expected rates of return

The assets in the plans and the expected rates of return for the Group were:

Sectionalised RMPP	Market value 2013 £m	Long-term expected rate of return 2013 % pa
Equities	29	n/a
Bonds	205	n/a
Property	-	n/a
Other assets	9	n/a
Fair value of RMPP assets	243	
Present value of RMPP liabilities	(144)	
Surplus in plan	99	

Share of RMSEPP	Market value 2013 £m	Long term expected rate of return 2013 % pa
Equities	146	n/a
Bonds	193	n/a
Property	19	n/a
Other assets	3	n/a
Fair value of plan assets for RMSEPP	361	
Present value of plan liabilities for RMSEPP	(347)	
Surplus in plan for RMSEPP	14	
Surplus in plan for the POL share (at approximately 7%) of RMSEPP	1	

A retirement benefit surplus of £97m is disclosed on the balance sheet, representing the surplus in plans of £99m and £1m for RMPP and RMSEPP respectively, and net of tax of £3m at a rate of 35% on the element of the surplus which is recoverable through a refund from the plans.

	Market value 2012 £m	Market value 2011 £m	Long term expected rate of return 2012 % pa	Long term expected rate of return 2011 % pa
Combined plans				
Equities	3,385	4,268	7.7	8.2
Bonds	25,610	21,409	5.7	6.2
Property	1,417	1,590	6.8	6.5
Other assets	333	418	3.4	4.2
Fair value of plans' assets for the combined plans	30,745	27,685		
Present value of plans' liabilities for the combined plans	(33,667)	(32,186)		
Deficit in schemes for the combined plans	(2,922)	(4,501)		
Deficit in schemes for share (at approximately 7%) of combined plans	(206)	(316)		

There is no element of the above present value of liabilities that arises from plans that are wholly unfunded.

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**c) Movement in plans' assets and liabilities**

Changes in the fair value of the plans' assets are analysed as follows:

<b>Assets</b>	<b>Sectionalised RMPP 2013 £m</b>
Assets in sectionalised RMPP at beginning of period	2,108
Transfer of pension assets to government	(1,953)
Contributions paid	25
Employee contributions paid	8
Finance income (expected rate of return)	11
Actuarial gains (additional increases in market values)	43
Benefits paid to members	(2)
<b>Assets in sectionalised RMPP at end of period</b>	<b>240</b>

<b>Assets</b>	<b>Share of RMSEPP 2013 £m</b>
Share of assets in RMSEPP at beginning of period	21
Contributions paid	2
Movement in contributions accrued	-
Employee contributions paid	-
Finance income (expected rate of return)	1
Actuarial gains (additional increases in market values)	1
Benefits paid to members	-
<b>Share of assets in RMSEPP at end of period</b>	<b>25</b>

Assets combined plans	2012 £m	2011 £m
Share of assets in combined plans at beginning of period	1,923	1,797
Contributions paid	26	46
Movement in contributions accrued	(3)	2
Employee contributions paid	10	11
Finance income (expected rate of return)	124	120
Actuarial gains (additional increases in market values)	131	33
Benefits paid to members	(82)	(86)
<b>Share of assets in combined plans at end of period</b>	<b>2,129</b>	<b>1,923</b>

Changes in the present value of the defined benefit pension obligations are analysed as follows:

<b>Liabilities</b>	<b>Sectionalised RMPP 2013 £m</b>
Liabilities in sectionalised RMPP at beginning of period	(2,313)
Transfer of pension liabilities to government	2,239
Current service cost	(24)
Curtailed costs*	(2)
Finance cost	(9)
Employee contributions	(8)
Actuarial loss (recognised in statement of comprehensive income)	(29)
Benefits paid	2
<b>Liabilities in sectionalised RMPP at end of period</b>	<b>(144)</b>

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Liabilities	Share of RMSEPP 2013 £m
Share of liabilities in RMSEPP plans at beginning of period	(22)
Current service cost	-
Curtailement costs*	-
Finance cost	(1)
Employee contributions	-
Actuarial gain/(loss) (recognised in statement of comprehensive income)	(1)
Benefits paid	-
<b>Share of liabilities in RMSEPP at end of period</b>	<b>(24)</b>

Liabilities combined plans	2012 £m	2011 £m
Share of liabilities in combined plans at beginning of period	(2,239)	(2,361)
Current service cost	(23)	(25)
Curtailement costs*	-	(3)
Finance cost	(122)	(132)
Employee contributions	(10)	(11)
Actuarial gain/(loss) (recognised in statement of comprehensive income)	(23)	207
Benefits paid	82	86
<b>Share of liabilities in combined plans at end of period</b>	<b>(2,335)</b>	<b>(2,239)</b>

\*The curtailment costs in the profit and loss account are recognised on a consistent basis with the associated compensation costs. Estimates of both are included, for example, in any redundancy provisions raised. The curtailment costs above represent the costs associated with those people paid compensation in respect of redundancy during the accounting period. Such payments may occur in an accounting period subsequent to the recognition of costs in the income statement.

**d) History of experience gains and losses**

The cumulative amount of actuarial gains and losses recognised since transition to IFRS as adopted by the European Union at 26 March 2012 in the consolidated statement of comprehensive income is a gain of £14m.

	Sectionalised RMPP	Share of RMSEPP	7% share of combined plans			
	2013 £m	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Fair value of assets	243	25	2,168	1,944	1,811	1,407
Present value of liabilities	(144)	(24)	(2,374)	(2,260)	(2,375)	(1,882)
Surplus/(Deficit) in schemes	99	1	(206)	(316)	(564)	(475)
Experience adjustment on assets	46	1	131	33	313	(384)
Experience adjustment on liabilities	(20)	-	-	(1)	47	(1)
	2013 %	2013 %	2012 %	2011 %	2010 %	2009 %
Experience adjustment on assets as a % of scheme assets	18.9	5.5	6.1	1.7	17.4	(27.3)
Experience adjustment on liabilities as a % of scheme liabilities	(13.9)	1.4	0.0	0.0	(2.0)	0.1
Deficit in the scheme as a % of scheme liabilities	-	-	8.8	14.1	23.9	25.3

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**e) Recognised charges**

An analysis of the separate components of the amounts recognised in the performance statements of the Group is as follows:

	2013 sectionalised RMPP £m
<b>Analysis of amounts recognised in the income statement</b>	
<b>Analysis of amounts charged to operating profit before exceptional items:</b>	
Current service cost	24
<b>Total charge to operating profit before exceptional items</b>	
<b>Analysis of amounts charged to operating exceptional items:</b>	
Loss due to curtailments (within provision – note 16)	2
<b>Total charge to operating profit</b>	
<b>Analysis of amounts charged/(credited) to net pensions interest:</b>	
Interest on plan liabilities	9
Expected return on plan assets	(11)
<b>Net pensions credit to financing</b>	
<b>Net charge to the income statement before deduction for tax</b>	
<b>Analysis of amounts recognised in the statement of comprehensive income</b>	
Transfer of pension liabilities to government	2,239
Transfer of pension assets to government	(1,953)
Gain on transfer to government	286
Actual return on plan assets	57
Less: expected return on plan assets	(11)
Less: taxation on surplus recoverable through plan refunds	(3)
Actuarial gains on assets (all experience adjustments)	43
Experience adjustments on liabilities	(20)
Effects of changes in actuarial assumptions on liabilities	(9)
Actuarial losses on liabilities	(29)
<b>Total actuarial gains recognised in the statement of comprehensive income</b>	

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	2013 share of RMSEPP £m
<b>Analysis of amounts recognised in the income statement</b>	
<b>Analysis of amounts charged to operating profit before exceptional items:</b>	
Current service cost	1
<b>Total charge to operating profit before exceptional items</b>	
<b>Analysis of amounts charged to operating exceptional items:</b>	
Loss due to curtailments (within provision for organisational review – note 16)	-
<b>Total charge to operating profit</b>	
<b>Analysis of amounts charged/(credited) to net pensions interest:</b>	
Interest on plan liabilities	16
Expected return on plan assets	(18)
<b>Net pensions interest</b>	
	(2)
<b>Share of net pensions interest (at approximately 7%)</b>	
	-
<b>Net charge to the income statement before deduction for tax</b>	
	-
<b>Analysis of amounts recognised in the statement of comprehensive income in the Royal Mail Holdings Group financial statements</b>	
Actual return on plan	38
Less: expected return on plan	(18)
Actuarial gains on assets (all experience adjustments)	20
Experience adjustments on liabilities	5
Effects of changes in actuarial assumptions on liabilities	(23)
Actuarial losses on liabilities	(18)
<b>Total actuarial gains recognised in statement of comprehensive income in the Royal Mail Holdings Group financial statements</b>	
	2
<b>Share of actuarial gains/(losses) recognised in statement of comprehensive income (at approximately 7%)</b>	
	-

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Combined plans	2012 £m	2011 £m
<b>Analysis of amounts recognised in the income statement</b>		
<b>Analysis of amounts charged to operating profit before exceptional items:</b>		
Current service cost	23	25
<b>Total charge to operating profit before exceptional items</b>	<b>23</b>	<b>25</b>
<b>Analysis of amounts charged to operating exceptional items:</b>		
Loss due to curtailments (within provision for organisational review – note 16)	-	2
<b>Total charge to operating profit</b>	<b>23</b>	<b>27</b>
<b>Analysis of amounts charged/(credited) to net pensions interest:</b>		
Interest on plans' liabilities for the combined plans	1,749	1,881
Expected return on plans' assets for the combined plans	(1,775)	(1,714)
<b>Net pensions interest for the combined plans</b>	<b>(26)</b>	<b>167</b>
<b>Share of net pensions interest (at approximately 7%)</b>	<b>(2)</b>	<b>12</b>
<b>Net charge to the income statement before deduction for tax</b>	<b>21</b>	<b>39</b>
<b>Analysis of amounts recognised in the statement of comprehensive income in the Royal Mail Holdings Group financial statements</b>		
Actual return on plans' assets for the combined plans	3,644	2,184
Less: expected return on plans' assets for the combined plans	(1,775)	(1,714)
Actuarial gains on assets for the combined plans (all experience adjustments)	1,869	470
Experience adjustments on liabilities for the combined plans	(5)	(8)
Effects of changes in actuarial assumptions on liabilities for the combined plans	(320)	2,962
Actuarial (losses)/ gains on liabilities for the combined plans	(325)	2,954
<b>Total actuarial gains recognised in statement of comprehensive income in the Royal Mail Holdings Group financial statements</b>	<b>1,544</b>	<b>3,424</b>
<b>Share of actuarial gains/(losses) recognised in statement of comprehensive income (at approximately 7%)</b>	<b>108</b>	<b>240</b>

**20. Called up share capital**

	2013 £	2012 £	2011 £
<b>Authorised</b>			
Ordinary shares of £1 each	<b>51,000</b>	51,000	51,000
<b>Total</b>	<b>51,000</b>	51,000	51,000
<b>Allotted and issued</b>			
Ordinary shares of £1 each	<b>50,003</b>	50,003	50,003
<b>Total</b>	<b>50,003</b>	50,003	50,003

## Post Office Limited

### 21. Commitments

Capital commitments contracted for but not provided in the financial statements amount to £48m (2012 £15m).

The Group is committed to the following minimum lease payments under non-cancellable operating leases:

	Land and buildings			IT equipment		
	2013 £m	2012 £m	2011 £m	2013 £m	2012 £m	2011 £m
Within one year	16	16	16	15	16	16
Between one and five years	42	44	43	-	-	-
Beyond five years	38	43	45	-	-	-
<b>Total</b>	<b>96</b>	<b>103</b>	<b>104</b>	<b>15</b>	<b>16</b>	<b>16</b>

### 22. Finance lease liabilities

	2013		2012		2011	
	Minimum payments	Present value of minimum lease payments	Minimum payments	Present value of minimum lease payments	Minimum payments	Present value of minimum lease payments
	£m	£m	£m	£m	£m	£m
Within one year	4	3	4	4	4	4
Between one and five years	4	4	8	6	12	9
Beyond five years	-	-	-	-	-	-
<b>Total minimum lease payments</b>	<b>8</b>	<b>7</b>	<b>12</b>	<b>10</b>	<b>16</b>	<b>13</b>
Less amounts representing finance charges	(1)	-	(2)	-	(3)	-
<b>Present value of minimum lease payments</b>	<b>7</b>	<b>7</b>	<b>10</b>	<b>10</b>	<b>13</b>	<b>13</b>
Of which:						
Current	3	3	4	4	4	4
Non-current	4	4	6	6	9	9

The aggregate finance charges allocated for the period in respect of finance leases was £738,859 (2012 £1,011,232). The fair value of finance lease liabilities is not materially different from the carrying value.

The Group has finance lease contracts for equipment. The leases have no terms for renewal, purchase options or escalation clauses and there are no restrictions concerning dividends, borrowings or additional leases. The leases have an average term of six years.

## Post Office Limited

### 23. Related party disclosures

#### Joint venture

The following company is a joint venture of the Group:

Company	Country of incorporation	% Holding	Principal activities
First Rate Exchange Services Holdings Limited	United Kingdom	50	Bureau de Change

#### Associates

The following company was an associate of Post Office Limited during the year: The Group's interest was disposed of in September 2012.

Company	Country of incorporation	% Holding	Principal activities
Midasgrange Limited	United Kingdom	50	Financial services

All shareholdings are equity shares.

#### Related party transactions

During the year the Group entered into transactions with the following related parties. The transactions were in the ordinary course of business. The transactions entered into and the balances outstanding at the financial year end were as follows:

	Sales/recharges to related party			Purchases/recharges from related party			Amounts owed from related party including outstanding loans			Amounts owed to related party including outstanding loans		
	2013 £m	2012 £m	2011 £m	2013 £m	2012 £m	2011 £m	2013 £m	2012 £m	2011 £m	2013 £m	2012 £m	2011 £m
Royal Mail Group Limited	371	359	346	37	33	35	-	-	-	4	8	11
Camelot Group plc	-	-	10	-	-	-	-	-	-	-	-	-
Romec Limited	-	-	-	8	8	8	-	-	-	2	1	1
Midasgrange Limited	35	41	30	1	1	3	-	14	10	-	1	-
First Rate Exchange Services Holdings Limited	27	31	30	125	128	132	7	3	9	11	8	1

The sales to and purchases from related parties are made at normal market prices. Balances outstanding at the year end are unsecured, interest free and settlement is made by cash. Royal Mail Group Limited is a subsidiary company of the Group's parent company, Royal Mail Holdings plc. Camelot Group plc was an associate within the Royal Mail Holdings Group but was disposed of in 2010-11. Romec Limited is a subsidiary of Royal Mail Group Limited. Midasgrange Limited was an associate of the Group until September 2012 and First Rate Exchange Services Holdings Limited is a joint venture of the Group.

The Group trades with numerous Government bodies on an arm's length basis. Transactions with these entities are not disclosed owing to the significant volume of transactions that are conducted.

Separately:

- the Group has certain loan facilities with Government (note 15);
- almost all of the pension assets and liabilities of the Royal Mail Pension Plan to Government (note 19);
- the Group has received a Government Grant of £200m, £98m of which was recognised through the income statement (note 5) and £102m of which is deferred income within trade and other payables (note 14); and
- the Group has received the Network Subsidy Payment from Government (note 1).

Key management comprises Executive and Non-Executive Directors of the Post Office Limited Board and the members of the Executive Committee at 31 March 2013. The aggregate remuneration of the key management personnel of the Post Office Group is set out below:

	2013 £000	2012 £000
Short-term employee benefits	3,568	3,077
Post-employment benefits	119	232
Other long-term benefits	651	-
Termination benefits	-	-
<b>Total</b>	<b>4,338</b>	<b>3,309</b>

## Post Office Limited

### **24. Post balance sheet events**

In accordance with the funding agreement with Government announced on 27 October 2010, for which State Aid approval was received on 28 March 2012, Post Office Limited received £415m of funding on 2 April 2013.

### **25. Immediate and ultimate parent company**

At 31 March 2013, the Directors regarded Royal Mail Holdings plc as the immediate and ultimate parent company. The largest group to consolidate the results of the company is Royal Mail Group Holdings plc, a company registered in the United Kingdom. Royal Mail Group Holdings plc financial statements can be obtained from the company website, [www.royalmailgroup.com](http://www.royalmailgroup.com)

**Post Office Limited**

**Post Office Limited**  
**Parent Company Financial Statements**  
**2012-2013**

## Post Office Limited

### Independent auditor's report to the members of Post Office Limited

We have audited the parent company financial statements of Post Office Limited for the 53-week period ended 31 March 2013 which comprise the company balance sheet, the company statement of total recognised gains and losses, the company reconciliation of movements in shareholder's and the related notes 1 to 14. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report 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 members as a body, for our audit work, for this report, or for the opinions we have formed.

#### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page X, the directors are responsible for the preparation of the parent company financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the parent company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

#### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### Opinion on financial statements

In our opinion the parent company financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2013;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

#### Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial period for which the financial statements are prepared is consistent with the parent company financial statements.

#### Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

#### Other matter

We have reported separately on the consolidated financial statements of Post Office Limited for the 53-week period ended 31 March 2013.

#### Ernst & Young LLP

Angus Grant (Senior statutory auditor)  
for and on behalf of Ernst & Young LLP, Statutory Auditor  
London  
Date

1. The maintenance and integrity of the Post Office Limited's web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.

2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## Post Office Limited

Balance sheet of the company  
at 31 March 2013 and 25 March 2012

	Notes	2013 £m	2012 £m
Intangible assets	2	-	-
Tangible assets	3	11	11
Investments in joint ventures and associates	4	1	5
Retirement benefit surplus	12	97	-
<b>Total fixed assets</b>		<b>109</b>	<b>16</b>
<b>Current assets</b>			
Stocks		8	6
Debtors - receivable within one year	5	362	226
Financial assets - investments	6	92	62
Financial assets - derivatives		1	-
Cash at bank and in hand	7	879	758
		<b>1,342</b>	<b>1052</b>
<b>Current liabilities</b>			
Creditors - amounts falling due within one year	8	(901)	(587)
Financial liabilities - interest bearing loans and borrowings	9	(291)	(377)
<b>Net current assets</b>		<b>150</b>	<b>88</b>
<b>Total assets less current liabilities</b>			
		<b>259</b>	<b>104</b>
Creditors - amounts falling due after more than one year	10	(4)	(8)
Provisions for liabilities	11	(26)	(14)
Retirement benefit obligation	12	-	(206)
<b>Net assets/(liabilities)</b>		<b>229</b>	<b>(124)</b>
<b>Capital and reserves</b>			
Called up share capital	13	-	-
Share premium	14	465	465
Profit and loss account	14	(236)	(589)
<b>Shareholder's surplus/(deficit)</b>		<b>229</b>	<b>(124)</b>

The financial statements on pages XX to XX were approved by the Board of Directors on XXX 2013 and signed on its behalf by:

**P A Vennells**  
Chief Executive

**C M Day**  
Chief Financial Officer

## Post Office Limited

**Statement of total recognised gains and losses**  
for the 53 weeks ended 31 March 2013 and the 52 weeks ended 25 March 2012

	Notes	2013 £m	2012 £m
<b>Profit for the financial year</b>	14	<b>74</b>	37
Actuarial gains on defined benefit pension schemes	12	<b>14</b>	108
Taxation on items taken directly to equity		<b>(21)</b>	-
<b>Total recognised gains for the financial year</b>	14	<b>67</b>	145

There is no statement of historical cost profits and losses as the financial statements are produced under the historic cost accounting convention.

**Reconciliation of movements in shareholder's funds**  
for the year ended 31 March 2013 and 25 March 2012

	Notes	2013 £m	2012 £m
Opening shareholder's deficit	14	<b>(124)</b>	(269)
Total recognised gains for the financial year (see above)		<b>67</b>	145
Transfer of pension deficit to government		<b>286</b>	-
<b>Closing shareholder's surplus/ (deficit)</b>		<b>229</b>	(124)

## Post Office Limited

### Notes to the financial statements

#### 1. Accounting Policies

The following accounting policies apply throughout Post Office Limited (the Company):

##### Financial year

The financial year ends on the last Sunday in March and accordingly, these financial statements are made up to the 53 weeks ended 31 March 2013 (2012 52 weeks ended 25 March 2012).

##### Basis of preparation

The financial statements on pages ~~XX~~ to ~~XX~~ have been prepared in accordance with applicable UK Accounting Standards and law, including the requirements of the Companies Act 2006. Unless otherwise stated in the accounting policies below, the financial statements have been prepared under the historic cost accounting convention.

As permitted by Section 408 of the Companies Act 2006 Post Office Limited has not presented its own profit and loss account. The result dealt with in the accounts of the company amounted to £74m profit (2012 £37m profit).

No cash flow statement has been presented as the Company is part of the Post Office Limited Group which has presented a consolidated cash flow statement within its Group financial statements.

The company has taken advantage of the exemption conferred by FRS 29 not to disclose financial instrument information as the Company is part of the Post Office Limited Group which has presented such disclosures in its Group financial statements.

##### Changes in accounting policy

The accounting policies are consistent with those of the previous year.

##### Intangible fixed assets

Intangible assets acquired separately or generated internally are initially recognised at cost and are reviewed for impairment. An impairment loss is recognised in the profit and loss account for the amount by which the carrying value of the asset exceeds its recoverable amount, which is the higher of an asset's net realisable value and its value in use.

Amortisation of intangible assets with finite lives is charged annually to the income statement on a straight-line basis as follows.

Software	1 to 6 years
----------	--------------

##### Tangible fixed assets

Tangible fixed assets are recognised at cost, including attributable costs in bringing the asset into working condition for its intended use.

Depreciation of tangible fixed assets is provided on a straight-line basis by reference to net book value and to the remaining useful economic lives of assets and their estimated residual values. The lives assigned to major categories of tangible fixed assets are:

	Range of asset lives
Land and buildings:	
Freehold land	Not depreciated
Freehold buildings	Up to 50 years
Leasehold buildings	The shorter of the period of the lease, 50 years or the estimated remaining useful life
Plant and Machinery	3 - 15 years
Motor vehicles and trailers	2 - 12 years
Fixtures and equipment	2 - 15 years

##### Impairment reviews

Unless otherwise disclosed in these accounting policies, fixed assets are reviewed for impairment if events or changes in circumstances indicate that the carrying value may be impaired. The Company assesses at each reporting date whether such indications exist. Where appropriate, an impairment loss is recognised in the profit and loss account for the amount by which the carrying value of the asset (or cash generating unit) exceeds its recoverable amount, which is the higher of an asset's net realisable value and its value in use.

##### Leases

Finance leases, where substantially all the risks and rewards incidental to ownership of the leased item have passed to the Company are capitalised at the inception of the lease with a corresponding liability recognised for the fair value of the leased item or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability.

Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term.

Leases where substantially all the risks and rewards of ownership of the asset are retained by the lessor, are classified as operating leases and rentals are charged to the profit and loss account over the lease term. The aggregate benefit of incentives are recognised as a reduction of rental expenses over the lease term on a straight-line basis.

## Post Office Limited

### Investments in joint ventures and associates

Investments in joint ventures and associates within the Company's financial statements are stated at cost less any accumulated impairment losses.

### Investments in subsidiaries

Investments in subsidiaries within the Company's financial statements are stated at cost less any accumulated impairment losses. The carrying value relates solely to the Company's investment in Post Office Management Services Limited, a 100% subsidiary of the Company and is less than £1m.

### Stocks

Stocks, which include printing and stationery, retail and lottery products, are carried at the lower of cost and net realisable value after adjusting for obsolete or slow-moving stock.

### Deferred tax

Deferred tax is generally provided in full on timing differences at the balance sheet date, at rates expected to apply when the tax liability (or asset) crystallises based on substantively enacted tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements.

Deferred tax is not recognised in the following instances:

- on gains on disposal of fixed assets where, on the basis of available evidence, it is more likely than not that the taxable gain will be rolled over into replacement assets and charged to tax only when there is a commitment to dispose of those replacement assets;
- on unremitted earnings of subsidiaries and associates where there is no commitment to remit those earnings; and
- deferred tax assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax assets and liabilities are not discounted. Deferred tax is charged or credited directly to reserves if it relates to items that are credited or charged directly to reserves. Otherwise it is recognised in the profit and loss account.

### Pensions and other post-retirement benefits

People working for the Company were employed by Royal Mail Group Limited and seconded to the Company until 31 March 2012. On 1 April 2012 they were transferred to be directly employed by the Company. Membership of occupational pension schemes is open to most permanent UK employees of the Company. All members of defined benefit schemes are contracted out of the earnings-related part of the State pension scheme.

The pension plans' assets of the defined benefit schemes are measured at fair value. Liabilities are measured on an actuarial basis using the projected unit credit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term. The resulting defined benefit asset or liability is presented separately on the face of the balance sheet, net of any associated deferred tax balance. Full actuarial valuations are carried out at intervals not normally exceeding three years as determined by the Trustees and, with appropriate updates and accounting adjustments at each balance sheet date, form the basis of the deficit disclosed.

For defined benefit schemes, the amounts charged to operating profit, as part of staff costs, are the current service costs and any gains and losses arising from settlements, curtailments and past service costs.

The net difference between the interest costs and the expected return on plan assets is recognised as net pensions interest in the profit and loss account. Actuarial gains and losses are recognised immediately in the statement of total recognised gains and losses (STRGL). Any deferred tax movement associated with the actuarial gains and losses is also recognised in the STRGL.

For defined contribution schemes, the Company's contributions are charged to operating profit, as part of staff costs, in the period to which the contributions relate.

### Foreign currencies

The functional and presentational currency of the Company is sterling (£).

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction (or at the contracted rate if the transaction is covered by a forward foreign currency contract). Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date (or the appropriate forward contract rate). All differences are taken to the profit and loss account.

### Debtors

Debtors are recognised and carried at original invoice amount less an allowance for any non-collectable amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

### Financial assets – investments (current assets)

Financial assets – investments in the balance sheet comprise short-term deposits and money market funds. All financial assets – investments are classified as loans and receivables and are measured at amortised cost using the effective interest rate method. Gains and losses are recognised in the profit and loss account when the investments are derecognised or impaired, as well as through the amortisation process.

## Post Office Limited

### 1. Accounting Policies (continued)

#### Financial liabilities – interest-bearing loans and borrowings

All loans and borrowings are classified as financial liabilities measured at amortised cost. Borrowing costs are recognised as an expense when incurred.

#### Financial liabilities – obligations under finance lease and hire purchase contracts

All obligations under finance lease and hire purchase contracts are classified as financial liabilities measured at amortised cost.

#### Borrowing costs

Borrowing costs are recognised as an expense when incurred unless they are directly attributable to the construction or development of a qualifying asset, in which case they are capitalised using the weighted average cost of borrowing for the period of construction/development.

#### Fair value measurement of financial instruments

The fair value of quoted investments is determined by reference to bid prices at the close of business on the balance sheet date. Where there is no active market, fair value is determined using valuation techniques. These include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; and discounted cash flow analysis and pricing models.

For the purposes of disclosing the fair value of investments held at amortised cost in the balance sheet, in the absence of quoted market prices, fair values are calculated by discounting the future cash flows of the financial instrument using quoted equivalent interest rates as at close of business on the balance sheet date.

#### Derecognition of financial instruments

A financial asset or liability is derecognised when the contract that gives rise to it is settled, sold, cancelled or expires.

#### Government grants

Government grants of a revenue nature are recognised to match costs in relation to the performance of certain specified activities.

### 2. Intangible assets

Cost	2013 £m	2012 £m
At 26 March 2012 and 28 March 2011	183	166
Additions	25	17
Disposals	-	-
<b>At 31 March 2013 and 25 March 2012</b>	<b>208</b>	<b>183</b>
<b>Amortisation and impairment</b>		
At 26 March 2012 and 28 March 2011	183	166
Impairment	25	17
<b>At 31 March 2013 and 25 March 2012</b>	<b>208</b>	<b>183</b>
<b>Net book value</b>		
<b>At 31 March 2013 and 25 March 2012</b>	<b>-</b>	<b>-</b>

The above intangible assets relate to software.

## Post Office Limited

## 3. Tangible fixed assets

	Land and Buildings						Total £m
	Freehold	Long leasehold	Short leasehold	Motor vehicles	Plant and machinery	Fixtures and equipment	
	£m	£m	£m	£m	£m	£m	
<b>Cost</b>							
At 26 March 2012	79	17	114	34	1	709	954
Reclassification	-	1	(1)	-	-	-	-
Additions	9	-	1	9	-	22	41
Disposals - external	(1)	-	-	(1)	-	(12)	(14)
<b>At 31 March 2013</b>	<b>87</b>	<b>18</b>	<b>114</b>	<b>42</b>	<b>1</b>	<b>719</b>	<b>981</b>
<b>Depreciation</b>							
At 26 March 2012	69	16	114	34	1	709	943
Depreciation	-	-	-	-	-	-	-
Impairment (see note 5)	9	1	-	9	-	22	41
Disposals - external	(1)	-	-	(1)	-	(12)	(14)
<b>At 31 March 2013</b>	<b>77</b>	<b>17</b>	<b>114</b>	<b>42</b>	<b>1</b>	<b>719</b>	<b>970</b>
<b>Net book value</b>							
<b>At 31 March 2013</b>	<b>10</b>	<b>1</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>11</b>
At 26 March 2012	10	1	-	-	-	-	11

Depreciation rates are disclosed within accounting policies (note 1). No depreciation is provided on freehold land, which represents £3m (2012 £3m) of the total cost of properties.

## 4. Investments in joint ventures and associates

	2013 £m	2012 £m
Investment in joint ventures and associates	1	5

## Joint ventures

During 2012-13 and 2011-12, the Company's only joint venture investment was a 50% interest (1,000 £1 ordinary A shares) in First Rate Exchange Services Holdings Limited with a carrying value of £0.6m (2012 £0.6m), whose principal activity is the provision of Bureau de Change. First Rate Exchange Services Holdings Limited is a company registered in the United Kingdom.

## Associates

During 2011-12, the Company's only associate investment was a 49.99% interest (4,999 £0.01 ordinary A shares) in Midasgrange Limited with a carrying value of £4.6m (2011 £4.6m), whose principal activity is the provision of personal financial products. This investment was disposed of during the year ended 31 March 2013.

## 5. Debtors - receivable within one year

	2013 £m	2012 £m
Trade debtors	32	39
Prepayments and accrued income	81	39
Client debtors	240	138
Other receivables	9	10
<b>Total</b>	<b>362</b>	<b>226</b>

## Post Office Limited

**6. Current financial assets - investments**

	<b>2013</b>	2012
	<b>£m</b>	£m
Money market funds	<b>86</b>	43
Short-term deposits - bank	<b>6</b>	19
<b>Total</b>	<b>92</b>	62

**7. Cash at bank and in hand**

	<b>2013</b>	2012
	<b>£m</b>	£m
Cash in the Post Office Limited network	<b>879</b>	758

**8. Creditors - amounts falling due within one year**

	<b>2013</b>	2012
	<b>£m</b>	£m
Trade creditors and accruals	<b>178</b>	172
Advance customer payments	<b>50</b>	48
Social security	<b>10</b>	9
Client creditors	<b>528</b>	332
Obligations under finance lease and hire purchase contracts	<b>3</b>	4
Amount due to other group companies	<b>5</b>	9
Capital creditors	<b>18</b>	10
Business transformation payments	<b>7</b>	3
Government Grant	<b>102</b>	0
<b>Total</b>	<b>901</b>	587

**9. Financial liabilities - interest bearing loans and borrowings****Analysis of loans and committed facilities:**

	<b>2013</b>	2012
	<b>£m</b>	£m
Loans drawn down	<b>291</b>	377
<b>Total facility</b>	<b>1,150</b>	1,150

The loans under the facility are short dated on a programme of liquidity management and mature on average 1 day after the year end (2012 1 day). On maturity it is expected that further loans will be drawn down under this facility, which expires in 2016. The undrawn committed facility, in respect of which all conditions precedent had been met at the balance sheet date is £859m (2012 £773m.) The average interest rate on the drawn down loans is 1.0% (2012 0.8%).

The facility is currently restricted to funding the cash and near cash items held within the Post Office Limited network.

The facility (including drawn down loans) is secured by a floating charge over all assets of Post Office Limited and a negative pledge over cash and near cash items. The negative pledge is an agreement not to grant security over the assets or to set up a vehicle that has the same effect.

## Post Office Limited

**10. Creditors - amounts falling due after more than one year**

	<b>2013</b>	2012
	<b>£m</b>	£m
Obligations under finance lease and hire purchase contracts	<b>4</b>	6
Other payables	-	2
<b>Total</b>	<b>4</b>	8

**11. Provisions for liabilities**

	<b>Crown Conversions Project £m</b>	<b>Network Transformation £m</b>	<b>Other £m</b>	<b>Total £m</b>
At 26 March 2012	9	-	5	<b>14</b>
Charged in operating exceptional items	-	10	12	<b>22</b>
Charged in operating costs		-	6	<b>6</b>
Charged in financing costs	1	-	-	<b>1</b>
Utilisation	(3)	-	(14)	<b>(17)</b>
<b>At 31 March 2013</b>	<b>7</b>	<b>10</b>	<b>9</b>	<b>26</b>

Other provisions of £9m (2012 £5m) include property contracts, comprising amounts from onerous lease obligations and personal injury claims.

Amounts charged in financing costs relate to the unwinding of discounted long-term provisions.

The Crown Conversions project relates to past franchising of Crown offices and onerous property lease provisions are expected to be utilised within 5 years.

## Post Office Limited

### 12. Pensions

On 1 April 2012, almost all of the pension assets and liabilities of the Royal Mail Pension Plan (RMPP) were transferred to HM Government. On this date the RMPP was also sectionalised with Royal Mail Group Limited and Post Office Limited responsible for their own sections. All employees were transferred to be directly employed by Post Office Limited on the same date.

Royal Mail Group Limited is the principal employer in Royal Mail Senior Executive Pension Plan (RMSEPP) and Post Office Limited became a participating employer with effect from 1 April 2012. Post Office Limited continues to account for approximately 7% of the RMSEPP scheme as it has done previously.

Prior to 1 April 2012, Royal Mail Group Limited had the legal relationship with the Trustees of both RMPP and RMSEPP and, as such, the Trustees held Royal Mail Group liable for the actuarial deficit in the scheme. All employees were employed by Royal Mail Group Limited and seconded to Post Office Limited under an agreement between Post Office Limited and Royal Mail Group Limited. Post Office Limited met the full costs of employment and was responsible for the funding of the pension deficit attributable to these employees. Consequently Post Office Limited recognised a balance sheet deficit based on employee numbers over 12 years and represented approximately 7% of the total balance sheet deficit at that time. The net pensions interest, deficit recovery payments and actuarial gains or losses were also allocated on this basis, giving the Post Office Limited approximately 7% of the total balance sheet deficit at the balance sheet date. The current service cost, regular future service contributions and curtailments were computed separately for Royal Mail Group Limited and Post Office Limited based on common factors/rates.

The disclosures in this note relating to the year ended 31 March 2013 reflect the Post Office Limited sectionalised RMPP scheme which is independently operated by Post Office Limited and the approximate 7% share of the RMSEPP scheme. The comparative figures for the year ended 25 March 2012 and the opening position at 28 March 2011 represent approximately 7% of the previous combined RMPP and RMSEPP plans.

The disclosures in this note relate to the year ending 31 March 2013 and show how the value of the assets and liabilities have been calculated at the balance sheet date.

The Company participates in pension schemes as detailed below.

Name	Eligibility	
Royal Mail Pension Plan (RMPP)	UK employees	Defined benefit
Royal Mail Senior Executive Pension Plan (RMSEPP)	UK senior executives	Defined benefit
Royal Mail Defined Contribution Plan (RMDCP)	UK employees	Defined contribution

#### Defined Contribution

The charge in the profit and loss account for the defined contribution schemes and the Company contributions to these schemes was £1m (2012 £1m) during the year. A new defined contribution plan (RMDCP) was launched in April 2009. New recruits joining from 31 March 2008 are able to begin paying contributions to the new plan after they have worked for the Company for a year.

#### Defined Benefit

Both RMPP and RMSEPP are funded by the payment of contributions to separate trustee administered funds. The latest full actuarial funding valuation of both schemes was carried out as at 31 March 2009 using the projected unit method. For RMPP, this valuation was concluded at £10.3bn deficit. For RMSEPP, the valuation was concluded at £100m deficit. RMPP includes sections A, B and C each with different terms and conditions:

- Section A is for members (or beneficiaries of members) who joined before 1 December 1971;
- Section B is for members (or beneficiaries of members) who joined after 1 December 1971 and before 1 April 1987 or to members of Section A who chose to receive Section B benefits;
- Section C is for members (or beneficiaries of members) who joined after 1 April 1987 and before 1 April 2008.

A series of changes to RMPP and RMSEPP began to take effect on 1 April 2008.

The changes encompass:

- the Plans closed to new members from 31 March 2008;
- all pensions and benefits earned before 1 April 2008 are still linked to final salary at the time of retirement;
- from 1 April 2008, defined benefits building up for employee members of the Plan are earned on a career salary basis;
- employees can continue to take their pension on reaching 60 but the normal retirement age increased to 65 for benefits earned from 1 April 2010; and
- from 1 April 2010 it is possible to draw pension earned before the change to normal retirement age at 55, and continue working while still contributing to the Pension Plan until the maximum level of benefits has been reached.
- on 31 December 2012 RMSEPP was closed.

## Post Office Limited

Payment of £24m (2012 £23m) was made by the Company during the year in respect of regular future service contributions, nearly all relating to RMPP. The regular future service contributions for RMPP, expressed as a percentage of pensionable pay, has remained at 17.1% (2012 17.1%), effective from April 2010. This rate is not expected to change materially during 2013-14. For RMSEPP, these contributions have remained at 35.9% (2012 35.9%) until its closure.

The Company pays 7% of the total deficit payment required to fund the deficit in RMSEPP and a payment of £2m (2012 less than £1m) was made by the Company during the year. Following the State Aid clearance granted on 21 March 2012 and the subsequent transfer of the historical pension deficit to HM Government on 1 April 2012 no RMPP deficit payment was made during 2011-12 or 2012-13. For RMSEPP, deficit recovery payments will be £1m per annum, from 1 April 2010 to 31 January 2024.

A current liability of £nil (2012 £nil) has been recognised for payments to the pension schemes relating to redundancy. During the year, payments of £2m (2012 £3m) relating to redundancy were made.

The following disclosures relate to the gains/losses and surplus/deficit in the scheme recognised for RMPP and RMSEPP defined benefit plans in the financial statements of the Company:

### b) Major long-term assumptions

The size of the RMPP pension surplus, which is large in the context of the Company and its finances, is materially sensitive to the assumptions adopted. Small changes in these assumptions could have a significant impact on the surplus and overall income statement charge. The major long-term assumptions were:

	At 31 March 2013 % pa	At 25 March 2012 % pa	At 28 March 2011 % pa
Rate of increase in salaries	4.3	4.3	4.5
Rate of pension increases – RMPP sections A/B	2.3	2.3	2.8
Rate of pension increases – RMPP section C	3.2	3.3	3.5
Rate of pension increases – RMSEPP all members	3.3	3.3	3.5
Rate of increase for deferred pensions – RMSEPP members transferred from Section A or B of RMPP	3.3	3.3	3.5
Rate of increase for deferred pensions	2.3	2.3	2.8
Discount rate	4.8	5.1	5.5
Inflation assumption (RPI)	3.3	3.3	3.5
Inflation assumption (CPI)	2.3	2.3	2.8
Expected average rate of return on assets	n/a	5.9	6.5

In June 2010, the Government announced that it was intending to change the inflation measure used to determine statutory minimum indexation in deferment and in payment from RPI to CPI from April 2011. Where relevant, the inflation assumption has changed from RPI to CPI.

The above assumptions relate to both defined benefit plans with the exception of the expected average rate of return on assets which was computed for the combined assets of the plans. The expected average rate of return on assets was a weighted average of the long-term expected rate of return of each principal asset class (see section b). The expected average rate of return was computed at each balance sheet date based on the market values and long-term rate of return of each principal asset class as at that date. The change in IAS 19 that will be implemented with effect from 1 April 2013 means that the expected average rate of return on assets is no longer required.

The following table shows the potential impact on the RMPP assets and pension surplus of changes in key assumptions:

	£m
Changes in RPI and CPI inflation of +0.1% pa	(4)
Changes in discount rate of +0.1%pa	4
Changes in real salary growth of +0.1% pa	(6)
Changes in CPI assumptions of +0.1% pa	(1)
An additional 1 year life expectancy	(4)

## Post Office Limited

### Mortality

The mortality assumptions for the RMPP sectionalised scheme are based on the latest self administered pension scheme (SAPS) mortality tables with appropriate scaling factors (106% for male pensioners and 101% for female pensioners). For future improvements the assumptions allow for 'medium cohort' projections with a 1.25% floor. These are detailed below:

Average expected life expectancy from age 60:	2013	2012	2011
For a current 60 year old male RMPP member	26 years	26 years	26 years
For a current 60 year old female RMPP member	29 years	29 years	29 years
For a current 40 year old male RMPP member	29 years	29 years	29 years
For a current 40 year old female RMPP member	32 years	32 years	32 years

### b) Plans' assets and expected rates of return

The assets in the plans and the expected rates of return for the Company were:

Sectionalised RMPP	Market value 2013 £m	Long-term expected rate of return 2013 % pa
Equities	29	n/a
Bonds	205	n/a
Property	-	n/a
Other assets	9	n/a
Fair value of RMPP assets	243	
Present value of RMPP liabilities	(144)	
Surplus in plan	99	

Share of RMSEPP	Market value 2013 £m	Long term expected rate of return 2013 % pa
Equities	146	n/a
Bonds	193	n/a
Property	19	n/a
Other assets	3	n/a
Fair value of plan assets for RMSEPP	361	
Present value of plan liabilities for RMSEPP	(347)	
Surplus in plan for RMSEPP	14	
Surplus in plan for the POL share (at approximately 7%) of RMSEPP	1	

A retirement benefit surplus of £97m is disclosed on the balance sheet, representing the surplus in plans of £99m and £1m for RMPP and RMSEPP respectively, and net of tax of £3m at a rate of 35% on the element of the surplus which is recoverable through a refund from the plans.

	Market value 2012 £m	Market value 2011 £m	Long term expected rate of return 2012 % pa	Long term expected rate of return 2011 % pa
Combined plans				
Equities	3,385	4,268	7.7	8.2
Bonds	25,610	21,409	5.7	6.2
Property	1,417	1,590	6.8	6.5
Other assets	333	418	3.4	4.2
Fair value of plans' assets for the combined plans	30,745	27,685		
Present value of plans' liabilities for the combined plans	(33,667)	(32,186)		
Deficit in schemes for the combined plans	(2,922)	(4,501)		
Deficit in schemes for share (at approximately 7%) of combined plans	(206)	(316)		

There is no element of the above present value of liabilities that arises from plans that are wholly unfunded.

## Post Office Limited

**c) Movement in plans' assets and liabilities**

Changes in the fair value of the plans' assets are analysed as follows:

<b>Assets</b>	<b>Sectionalised RMPP 2013 £m</b>
Assets in sectionalised RMPP at beginning of period	2,108
Transfer of pension assets to government	(1,953)
Contributions paid	25
Employee contributions paid	8
Finance income (expected rate of return)	11
Actuarial gains (additional increases in market values)	43
Benefits paid to members	(2)
<b>Assets in sectionalised RMPP at end of period</b>	<b>240</b>

<b>Assets</b>	<b>Share of RMSEPP 2013 £m</b>
Share of assets in RMSEPP at beginning of period	21
Contributions paid	2
Movement in contributions accrued	-
Employee contributions paid	-
Finance income (expected rate of return)	1
Actuarial gains (additional increases in market values)	1
Benefits paid to members	-
<b>Share of assets in RMSEPP at end of period</b>	<b>25</b>

Assets combined plans	2012 £m	2011 £m
Share of assets in combined plans at beginning of period	1,923	1,797
Contributions paid	26	46
Movement in contributions accrued	(3)	2
Employee contributions paid	10	11
Finance income (expected rate of return)	124	120
Actuarial gains (additional increases in market values)	131	33
Benefits paid to members	(82)	(86)
<b>Share of assets in combined plans at end of period</b>	<b>2,129</b>	<b>1,923</b>

Changes in the present value of the defined benefit pension obligations are analysed as follows:

<b>Liabilities</b>	<b>Sectionalised RMPP 2013 £m</b>
Liabilities in sectionalised RMPP at beginning of period	(2,313)
Transfer of pension liabilities to government	2,239
Current service cost	(24)
Curtailed costs*	(2)
Finance cost	(9)
Employee contributions	(8)
Actuarial loss (recognised in statement of comprehensive income)	(29)
Benefits paid	2
<b>Liabilities in sectionalised RMPP at end of period</b>	<b>(144)</b>

## Post Office Limited

<b>Liabilities</b>	<b>Share of RMSEPP 2013 £m</b>
Share of liabilities in RMSEPP plans at beginning of period	<b>(22)</b>
Current service cost	-
Curtailment costs*	-
Finance cost	<b>(1)</b>
Employee contributions	-
Actuarial gain/(loss) (recognised in statement of comprehensive income)	<b>(1)</b>
Benefits paid	-
<b>Share of liabilities in RMSEPP at end of period</b>	<b>(24)</b>

Liabilities combined plans	2012 £m	2011 £m
Share of liabilities in combined plans at beginning of period	(2,239)	(2,361)
Current service cost	(23)	(25)
Curtailment costs*	-	(3)
Finance cost	(122)	(132)
Employee contributions	(10)	(11)
Actuarial gain/(loss) (recognised in statement of comprehensive income)	(23)	207
Benefits paid	82	86
<b>Share of liabilities in combined plans at end of period</b>	<b>(2,335)</b>	<b>(2,239)</b>

\*The curtailment costs in the profit and loss account are recognised on a consistent basis with the associated compensation costs. Estimates of both are included, for example, in any redundancy provisions raised. The curtailment costs above represent the costs associated with those people paid compensation in respect of redundancy during the accounting period. Such payments may occur in an accounting period subsequent to the recognition of costs in the income statement.

**d) History of experience gains and losses**

The cumulative amount of actuarial gains and losses recognised since transition to IFRS as adopted by the European Union at 26 March 2012 in the consolidated statement of comprehensive income is a gain of £14m.

	<b>Sectionalised RMPP</b>	<b>Share of RMSEPP</b>	7% share of combined plans			
	<b>2013 £m</b>	<b>2013 £m</b>	2012 £m	2011 £m	2010 £m	2009 £m
Fair value of assets	<b>243</b>	<b>25</b>	2,168	1,944	1,811	1,407
Present value of liabilities	<b>(144)</b>	<b>(24)</b>	(2,374)	(2,260)	(2,375)	(1,882)
Surplus/(Deficit) in schemes	<b>99</b>	<b>1</b>	(206)	(316)	(564)	(475)
Experience adjustment on assets	<b>46</b>	<b>1</b>	131	33	313	(384)
Experience adjustment on liabilities	<b>(20)</b>	-	-	(1)	47	(1)
	<b>2013 %</b>	<b>2013 %</b>	2012 %	2011 %	2010 %	2009 %
Experience adjustment on assets as a % of scheme assets	<b>18.9</b>	<b>5.5</b>	6.1	1.7	17.4	(27.3)
Experience adjustment on liabilities as a % of scheme liabilities	<b>(13.9)</b>	<b>1.4</b>	0.0	0.0	(2.0)	0.1
Deficit in the scheme as a % of scheme liabilities	-	-	8.8	14.1	23.9	25.3

## Post Office Limited

**e) Recognised charges**

An analysis of the separate components of the amounts recognised in the performance statements of the Company is as follows:

	<b>2013 sectionalised RMPP £m</b>
<b>Analysis of amounts recognised in the income statement</b>	
<b>Analysis of amounts charged to operating profit before exceptional items:</b>	
Current service cost	24
<b>Total charge to operating profit before exceptional items</b>	
<b>Analysis of amounts charged to operating exceptional items:</b>	
Loss due to curtailments (within provision – note 11)	2
<b>Total charge to operating profit</b>	
<b>Analysis of amounts charged/(credited) to net pensions interest:</b>	
Interest on plan liabilities	9
Expected return on plan assets	(11)
<b>Net pensions credit to financing</b>	
<b>Net charge to the income statement before deduction for tax</b>	
<b>Analysis of amounts recognised in the statement of comprehensive income</b>	
Transfer of pension liabilities to government	2,239
Transfer of pension assets to government	(1,953)
Gain on transfer to government	286
Actual return on plan assets	57
Less: expected return on plan assets	(11)
Less: taxation on surplus recoverable through plan refunds	(3)
Actuarial gains on assets (all experience adjustments)	43
Experience adjustments on liabilities	(20)
Effects of changes in actuarial assumptions on liabilities	(9)
Actuarial losses on liabilities	(29)
<b>Total actuarial gains recognised in the statement of comprehensive income</b>	

## Post Office Limited

	2013 share of RMSEPP £m
<b>Analysis of amounts recognised in the income statement</b>	
<b>Analysis of amounts charged to operating profit before exceptional items:</b>	
Current service cost	1
<b>Total charge to operating profit before exceptional items</b>	
<b>Analysis of amounts charged to operating exceptional items:</b>	
Loss due to curtailments (within provision for organisational review – note 11)	-
<b>Total charge to operating profit</b>	
<b>Analysis of amounts charged/(credited) to net pensions interest:</b>	
Interest on plan liabilities	16
Expected return on plan assets	(18)
<b>Net pensions interest</b>	
	(2)
<b>Share of net pensions interest (at approximately 7%)</b>	
	-
<b>Net charge to the income statement before deduction for tax</b>	
	-
<b>Analysis of amounts recognised in the statement of comprehensive income in the Royal Mail Holdings Group financial statements</b>	
Actual return on plan	38
Less: expected return on plan	(18)
Actuarial gains on assets (all experience adjustments)	20
Experience adjustments on liabilities	5
Effects of changes in actuarial assumptions on liabilities	(23)
Actuarial losses on liabilities	(18)
<b>Total actuarial gains recognised in statement of comprehensive income in the Royal Mail Holdings Group financial statements</b>	
	2
<b>Share of actuarial gains/(losses) recognised in statement of comprehensive income (at approximately 7%)</b>	
	-

## Post Office Limited

Combined plans	2012 £m	2011 £m
<b>Analysis of amounts recognised in the income statement</b>		
<b>Analysis of amounts charged to operating profit before exceptional items:</b>		
Current service cost	23	25
<b>Total charge to operating profit before exceptional items</b>	<b>23</b>	<b>25</b>
<b>Analysis of amounts charged to operating exceptional items:</b>		
Loss due to curtailments (within provision for organisational review – note 11)	-	2
<b>Total charge to operating profit</b>	<b>23</b>	<b>27</b>
<b>Analysis of amounts charged/(credited) to net pensions interest:</b>		
Interest on plans' liabilities for the combined plans	1,749	1,881
Expected return on plans' assets for the combined plans	(1,775)	(1,714)
<b>Net pensions interest for the combined plans</b>	<b>(26)</b>	<b>167</b>
<b>Share of net pensions interest (at approximately 7%)</b>	<b>(2)</b>	<b>12</b>
<b>Net charge to the income statement before deduction for tax</b>	<b>21</b>	<b>39</b>
<b>Analysis of amounts recognised in the statement of comprehensive income in the Royal Mail Holdings Group financial statements</b>		
Actual return on plans' assets for the combined plans	3,644	2,184
Less: expected return on plans' assets for the combined plans	(1,775)	(1,714)
Actuarial gains on assets for the combined plans (all experience adjustments)	1,869	470
Experience adjustments on liabilities for the combined plans	(5)	(8)
Effects of changes in actuarial assumptions on liabilities for the combined plans	(320)	2,962
Actuarial (losses)/ gains on liabilities for the combined plans	(325)	2,954
<b>Total actuarial gains recognised in statement of comprehensive income in the Royal Mail Holdings Group financial statements</b>	<b>1,544</b>	<b>3,424</b>
<b>Share of actuarial gains/(losses) recognised in statement of comprehensive income (at approximately 7%)</b>	<b>108</b>	<b>240</b>

**13. Called up share capital**

	2013 £	2012 £
<b>Authorised</b>		
Ordinary shares of £1 each	<b>51,000</b>	51,000
Total	<b>51,000</b>	51,000
<b>Allotted and issued</b>		
Ordinary shares of £1 each	<b>50,003</b>	50,003
Total	<b>50,003</b>	50,003

## Post Office Limited

## 14. Reserves

	Share premium £m	Retained earnings £m	2013 Total £m
<b>Balance at 26 March 2012</b>	465	(589)	<b>(124)</b>
Profit for the financial year	-	74	<b>74</b>
Actuarial gains on defined benefit pension schemes	-	14	<b>14</b>
Taxation on items taken directly to equity	-	(21)	<b>(21)</b>
Transfer of pension deficit to government	-	286	<b>286</b>
<b>At 31 March 2013</b>	<b>465</b>	<b>(236)</b>	<b>229</b>

## Post Office Limited

### Corporate information

**Registered Office**

Post Office Limited  
148 Old Street  
LONDON  
EC1V 9HQ

**Auditor**

Ernst & Young LLP  
1 More London Place  
LONDON  
SE1 2AF

**Solicitor**

Linklaters LLP  
One Silk Street  
LONDON  
EC2Y 8HQ

**Actuary**

Towers Watson Limited  
Watson House  
London Road  
REIGATE  
Surrey  
RH2 9PQ

**Consumer Body**

Consumer Focus  
4th Floor  
Artillery House  
Artillery Row  
London  
SW1P 1RT



# The fabric of our society

Annual Report and Accounts 2013

Internal Revenues - m)

,270

2:1,160

Operating profit - m)

51

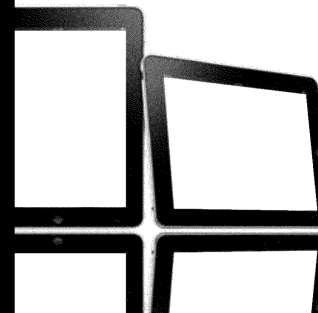
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Post Office branches

1,820

2:11,818

- Revenue increased in 2012/13 by £xx million to £1,xxx million, with growth in our Mails, Retail and Financial Services businesses
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For more information visit  
our online annual report at  
[www.postoffice/ar2013.com](http://www.postoffice/ar2013.com)

## Who we are

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**3 million**

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**£2.3bn**

The amount of social value we have delivered to businesses and the public according to an independent study

**93.1%**

The percentage of people in the UK living within a mile of a Post Office

**6,000**

The number of branches to be transformed in the next three years

**20 million**

The number of people who visit a Post Office every week

**90%**

The percentage of our customers who say they are satisfied with our services



# Chairman's statement

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### Overview

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**GRO**

Alice Perkins  
Chairman

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### A year of significant progress

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### Post Office network

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### Heading

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### Harum fuga (Em)

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### Car insurance claims

+16%



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### Insurance programme

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### Financial Services

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### Outlook

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### Life insurance sales

+21%



### Ipsum berehendi blaut

12,112

2012: 11.124

# Chief Executive's review

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## Overview

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**GRO**

Paula Vennells  
Chief Executive

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## A year of significant progress

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## Post Office network

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## Heading

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**98**

2012:1160

## Car insurance claims

**+16%**



## Stable growth

**£2,147** +03%

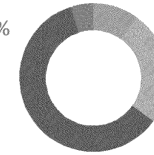


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## Quiaspe audam

**£1,398** +12%



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## Renisation programme

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## Financial Services

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## Life insurance sales

**+21%**



## Ipsum berehendi

**12,112**

2012:11124

# Business at a glance

## Government services



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**1.2 million**  
2012: 0.9 million

### Overview

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To read more about Government Services go to page xx

## Mails and retail



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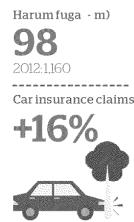
**3 million**  
2012: 2.1 million

### Overview

- Evellabo repudanda cus as volutem acil iur quidebi tatur, invenis moluptas demodi descium quatios tiscidessunt quuntot atquas cullaboris quaes eniti unt es eumquid maximo maximamaximusa cumquo vollest, sum quiatit ditat.
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To read more about Government Services go to page xx



## Financial services



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**0.1 million**  
2012: 0.01 million

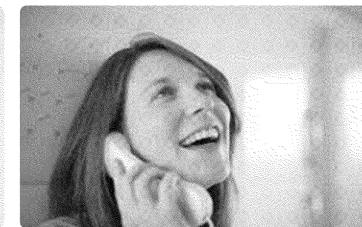
### Overview

- Evellabo repudanda cus as volutem acil iur quidebi tatur, invenis moluptas demodi descium quatios tiscidessunt quuntot atquas cullaboris quaes eniti unt es eumquid maximo maximamaximusa cumquo vollest, sum quiatit ditat.
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To read more about Government Services go to page xx

## Telephony



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Quiaspe audam

**6 million**  
2012: 3.1 million

### Overview

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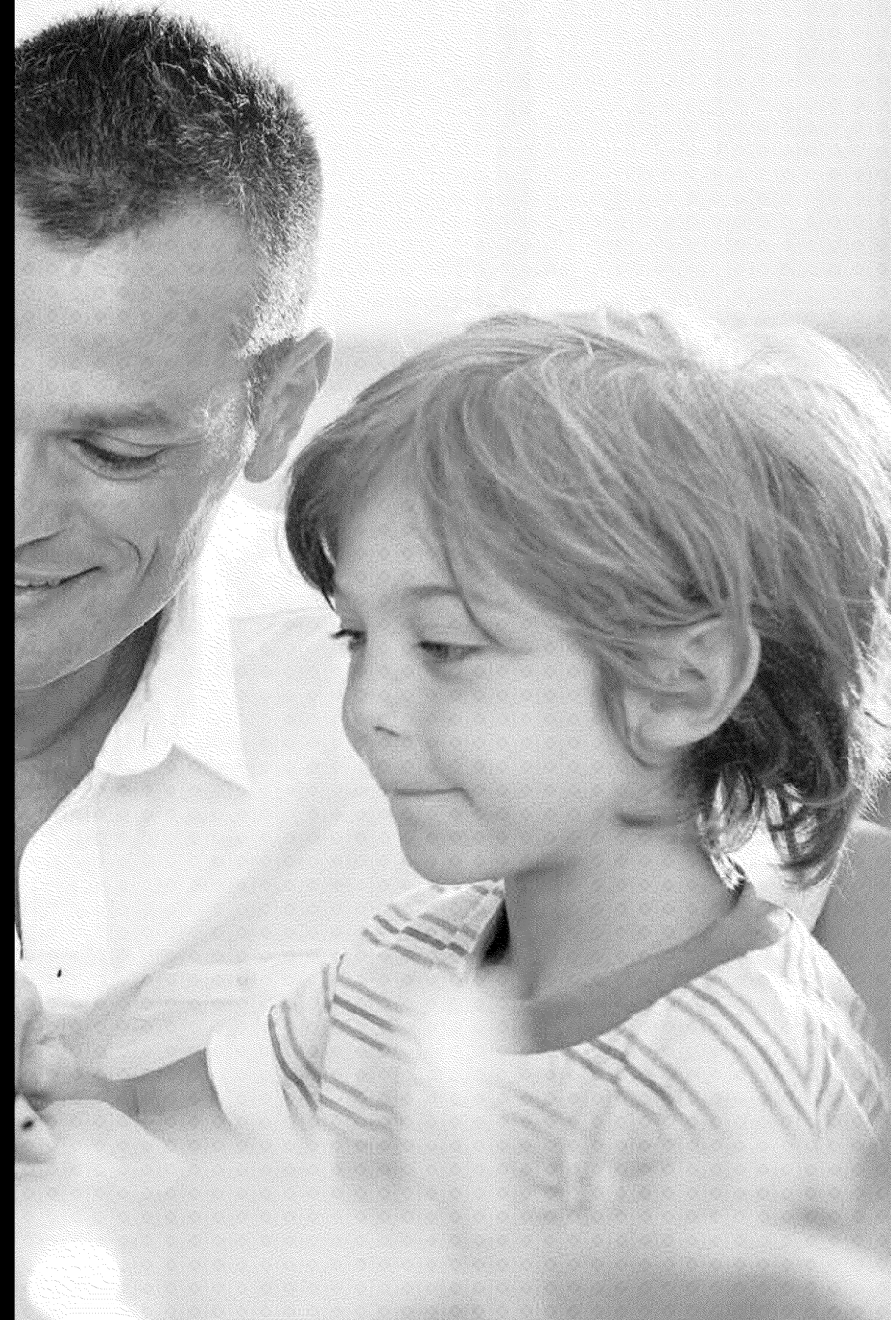


To read more about Government Services go to page xx



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## Our people

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### Improving career management

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### Safety: an enduring priority

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### Developing skills for a changing business

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### The Post Office Apprenticeship scheme

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“The apprenticeship is a good way of entering the engineering environment. I'm looking forward to working my way up.”

Alexandra Allsop  
Programme participant

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# Board of Directors



## Consolidated income statement

	Note	2012 £m	2011 £m
<b>Non-current assets</b>			
Goodwill	11	58.2	69.7
Distribution rights	12	132.8	124.0
Other intangible assets		50.8	45.5
Property, plant and equipment		26.4	28.4
Interests in joint ventures and associates	13	28.9	34.0
Investments		4.4	2.5
Deferred tax assets		9.4	22.9
Derivative financial assets		1.2	1.0
		312.1	328.0
<b>Current assets</b>			
Programme rights and other inventories	14	104.8	83.5
Trade and other receivables		296.5	285.8
Derivative financial assets		2.6	3.5
Cash and cash equivalents		31.1	63.1
Assets classified as held for sale		11.9	44.4
		446.9	480.3
<b>Total assets</b>		<b>759.0</b>	<b>808.3</b>

## Group statement of total recognised gains and losses

	Note	2012 £m	2011 £m
<b>Non-current assets</b>			
Goodwill	11	58.2	69.7
Distribution rights	12	132.8	124.0
Other intangible assets		50.8	45.5
Property, plant and equipment		26.4	28.4
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Cash and cash equivalents		31.1	63.1
Assets classified as held for sale		11.9	44.4
		446.9	480.3
<b>Total assets</b>		<b>759.0</b>	<b>808.3</b>

## Group balance sheet

	Note	2012 £m	2011 £m
<b>Current assets</b>			
Goodwill	11	58.2	69.7
Distribution rights	12	132.8	124.0
Other intangible assets		50.8	45.5
Property, plant and equipment		26.4	28.4
Interests in joint ventures and associates	13	28.9	34.0
Investments		4.4	2.5
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Trade and other receivables		296.5	285.8
Derivative financial assets		2.6	3.5
Cash and cash equivalents		31.1	63.1
Assets classified as held for sale		11.9	44.4
		446.9	480.3
<b>Total assets</b>		<b>759.0</b>	<b>808.3</b>
<b>Current liabilities</b>			
Interest-bearing loans and borrowings	15	30.5	20.1
Trade and other payables		372.0	363.4
Income tax liabilities		2.4	8.7
Provisions		2.5	7.2
Derivative financial liabilities		1.8	5.0
Assets relating to assets held for sale		-	36.5
		409.2	440.9
<b>Current liabilities</b>			
Interest-bearing loans and borrowings	15	65.0	95.3
Trade and other payables		3.0	9.9
Provisions		9.7	11.4
Derivative financial liabilities		4.5	4.2
Income tax liabilities		5.6	15.3
		87.8	136.1
<b>Total liabilities</b>		<b>497.0</b>	<b>577.0</b>
<b>Assets</b>		<b>262.0</b>	<b>231.3</b>
<b>Equity</b>			
Share capital		0.2	0.2
Reserve		1.2	0.8
Retention reserve		34.1	33.0
Retained earnings		219.3	190.8
Attributable to owners of the parent company		254.8	224.8
Controlling interests		7.2	6.5
<b>Equity</b>		<b>262.0</b>	<b>231.3</b>

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Thanks to.....	Post Office Limited
	Annual Report 2013
	Strapline introducing the theme

OBC

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Client  
Post Office Limited

Project  
Annual Report 2013

Job no.

Date  
25 April 2013

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- Financial	
- Operational	

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Karen Hamer	Karen Hamer

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**Post Office Limited**  
**Audit, Risk and Compliance Board Sub-Committee**  
**Briefing Book**  
**Full Year ended 31 March 2013**

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## 1 Glossary review

Below is a listing of key abbreviations used throughout this document with the full meaning given:

<b>Abbreviation</b>	<b>Meaning</b>
ATM	Automated teller machine
BIS	Department for Business Innovation & Skills
CWU	Communications Workers Union
DVLA	Driver & Vehicle Licensing Authority
DWP	Department of Work & Pensions
Eagle	Deal in August 2012 to sell POFS to the Bank of Ireland, restructure commission rates for personal financial services and extend the contract to 2023
FOoG	Front Office of Government
FRES	First Rate Exchange Services
Gamma	A contract variation made in 2007 with POFS generating £100m cash and income over a number of years in return for a series of commitments through to 2020
Horizon	Horizon Next Generation- Counter system
JV	Joint venture
LTIP	Long Term Incentive Programme
NBV	Net Book Value
NS&I	National Savings & Investments
NSP	Network Subsidy Payment
NTP	Network Transformation Programme
POCA	Post Office Card Account
PFS	Personal Finance Services
POFS	Post Office Financial Services
POOC	Project One Off Costs
RMPP	Royal Mail Pension Plan
RMSEPP	Royal Mail Senior Executive Pension Plan
RMDCP	Royal Mail Defined Contribution Plan
SGEI	Services of General Economic Interest
UKBA	United Kingdom Borders Agency

## **2. Introduction**

This Briefing Book has been prepared to explain the Post Office Limited results for the year ended 31 March 2013. It is a summary of the key data, trends and analyses to be read in conjunction with the Annual Report & Financial Statements, which readers may find useful to further their own understanding of the results for 2012-13. Post Office Limited has opted not to take advantage of the Companies Act exemption from the preparation of consolidated accounts as it is a wholly owned subsidiary within the Royal Mail Holdings plc group which prepares group accounts. The Annual Report & Financial Statements therefore report consolidated results.

Most of the analyses are based on the comparison of this year's actual results to prior year. This year consists of 53 weeks (2012 was 52 weeks).

Comparison against budget is discussed in the Monthly Performance Report presented to the Post Office Limited Board on a monthly basis.

## **3. Accounting policies**

This is the first year that Post Office Limited has reported its results since operating independently and it has been decided to report under International Financial Reporting Standards (IFRS). The changes to accounting policies and disclosures, which have been necessary as part of the transition to reporting under IFRS as adopted by the European Union, have had no effect on the income statement or net asset position.

## 4. Primary Statements

### 4.1 Post Office Limited Consolidated Income Statement.

#### Post Office Limited Consolidated income Statement for the year ended 31 March 2013 and 25 March 2012

	Section	2012-13 £m	2011-12 £m
Continuing operations			
Turnover		1,024	980
Network Subsidy Payment		210	180
Revenue	6	1,234	1,160
People Costs	7.2	(259)	(254)
Subpostmasters costs	7.2.4	(478)	(483)
Other operating costs	7.3	(435)	(393)
Share of post tax profit from joint venture and associates		32	31
Operating profit before operating exceptional items	5	94	61
Operating exceptional items	10	(47)	(38)
Operating profit		47	23
Profit on disposal of fixed assets	10	2	1
Loss on sale of associate	10	(30)	
Profit before financing and taxation		19	24
Net interest payable	11.1	(4)	(7)
Finance income		1	1
Net pensions interest		2	2
Profit before taxation		18	20
Taxation credit		31	10
Profit for the financial year from continuing operations		49	30

## 4.2 Post Office Limited Consolidated Cashflow Statement

**Post Office Limited consolidated cashflow statement for the full year to 31 March 2013**

	Notes	2013 £m	2012 £m
<b>Cash flows from operating activities</b>			
Operating profit before exceptional items		94	61
Adjustment for:			
Depreciation and amortisation		-	1
Share of profit from joint ventures and associates	14.3	(32)	(31)
Pension operating costs		25	24
Working capital movements:		71	24
(Increase)/Decrease in trade and other receivables		(138)	11
Increase in trade and other payables		207	15
(Increase) in inventories		(2)	-
Increase/(Decrease) in non-exceptional provisions		4	(2)
Pension operating costs paid		(26)	(27)
Cash payments in respect of operating exceptional items:		133	(27)
Business transformation		(44)	(12)
Government grant		200	-
Restructuring costs		(11)	(15)
Other		(12)	-
Net cash inflow from operating activities		265	25
Income tax recovered		11	12
<b>Cash flows from investing activities</b>			
Investment in associate		(11)	-
Dividends received from joint ventures and associates	14.3	40	38
Finance income received		1	-
Proceeds from sale of property, plant and equipment		2	2
Proceeds from disposal of associate		2	-
Purchase of property, plant and equipment		(66)	(33)
<b>Net cash (outflow)/inflow from investing activities</b>		<b>(32)</b>	<b>7</b>
<b>Net cash inflow before financing activities</b>		<b>244</b>	<b>44</b>
<b>Cash flows from financing activities</b>			
Finance costs paid		(3)	(4)
Payments to finance lease creditors		(3)	(3)
(Repayment)/proceeds from bank borrowings		(86)	2
<b>Net cash (outflow) from financing activities</b>		<b>(92)</b>	<b>(5)</b>
<b>Net increase in cash and cash equivalents</b>		<b>152</b>	<b>39</b>
Effect of exchange rates on cash and cash equivalents		(1)	(1)
Cash and cash equivalents at the beginning of the year		820	782
<b>Cash and cash equivalents at the end of the year</b>	11.2	<b>971</b>	<b>820</b>

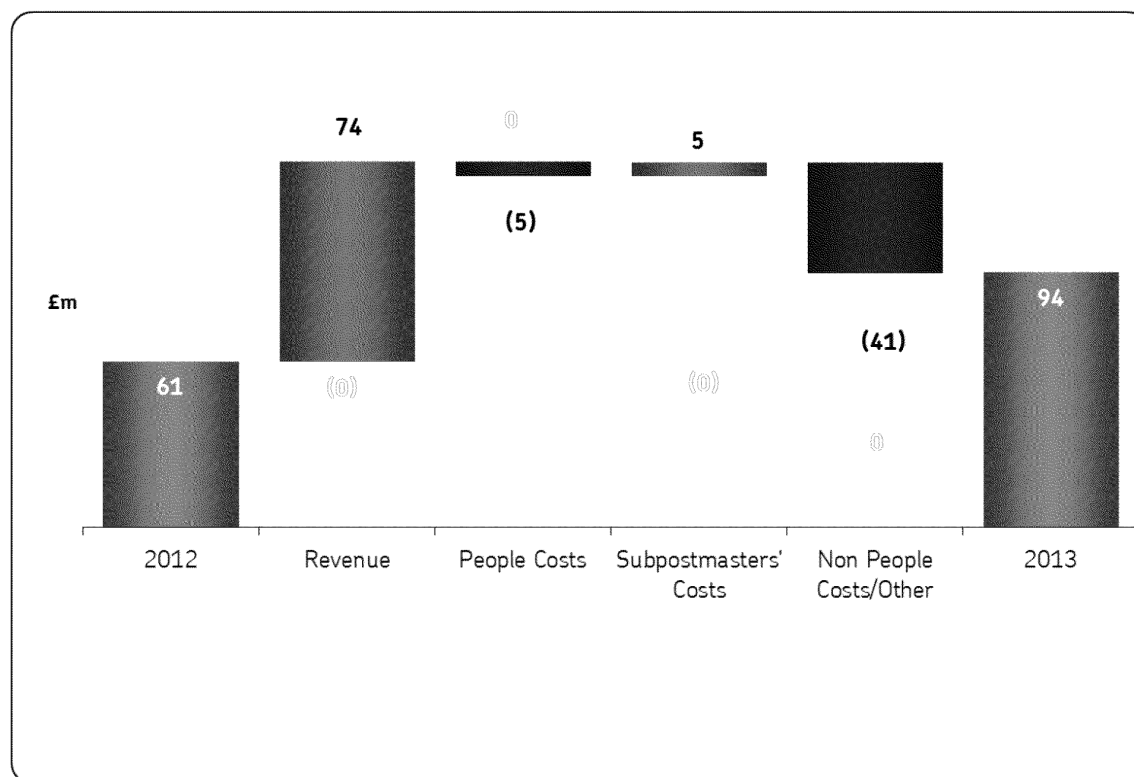
## 4.3 Post Office Limited Consolidated Balance Sheet

**Post Office Limited consolidated balance sheet at 31 March 2013 and 25 March 2012 and 28 March 2011**

	Notes	2013 £m	2012 £m	2011 £m
<b>Non-current assets</b>				
Intangible assets		-	-	-
Property, plant and equipment	13	11	11	12
Investments in joint ventures and associates	14.1	60	89	96
Retirement benefit surplus		97	-	-
<b>Total non-current assets</b>		<b>168</b>	100	108
<b>Current assets</b>				
Inventories	15.1	8	6	5
Trade and other receivables	15.2	362	226	241
Cash and cash equivalents	11.2	971	820	782
Financial assets – derivatives		1	-	-
<b>Total current assets</b>		<b>1,342</b>	1,052	1,028
<b>Total assets</b>		<b>1,510</b>	1,152	1,136
<b>Current liabilities</b>				
Trade and other payables	15.3	(898)	(583)	(579)
Financial liabilities – interest bearing loans and borrowings	11.2	(291)	(377)	(375)
– obligations under finance leases	11.2	(3)	(4)	(4)
Provisions	16	(19)	-	-
<b>Total current liabilities</b>		<b>(1,211)</b>	(964)	(958)
<b>Non-current liabilities</b>				
Financial liabilities – obligations under finance leases	11.2	(4)	(6)	(9)
Other payables		-	(2)	(5)
Provisions	16	(7)	(14)	(26)
Retirement benefit obligation		-	(206)	(316)
<b>Total non-current liabilities</b>		<b>(11)</b>	(228)	(356)
<b>Net assets/(liabilities)</b>		<b>288</b>	(40)	(178)
<b>Equity</b>				
Share capital		-	-	-
Share premium		465	465	465
Retained earnings		(179)	(552)	(690)
Other Reserves		2	47	47
<b>Total equity/(deficit)</b>		<b>288</b>	(40)	(178)

## 5. Operating profit

### 5.1 Operating profit bridge analysis



### 5.2 Explanations for key movements are as follows:

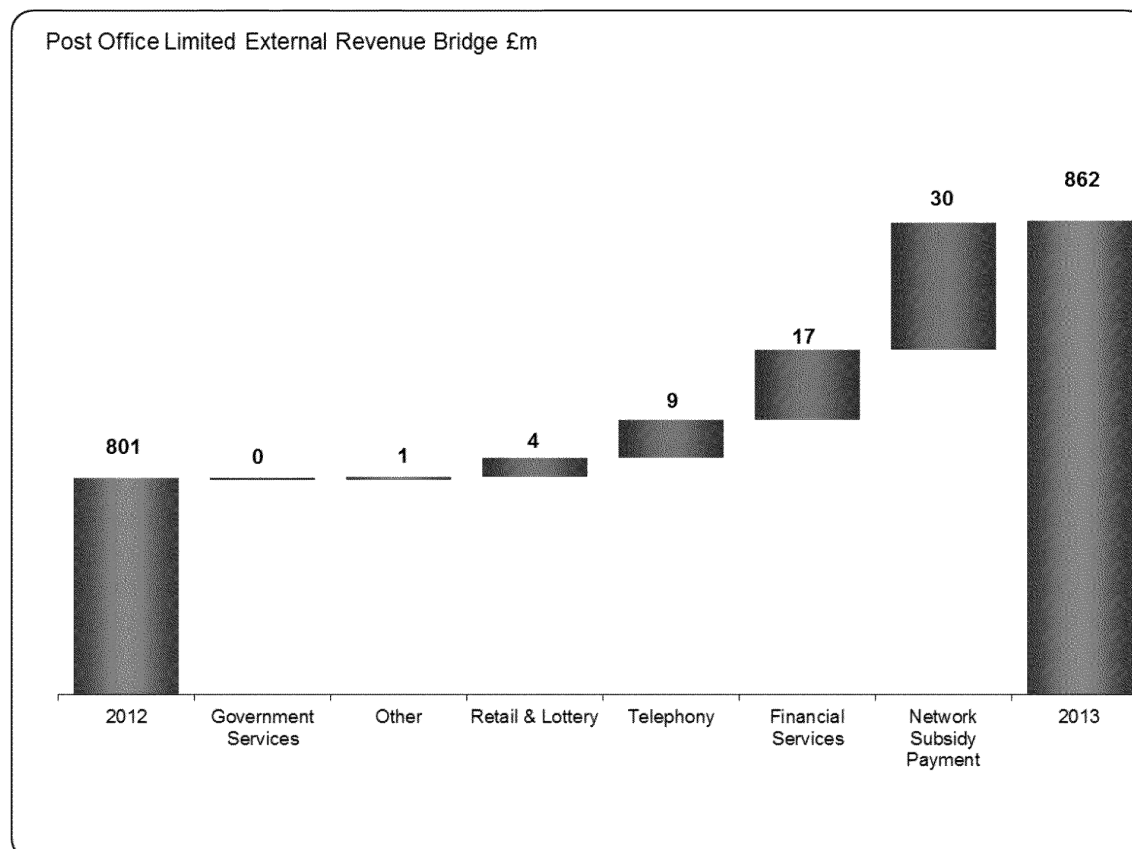
- Revenue explanation is in section 6.
- The £5.4m increase in People costs was mainly due to:
  - Higher wages and salaries and NI costs of £5.2m due to pay awards, increased use of people, both temporary and permanent such as F0oG and the new Communications Directorate and the impact of the 53<sup>rd</sup> week,
  - Higher pension costs of £1.4m due to the higher IAS19 rate,
  - Higher temporary resource costs of £2.1m driven by modernisation and separation programmes, and higher agency labour in Network prior to change implementation. Year on year the headcount figure has increased by 88, primarily due to the NTP programme,
  - This was offset by lower productivity & bonus costs of £3.8m, largely due to long term incentive scheme costs over accrued in the prior year by £1.9m and corrected in 2012-13.
- Subpostmasters' costs were £4.8m lower than last year, this includes decreases in fixed costs arising from the introduction of new network models.
- Non people costs/other (including project one off costs) were higher by £40.5m mainly due to:
  - £26.3m higher project one off costs (POOC), (see section 7.3.15),
  - Last year's compensation costs included a £2.4m release relating to WHS TUPE transfers,

- £3.5m increase in marketing and legal fees (after offsetting the £10m skills group costs within the People and Agent Related line) due to marketing costs of £2.2m relating to brand development, and legal costs of £1.3m relating to primarily to separation and modernisation programmes,
- £4.3m increase in property facilities and maintenance costs, due work transferred in post separation and increased rates relating to a higher number of ATM machines,
- £6.9m higher cost of sales was mainly driven by increased Telephony bandwidth costs and higher UKBA volumes as a result of rolling out more ID Services terminals, and also due to higher Retail costs due to the Olympic and Jubilee collectables,
- This was offset by £5.0m lower Group overheads costs as a result of separation.

## 6. Revenue

	2012-13 £m	2011-12 £m	Variance £m
External Revenue	862	801	61
Internal Revenue	372	359	13
<b>Total Revenue</b>	<b>1,234</b>	<b>1,160</b>	<b>74</b>

### 6.1 Post Office Limited – External revenue analysis



The increase in year on year external revenue of £61m (7%) to £862m (2011 £801m) is driven by the £30m increase in the Network Subsidy Payment, and an increase of £31m in like for like income.

The following commentary gives further detail on the external revenue variances by category:

#### 6.1.1 Financial Services

Financial Services income has increased by £16.5m (6.2%) year on year. This continues the trend of increases in new products offsetting the decline of traditional products. The main variances are:

- a £23.7m increase in PFS savings products (Online Saver, Growth Bonds, Reward Saver and Instant Saver- £6.5m, £6.4m, £4.5m and £3.0m favourable respectively).

This includes the benefit of the renegotiated commission rates following the 'Eagle' deal, and

- a £0.9m increase in ATM revenue, driven by increased volumes as machines reach maturity and the rollout of new machines.

This was offset by

- a £3.3m decline in NS&I revenues as NS&I look to provide most of their products, particularly savings, through their own direct channel,
- a £1.6m net decrease in Banking revenue from:
  - a £4.0m fall from the DWP. Volumes continue to fall as the Government is migrating customers to other payment methods, offset by
  - a £0.2m increase in business banking revenues due to rate reduction from renegotiated contract, and
  - an increase of £2.2m in personal banking driven by the new RBS contract and adjustment in the prior year.
- A £2.1m decrease from Payment Services due to:
  - a £1.0m decline from bill payments, as utilities and other bill payment clients continue to migrate customers to other payment methods such as direct debit and online, and
  - a £2.7m decrease in Postal Order income (including write back of uncashed Postal Orders over 2 years old).

### 6.1.2 Telephony

The Telephony Services pillar includes the Post Office Homephone and Broadband services, as well as mobile top-up services and phonecards.

Telephony Services revenue of £129m (2012: £120m) has increased by £9m. Income from the Post Office Homephone and Broadband product rose by £10m, primarily due to higher customer numbers, following the introduction in May 2012 of more competitive service packages to attract and retain customers. Income from mobile top-ups was £2m below prior year, as transaction volumes declined due to the mobile networks actively migrating customers away from pre-pay, and also reducing their transaction fees. Despite this reduction in income, Post Office is still a significant player in the top-up market. Our share of the retail market has been maintained as we have seen a slower decline in volumes than many retailers.

### 6.1.3 Retail & Lottery

Retail and Lottery revenues have increased by £4.4m (9.5%):

- Lottery is £2.0m higher than last year, driven by the large amount of rollovers, new draws (Euromillions twice a week) and more terminals,
- Retail up £2.4m benefiting from collectibles for the Olympic and Paralympic games, as well as the Diamond Jubilee.

#### 6.1.4 Government Services

Government Services revenue is flat year on year but included the following movements:

- £2.6m higher Passport income due to both higher price and higher volumes,
- £5.5m higher AEI UKBA income as this is a new product,

This was offset by

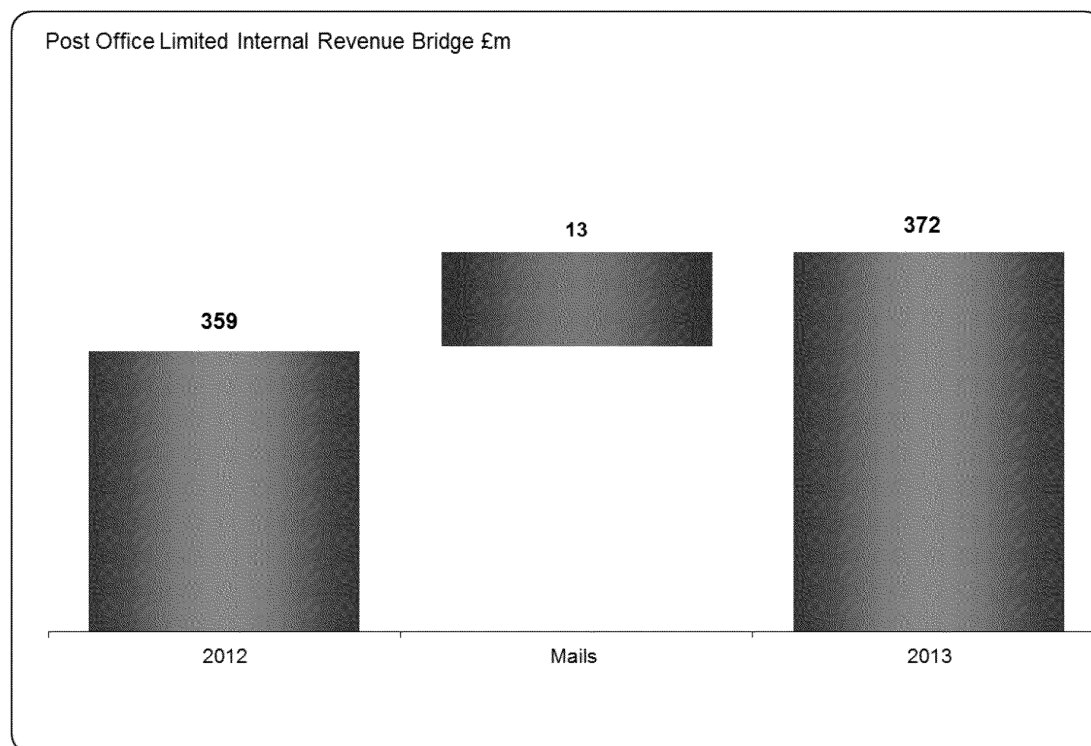
- £4.1m adverse variance from AEI DVLA, due to last year having a one off payment of £3.0m relating to service levels
- £4.2m adverse from falling numbers of POCA accounts, through natural attrition, migration of customers to bank accounts and lower commissions linked to lower LIBOR.

#### 6.1.5 Other

Year on year increase of £0.6m was primarily due to:

- Increased revenues from External Cash in transit services and the remainder from Gamma income.

## 6.2 Post Office Limited – Internal Revenue Analysis



## 6.2.1 Mails

The £13.0m (3.8%) increase in Mails Revenue is driven by strong volumes and the price increase in May 2012.

- Approximately £8.8m was driven by price, and £4.2m by volume increases.
- The new Mails Distribution Agreement resulted in a reduction in fixed fee of £30.3m, which is more than offset by increases in variable commissions across the product range.

Mails Income is analysed in the table below:

	2012-13	2011-12	Variance	Volume	Price
	£m	£m	£m	£m	£m
Special Delivery	53.2	53.3	(0.1)	0.7	(0.8)
Parcelforce 24/48	8.3	6.5	1.7	2.5	(0.7)
Labels	100.2	83.9	16.3	2.8	13.5
Stamps	35.2	31.8	3.4	(1.7)	5.2
Royal Mail Parcels	6.2	7.5	(1.3)	(0.4)	(1.0)
International Express & Non Express	34.9	29.9	5.0	(0.8)	5.8
Other Parcelforce	8.1	8.2	(0.1)	0.4	(0.5)
Other Royal Mail	37.8	19.4	18.4	0.7	17.7
Total Variable Income	283.9	240.6	43.3	4.2	39.0
Fixed Fee	74.4	104.7	(30.3)	-	(30.3)
Total Mails	358.3	345.3	13.0	4.2	8.8

## 7. Costs and People

This section discusses expenditure, excluding exceptionals.

### 7.1 Total Costs Analysis (excluding exceptionals)

The following provides a breakdown of costs for the year ending 31 March 2013 compared to the year ending 25 March 2012

	Section	2012-13 £m	2011-12 £m	Variance £m	
Expenditure - (pre- exceptional)					
Wages & Salaries		182	179	(3)	(2%)
Overtime		9	8	(1)	(15%)
Productivity/Bonus		15	19	4	20%
Employers NI		19	17	(2)	(12%)
Pensions		25	24	(1)	(6%)
Projects (temp people resource)		2	3	1	28%
Temporary Resource		7	5	(2)	(45%)
<b>PEOPLE COSTS</b>	<b>7.2.1</b>	<b>259</b>	<b>254</b>	<b>(5)</b>	<b>(2%)</b>
Subpostmasters' costs	7.2.4	478	483	5	1%
Collection, Delivery & Conveyance Charges	7.3.1	1	1	(0)	(12%)
Compensation	7.3.2	1	(2)	(3)	127%
Property Facilities	7.3.3	8	6	(2)	(39%)
Property Maintenance	7.3.4	6	4	(2)	(48%)
Vehicles	7.3.5	2	2	(0)	(10%)
Computers & Telephones	7.3.6	79	79	0	0%
Consultancy, Marketing & Legal Fees	7.3.7	27	13	(14)	(103%)
Staff & Agent Related Costs & Consumables	7.3.8	2	12	10	86%
Finance	7.3.9	16	16	0	0%
Cost of Sales	7.3.10	121	114	(7)	(6%)
Other Operating Costs	7.3.11	21	18	(3)	(16%)
Depreciation	7.3.12	0	0	0	6%
Interbusiness Expenditure	7.3.13	85	85	0	0%
Group Overheads	7.3.14	15	20	5	24%
Projects (excluding temporary people resource & IB)	7.3.15	50	24	(26)	(110%)
<b>Total Other Operating Costs</b>	<b>7.3</b>	<b>435</b>	<b>393</b>	<b>(42)</b>	<b>(11%)</b>
<b>TOTAL EXPENDITURE (Pre Exceptionals)</b>		<b>1172</b>	<b>1130</b>	<b>(42)</b>	<b>(4%)</b>

## 7.2 People Costs (2013 £259m vs 2012 £254m)

### 7.2.1 People costs (2013 £259m vs 2012 £254m)

People costs have increased in total by £5.4m (2.1%) to £259.3m, representing 22.1% (2012 22.5%) of the cost base. The number of people employed increased by 88 to 7,886 at 31 March 2013 (2012 7,798), primarily due to the Network Transformation Programme. NTP people costs are included within exceptional costs.

The people cost movement comprises:

- A total increase of £3.1m (2%) in Wages and Salaries an increase reflecting the impact of the agreed pay awards and the 53<sup>rd</sup> week.
- Overtime has increased by £1.2m (15%).
- Employers NI has increased by £2.1m (2%).
- Pension costs have increased by £1.4m (6%), as a result of a change in the IAS 19 rate for the RMPP service cost to 18.2% (2012 17.1%), driven by market conditions at 25 March 2012.
- Productivity costs have decreased by £3.8m (20%), largely due to long term incentive scheme costs over accrued in the prior year by £1.9m and corrected in 2012-13.
- Temporary resource costs have increased by £2.1m (45%), driven by recruitment to support various projects and higher agency labour in Network. This has been offset by a decrease in other project resource of £0.7m.

### 7.2.2 People Numbers

The following analysis shows the movements in the number of people employed during the year.

The People numbers were as follows:

	Period end employees		Average employees	
	31 March 2013	25 March 2012	2013	2012
Total employees	<b>7,886</b>	7,798	<b>7,842</b>	7,734

### 7.2.3 Average Cost Per Employee

The 2013 average number of employees for the year ending 31 March 2013 was 7,842 (2012 7,734). The average annual cost per employee (excluding exceptional costs and exceptional heads) based on these averages has increased by £1,415 (4.3%) to £34,000 (2012 £32,585) due to pay awards and recruitment.

## 7.2.4 Subpostmasters costs (2012 £478m vs 2011 £483m)

Total subpostmasters costs decreased by £4.7m (1%) due to the one off payment made in 2012 of £400 to all subpostmasters and this has offset the increase of £4.2m reflecting the increase in stamps tariff and increase sales.

There have been savings of £2.0m in fixed pay arising from the introduction of new local models and savings in VAT/Ni of £2.6m largely due to the improved VAT recoverable rate.

The average annual cost per subpostmaster branch (excluding VAT and Ni) is £43,727 (2011 £43,568). This is a 0.4% increase on the prior year.

	2012-13	2011-12
MAIN	178	25
LOCAL	329	177
Franchise	367	409
MSPO	580	603
SPSO	8,882	9,209
Locally Funded	11	12
Total Subpostmaster Branches	10,347	10,435
Outreach	939	888
Satellite	121	123
Crown	373	373
Total Branches	11,780	11,819

## 7.3 Other Operating Costs (2012 £435m vs 2011 £393m)

7.3.1 Collection, Delivery & Conveyance charges have generally remained flat year on year.

7.3.2 Compensation costs have increased by £3.0m, mainly due to a one off provision release relating to the CWU TUPE claim for the WHS transfers in 2011-12 of £2m.

7.3.3 Property Facilities costs have increased by £2.3m, due to a provision for ATM business rates £1.7m (see section 16) and electricity charges.

7.3.4 Property Maintenance costs have increased by £2.0m, due to the increased number of Post & Go machines requiring annual maintenance.

7.3.5 Vehicles costs have remained flat.

7.3.6 Computers and Telephones costs have decreased by £0.4m year on year. £1.5m is due to cheque processing now classified as other operating costs, therefore the underlying variance is an increase of £1.0m which is due to increased Prism charge.

7.3.7 Consultancy, Marketing & Legal Fees have increased by £13.8m. £10m of this is offset with the line staff and agent related costs below for Skills group off charges for the greater

project activity. The remainder relates to increased marketing costs and increased legal costs relating primarily to separation.

7.3.8 Staff & Agent Related Costs & Consumables have decreased by £10.3m. This needs to offset with the line above as £10m is due to Skills group off charging to projects. Other variances in this section were reduced training and printing costs.

7.3.9 Finance costs have remained flat.

7.3.10 Cost of Sales has increased by £6.9m (6%), driven by bandwidth payments of £5.4m for Telephony customers and £2.0m due to new UKBA volumes as a result of rolling out more ID Services terminals. The main reasons are detailed below:

Cost of Sales

	2013	2012	Variance		Comments
	£m	£m	£m	%	
Home Phone	85	79	(6)	(7%)	Increase bandwidth charges of £5m partly due to higher customers
Retail	5	4	(1)	(24%)	Increase sales due to collectable products for the Jubilee and the Olympics
Financial Services	1	3	2	52%	Decrease in Travel Insurance sales
AEI UKBA	30	28	(2)	(7%)	Increase due to higher UKBA volumes as a result of rolling out more ID Services terminals
<b>Total</b>	<b>121</b>	<b>114</b>	<b>(7)</b>	<b>(6%)</b>	

7.3.11 Other Operating costs have increased by £3.0m (16%) primarily due to reclassification of cheque processing costs. (see 7.3.6).

7.3.12 Depreciation costs have remained flat.

7.3.13 Interbusiness expenditure has remained flat and is detailed below:

Interbusiness	2012-13	2011-12	Variance
	£m	£m	£m
Official Mail	16	14	(2)
Call Centres	5	4	(1)
Facilities Management	15	17	2
Vehicle Services	6	6	0
Romec	10	8	(2)
Property	32	35	3
Other	1	1	0
<b>Total Interbusiness</b>	<b>85</b>	<b>85</b>	<b>0</b>

7.3.14 Group overhead expenditure has decreased by £4.8m due to separation as work transfers over to the Post Office.

7.3.15 Project expenditure (excluding temporary people resource and IB) has increased by £26.3m to £50.0m due to the acceleration of work towards full implementation of major transformation programmes. This includes Brand Marketing, IT Delivery, Finance Roadmap and Front Office of Government as well as the costs of separation from Royal Mail.

The £50m spent on projects is analysed below:

2012-13 Project Expenditure	£m
Customer Engagement (Brand & Mortgage Campaign)	18
Financial Services (Eagle -Sales Capability & Current Account)	6
FOoG (DVLA Tender & Home Office Development)	5
Telephony (Fixed Line Tender, Contract negotiations and Migration)	4
Independence (Legal & Consultancy)	3
Mails (Collections & Returns, Drop & Go Rollout, and Online Retail Shop)	3
Finance (Road Map)	2
HR & Compliance (Recruitment & Training)	2
IT Delivery (Salesforce Licences & Horizon Evolution)	2
Property ( Across Network & 148 Old Street Re-design Project)	2
Communications	1
London Games Programme	1
Supply Chain (ATM Replenishment & Joining the Scottish Notes Circulation Scheme)	1
Grand Total	50

## 8 Quality of Earnings

	2012-13	2011-12	Growth	
Post Office Limited (consolidated)	£m	£m	£m	%
Reported profit before other exceptional items	94	61	33	54%
Network Subsidy Payment	(210)	(180)	(30)	(17%)
Project one off costs (including temporary resource & interbusiness)	53	26	27	(104%)
Reported profit before project one off costs, exceptional items and NSP	(63)	(93)	30	32%
Litigation re 2007-08		(2)		
Release of savings stamps provision		(1)		
VAT/NI recovered re prior year Subpostmasters' fees	(1)	0		
VAT recovery re earlier years	(2)	2		
LTIP over -accrued in 2011-12	(2)	2		
Total adjustments	(5)	1		
Total	(68)	(92)	24	26%

This table shows underlying operating profit performance adjusted for one off items and items relating to previous years. Each item in the table is explained further below:

- 8.1 NSP has increased from £180m in 2011-12 to £210m in 2012-13 and has been accounted for as a government grant in both years.
- 8.2 Project one off costs. Project one off costs are non exceptional costs of project activity in the year. They increased in 2012-13 as work increased, particularly to build the brand and drive future revenue growth. These costs do not form part of the underlying ongoing performance of the company.
- 8.3 Litigation relating to 2007-08. This cost relates to a provision for litigation relating to the CWU challenge regarding the transfer of people to WH Smith during 2007-08. £6m was raised in 2008-09 and £4m of it released in 2009-10 when the CWU lost their initial challenge. All routes of challenge were exhausted during 2011-12 and the remaining £2m was released.
- 8.4 Release of savings stamps provision. Post Office Savings Stamps were found to be vulnerable to fraud and a provision was raised for potential fraudulent encashments made. They were withdrawn from sale in May 2010 and holders of savings stamps were encouraged to cash them. The level of encashment was less than anticipated and the provision was reduced substantially in 2010-11. Savings stamps continue to be cashed but the levels are low and the provision was further reduced during 2011-12.
- 8.5 VAT/NI recovered relating to Subpostmasters' fees is a correction of the VAT rate. VAT and NI claims are often completed a year or more after the year to which they relate. During 2012-13 £1.8m of VAT was recovered relating to 2011-12 following a rate change. £0.8m of NI was recovered relating to Subpostmasters' fees of which most related to 2011-12. During 2011-12 £1m of NI was recovered relating to 2010-11 and earlier.
- 8.6 VAT recovery re earlier years reflects the refund received following a correction of the recovery rate for 2011-12 during 2012-13.
- 8.7 Long term incentive scheme costs (LTIP) over accrued in the prior year by £1.9m and corrected in 2012-13.

## 9. Pensions

### 9.1 Background

The UK pension plans were sponsored by Royal Mail Group Limited until 1 April 2012 and are set out below. On 1 April 2012 almost all of the assets and liabilities of the Royal Mail Pension Plan (RMPP) were transferred to HM Government. On this date the RMPP was also sectionalised with Royal Mail Group Limited and Post Office Limited responsible for their own sections. Deferred pensioner members and pensioner members were transferred to the Government's new Royal Mail Statutory Pension Scheme. Royal Mail Group Limited is the principal employer in the Royal Mail Senior Executive Pension Plan (RMSEPP) and the Royal Mail Defined Contribution Plan (RMDCP). Post Office Limited became a participating employer in both with effect from 1 April 2012.

Royal Mail Pensions Trustees Limited manages the main defined benefit scheme Royal Mail Pension Plan (RMPP) which has around 5,200 Post Office active members.

Scheme	Eligibility	Type
Royal Mail Pension Plan (RMPP)	UK employees	Defined benefit
Royal Mail Senior Executive Pension Plan (RMSEPP)	UK senior executives (closed)	Defined benefit
Royal Mail Defined Contribution Plan (RMDCP)	UK employees	Defined contribution

A series of changes to RMPP began to take effect on 1 April 2008 as follows:

- the plan closed to new members from 31 March 2008;
- all pensions and benefits earned before 1 April 2008 are still linked to final salary at the time of retirement;
- from 1 April 2008, defined benefits building up for employee members of the plan are earned on a career salary basis;
- employees can continue to take their pension on reaching 60 but the normal retirement age increased to 65 for benefits earned from 1 April 2010; and
- since 1 April 2010 it has been possible to draw pension earned before the change to normal retirement at 60, and continue working while still contributing to the pension plan until the maximum level of benefits has been achieved.

A new defined contribution plan (RMDCP) was launched in April 2009. New recruits joining from 31 March 2008 are able to begin paying contributions to the new plan after they have worked for the Post Office for a year.

RMSEPP closed on 31 December 2012.

### 9.2 Pension Accounting within Post Office Limited

Since 1 April 2012, Post Office Limited employees are in a separate section of RMPP and the assets and liabilities are assessed independently. The Post Office Limited Directors are responsible for the selection of the pension assumptions for the Post Office section for the 2012-13 year. Details of these are in Section 9.3 below. The Post Office continues to account for a 7% share of RMSEPP in the same way as previously and as explained below.

Prior to 1 April 2012, the assets and liabilities of both of the defined benefit schemes, as measured under accounting standards, were reported as a net pension deficit in the consolidated balance sheet of Royal Mail Holdings plc, the ultimate parent company. The gross assets and liabilities and Post Office Limited's share of the net deficit were significant assets and liabilities. The Directors of Royal Mail Holdings plc were responsible for the selection of the pension assumptions for the 2011-12 year.

Before 1 April 2012 Royal Mail Group Limited had the legal relationship with the Trustees of the defined benefit schemes and, as such, the Trustees held Royal Mail Group Limited liable for the actuarial deficit in the schemes. However, under an agreement between Post Office Limited and Royal Mail Group Limited, Royal Mail Group Limited provided employees engaged in the business of Post Office Limited. Post Office Limited met the full costs of employment, and was responsible for the funding of the pension deficit attributable to these employees. Consequently, Post Office Limited recognised a balance sheet deficit on full adoption of FRS 17 and its international equivalent, IAS 19. This was based on employee numbers over 12 years and represented approximately 7% of the total balance sheet deficit (pre deferred tax) at that time. The net pensions interest, deficit recovery payments and actuarial gains or losses were also allocated on this basis, giving the Post Office approximately 7% of the total balance sheet deficit (pre deferred tax) at the balance sheet date. The current service cost, regular future service contributions and curtailments were computed separately for Royal Mail Group Limited and Post Office Limited, based on common factors/rates.

### 9.3 Assumptions

IAS 19 requires a number of assumptions. The choice of assumptions used for the calculations is the responsibility of the Directors, based upon advice given by an independent actuary. The assumptions cover price inflation, discount rate, salary increases and increases to pensions in deferment and payment. The key assumptions based on market conditions at 31 March 2013 are set out in the table below. The assumptions for the year ended 25 March 2012 and earlier years, were made by the Directors of Royal Mail Holdings plc with the advice of the actuarial advisors to the Group.

Towers Watson has confirmed that the assumptions have been determined in a manner consistent with those used for the disclosures at 25 March 2012, and previous reporting dates with two adjustments overlaid. In previous years, no allowance has been made for the impact of maximum and minimum pension increases, or to lower the retail prices index price inflation assumption to reflect a price inflation risk premium. These are included for this financial year as many other schemes apply these adjustments and they are appropriate to make. The table below also shows a column excluding these adjustments for comparison.

Conversations with Royal Mail management indicate that it is their intention to adopt the assumptions as set out below, although this will not be formally agreed until their Board meeting in May.

Royal Mail Group Limited will set the assumptions for the RMSEPP. Post Office Limited will be allocated a 7% share of gains and losses consistent with previous years. These assumptions will be consistent with those used for RMPP.

	<b>March 2013</b>	March 2013 (for comparison)	March 2012	March 2011	March 2010	March 2009
<b>% pa Nominal</b>						
Inflation (RPI)	<b>3.3</b>	3.6	3.3	3.5	3.6	3.2
Inflation (CPI)	<b>2.3</b>	2.6	2.3	2.8	3.6	3.2
Rate of increase in pensions RPI <sup>(1)</sup>	<b>3.3</b>	3.6	3.3	3.5	3.6	3.2
Rate of increase in pensions RPI (capped) <sup>(1)</sup>	<b>3.2</b>	3.6	3.3	3.5	3.6	3.2
Rate of increase in pensions CPI <sup>(2)</sup>	<b>2.3</b>	2.6	2.3	2.8	3.6	3.2
Rate of increase in salaries <sup>(3)</sup>	<b>4.3</b>	4.6	4.3	4.5	4.6	4.2
Expected average rate of return <sup>(4)</sup>	<b>n/a</b>	n/a	5.9	6.5	6.7	6.9
Discount rate (i.e. bond rate)	<b>4.8</b>	4.8	5.1	5.5	5.6	6.4

<sup>(1)</sup> Pension increases in accordance with RPI are applicable to pensions in payment for RMPP Section C and all RMSEPP members, and RMSEPP deferred pensions for members not transferred from Section A/B of RMPP. The RMPP Section C increases are capped at 5% resulting in a lower assumption of increases by 10 basis points

<sup>(2)</sup> Pension increases in accordance with CPI are applicable to RMPP Section A/B pensions in payment and all other deferred pensions not mentioned above.

<sup>(3)</sup> The rate of increases in salaries is set at RPI + 1%.

<sup>(4)</sup> The expected rate of return is not required due to changes in IAS 19.

Demographic assumptions, for example mortality, remain unchanged from those made in March 2012. It is normal practice for these to be updated following the conclusion of a funding valuation and, given the ongoing discussions with the RMPP Trustee, it would be anticipated that the demographic assumptions will be reviewed for the 2014 financial year end.

#### 9.4 Income Statement

Post Office Limited recognised pension costs of £25m (2012 £24m) in operating profit before exceptional items. Of this charge, £1m (2011 £1m) related to the defined contribution scheme. The amount charged to the loss before taxation for the defined benefit schemes is analysed below.

<b>RMPP &amp; RMSEPP: Amounts recognised within profit before taxation</b>	<b>2012-13 £m</b>	2011-12 £m	Variance £m
Current service cost	<b>24</b>	23	(1)
<b>Net pension charge to operating profit before exceptionals</b>	<b>24</b>	23	(1)
Loss due to curtailments (exceptional charge included within provision for restructuring charge)	<b>2</b>	0	(2)
<b>Net pension charge to operating profit</b>	<b>26</b>	23	(3)
Net interest (credit)/charge to financing	<b>(2)</b>	(2)	-
<b>Net pension charge to income statement before taxation</b>	<b>24</b>	21	(3)

Overall, the net pension charge to income statement before taxation has increased by £3m (14%). The impact on the income statement is a £1m (4%) increase in the charge to operating profit before exceptionals (£3m after exceptionals).

The current service cost is intended to represent the amount by which the liabilities will increase due to employing active members for one more year. The current service cost, expressed as a percentage of pensionable pay, has increased to 18.2% for RMPP (2012 17.1%) and 37.6% for RMSEPP (2012 34.9%), as a result of market conditions at 25 March 2012.

The curtailment cost of £2m (2012 £nil) is the cost within the net exceptional redundancy provisions charge that relates to the receipt of early pensions. The timing of exit and hence the crystallisation of the liability to the scheme may occur in an accounting period subsequent to the recognition of costs in the income statement i.e. in a different period to which the redundancy provision was charged. This liability is matched by payments from the Post Office and is within the short-term pension redundancy payable recognised on the balance sheet. These curtailments therefore do not appear in the analysis of the movement in the pension deficit. (see section 9.7 below).

The net interest credit of £2m (2012 £2m), a non-cash item, is reported under finance income and reassessed annually. It consists of two components:

- a 7% share of the Royal Mail Group expected return on plan assets of £158m for the year (2012 £1,775m). Assessed by applying the expected average rate of return on assets as at the prior year end, to the expected average fair value of scheme assets for the year; and
- a 7% share of the Royal Mail Group interest on plan liabilities of £123m for the year (2012 £1,749m). Assessed by applying the discount rate as at the prior year end to the expected average scheme liabilities for the year.

For 2013-14 this will be calculated on the Post Office section of RMPP and will continue to include a 7% share of RMSEPP. IAS 19 has changed for the coming year so that the expected average rate of return applied to the assets will be the discount rate.

## 9.5 Cashflow

The following cash flows exclude payments made by employees:

	<b>2012-13</b>	2011-12	Variance
	<b>£m</b>	£m	£m
<b>Defined Benefit Schemes (RMPP &amp; RMSEPP):</b>			
Regular pension contributions	<b>23</b>	23	-
Funding of pension deficit	<b>2</b>	0	(2)
Payments relating to redundancy	<b>2</b>	3	1
	<b>27</b>	26	(1)
<b>Defined Contribution Schemes: Regular pension contributions</b>			
	<b>1</b>	1	-
	<b>28</b>	27	(1)

Regular contributions of £23m have remained flat. The regular rate of employer contributions for the RMPP remained at 17.1% of pensionable pay (2012 17.1%), effective from April 2010. The regular rate of employee contributions for the RMPP remains unchanged at 6%. The regular future service contributions for RMSEPP remained unchanged at 35.9% of pensionable pay (2011 35.9%) from April 2010 until the scheme closed on 31 December 2012.

These contribution rates, at 17.1% for RMPP and 35.9% for RMSEPP, are likely to be different to the current service cost charged to operating profit of 18.2% and 37.6% respectively during the period (see above). However, the rates are not directly comparable. For example, the cash rate is adjusted for expected returns on past investments, but this is excluded from the income statement rate – hence the separate income statement interest charge.

There was no RMPP deficit payment (2012 £nil) as a result of State Aid clearance granted on 21 March 2012 and the subsequent transfer of the historical pension deficit to HM

Government on 1 April 2012. RMSEPP deficit payments of £2m (2012 <£1m) have been made during the year. There have been no employee deficit contributions.

## 9.6 Balance Sheet

The following amounts in the balance sheet relate to pensions:

	<b>31 March 2013</b>	25 March 2012
<b>RMPP &amp; RMSEPP: Amounts recognised in the balance sheet</b>	<b>£m</b>	<b>£m</b>
Pension deficit (non current "retirement benefit obligation")	<b>97</b>	(206)
Pension redundancy payable (within current "provisions")	<b>nil</b>	nil

## 9.7 Pension Surplus/(Deficit)

Scheme assets are assessed at fair value at the balance sheet date. For example, quoted equities are valued at the latest 'bid' price. Scheme liabilities are discounted using a high quality corporate bond rate. The IAS 19 surplus/deficit is usually therefore different to the cash funding surplus/deficit (the "actuarial" valuation) assessed by the Trustees, for which the scheme liabilities are discounted using the expected returns available on scheme assets.

The IAS 19 pension valuation has changed from a deficit of £206m at 25 March 2012 to a surplus of £97m at 31 March 2013. The improvement of £303m principally relates to the transfer of historic liabilities to Government. The movements in the pension position during the year were as follows:

<b>RMPP &amp; RMSEPP: Pension deficit</b>		<b>£m</b>	<b>£m</b>	
	Pension deficit at beginning of year		(206)	
Pre Exceptionals	{	Company's pension costs (current & past service cost)	(24)	
		Company's pension payments (regular & deficit contributions)	25	
		Operating pension payments excess over pension costs by		1
		Net interest credit		2
		Transfer to Government		286
		Actuarial gain (net of withholding tax of £3m)		14
		<b>Pension surplus at end of year</b>		<b>97</b>

The actuarial gain includes the difference between the long-term expected rate of return on plan assets and the actual return during the period, and the impact of changes in assumptions. Actuarial gains and losses are recorded directly in the statement of total recognised gains and losses (and not the profit and loss account). The actuarial gain of £14m during the year arose primarily due to a greater than expected increase in assets as a result of changes in market conditions, partly offset by an increase in liabilities due to changes in long term assumptions.

## 9.8 Pension Redundancy Payable

The pension redundancy payable of £nil (2012 £nil) relates to the additional "top up" payments made to the pension schemes for members that have exited the business on redundancy and will be paid an early pension, and is partly based on estimates. All amounts had been settled at the year end.

## 9.9 Assessment of recoverability of surplus under IFRIC 14

In order to recognise a surplus it is necessary to prove that the Post Office could recover the surplus either through lower future contributions or through a refund. Royal Mail took legal advice both before and after sectionalisation. This confirmed that Post Office Limited and Royal Mail Group Limited have absolute rights to the assets left over in their individual sections after benefits have been secured if the RMPP terminates. There is no trigger for termination in the Trust Deed but that does not mean that the RMPP cannot terminate. It would be wound up by the courts, or the Regulator, or when the last beneficiary dies. Towers Watson has calculated that Post Office Limited would be able to recover £91 million of the £99 million surplus in RMPP through lower contributions and the remaining £8 million could therefore be recovered through a refund. For the RMSEPP scheme, Royal Mail has advised that the £1m surplus could be covered through a refund. The element of surplus that is recoverable through a refund would be subject to a 35% withholding tax and therefore the overall surplus on the balance sheet has been reduced by £3 million to £97 million. The element that is recoverable through lower contributions has resulted in a deferred tax liability of £21m (see section 18.2).

## 10. Exceptional Items and Provisions

This section discusses the exceptional items on the income statement together with movements in the related balance sheet provisions/payables.

### 10.1 Exceptional items summary

The following exceptional items were recognised in the consolidated income statement for the years ended 31 March 2013 and 25 March 2012

Exceptional items	Section	2012-13 £m	2011-12 £m
<b>Operating Exceptionals:</b>			
Government Grant	10.2	98	-
Restructuring costs including Subpostmasters compensation	10.3	(79)	(2)
Impairments	10.4	(66)	(36)
<b>Total operating exceptionals</b>		<b>(47)</b>	<b>(38)</b>
<b>Non operating exceptionals:</b>			
Profit on disposal of property		2	1
Loss on sale of associate	10.5	(30)	-
<b>Net Exceptional costs</b>		<b>(86)</b>	<b>(37)</b>

10.2 Government Grant – In April 2012 the Post Office received grants totalling £200m from the Government, primarily to fund capital projects and subpostmasters’ compensation. £98m of this sum has been utilised during the year, the remainder is brought forward into 2013-14 and is included as deferred income in the March 2013 financial statements.

10.3 Restructuring costs – include the costs of delivery of a major change in the network. Network Transformation introduces new style agency offices and seeks to improve fundamentally the profitability of the Crown network. IT Transformation will create the IT infrastructure appropriate for an independent group with ambitious growth plans.

Network Transformation resulted in costs of £12m for Subpostmasters’ compensation and £40m programme costs. Redundancy costs of £11m mainly related to the Crown network, costs of £10m related to transforming our IT infrastructure and there was £2m related to the professional fees associated with the sale of Midasgrange Limited.

The £40m spent on Network Transformation is analysed below:

Network Transformation	£m
Branch Fit Out (Inc. Signage /Scales etc)	8
Horizon Implementation	3
Legal-New Operating Model Contracts	2
Management Consultancy	2
Marketing	3
CTP Pilot design/scoping	1
Professional Fees -Site Survey	1
Staff	15
Skills Group Internal Consultancy Resource	4
Project Management (Roll Out)	1
Total	40

## 10.4 Impairments (2013 £66m vs 2012 £36m)

Other impairments charged in exceptional items comprise:

<b>Impairment</b>	<b>Section</b>	<b>2012-13 £m</b>	2011-12 £m
Property, plant and equipment	13.3	<b>41</b>	19
Intangible assets	13.3	<b>25</b>	17
<b>Total impairments</b>		<b>66</b>	36

Section 13.3 identifies the impaired capital expenditure as summarised above.

## 10.5 Loss on sale of associate (2013 £30m vs 2012 £0m)

During the year the investment in Midasgrange Limited was sold for proceeds of £2m. At the date of sale the investment had a carrying value of £32m giving a loss on disposal of £30m.

## 11. Interest, Cash, Debt, Funding and Hedging

### 11.1 Net finance costs (interest) (2013 £3m vs 2012 £6m)

The Post Office incurred net finance costs of £3m in the year to 31 March 2013 (2012 £6m).

	2012-13	2011-12
	£m	£m
<b>Finance costs &amp; investment income</b>		
Interest received on investments – UK	1	1
<b>Total finance income</b>	<b>1</b>	<b>1</b>
Interest charged on Government borrowings	(1)	(3)
Interest payable on finance leases	(1)	(1)
Unwinding of discounts	(1)	(1)
Other finance costs	(1)	(2)
<b>Total finance costs</b>	<b>(4)</b>	<b>(7)</b>
<b>Net finance cost</b>	<b>(3)</b>	<b>(6)</b>

Interest payable on the BIS Loan reduced during 2012-13 as the average borrowing volume significantly decreased from the previous year. This arose through the receipt of £200m government grants, of which £102m was not utilised during the year, plus an increase of £30m in the NSP.

The discount unwind relates to the provision in respect of the WH Smith onerous contract.

Other finance costs include commitment fees to BIS for the Post Office credit facility, and charges to RBS for their note sorting facility.

### 11.2 Cash, cash equivalents and debt within the balance sheet

The following table highlights the movements in cash, cash equivalents, debt and investments during the year:

		31 March	25 March
	Section	2013	2012
<b>Net cash/debt analysis</b>		<b>£m</b>	<b>£m</b>
Cash in the Post Office Limited network	11.3	<b>870</b>	759
Other cash at bank		<b>9</b>	(1)
Cash equivalent investments		<b>92</b>	62
<b>Total cash and cash equivalents</b>		<b>971</b>	820
Loans, repayable on demand or less than 1 year	11.4	<b>(291)</b>	(377)
Obligations under finance leases (current)	11.5	<b>(3)</b>	(4)
<b>Total current financial liabilities</b>		<b>(294)</b>	(381)
Obligations under finance leases (non-current)	11.5	<b>(4)</b>	(6)
<b>Total</b>		<b>673</b>	433

## 11.3 Cash within the Post Office Limited network (2013 £870m vs 2012 £759m)

The £111m (15%) increase in Post Office network cash year on year is mainly due to the year end coinciding with Easter which necessitated increased branch and cash centre holdings to respond to customer behaviour.

## 11.4 Loans and borrowings (2013 £291m vs 2012 £377m)

The table below details the breakdown and movement on the loans and borrowings year on year:

	<b>31 March 2013</b>	25 March 2012	Net (repayment)
<b>Loans and Borrowings</b>	<b>£m</b>	£m	£m
Working Capital loan	<b>291</b>	377	(86)

## 11.5 Obligations under finance leases (current &amp; non-current) (2013 £7m vs 2012 £10m)

The obligations under finance leases have decreased by £3m during the year attributable to lease repayments in 2012-13. Lease types are shown in section 13.2.

## 11.6 Loan facilities

At year end the Post Office had no external (non Government) borrowing facilities in place.

## 11.7 Derivative assets

A derivative asset of £1m has been recognised on the balance sheet representing the gain on open foreign exchange forward contracts that were in place at the year end.

## 12. Going concern

Post Office Limited has net cash and cash equivalents of £971m (section 11.2) and a borrowing facility of £1,150m of which £291m (section 11.4) was drawn down at 31 March 2013.

### 12.1 Background

On 24 March 2010 a funding agreement was agreed that provided up to £180m for compensation for losses sustained in parts of the network in 2011-12, as well as providing access to the working capital facility to 31 March 2016. These arrangements received State Aid approval on 23 March 2011 through the working capital facility was limited until 31 March 2012.

A further funding agreement with Government was announced on 27 October 2010 which provided for:

- Funding of £410m for 2012-13 (received 2 April 2012)
- Funding of £415m for 2013-14 (received 2 April 2013)
- Funding of £330m for 2014-15
- Extension of the existing working capital facility with BIS of £1.15bn up to 31 March 2016

State Aid approval for the funding for 2012-13 to 2014-15 was received on 28 March 2012. It was also recognised that the working capital facility was no longer deemed State Aid. However, no drawing under the Facility may extend past the Final Maturity Date (31 March 2016).

The going concern analysis is based on the latest draft 2020 strategic plan financials presented to the Post Office Board on 27 February 2013. The Post Office Board approved the 2013-14 budget on 20 March 2013 but the cash flow budget has since changed, reflecting the reversal of the significant inflow in 2012-13 in excess of forecast. The cumulative position across the two years is unchanged.

### 12.2 Assessment for the Post Office

Post Office has finished implementing its 2005-11 strategic plan and has completed its closure programme. It posted an operating profit before exceptional items for the first time for a number of years in 2008-09 and has continued to do so, but still operates with a cash outflow with the exception of 2012-13. The 2011-15 plan is intended to reverse the trend of an increasing Network Subsidy Payment (NSP) with the draft strategic plan beyond 2014-15 continuing that reducing trend.

The 2011-15 strategic plan updated for latest views has been shown in Table 1 of this section, and shows that Post Office has sufficient cash headroom to continue to trade. The available facility has been defined to include network cash, ATM cash, ATM debtor, POCA debtor and SGEI cheques.

The one year funding deal for 2011-12 added the ability to borrow up to £50m from other sources, as well as the up to £50m in finance leases previously allowed, which would improve the headroom capacity shown if required.

## 12.3 Summary conclusion

Based on the analysis there is available borrowing headroom until March 2016. Royal Mail Group Limited is a key trading partner with Post Office Limited and, in arriving at the conclusion that Post Office Limited is a going concern, the assumption is made that Royal Mail Group Limited is a going concern or that an alternative mails provider would work similarly with Post Office Limited providing a similar level of income.

It is believed that Post Office Limited will be able to meet its liabilities as they fall due in the foreseeable future. It is therefore expected that the directors will consider it appropriate to prepare the accounts on a going concern basis.

**Post Office Limited Funding Analysis**

£m (cumulative apart from free cash flow)	2011-12	2012-13	2013-14	2014-15	2015-16
Opening Funds	(321)	(336)	(204)	(222)	(279)
Borrowing facilities	1,150	1,150	1,150	1,150	1,150
Restriction due to level of network cash	(326)	(98)	(350)	(350)	(350)
Borrowing from other sources - finance leases, bank overdraft etc	21	14	9	4	
Latest plan free cashflow before assumed non NSP grant injection	(15)	*(68)	** (233)	(227)	(231)
Non NSP grant injection per October 2010 plan		*200	**215	170	
Closing Funds Headroom	509	862	587	525	290
Downside impact of no NSP beyond March 2015					(130)
Adjusted Headroom pre risk	509	862	587	525	160

£m	Q3 FYF and board approved budget	Outturn and latest budget
2012-13	(28)	*132
2013-14	140	** (18)
Cumulative	112	114

\*/\*\* See breakdown in table 1 above

£m (cumulative)	2011-12	2012-13	2013-14	2014-15	2015-16
Headroom pre risk (as above)	509	862	587	525	160
Risks					
Financial Services growth slower than plan			(3)	(8)	(18)
Network Transformation benefits are not fully delivered			(2)	(6)	(9)
Crown Transformation benefits are not fully delivered			(5)	(10)	(15)
Pension contribution rates increase			(4)	(8)	(12)
Headroom post risks	509	862	573	493	106

Notes:

2011-12 shows the year end outturn and last years are the latest view of the strategic plan.

Available facilities are defined as network cash, ATM cash, ATM debtor, POCA debtor and SGFI cheques.

## Table 1

This table shows the October 2010 strategic plan cashflow updated for the 2013-14 budget, and the initial 2020 strategic plan projections for 2014-15 and beyond. It demonstrates positive headroom throughout the plan period.

## Table 2

This table sets out the impact of theoretical downside scenarios if the plan does not generate the income streams anticipated, the network programmes fail to deliver the benefits and if the pension scheme costs increase.

Clearly mitigating management actions could be initiated but there remains sufficient headroom, even if they are not taken. There are a range of management actions including implementing non-people cost saving initiatives and closing non NSP offices without compensation, and the overriding principle is that management will take whatever action is required to mitigate any risk that materialises.

There are further actions that could be taken but are not required. These include the sale of property and/ or tax losses.

**13. Property, plant and equipment and non-current assets held for sale**

## 13.1 Net Book Values

The net book value (NBV) of land and buildings, plant and fixtures and intangible fixed assets was £11m (2012 £11m). The movements in the year were as follows:

<b>Movement in NBV</b>	<b>Land and buildings £m</b>	<b>Vehicles, plant and fixtures £m</b>	<b>Intangible fixed assets £m</b>	<b>Total £m</b>
NBV at 26 March 2012	11	-	-	11
Add capital expenditure	10	31	25	66
Less disposals	-	-	-	-
Less depreciation	-	-	-	-
Less impairment	(10)	(31)	(25)	(66)
<b>NBV at 31 March 2013</b>	<b>11</b>	<b>-</b>	<b>-</b>	<b>11</b>

## 13.2 Assets held under finance leases

The value of equipment held under finance leases is £nil (2011: £nil) having been impaired in the years in which it was acquired. The two finance leases held are:

- Counter printers, capitalised and impaired in 2006-7 with an asset value of £10m, expires 2014-15;
- Identity equipment in branches, capitalised and impaired in 2010-11, with an asset value of £8m, expires 2014-15.

The finance lease for Supply Chain cash boxes expired during 2012-13.

## 13.3 Capital expenditure

The following table summarises capital expenditure to 31 March 2013:

<b>Capital expenditure analysis</b>	<b>Land &amp; buildings £m</b>	<b>Vehicles, plant &amp; fixtures £m</b>	<b>Intangibles £m</b>	<b>Total £m</b>
Technology Roadmap	-	-	14	14
Network Transformation	2	14	2	18
Pinpads	-	4	-	4
Telephony	-	1	-	1
Finance Roadmap	-	-	2	2
FOoG Front Office of Govt	-	-	2	2
Mails, Retail	-	-	2	2
Vehicles	-	9	-	9
Property	8	-	-	8
Other (items <£1m)	-	3	3	6
<b>Total</b>	<b>10</b>	<b>31</b>	<b>25</b>	<b>66</b>

**14. Goodwill, investments and intangibles**

## 14.1 Investments in joint ventures and associates

	<b>2012-13</b>	2011-12
	<b>£m</b>	£m
Investment in joint ventures and associates	<b>60</b>	89

## Joint ventures

During 2012-13 and 2011-12, Post Office Limited's only joint venture investment was a 50% interest) in First Rate Exchange Services Holdings Limited, whose principal activity is the provision of Bureau de Change.

## Associates

During 2011-12 Post Office Limited's only associate investment was a 49.99% interest in Midasgrange Limited whose principal activity is the provision of personal financial products. This investment was disposed of to the Bank of Ireland during 2012-13.

## 14.2 Movements in investments in JV and associate

	<b>Joint venture</b>	<b>Associate</b>	<b>Total</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Share of net assets			
Total net investment at 26 March 2012	67	22	89
Share of post tax pre dividend profit/(loss)	33	(1)	32
Investment in associate	-	11	11
Disposal	-	(32)	(32)
Dividend	(40)	-	(40)
<b>Total net investment at 31 March 2013</b>	<b>60</b>	<b>-</b>	<b>60</b>

## 14.3 Joint venture and associate

The table below contains details of the share of post tax profits and dividend payments.

	<b>Consolidated (Share of Profit)</b>			<b>Company (Dividend)</b>		
	<b>2012-13</b>	2011-12	Variance	<b>2012-13</b>	2011-12	Variance
<b>Joint ventures and associates</b>	<b>Share of post tax profit</b>	Share of post tax profit	£m	<b>Dividends Received</b>	Dividends Received	£m
	<b>£m</b>	£m	£m	<b>£m</b>	£m	£m
First Rate (FRES)	<b>33</b>	32	1	<b>40</b>	38	2
Midasgrange Limited(POFS)	<b>(1)</b>	(1)	-	-	-	-

The share of post tax profit from FRES has remained consistent year on year.

**15 Working capital**

## 15.1 Inventories (2013 £8m vs 2012 £6m)

	31 March 2013 £m	25 March 2012 £m
Scratchcards	5	4
Retail	3	2
<b>Total</b>	<b>8</b>	<b>6</b>

The movement in inventory is immaterial year on year.

## 15.1.1 Cost of Sales, Retail

Cost of sales in 2012-13 was £5.1m (2011-12: £4.1m).

## 15.1.2 Inventory written off

The provision for stock write downs and discrepancies has increased to £0.5m in 2013 from £0.2m in 2012. Shrinkage and obsolete stock written off in 2012-13 was £0.4m (2011-12 £0.4m).

## 15.2 Trade receivables

Receivables are tabulated below, followed by a detailed explanation of the various balances.

<b>Receivables</b>	31 March 2013	25 March 2012
Trade receivables	32	39
Client receivables	240	138
Prepayments and accrued income	81	39
Other receivables	9	10
<b>Total</b>	<b>362</b>	<b>226</b>

## 15.2.1 Trade receivables: Current (due within one year)

<b>Trade receivables</b>	31 March 2013	25 March 2012
Sales ledger	18	22
Doubtful debt provision	(1)	(1)
Homephone debtors	14	12
Homephone provision	(6)	(5)
Subpostmasters debt	14	16
Subpostmasters debtors provision	(9)	(9)
POFS, FRES cost recovery	2	5
<b>Total</b>	<b>32</b>	<b>39</b>

The decrease in invoiced debt year on year is largely explained by the £nil debtor at March 2013 for DWP card account income (March 2012 DWP debtor: £5m). Mainly the DWP adhere to agreed terms and pay the month following invoice receipt though there are instances when the DWP settle in-month, including March 2013.

Other variances largely net off, however note that the Bank of Ireland March 2013 balance includes £6m of cost recovery and £5m transactional debt. (March 2012 £2m and £2m). Transactional invoices are larger following the sale of Midasgrange. The process for cost recovery has also changed following the sale, with invoicing in advance such that the Bank of Ireland is in a creditor position. However delays in settling these invoices explain why a debtor continues to exist.

Receivable balances remaining in relation to former subpostmasters of £9m have been provided for in full in line with previous years. This is due to the difficulty in recovering these amounts. The remaining £5m of subpostmaster debt which is unprovided against relates to current subpostmasters debt which are usually settled through a deduction from remuneration. The balances are provided for when they reach 60 days old for single subpostmasters or 90 days for multiples.

A profile of the trade receivables is as follows:

<b>Trade receivables</b>	31 March 2013	25 March 2012
DWP	-	5
Bank of Ireland (2012: POFs)	11	4
FRES	-	3
Partner banks	-	2
Bank of Ireland (ATM commission)	2	2
Bill payment partners	1	1
Subpostmasters	1	1
Others	3	4
<b>Total</b>	<b>18</b>	<b>22</b>

Ageing of trade receivables:

Debtors over 60 days overdue: March 2013 £0.4m (March 2012: £0.4m).

The Post Office does not have a general risk in relation to bad debts due to the agency nature of our client base. Among those ageing at March 2013 are £0.5m RBS, £0.5m Bank of Ireland and £0.1m Lloyds.

Debts written off during the year did not originate from the trade debtor base. Write-offs included £1.5m for Homephone debtors which are provided for in full when the debt is over 60 days old.

## 15.2.2 Client receivables

Analysis of the significant client balances at year end is as follows:

<b>Client receivables</b>	31 March 2013	25 March 2012
ATM (Bank of Ireland)	123	77
Card Account (JP Morgan)	76	31
Partner banks	29	18
Others	12	12
<b>Total</b>	<b>240</b>	<b>138</b>

The reason for the significant increase in Client levels over March 2012 due to the coinciding of the March 2013 year end with Easter, which has increased transactional activity and also temporarily extended settlement feel into 2013-14 because of the bank holiday.

The trend for the ATM debtor to increase year on year as more ATMs are installed and also through increased usage of the existing estate continues. Additionally partner bank debtors have increased through increased transaction activity, and also HSBC joining as a trading partner during 2012-13.

## 15.2.3 Prepayments and accrued income 2013 £81m (2012 £39m)

Accrued income represents the majority of this amount (March 2013: £34m, March 2012: £35m), and year on year the product components are similar. The larger accruals at March 2013 are: DWP card account income for March £7m, Homephone £6m and Bank of Ireland commissions £8m.

Additionally there are prepayments of £47m of on the balance sheet at March 2013 (March 2012 £3m). There are two main elements: a £28m advance payment to Fujitsu in respect of the 2013-14 managed service, and £13m – also to Fujitsu – for set-up costs for their take-on of the Telephony contract, this latter prepayment will be amortised over the life of that contract.

## 15.3 Payables: amounts due within one year

A summary of payables categories is:

	Section	31 March 2013	25 March 2012
Trade payables	15.3.1	43	32
Accruals and deferred income	15.3.1	134	140
Client payables	15.3.2	528	332
Advance customer payments	15.3.3	50	48
Capital payables	15.3.4	18	10
Social security		10	9
Business transformation		7	3
Amounts due to group companies		6	9
Government grant deferred income	10.2	102	-
<b>Total</b>		<b>898</b>	<b>583</b>

## 15.3.1 Trade payables and accruals

<b>Trade payables and accruals</b>	31 March 2013	25 March 2012
Trade payables	43	32
Accruals, GRNI	57	50
Agent, employee pay balances	24	61
Productivity, bonus schemes	16	17
Deferred income (Gamma)	31	-
Others	6	12
<b>Total</b>	<b>177</b>	<b>172</b>

The increase in purchase ledger and GRNI accruals is driven by the current significant levels of project activity.

Agent and employee pay balances represents March salaries and remuneration which were paid in March 2013 (2012: paid following year end).

During the year POFS and the Bank of Ireland paid a total of £40m of contractual Gamma payments of which £31m remains to be amortised at March 2013.

## 15.3.2 Client payables

	31 March 2013	25 March 2012
Santander	183	139
NS&I	28	15
DVLA	107	18
Utility companies	24	15
Bank of Ireland	8	13
BACS	59	33
Others	119	99
<b>Total</b>	<b>528</b>	<b>332</b>

All balances are impacted by the Easter bank holiday coinciding with the Post Office's year end, having the effect of increasing the settlement timescale temporarily. Additionally the DVLA balance relates to car tax renewals and was most affected by the coinciding of year end with calendar month end.

## 15.3.3 Client advances

This category also includes specific, non-client, creditors as follows:

<b>Client advances</b>	31 March 2013	25 March 2012
Client advances, deferred income	23	20
Postal order liability	17	18
Homephone line rental advance payments	10	10
<b>Total</b>	<b>50</b>	<b>48</b>

## 15.3.4 Capital payables

The increase over 2011-12 reflects the increased pace of capital project activity in Q4, particularly Network Transformation and Technology roadmap.

## 15.4 Payables: amounts due after one year

<b>Payables due after one year</b>	31 March 2013	25 March 2012
Amounts due under finance leases	4	6
Bank of Ireland deferred brand income	-	2
<b>Total</b>	<b>4</b>	<b>8</b>

The 10 year brand income contract with Bank of Ireland becomes fully amortised during 2013-14, the remaining one year's amortisation is included within accruals and deferred income.

**16. Provisions**

Provisions (2013 £26m vs 2012 £14m)

	<b>Crown Conversions Project £m</b>	<b>Network Transformation £m</b>	<b>Other £m</b>	<b>Total £m</b>
At 26 March 2012	9	-	5	<b>14</b>
Charged in operating exceptional items	-	10	12	<b>22</b>
Charged in operating costs		-	6	<b>6</b>
Charged in financing costs	1	-	-	<b>1</b>
Utilisation	(3)	-	(14)	<b>(17)</b>
At 31 March 2013	7	10	9	<b>26</b>
				<b>19</b>
				<b>7</b>

The network transformation provision relates to compensation payments due to subpostmasters who have signed up to the new contract terms at March 2013.

Other provisions include property contracts, being amounts from onerous lease obligations, and personal injury claims. Additionally at March 2013 the provisions balance includes £2.1m for sales capability investment arising from the revised contract with Bank of Ireland (Eagle provision) and £1.7m following a recent court case in Scotland in which it was decided that external ATMs were subject to business rates. The Ratings Agency intends to seek application of this judgement to the rest of the UK and therefore a provision has been made for rates backdated to 2010.

## **17. Litigation and Claims- Potential Claims regarding Horizon**

- 17.1 Post Office Limited has received notification of five potential claims from former subpostmasters. Each of these subpostmasters had their appointments terminated following the discovery at audit of significant cash losses at their respective branches. Two of the subpostmasters were subsequently prosecuted and pleaded guilty to false accounting.
- 17.2 Each has claimed wrongful termination of contract on the basis that the losses are alleged to have arisen due to the unfairness of the system devised by Post Office Limited and/or have been generated by a computer error in the Horizon system. More specifically, it is alleged that (a) the accounting procedures in place are unfair in that they do not permit subpostmasters to properly verify losses which are alleged to have been incurred, (b) the Horizon system itself contains inherent defects and/or (c) the training and support for subpostmasters using the system is inadequate,
- 17.3 Each subpostmaster is claiming circa £150,000 by way of damages.
- 17.4 Four of the claims have not progressed beyond the pre-action stage (i.e. there are no live court proceedings). Post Office Limited has strongly denied liability and rebutted the allegations made. The fifth claim was struck out by the Court and cannot be pursued further.
- 17.5 The last correspondence received on these matters was in December 2011. Post Office Limited is not aware of any further substantive steps having been taken to advance these claims through the Courts since that date.
- 17.6 Post Office Limited continues to receive challenges to the integrity of the Horizon system and it is possible that further claims may be received. Reports in the press have previously suggested that solicitors Shoosmiths may have consulted on between 85 and 150 potential cases in total.
- 17.7 Subpostmasters have also made complaints about Horizon to Members of Parliament, and through the "Justice for Subpostmasters Alliance", an organisation "established to raise awareness of the issues within the Post Office Horizon system".
- 17.8 Post Office Limited has commissioned an independent third party, Second Sight Support Services Limited, to investigate these cases, which investigation is ongoing.
- 17.9 On the basis of the evidence to date, no provision has been made and it is not considered appropriate to make any disclosure on this matter. This position is being actively monitored.

**18. Taxation**

## 18.1 Income statement – taxation credit 2013 £(17)m (2012 £(10)m)

A breakdown of the tax credit is shown in the table below:

	<b>2012-13</b>	2011-12
	<b>£m</b>	£m
Corporation tax credit for year	<b>(10)</b>	(11)
Tax over provided in previous years	-	1
Current tax	<b>(10)</b>	(10)
Deferred tax	<b>(21)</b>	-
<b>Taxation credit in the consolidated income statement</b>	<b>(31)</b>	(10)

## 18.2 Factors affecting tax credits

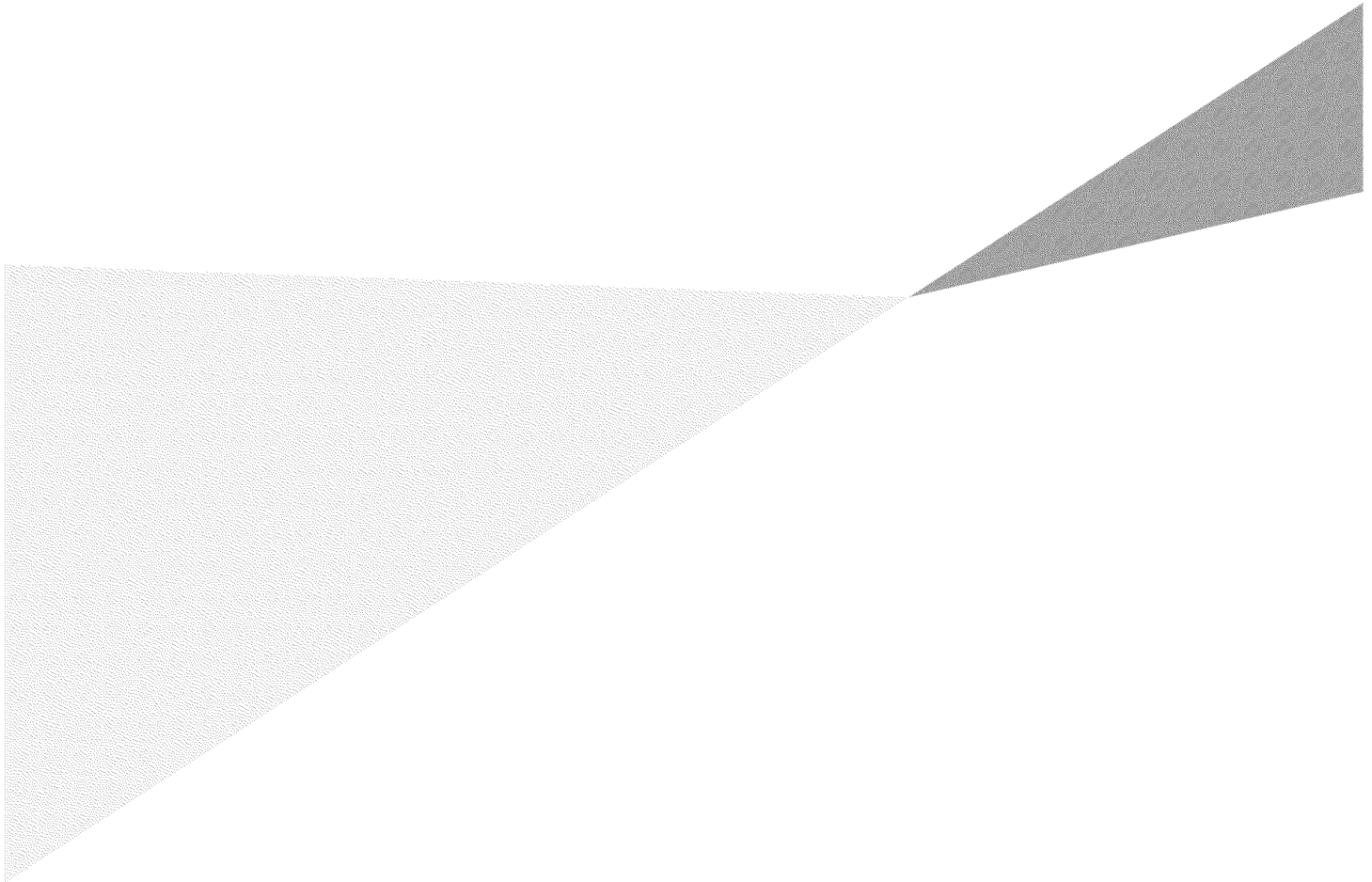
A deferred tax credit of £21m has been recognised in relation to the retirement benefit surplus on the balance sheet. During 2012-13 the pension deficit was transferred to government and consequently the defined benefit pension scheme is now in surplus. A proportion of this surplus is considered to be recoverable through future contributions and therefore creates a deferred tax liability which is taken through Group reserves. The equivalent amount of deferred tax asset has been recognised through the income statement as the credit detailed above.

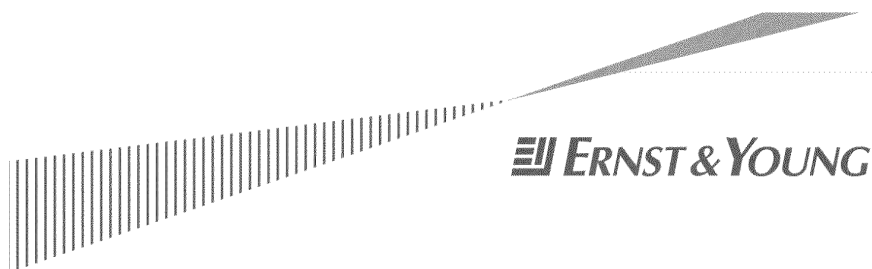
The Group has significant tax losses of £57m (2012 £128m) that are available for offset against future taxable profits. It also has £133m (£157m) of unrecognised deferred tax assets relating to fixed asset timing differences. These tax losses/deferred tax assets could be recognised in the future should suitable taxable profits arise. The tax losses/unrecognised deferred tax assets means that the Group should not incur any tax charges for the foreseeable future.

# Post Office Limited

## Report to the Audit and Risk Committee 2012-13 Audit Results Report

14 May 2013





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**Private and confidential**

14 May 2013

Audit and Risk Committee  
Post Office Limited  
148 Old Street  
London  
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Dear Members of the Audit and Risk Committee

**Audit results report**

We are pleased to attach our audit results board report for the forthcoming meeting of the Audit Committee. This report summarises our preliminary audit conclusion in relation to Post Office Limited's financial position and results of operations for the 53 week period ended 31 March 2013 (the period). We plan to issue our final conclusion following the Audit Committee scheduled for 21 May 2013.

Our audit is designed to express an opinion on the Group and Company financial statements for the period ended 31 March 2013 and address current statutory and regulatory requirements. This report contains our findings related to the areas of audit emphasis, our views on the group and company's accounting policies and judgements and material internal control findings.

This report also contains our final summary of audit differences, communications regarding our independence, a summary of communications we are required to make to you and a draft management representation letter.

This report is intended solely for the information and use of the Board of Directors and Management. It is not intended to be and should not be used by anyone other than these specified parties.

We welcome the opportunity to discuss the contents of this report with you at the meeting on 21 May 2013.

Yours faithfully

Angus Grant  
Engagement Partner  
For and on behalf of Ernst & Young LLP



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The contents of this report are subject to the terms and conditions of our appointment as set out in our engagement letter of 25 February 2013.

This report is made solely to the Audit Committee, Board of Directors and management of Post Office Limited in accordance with our engagement letter. Our work has been undertaken so that we might state to the Audit Committee, Board of Directors and management of Post Office Limited those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Audit Committee, Board of Directors and management of Post Office Limited for this report or for the opinions we have formed. It should not be provided to any third party without our prior written consent.

Section 1

# Executive summary



# Executive summary

## 1. Overview

Following Post Office Limited's (POL) official separation from Royal Mail Group (RMG), significant change is underway throughout the business. Within the network, POL has started their network transformation programme by converting 1,450 branches by the end of this year. This year has also seen POL prepare their first consolidated financial statements under IFRS, and begin to articulate its own identity in the eyes of its stakeholders.

Despite the challenges faced by the finance team as a result of separation-related matters and its first time in preparing standalone Group and Company financial statements, the annual results close process of POL was well executed. We did not perceive any adverse impact on the quality or timeliness of the information provided for audit.

We have received full co-operation from both management and the teams with whom we work and, subject to a few routine outstanding matters, as noted at the end of this section, we have received all information necessary to enable us to complete our audit.

We have carried out our audit in accordance with the plan presented to the Audit Committee in November, with no changes made to our scoping. On the basis of our work performed to date, we expect to issue unqualified audit reports for both the Group and Company financial statements.

The year ahead poses additional challenges and opportunities with further separation-related activity and the continuation of network transformation projects across the business.

In the following pages, we provide you with a summary of our audit scope and status, our areas of focus around significant audit and accounting issues, findings from our controls testing, our required independence communications and a draft management representation letter for your review.



## Executive summary (cont'd)

### 2. Significant Accounting and Audit Issues

Refer to section two 'Areas of Audit Emphasis' for a detailed discussion of significant accounting and audit issues

We have concluded on the following accounting and audit issues with management following discussions with management at the planning and year-end audit stages:

#### Significant Risks (as identified in our Audit Planning Report)

- ▶ **Revenue Recognition across diverse range of revenue streams:** We tested controls on a sample of POL's revenue lines to ascertain whether controls over revenue recognition were effective over the period. We have also carried out substantive testing of revenue, which included cut-off testing at period end over accrued income and deferred income balances and concur with management's revenue recognition accounting.
- ▶ **Counterparty Credit Risk:** Management continues to be proactive in its assessment of counterparty risk. We noted that all significant counterparty receivables have been recovered post-year end, and note that management continues to manage and monitor its credit risk on an ongoing basis.
- ▶ **Pensions valuation and accounting:** Following the pension solution on 1 April 2012 and annual accounting valuation by Towers Watson at period end, Post Office Limited has recognised a gross pension asset for its RMPP scheme of £99 million on its balance sheet at 31 March 2013. We have independently assessed the key actuarial assumptions underpinning the £99m asset and concluded they lie within acceptable ranges.

#### Other accounting and audit matters

- ▶ **Exceptional costs & classification:** POL's policy of reporting exceptional items allows management to highlight those items incurred during the year that are both material and fall outside the definition of 'business as usual' activity. In the body of this report, we present our view on each of the key areas of judgement and concur with management's treatment and presentation.
- ▶ **Higher inherent risk of transitioned accounts impacted by POL separation:** The POL finance team now has direct responsibility for the vast majority of its finance functions for the first time, some of which were previously operated by Royal Mail Group. Overall, we did not note any issues with the accounting of the 'transitioned' finance functions.
- ▶ **State Aid Funding (Government Grants):** We are satisfied that POL's government grants have been appropriately recognised in the P&L in accordance with the contract from the Department of Business, Innovation & Skills and IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*, and that the related deferred income balances at year end are appropriately stated.

Additionally, in light of POL's receipt of State Aid funding up to 2014/15, extension of its working capital facility until 31 March 2016 and review of management's forecasts underlying its going concern assessment, we concur with management's assessment that POL can continue as a going concern.



## Executive summary (cont'd)

### 3. Control themes and observations

Refer to section three 'Control themes and observations'

The key internal control findings arising from our audit work are:

- ▶ Key controls tested around revenue and payroll were deemed to be operating effectively.
- ▶ No significant findings were noted in the ISAE 3402 report commissioned by Fujitsu, and we have therefore been able to rely upon it for our IT audit. We were also able to place reliance on the effectiveness of automated controls within HNGX and POLSAP for financial statement audit purposes.
- ▶ We noted that for the RMG-provided HRSAP system, our team identified logical access-related issues which have required us to modify our audit approach by testing and placing more reliance on the manual business process controls. Given the changed nature of POL's relationship with RMG and impending separation, we believe POL should take a proactive approach in resolving the issue with RMG.
- ▶ In light of the continued separation of POL from Royal Mail, with POL taking on more activities which Royal Mail had previously carried out on their behalf (including the consolidated financial statement preparation process), the finance team was resilient and well prepared for the year end. We noted no adverse impact on the quality of information produced.

Detailed control observations and recommendations are currently being discussed with management and will be reported in our forthcoming management letter.

### 4. Summary of audit differences

Refer to section five

- ▶ We report two unrecorded reclassification audit differences totalling £9.9m which we believe should be reclassified from accruals to provisions. These relate to £6.7m with regards to a commitment to Crown branch staff for business transformation payments, and £3.2m which relates to DVLA remuneration payments to subpostmasters. We note these two adjustments have no profit and loss impact.
- ▶ We also report a turnaround adjustment to decrease profit before tax by £1.9m with regards to the LTIP bonus scheme as it was over-accrued and unadjusted for in the prior year.
- ▶ The impact of the current year unadjusted audit differences would be to decrease profit after tax by £1.4m, which is solely due to the turnaround adjustment described above.
- ▶ We have internally consulted on the unadjusted reclassification differences and await conclusion of this consultation at the time writing this report.

### 5. Our opinions and confirmations

- ▶ We anticipate issuing an unqualified audit opinion on the POL Group and Company financial statements for the period ended 31 March 2013.
- ▶ We confirm that our fees for non-audit services during 2012/13 have been reviewed in order to make sure that they do not compromise our independence as your external auditor.
- ▶ We confirm our independence as your external auditor in this report in **Appendix A**.

## Executive summary (cont'd)

### 6. Status of the audit

Our audit work in respect of the opinion on Post Office's consolidated financial statements is substantially complete. The following items relating to the completion of our audit procedures were outstanding at the date of drafting this report.

Item	Actions to resolve	Responsibility
Letter of representation	To be signed/ dated contemporaneous with our audit opinion on the Group and Company financial statements, which is anticipated to be in June 2013.	Management Audit Committee
Subsequent events procedures	To be completed through the date of our audit opinion on the Group and Company financial statements (matters to be updated include: management enquiries, review of latest management accounts, unrecorded liabilities testing and board minute review to date of signing).	Management Ernst & Young
Confirmations	Awaiting receipt of all bank, derivative and pension asset confirmations, anticipated to be received by 24 May 2013.	Management
Annual report and accounts	<ul style="list-style-type: none"> <li>▶ Review of 'front end' statements including audit aspects of the Directors' Remuneration Report, Chairman's and CEO's statements and completion of EY technical review thereon;</li> <li>▶ Review of directors' emoluments disclosures once final bonus outturns confirmed;</li> <li>▶ Post balance sheet events review;</li> <li>▶ Finalisation of Ernst &amp; Young review comments on disclosure notes; and</li> <li>▶ Financial statements to be approved by management and audit report to be signed by Ernst &amp; Young.</li> </ul>	Management Ernst & Young
Tax	The review is in process and no adjustments have been noted to date.	Management Ernst & Young
Interoffice reporting deliverables	<ul style="list-style-type: none"> <li>▶ Final signed deliverables from PwCFRES team</li> </ul>	Management Ernst & Young

Section 2

# Areas of audit emphasis



# Areas of audit emphasis



The following table summarises the significant accounting matters outlined in this report. It seeks to provide the Audit Committee with an overview of the areas of audit emphasis, as identified in our audit planning report, and our assessment of management's accounting treatment.

Areas of audit emphasis highlighted in our audit planning report	Ernst & Young assessment
Significant risk - Revenue recognition across diverse range of revenue streams	Refer to section 2.1
Significant risk - Counterparty Risk	Refer to section 2.2
Significant risk - Pension valuation and accounting	Refer to section 2.3
Valuation of provisions including Network Transformation provisions and classification of exceptional costs	Refer to section 2.4
Higher inherent risk of transitioned accounts impacted by POL separation	Refer to section 2.5
Risk of fraud/burglary arising from the logistics network and the branch network	Refer to section 2.6
Project Eagle/Gamma Accounting	Refer to section 2.7

Accounting and audit matters during the period end audit:	Ernst & Young assessment
Exceptional Charge: Fixed assets impairment	Refer to section 2.8
State Aid Funding (Government Grant)	Refer to section 2.9
Consolidation Considerations - First Rate Exchange Services	Refer to section 2.10
Tax	Refer to section 2.11

## Areas of audit emphasis (cont'd)

### 2.1 Significant risk - Revenue recognition across diverse range of revenue streams

The Company continues to sell a large variety of products/services across a number of revenue streams. Total revenues for POL (excluding the network subsidy payment, which is also included in total revenue and is discussed in Section 2.9) continued to grow during FY2013, increasing by 4.4% to £1,024m (FY2012: £980m).

As noted in our planning report, most of POL's revenues are not overly complex in their calculation. The main risk associated with the diverse range of streams is in the correct contractual terms being applied. We performed controls testing on revenue as part of our interim procedures, where a sample of revenue lines was tested to ascertain whether the controls over revenue recognition were effective throughout the period. No exceptions were noted in our testing. Further, we were able to obtain comfort over the contractual rates and volumes used in the revenue calculations and that an adjustment for actual income is made where estimates are used.

We also performed detailed analytical reviews of each major revenue stream, considering and evaluating the movements in the key revenue lines across the business. We did not note any unusual results or variances. We also considered the accounting treatment for significant new products or revenue streams where applicable, noting no exceptions with management's application of its revenue recognition policy.

In addition to the above, we performed cut-off testing procedures to give further comfort that revenue has been recorded in the correct period. We also carried out substantive testing of accrued and deferred income that included investigating any estimates made and comparing this to the actual amounts received subsequent to year-end for any material differences, and noted none as part of our year end review.

Based on the procedures performed, we conclude that revenue, accrued income and deferred income balances at year end are appropriately stated.

## Areas of audit emphasis (cont'd)

### 2.2 Significant Risk – Counterparty Credit Risk

In light of the current economic environment, POL undertakes a review of all counterparties to assess their level of exposure and relative risks. In particular, given the concentration of risk associated with the Bank of Ireland (BOI), POL has performed a more detailed assessment to determine if steps should be taken to mitigate any risk exposure perceived excessive. As part of their assessment, the appropriate detailed contingency plans have been put in place, in particular focusing on Instant Saver and general banking areas.

Given the concentration of risk associated with the Bank of Ireland, POL performs a more detailed assessment. This plan was prepared in October 2010 at the height of the banking crisis and management continues to believe it to be relevant in the current year. Management noted that the first stages of the contingency plan were deployed successfully when the Irish banking crisis was widely reported in the media in previous years. This plan takes into account all similar types of banking and how they would cope with customer related issues (e.g. all deposits taken in one day) and/or counterparty related issues such as liquidation of a third party.

Counterparty	Exposure at 31/03/13 (£m)	Nature of business with POL to cause exposure
Bank of Ireland	123	ATM Debtor
JP Morgan	76	Processing benefit settlements
HSBC	56	Card payments in network

#### **Top three counterparty receivables for POL as at 31 March 2013**

We tested the recoverability of the material counterparty receivables due to POL, which included vouching the most significant counterparty debtors to bank receipts received post year-end.

We have also held meetings with the Head of Corporate Finance to discuss how POL manage and mitigate counterparty risk. We noted that POL mitigates trading counterparty credit risk by imposing the recommended credit terms and credit limits as advised by a credit agency (Experian) and monitors amounts overdue from key counterparties via circulating weekly reports to the Corporate Finance department.

Based on the procedures performed, we conclude that the counterparty credit risk is monitored and managed and that all counterparty receivables have been recovered post year end.

## Areas of audit emphasis (cont'd)

### 2.3 Significant Risk - Pension Valuation and Accounting

Post Office Limited has recognised a pension asset of £97m, representing the surplus in plans of £99m and £1m for RMPP and RMSEPP respectively, net of withholding tax of £3m at a rate of 35% on the element of the surplus which is recoverable through a refund from the plans. This has been recorded in accordance with IAS 19 *Employee Benefits* and *IFRIC 14 The Limit on a Defined Benefit Asset*.

#### RMPP Scheme

Post Office Limited has recognised a net pension asset for its RMPP scheme of £99 million on its balance sheet at 31 March 2013 (March 2012: £205 million liability). This amount comprises £243 million of scheme assets offset by £144 million of defined benefit pension obligation.

The change in the Post Office Limited position from net pension liability position to net pension asset position is primarily due to the implementation of the pension solution, which meant that POL was fully funded (and therefore at a £nil net pension position) at the start of the current period. The change to surplus position in the current period was principally driven by the pension solution and favourable performance of the scheme assets during the period.

#### Pension Assumptions

We have reviewed the key financial assumptions underpinning the measurement of the defined benefit obligation, with input from EY pension specialists where appropriate. We have also discussed and reviewed the methodology used in preparing the assumptions with Post Office's actuaries. In our opinion, Post Office has used reasonable assumptions in valuing their pension obligation in accordance with the measurement criteria set out in IAS 19.

A summary of the main assumptions used to calculate the defined benefit obligation were as follows:

Financial assumptions	RMPP		
	March 2013	March 2012	Change
Discount rate	4.80	5.10	-0.30
Inflation rate (RPI)	3.30	3.30	0.00
Inflation rate (CPI)	2.30	2.30	0.00
Return on assets	n/a	7.70	n/a
Expected rate of non promotional salary increases	4.30	4.30	0.00

The critical assumptions and our view on Management's choice of assumptions are set out below:

#### Discount rates

Continued volatility in financial markets has meant that AA corporate bond yields continued to decline in 2012-13, resulting in a decrease in discount rates for the RMPP scheme. We acknowledge that there is no single correct approach to deriving the discount rate and the assumption is highly subjective. The methodology used by Towers Watson to calculate this rate is appropriate and takes into account the duration of the scheme's liabilities and market conditions as at 31 March 2013.

## Areas of audit emphasis (cont'd)

### 2.3 Significant Risk - Pension Valuation and Accounting (cont'd)

#### Inflation rates

Consistent with the prior year approach taken by RMG, POL continues to use a combination of RPI and CPI as its basis for measuring the inflation rate. There is subjectivity in the CPI assumption given limited market data with derivation based on the reduction of the RPI rate by 1.00%. Based on our experience we note that the differentials as adopted by Post Office are mid-point of what we consider to be an acceptable range.

#### Asset returns

Towers Watson has not provided expected rates of return on assets at 31 March 2013 as these will not affect next year's income statement given the changes to IAS19. Under the revised IAS 19, which comes into effect for accounting periods beginning on and after 1 January 2013, the expected return on assets will be replaced by the net interest cost, which will be the discount rate applied to the net balance sheet asset or liability as at the beginning of the period.

#### Demographic assumptions

We have reviewed the demographic assumptions related to salary increases and mortality. These are in line with the POL's latest experience and are consistent with those agreed between the Trustees and POL. We note that the mortality assumptions are consistent with prior year, and are based on an investigation of scheme experience that was performed for the full actuarial valuations as at 31 March 2009. We understand that the 31 March 2012 valuation is still in progress.

The basis applied for the current year IAS 19 valuation is considered appropriate for the current year. We do however note that mortality assumptions should be reviewed on a regular basis so that they take account of new research and scheme experience, where observable.

#### RMSEPP Scheme

The Royal Mail Senior Executive Pension Plan (RMSEPP) was not impacted by the pension solution and continues to be centrally accounted for by Royal Mail Group, with the appropriate POL section of the scheme allocated to it by the Royal Mail Group finance team. As a result, the Royal Mail Group team have separately audited the RMSEPP scheme, and reported back to our team that there were no issues to note. We note that POL recognised a pension surplus of £1m (2012: deficit of £1m) relating to the RMSEPP scheme.

#### IAS19 (Revised) Considerations

The Group is subject to the requirements of IAS 19 (Revised) effective 1 January 2013.

Changes expected as a result of the adoption of the revised standard that POL will need to consider for the following year's financial statements will include:

- ▶ Removal of the concept of separate expected return on assets and interest costs on liabilities and replaced by 'Net financing (income)/expense relating to pensions' described below;
- ▶ Net financing pension (income)/expense calculated as the net surplus or deficit multiplied by the discount rate applicable to the Scheme at the beginning of the financial year. Differences between this computed figure and the actual amount will be reported in other comprehensive income. The effect on adoption of IAS 19 Revised is not expected to be material to POL's financial statements.

## Areas of audit emphasis (cont'd)

### 2.4 Exceptional Items & Classification

As anticipated in our planning report, POL's Network Transformation programme during the current period led to a significant increase in exceptional costs which was partially offset by a £200m government grant from the Department of Business, Innovation & Skills (BIS). Management's disclosure of the exceptional costs on their financial statements is set out below. We consider each of these classifications below:

£m	FY2012-13	FY2011-12
Transformation and restructuring costs	(79)	(2)
Other (See section 2.8 for further consideration)	(66)	(36)
Government Grants (see Section 2.9 for further consideration)	98	-
<b>Total exceptional costs</b>	<b>(47)</b>	<b>(38)</b>

We note that 'other exceptional costs' consist entirely of the immediate full impairment charge on all fixed asset additions, which is consistent with prior year. Management's accounting treatment is discussed in detail in **Section 2.9** of this report. We also agree with management's disclosure of government grants within the exceptionals disclosure on the income statement. See **Section 2.9** for further discussion.

#### **Restructuring costs & business transformation costs**

Restructuring and business transformation exceptional items largely related to the costs of carrying out the network transformation programme.

Management note that the costs of network transformation are exceptional in nature given that a branch modernisation programme of this scale has not been carried out before. As such, management believe this would require separate presentation on the face of the income statement to allow a better understanding of financial performance in the year.

We noted no exceptions within our detailed testing, and concluded that the classification of these costs as exceptional was reasonable. The breakdown of restructuring and business transformation costs is given below and a summary of our considerations on the classification of each of these costs follows.

£m	FY2012-13
Network & Crown Transformation costs	(40)
Agents Compensation	(12)
Redundancy	(11)
IT Transformation Costs	(10)
Business Transformation costs	(4)
Other	(2)
<b>Total transformation &amp; restructuring costs</b>	<b>(79)</b>

## Areas of audit emphasis (cont'd)

### 2.4 Exceptional Items & Classification (cont'd)

#### Network & Crown Transformation costs (FY2012-13: £40m)

The Network Transformation & Crown Transformation costs are attributable to the modernisation of POL's existing branches as part of their transformation programme. In keeping with the one-off nature of the programme to modernise Post Office's network, management have classified these costs as exceptional.

#### IT Transformation costs (FY2012-13: £10m)

The current IT transformation was one of POL's key programmes to deliver the commitments made in 2010 in the Government funding and Strategic Plan. Management treats this specific transformation project as an exceptional cost given the project results in a fundamental change to the entire POL IT model. We understand from our discussions with management that this will go hand-in-hand with the Network Transformation project and act as a key enabler to the project as a whole. Management noted that the changes in the network transformation project would not be achievable without the IT transformation project - thus following that both, which are one-off non-recurring costs once these projects are completed at the same time in 2017/18, should be regarded as exceptional. We also note that management is not including standard IT maintenance or upgrades to its systems within these costs.

#### Redundancy costs (FY2012-13: £11m)

POL provided for redundancy costs of £11m during the current year the majority of which were paid leaving a £1m balance to be paid at period end. Management noted these were specific redundancy costs largely related to the Crown transformation programme and as such were treated as exceptional items.

#### Agents Compensation Costs (FY2012-13: £12m)

In the current year agents have been incentivised and compensated for ensuring their branches take part in the Network Transformation programme. Agents have been offered four different compensation schemes totalling £12m, and we agree with management's assessment that these should be included within exceptional items.

#### Business Transformation Costs (FY2012-13: £4m)

During the current year, management made an offer of 'business transformation' payments to staff working in their crown branches as part of their transformation programme, which included £3.3m of exceptional costs in the current year (rounded to £4m for presentation in the accounts and treated as an exceptional item) and an accrual of £3.4m from the prior year. We agree with management's treatment to treat this as an exceptional cost, and note this is consistent with the practice in prior year.

We also note that whilst we agree with management to treat the above as an exceptional, we have proposed an audit reclassification adjustment for business transformation costs, which we believe should be classified in provisions in accordance with IAS 37 - Provisions, as opposed to accruals. We have discussed this in greater detail within our 'Summary of Audit Differences' section.

The remaining £2m of 'other' costs consisted of one-off professional fees associated with the sale of Midasgrange during the period.

## Areas of audit emphasis (cont'd)

### 2.5 Separation Considerations

As a consequence of POL's separation from Royal Mail Group during the current year, the POL finance team has been directly responsible for nearly all of its finance functions for the first time, some of which were previously operated and accounted for at Royal Mail Group (with the exception of some minor accounting areas including the RMSEPP pension scheme). POL has also taken ownership of the accounting of the RMPP pension scheme (discussed in previous section). Overall, we did not note any issues with the accounting of the 'transitioned' finance functions. The key separation-related highlights which have not been discussed elsewhere in the report are mentioned below:

#### Treasury

One of the consequences of the POL/RMG separation has been the development and independence of POL's own treasury function. We discussed the treasury process with the Treasury and Corporate finance department and performed walkthrough procedures to gain an understanding of POL's treasury process. We noted that POL mitigates its foreign currency risk exposure through external foreign currency forward contracts with First Rate Exchange Services Holdings Limited, and also participates in the Royal Mail Group commodity hedging programme, to mitigate its exposure to the price risk of purchasing fuel, electricity and gas. At year-end, POL's net derivative assets on its balance sheet amounted to £1m, relating primarily to the forward purchase of foreign currencies. We obtained supporting documentation for the derivatives and recalculated the measurement of these assets in accordance with IFRS, noting no issues with management's treatment.

#### Property Transfer from Royal Mail

During the current year, Royal Mail transferred a portion of its freehold properties and long leaseholds to Post Office Limited, which had an original net book value to Royal Mail of £12m with a market value of £30m (as per an external valuation). As per IAS16 *Property, Plant and Equipment*, POL had two options to account for the transfer of land and buildings from Royal Mail; they could either account for these transferred assets at £nil or at fair value. As POL made a minimal contribution for these assets (of £1 each), they have elected to record these assets into their accounts at £nil cost. We understand that the market value of these assets will be disclosed in the directors' report to the accounts. At year end, we noted that these properties have been appropriately transferred to POL and that they have been recorded in accordance with IAS 16 *Property, Plant and Equipment*.

## Areas of audit emphasis (cont'd)

### 2.6 Risk of Fraud/Burglary arising from the logistics process

POL holds large quantities of cash within its retail centres, cash centres and in transit (£759m as at 31 March 2013), which is potentially subject to misappropriation or under the threat of burglary attempts by organised crime. As noted in our planning report, management has strong controls to prevent and detect any risk of fraud and attempted burglary, and we note that they continue to reassess whether they need to increase their security measures.

We visited both a cash centre and a Post Office branch to observe cash counts performed by internal audit, and observe security controls around cash management. We noted that management continue to have strong security controls in place to deter risk of fraud and burglary. Additionally, we held a meeting with the head of security at cash centres to gain insight into their assessment of risks and events of fraud in the logistics process and branch networks, and note no issues to report.

As part of our audit procedures, we have also performed detailed substantive tests on cash and bank reconciliations at year end, as well as testing cash cut-off. We noted no issues from our testing.

### 2.7 Project Eagle/Gamma accounting

As noted in our half-year review to the Committee, the BOI sells a number of financial services products through the POL branch network in the UK. Historically, the services were operated through Midasgrange Limited, which traded as Post Office Financial Services (POFS), an associate between POL and the Bank of Ireland (BOI).

During the year, POL sold its investments in POFS to the BOI for proceeds of approximately £2.7m (Project Eagle). This resulted in a loss on disposal of £30m. We have reviewed the accounting treatment for Project Eagle and agree with management's accounting for the transaction. We also concur with management's treatment of the future revenue profile for Gamma and the Project Eagle disposal accounting.

At year-end, we noted the new arrangement between POL and BOI to replace the previous POFS arrangement was 'commissions based', whereby POL would directly receive a contractual commission for each BOI product that it sells to customers through its branches. We noted no exceptions in the accounting related to the new deal.

### 2.8 Fixed Asset Impairment

POL continue to adopt a policy of fully impairing all fixed asset additions made during the year in which they are purchased, except for freehold land & buildings and building shells. Management's justification for adopting this policy is mainly due to the fact that POL has historically been, and continues to be, a loss making entity absent the Network Subsidy Payment it receives from the Government.

As an additional factor in the decision to impair, POL has been working on a major programme of network change costing £500m between the current year and FY2014-15, which is included within the current State Aid funding package. Investment of this scale will lead to significant cash outflows for the immediate years. The degree of transformational change and the impact on cash flows would impact the future profits of the Company and accordingly management believes that POL will continue to be a loss making entity in near to medium term.

We continue to agree that POL's accounting policy for impairment and disclosure of the charge as an exceptional item is reasonable, and in line with IAS 36, *Impairment of Assets*.

## Areas of audit emphasis (cont'd)

### 2.9 Government Grants

On 28 March 2012, POL received confirmation that its application for State Aid funding for 2012/13 to 2014/15 had been approved, which included an extension to its existing working capital facility of £1.15bn up to March 2016. In addition, POL received approval to obtain the following funding from the Department of Business, Innovation & Skills (BIS) by way of grants: FY2012/13 - £410m, FY2013/14 - £415m, FY2014/15 - £330m.

Of the amounts above, £210m (2012/13), £200m (2013/14) and £160m (2014/15) were agreed to be made by way of a network subsidy payment, which has been regularly paid by the government to POL over the last few years, enabling the company to keep branches open that would otherwise not be viable. We note that the network subsidy payments do not prescribe how these funds should be utilised. Management elected to use the 'Income Approach' relating to this grant since FY2006/07 when it was first received with the amounts recognised as part of revenue in the year in which they are received. We note this is in line with IAS20 *Accounting for Government Grants and Disclosure of Government Assistance*, the agreement with the government and consistent with prior years.

For the remaining £200m grant, whilst management has also elected to use the 'income approach', in line with the terms set out by BIS in their designation letter, management have matched the grant directly to the expense incurred, and have appropriately offset the government grant against expenses in the P&L. We have reviewed the accounting treatment for this and noted this is allowable by IAS20.

At year end, £98.2m of the funds have been utilised, with £65.8m spent on capital expenditure, £12.4m on agent's compensation and £20m on other expenses relating to the network transformation. This has left a £101.8m deferred government grant creditor at the year end. Based on our procedures performed, we conclude that the government grant has been appropriately recognised in the income statement in accordance with the contract from BIS and that deferred income balances at year end are appropriately stated.

Finally, as above, in light of POL's receipt of State Aid funding up to 2014/15, extension of its working capital facility until 31 March 2016 and review of management's forecasts underlying its going concern assessment, we concur with management's assessment that POL can continue as a going concern.

### 2.10 Consolidation Considerations - First Rate Exchange Services Joint Venture

This year saw POL financial statements prepared for the first time on a consolidated basis. When performing audit procedures on consolidated financial statements, we were required to set audit scopes for each reporting unit, based on size and risk factors, which when taken together, enable us to form an opinion on the POL group accounts as a whole.

POL's consolidation is made up of two reporting units; the Post Office Limited parent entity (which contains the majority of transactions) and the POL joint venture with the Bank of Ireland, known as First Rate Exchange Services (FRES), which is accounted for using the 'equity' method. The audit of FRES is performed by PricewaterhouseCoopers (PwC).

The PwC team reported to us on their planning and year-end audit procedures, which were undertaken according to our communicated scopes, materiality and instructions. The FRES team have sent us their preliminary conclusion with noted no issues, and we are awaiting their final reporting. We did not note any issues of Group audit importance.

## Areas of audit emphasis (cont'd)

### 2.11 Corporate Tax Considerations

The Group's tax charge for the period is as follows:

£m	FY2012-13	FY2011-12
Profit before tax	£18m	£20m
Tax credit - income statement	£(31)m	£(10)m
Tax charge - items taken directly to equity	£21m	£0m
<b>Net total tax credit recognised in year</b>	<b>£(10)m</b>	<b>£(10)m</b>

The total tax credit for the year of £10m arises from the surrender of tax losses to joint ventures and associates for payment at the statutory rate of 24%.

#### Deferred tax assets and liabilities

At 31 March 2013, the Group has a net deferred tax balance of £nil on the balance sheet. A deferred tax liability of £21m in respect of the pension surplus has been recorded through OCI. This is offset by the recognition of an equal deferred tax asset in respect of tax losses carried forward at 31 March 2013 which has been recorded in the Income Statement.

The deferred tax liability referred to above relates to the pension surplus of £100m (before withholding tax) recognised for accounting purposes. We understand that it is management's expectation that £91m of the pension surplus will be recovered solely through a reduction in future pension contributions over the life of the scheme. The reduction in future pension contributions will increase the future current tax liabilities of POL and therefore, a taxable temporary difference arises in respect of which a deferred tax liability should be recognised.

It is management's intention that the remaining element of the surplus of £9m will be recovered through refunds from the scheme. Accordingly, the surplus has been shown on the face of the balance sheet net of a 35% withholding tax of £3m. We agree this treatment is appropriate and in line with Ernst & Young's interpretation of IFRIC 14.

Consistent with prior years, no deferred tax assets have been recognised in respect of losses and other temporary differences for the year ended 31 March 2013, due to uncertainty around the availability of future taxable profits.

#### Other tax matters

##### 1) *Postal Services Act 2011*

On 1 April 2012, almost all of the UK Group's pension liabilities and assets were transferred to Her Majesty's Government. The Postal Services Act 2011 (the Act) provides that the transfer of the net pension deficit out of the UK Group should not have any UK tax consequences in itself. However, under the Act, certain trading losses of POL are extinguished with effect from 1 April 2013.

As these losses have not historically been recognised as a deferred tax asset, there is no impact on POL's balance sheet from this loss extinguishment. Under the terms of the Act, losses extinguished as at 1 April 2013 are currently estimated to be £175m. Losses of approximately £340m have been carried forward and are available for use in future periods.

## Areas of audit emphasis (cont'd)

### 2.11 Corporate Tax Considerations (cont'd)

#### 2) Government Grants

During the year, POL received £410m in grants from HM Government. Of this amount;

- a) £243m has been treated as taxable in 2012/13 (and is covered by current year losses and capital allowances claims).
- b) £67m has been allocated to capital expenditure. Of this amount, £52m relates to assets which qualify for capital allowances for tax purposes. Whilst this amount has been treated as non-taxable in the current year (as agreed with HMRC on the basis it relates to capital expenditure), no capital allowances will be claimed on these assets going forward. The remaining £15m relates to building and property additions on which no capital allowances are available for tax purposes. This is also non-taxable in the current year as it relates to capital expenditure. Upon disposal of the building and property assets in future periods, this amount taken into account when calculating any chargeable gain/loss.
- c) £100m has not yet been spent and is currently recorded as a creditor on the balance sheet. This may represent future taxable income to POL depending on how the grant is allocated in future periods. The grant is not subject to tax until realised in the Income Statement. In addition, whether or not this amount would represent taxable income in the future will depend on how the grant is allocated in future periods. If the remaining grant were to be fully taxable, there are sufficient taxable losses available to offset this amount in full. However, as there is uncertainty as to how the grant will be allocated and therefore uncertainty as to whether this will in fact constitute taxable income, no deferred tax asset in respect to the future loss utilisation has been recognised.

#### 3) VAT

Consistent with prior periods, POL is a member of a broader Royal Mail VAT group with Royal Mail Group Limited (RMG) being the representative member to HMRC and the entity responsible to HMRC for any VAT liabilities.

In respect of the FY 13/14 audit, the VAT implications associated with the separation of POL from the RMG should be reviewed next year. In particular, the VAT treatment of the recharges between POL and RMG, and the proposed 'stamp solution' to deal with it should be reviewed.

Section 3

# Control themes & observations



# Control themes & observations

## Gaining assurance through the control environment



As part of our audit of the financial statements, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Although our audit was not designed to express an opinion on the effectiveness of internal of internal control we are required to communicate to you any significant deficiencies in internal control.

We can confirm that on the basis of our audit work performed, we did not identify any significant deficiencies in internal controls other than the control deficiencies reported below. However, we anticipate providing a detailed letter incorporating certain recommendations for process improvements noted by us in the performance of our procedures at the conclusion of this year's audit cycle.

The following pages will detail our considerations.

## Observations on the IT Environment

### *Background*

Over the last two years the IT element of our audit identified significant control weaknesses, highlighting the need for improvement of Fujitsu's control environment and a change in POL's approach in terms of the governance, risk and control framework over its business critical systems. POL has implemented formal controls to address the control weaknesses and improve the overall IT control environment over the key applications in our audit scope, HNGX and POLSAP. POL also followed a formal risk acceptance process for areas where management has decided to accept certain risks highlighted by the audit process. In addition, Fujitsu commissioned an independent service organisation control report (ISAE 3402) in relation to controls operated by Fujitsu.

In light of these developments, our approach was to rely on the ISAE 3402 and report and perform independent testing of POL-operated controls.

### *Result of the IT audit*

- ▶ No significant findings were noted in the ISAE 3402 report, and we have therefore been able to rely upon it.
- ▶ In addition, we have not identified significant exceptions in our independent testing of POL-operated controls.
- ▶ We have, however, identified a small number of improvement opportunities to enhance the effectiveness of recently implemented controls and further improve some of POLSAP's security settings.
- ▶ It should be noted that these control enhancements did not have an adverse impact on our ability to place reliance on the effectiveness of automated controls within HNGX and POLSAP for financial statement audit purposes.



## Control themes & observations (cont'd)

### Gaining assurance through the control environment (cont'd)

#### Observations on the IT Environment (cont'd)

##### *RMG provided systems- Separation Considerations*

- ▶ Other key considerations for the IT audit this year are POL's separation from Royal Mail Group and the related IT. There are two key systems managed by RMG (where the support services have been outsourced to CSC, a third party service provider) that support POL's financially significant processes. These systems are SAP ESFS supporting the processing of branch, fixed assets, purchasing and general ledger transactions, and HRSAP supporting the payroll for POL employees. SAP ESFS is a common platform used by both RMG and POL whereas HRSAP is used by POL users only. As these systems are managed by RMG, the IT audit work is performed as part of the RMG audit procedures but the outcome of the work also impacts POL.
- ▶ For ESFS, the RMG IT audit team identified some control exceptions; however, the RMG team performed additional procedures to obtain evidence and information in mitigation of these issues, and as a result, the POL audit team is able to place reliance on ESFS for audit purposes.
- ▶ For HRSAP, the RMG IT audit team identified a key issue whereby a significant number of users have been granted inappropriate access to make changes directly to the production environment and these direct changes are not logged by the system. This creates a risk that these users may inadvertently make changes to critical payroll-related tables which would have an impact on the payroll run, such as employees' being paid incorrect amounts. This issue has required the POL financial audit team to modify its audit approach, by testing and placing more reliance on the manual business process controls.
- ▶ We recognise that POL has no direct contractual relationship with CSC which provides support services for the HRSAP system on behalf of RMG. However, given the changed nature of POL's relationship with RMG and impending separation, we believe POL should take a proactive approach in resolving the issue with RMG. We understand that POL has already taken steps to engage with RMG and CSC in order to address this concern.
- ▶ We also understand POL plans to implement a separate SAP system by April 2014 which will replace SAP ESFS. As POL progresses its plans on separation, it should consider the impact of these control weaknesses and how these will be addressed in a separated POL IT environment.



## Control themes & observations (cont'd)

### Gaining assurance through the control environment (cont'd)

#### Non-IT control environment observations

We continue to utilise a controls based approach in respect of the identified significant processes of revenue, purchasing, cash settlements and payroll. Our controls testing approach focuses on the controls implemented across the entire POL business, including the London head office, Bolton (payroll), Chesterfield (shared services), branches, cash centres and test controls in London, Bolton and Chesterfield annually.

#### *Financial statement close process*

- ▶ Management continues to employ a robust system of internal controls around its financial reporting and financial statement close process. We note that there continues to be appropriate rigour over both the P11 hard close and P12 year-end processes, with all key balances reconciled in a timely manner and supported by appropriate documentation.

#### *Payroll process*

- ▶ The POL payroll process is independent of the payroll process and systems that support the rest of Royal Mail Group Ltd. It covers approximately 16,000 employees and agents, which primarily include front line workers and agents working at Post Offices around the country. The system supporting this process is the HRSAP system provided by RMG.
- ▶ As highlighted in our IT observations on the previous page, logical access-related issues in the RMG-provided HRSAP system meant that we had to modify our audit approach, by testing and placing more reliance on the manual business process controls and carry out top-up procedures. Aside from this, our work on the manual business process controls for payroll was completed with no significant findings identified, and we were ultimately able to rely on controls in this area.

#### *Transactional, branch and cash centre process and controls*

- ▶ For the revenue, purchasing and cash settlements processes, we note that the controls framework remains consistent with the prior year with no significant findings from our testing. We have completed our walkthroughs and the results of our testing indicate that we will continue to be able to rely on controls.
- ▶ Additionally, our controls testing in respect of branches and cash centres was completed with no findings to communicate to you.

Section 4

# Looking forward



# Looking forward

## Considerations for the coming year



We highlighted in our communications to you last year on our thoughts on how the 'look and feel' of the audit would change as a result of the separation of Royal Mail Group and Post Office. Going forward, as Royal Mail Group continue to seek various options to be privatised, including a potential public offering, and Post Office continues its efforts to improve its business model and commerciality, we continue to see separation and network transformation dominating the agenda in the upcoming years.

These two factors are expected to have the following audit and IT implications, which is not meant to be exhaustive but is provided to indicate how the audit will continue to evolve as POL continues its journey in a post-separation world.

### Impact on substantive and non-IT related testing

- ▶ Assessment of tax implications of carve-out for POL once Royal Mail Group Ltd is not part of same group due to reasons such as a possible public offering; for example, use of tax losses and implications for charging VAT on transactions with Royal Mail Group Ltd;
- ▶ Consideration of completely separate tax and VAT teams for POL and need to acquire knowledge in these specialist areas;
- ▶ Development of accounting facilities for accounts payable and fixed assets function, for which some elements are still done by Royal Mail Group;
- ▶ Development of pension accounting facilities at POL level for RMSEPP scheme, and appointment of actuary to value the RMSEPP defined benefit plan;
- ▶ Consideration of IAS19 (revised) *Employee Benefits* accounting standards on RMPP and RMSEPP pension accounting;
- ▶ Continued development of strategy with regards to treasury function, to make fully independent of Royal Mail Group;
- ▶ Continue to monitor the risk of new financial services revenue line offerings and any audit regulatory related implications (such as FSA regulations);
- ▶ Management should continue to monitor classification of exceptional costs, especially those arising from Network Transformation to ensure such costs are not 'business as usual' and do not recur following the completion of the Network Transformation programme in the next five years.

### Impact on IT

- ▶ Implementation of the IT Transformation programme. Due to size and nature of the transformation, management should ensure that robust governance framework has been built into the model to address the inherent risks of the new IT model. .
- ▶ Implementation of separate SAP system by October 2014 which will replace SAP ESFS. We plan to engage early with management to help ensure we get sufficient assurances throughout the key stages of the implementation to enable us to place reliance on the new system once it goes live.

Section 5

# Summary of audit differences



# Summary of audit differences



In the normal course of any audit, we identify misstatements between amounts we believe should be recorded in the financial statements and amounts actually recorded. These differences are classified as 'known' or 'judgemental'. Known differences represent items that can be accurately quantified and relate to a definite set of facts or circumstances. Judgemental differences generally involve estimation and relate to facts or circumstances that are uncertain or open to interpretation.

We highlight the following misstatements which have not been corrected by management (all amounts in £ millions):

## **1 - Reclassification misstatement - Business Transformation Payments (£6.7m)**

In the prior year, POL had made a commitment to its Crown branch staff for making £3.4m of 'business transformation' payments. POL had accrued for this as a 'creditor' in the year-end accounts since the CWU indicated they were positive towards the offer, and management was highly confident that these payments would be agreed and paid post year-end. However, during the current year the programme did not progress as expected and this accrual remains unutilised.

During the current year, management has made a new offer of 'business transformation' payments totalling £6.7m (which includes the £3.4m which has already been accrued for last year) and these will be paid by POL in return for staff agreeing to the plan to make significant transformational changes to their working practices over the next 2 years. Management have written an accounting paper on their treatment, and we are satisfied that their profit and loss accounting treatment complies with IAS 37 and satisfy the definition of provisions.

POL has recorded this business transformation payment as an accrual rather than a provision. From our review, we believe that these payments are by nature a provision and not an accrual in accordance with IAS37, due to the element of uncertainty of whether the CWU will accept or reject POL's offer.

Accordingly, we have proposed that the amount of £6.7m be reclassified from accruals to provisions.

## **2- Reclassification misstatement - DVLA Remuneration Accrual (£3.2m)**

During the year, Management also made an offer of 'DVLA' remuneration payments totalling £3.2m, payable to Post Office's sub-postmaster agents (who work in Post Office branches) in order to partially compensate them for the reduced rates to be paid in relation to the DVLA road tax products. The payout of the DVLA payment offer is subject to acceptance of this offer by the National Federation of Subpostmasters (NFSP), who represent Post Office subpostmaster agents).

POL has recorded these DVLA payments as an accrual rather than a provision. However, similar to the business transformation payments discussed above, from our review of management's underlying work, we believe this accrual is also by nature a provision and not an accrual, as the NFSP could accept or reject this offer, which means that these payments have an element of uncertainty into whether the payout will actually be made.

Accordingly, we have proposed that the amount of £3.2m be reclassified to from accruals to provisions.

# Summary of audit differences

## 3 - Turnaround adjustment - LTIP Bonus Accrual (£1.9m)

The LTIP Bonus creditor was overstated by £1.9m at the prior year-end as management accrued for the full LTIP expense of the 2010/11 award and 2011/12 award by the end of the prior year. This was assessed by EY to be not in compliance with IAS19 *Employee Benefits* which requires that the award for such benefits be spread evenly over the lifetime of the bonus award until vested/paid. This was not adjusted for in the prior year accounts.

Management corrected the LTIP bonus creditor in the current period to ensure the closing 2012-13 accrual position is fairly stated as per IAS19. This has resulted in a turnaround adjustment impacting current year and prior year comparative profit before tax, where current year profit before tax is overstated by £1.9m, and prior year comparative profit before tax is understated by £1.9m.

Our summary of unadjusted audit differences is as follows:

Uncorrected misstatements	Assets current	Assets non- current	Liabilities current (£m)	Liabilities non- current	Income/ expenses	Equity
	Debit/ (Credit)	Debit/ (Credit)	Debit/ (Credit)	Debit/ (Credit)	Debit/ (Credit) Current period	Debit/ (Credit)
<b>Errors:</b>						
▶ <b>1) Business Transformation Payments Reclassification Misstatement</b>						
Dr. Accruals			6.7			
Cr. Provisions			(6.7)			
▶ <b>2) DVLA Remuneration Accrual Reclassification Misstatement</b>						
Dr. Accruals			3.2			
Cr. Provisions			(3.2)			
▶ <b>3) LTIP Bonus Accrual Turnaround Adjustment</b>						
Dr. Current Year P&L					1.9	
Cr. Prior Year P&L						(1.9)
Income statement total					(49)	
Balance sheet totals	1,342	168	(1,211)	(11)		
Income effect of uncorrected misstatements (before tax)					1.9	
Less: tax effect at current year marginal rate					0.5	
Cumulative effect of uncorrected misstatements before turnaround effect					1.4	
Turnaround effect					(1.4)	
Cumulative effect of uncorrected misstatements, after turnaround effect					-	

# Appendices

**Appendix A - Independence report**

**Appendix B - Draft letter of representation**

**Appendix C - Required communications with the Audit and Risk Committee**



## Appendix A

# Independence update

We confirm there are no changes in our assessment of independence since our confirmation in our planning board report. We complied with the APB Ethical Standards and in our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter that should be reviewed by both you and ourselves. It is therefore important that you and your Audit Committee consider the facts of which you are aware and come to a view. If you wish to discuss any matters concerning our independence, we will be pleased to do so at the forthcoming meeting of the Audit Committee on 21 May 2013.

## Relationships, services and related safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective.

Description of relationship or service and related independence threat	Period provided/duration	Safeguards adopted and reasons considered to be effective
<b>Service 1:</b> Fujitsu ISAE 3402 report - ISAE3402 report for the Fujitsu services supporting the POL account. This report will provide an assessment of the Fujitsu controls supporting POL business critical systems. The intention is to place reliance on the ISAE3402 as part of the 2012-13 financial statement audit.	April 2012 to February 2013	<ul style="list-style-type: none"> <li>▶ Not a prohibited service</li> <li>▶ A separate team from the POL IT team has been engaged for the review of the ISAE3402 report, and standard ring fencing applied between two teams.</li> <li>▶ Went through review exercise to ensure in line with Ernst &amp; Young independence rules</li> </ul>
<b>Service 2:</b> ISAE 3000 report on POL Note Circulation Scheme related services to the Bank of England for the FY2012-13 period and to be performed in May 2013.	Performed on continued annual basis	<ul style="list-style-type: none"> <li>▶ Not a prohibited service</li> <li>▶ These are standard agreed-upon-procedures, where management instructs us on exactly the procedures to be performed and we conclude by issuing a factual findings report only.</li> </ul>
<b>Service 3:</b> Agreed-upon procedures performed which relate to testing of covenants relating to the loan from the Department of Business, Innovation and Skills (BIS). This is a standard Agreed-Upon Procedures service which has been performed for the past five years and is in the process of being performed in May 2013.	Performed on continued annual basis	<ul style="list-style-type: none"> <li>▶ Not a prohibited service</li> <li>▶ These are standard agreed-upon-procedures, where management instructs us on exactly the procedures to be performed and we conclude by issuing a factual findings report only.</li> </ul>
<b>Service 4:</b> Agreed-upon procedures performed to ensure that the amount which is collected by Post Office Limited on behalf of the DVLA for road tax is subsequently paid over to the DVLA. This is a standard agreed-upon procedures service which has been performed for the past six years, and is in the process of being performed in May 2013.	Performed on continued annual basis	<ul style="list-style-type: none"> <li>▶ Not a prohibited service</li> <li>▶ These are standard agreed-upon-procedures, where management instructs us on exactly the procedures to be performed and we conclude by issuing a factual findings report only.</li> </ul>

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that Ernst & Young is independent and the objectivity and independence of the audit engagement partner and the audit engagement team have not been compromised.



## Appendix A

## Independence update (cont'd)

### Fees update

As part of our reporting on our independence, we set out below a summary of fees for the year ended 31 March 2013.

£000s	2012
- Post Office Limited audit fee*	330.6
<b>Total audit fees</b>	<b>330.6</b>
- Note Circulation Scheme ISAE 3000 Report*	78.0
- BIS Agreed Upon Procedures Report**/**	12.0
- DVLA Agreed Upon Procedures Report**/**	13.5
<b>Total non-audit services</b>	<b>103.5</b>
<b>Total</b>	<b>434.1</b>

\*Excludes out of pocket expenses incurred

\*\* Fees to be finalised

### Confirmations

Ernst & Young LLP (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Ernst & Young LLP Transparency Report which the Firm is required to publish by law. The most recent version of this Report is for the year ended 30 June 2012 and can be found here: <http://www.ey.com/UK/en/About-us/About-EY---Transparency-Report>.

We are not aware of any inconsistencies between the company's policy for the supply of non audit services and APB Ethical Standards. We are not aware of any apparent breach of that policy.

We confirm that in our professional judgment, the firm is independent.

We confirm that the engagement team and others within the firm, the firm and network firms have complied with relevant ethical requirements regarding independence.



Appendix B

# Management representation letter for statutory reporting

xx June 2013

Ernst & Young  
1 More London Place  
London SE1 2AF

Dear Sirs,

This representation letter is provided in connection with your audit of the consolidated and parent company financial statements of Post Office Limited (the Group and Company) for the 53 weeks ended 31 March 2013 (the period). We recognise that obtaining representations from us concerning the information contained in this letter is a significant procedure in enabling you to form an opinion as to whether the consolidated and parent company financial statements give a true and fair view of the financial position of the Group and Company financial position of Post Office Limited as of 31 March 2013 and of its results of operations and its cash flows for the period then ended in accordance with IFRS and UK GAAP respectively.

We understand that the purpose of your audit of our consolidated and parent company financial statements is to express an opinion thereon and that your audit was conducted in accordance with International Standards on Auditing (UK and Ireland), which involves an examination of the accounting system, internal control and related data to the extent you considered necessary in the circumstances, and is not designed to identify - nor necessarily be expected to disclose - all fraud, shortages, errors and other irregularities, should any exist.

Accordingly, we make the following representations, which are true to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

## A. Financial Statements and Financial Records

We have fulfilled our responsibilities, as set out in the terms of the audit engagement letter dated 25 February 2013, for the preparation of the consolidated financial statements in accordance with IFRS and the standalone company financial statements in accordance with UK GAAP.

We acknowledge, as members of management of the Group and Company, our responsibility for the fair presentation of the financial statements. We believe the financial statements referred to above give a true and fair view of (or 'present fairly, in all material respects') the financial position, results of operations and cash flows of the Group and Company in accordance with IFRS and UK GAAP respectively, and are free of material misstatements, including omissions. We have approved the consolidated and parent company financial statements.

The significant accounting policies adopted in the preparation of the financial statements are appropriately described in the financial statements.

As members of management of the Group and Company, we believe that the Group and Company have a system of internal controls adequate to enable the preparation of accurate Group financial statements in accordance with IFRS and the Company financial statements in accordance with UK GAAP that are free from material misstatement, whether due to fraud or error.

We believe that the effects of any unadjusted audit differences, summarised in the accompanying schedule, accumulated by you during the current audit and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the Group and Company financial statements taken as a whole. We have not corrected these differences identified by and brought to the attention from the auditor because we do not believe that they are material to the reader's understanding of the Group and Company financial statements.



## Appendix B

# Management representation letter for statutory reporting (cont'd)

## B. Fraud

We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.

We have disclosed to you the results of our assessment of the risk that the Group and Company financial statements may be materially misstated as a result of fraud.

We have disclosed to you all significant facts relating to any frauds, suspected frauds or allegations of fraud known to us that may have affected the Group and Company (regardless of the source or form and including, without limitation, allegations by 'whistle-blowers'), whether involving management or employees who have significant roles in internal control. Similarly, we have disclosed to you our knowledge of frauds or suspected frauds affecting the entity involving others where the fraud could have a material effect on the Group and Company financial statements. We have also disclosed to you all information in relation to any allegations of fraud or suspected fraud communicated by employees, former employees, analysts, regulators or others, that could affect the Group and Company financial statements.

## C. Compliance with Laws and Regulations

We have disclosed to you all known actual or suspected noncompliance with laws and regulations whose effects should be considered when preparing the Group and Company financial statements.

## D. Information Provided and Completeness of Information and Transactions

We have provided you with:

Access to all information of which we are aware that is relevant to the preparation of the Group and Company financial statements such as records, documentation and other matters as agreed in terms of the audit engagement.

Additional information that you have requested from us for the purpose of the audit and

Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.

All material transactions have been recorded in the accounting records and are reflected in the Group and Company financial statements.

We have made available to you all minutes of the meetings of shareholders, directors and committees of directors (or summaries of actions of recent meetings for which minutes have not yet been prepared) held through to the most recent meeting on xx May 2013.

We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the Group's related parties and all related party relationships and transactions of which we are aware, including sales, purchases, loans, transfers of assets, liabilities and services, leasing arrangements, guarantees, non-monetary transactions and transactions for no consideration for the period ended, as well as related balances due to or from such parties at the year end. These transactions have been appropriately accounted for and disclosed in the consolidated financial statements.

We have disclosed to you, and the Group and Company has complied with, all aspects of contractual agreements that could have a material effect on the Group and Company financial statements in the event of non-compliance, including all covenants, conditions or other requirements of all outstanding debt.

## E. Liabilities and Contingencies

All liabilities and contingencies, including those associated with guarantees, whether written or oral, have been disclosed to you and are appropriately reflected in the Group and Company financial statements.

We have informed you of all outstanding and possible litigation and claims, whether or not they have been discussed with legal counsel.



Appendix B

## Management representation letter for statutory reporting (cont'd)

We have recorded and/or disclosed, as appropriate, all liabilities related litigation and claims, both actual and contingent, and have disclosed in the Group and Company financial statements all guarantees that we have given to third parties.

### F. Subsequent Events

Other than those disclosed, there have been no events subsequent to period end which require adjustment of or disclosure in the Group and Company financial statements or notes thereto.

### G. Accounting Estimates

We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.

Accounting estimates recognized or disclosed in the Group and Company financial statements:

- We believe the measurement processes, including related assumptions and models, we used in determining accounting estimates is appropriate and the application of these processes is consistent.
- The disclosures relating to accounting estimates are complete and appropriate in accordance with the applicable financial reporting framework.
- The assumptions we used in making accounting estimates appropriately reflects our intent and ability to carry out specific courses of action on behalf of the entity, where relevant to the accounting estimates and disclosures.
- No subsequent event requires an adjustment to the accounting estimates and disclosures included in the Group and Company financial statements.

### H. Going Concern

Note 1 to the Group and Company financial statements discloses all of the matters of which we are aware that are relevant to the Company's ability to continue as a going concern, including significant conditions and events, our plans for future action, and the feasibility of those plans.

### I. Contingent Liabilities

We are unaware of any violations or possible violations of laws or regulations the effects of which should be considered for disclosure in the Group and Company financial statements or as the basis of recording a contingent loss (other than those disclosed or accrued in the Group and Company financial statements).

We are unaware of any known or probable instances of non-compliance with the requirements of regulatory or governmental authorities, including their financial reporting requirements, and there have been no communications from regulatory agencies or government representatives concerning investigations or allegations of non-compliance.

*Yours Faithfully,*

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Chief Financial Officer



## Appendix C

# Required communications with the Audit and Risk Committee

There are certain communications that we must provide to the Audit and Risk Committees. We have detailed these here together with a reference of where and when they were covered:

	Communicate when event occurs	Communicate on a timely basis, at least annually	Planned/actual timing of communication to the Audit and Risk Committee
<b>Communications required on all audits</b>			
Overview of planned scope and timing of the audit		✓	Refer to our 2012-13 Audit Planning Report dated 12 November 2013.
Major issues discussed with management in connection with initial or recurring retention	✓		Refer to our 2012-13 Audit Planning Report dated 12 November 2013.
Other information in documents containing audited financial statements		✓	Discussed within this report.
Significant audit adjustments		✓	Discussed within this report.
Unrecorded misstatements considered by management to be immaterial		✓	Discussed within this report.
Expected modifications to the audit report		✓	Not applicable, we do not anticipate any modifications to our audit report.
Our judgements/views about qualitative aspects of the Company's accounting practices and financial reporting		✓	Discussed within this report.
Disagreements with management	✓		Discussed within this report.
Consultations with other accountants	✓		Not applicable, no such instance noted during our audit.
Serious difficulties encountered in dealing with management when performing the audit	✓		Not applicable, no such instance noted during our audit.
The adoption of, or a change in, an accounting policy	✓	✓	We note that POL has adopted IFRS in its consolidated accounts, which will be prepared for the first time this year. This has also been discussed in this report as well as during the Planning Audit Committee meeting on 12 November 2012.



## Appendix C

# Required communications with the Audit and Risk Committee (cont'd)

	Communicate when event occurs	Communicate on a timely basis, at least annually	Planned/actual timing of communication to the Audit and Risk Committee
<b>Communications required on all audits (cont'd)</b>			
Methods of accounting for significant unusual transactions and for controversial or emerging areas	✓	✓	Discussed within this report.
Events or conditions that cause us to conclude that there is substantial doubt about the entity's ability to continue as a going concern	✓	✓	Not applicable - no such events and conditions to communicate to the committee.
Sensitive accounting estimates		✓	Discussed within this report.
Consideration of laws and regulations		✓	Discussed within this report.
Fraud and illegal acts involving senior management and fraud and illegal acts that cause a material misstatement of the financial statements	✓		No such instances of fraud to communicate.
Significant matters arising during the audit in connection with the entity's related parties		✓	Not applicable - no such matters to communicate to the committee.
Management's refusal for us to request external confirmations or our inability to obtain relevant and reliable audit evidence from other procedures		✓	No such instances to communicate.
Representations that the auditor is requesting from management		✓	We have attached management letters of representation in our appendix as part of this report.
Significant deficiencies and material weaknesses in internal control over financial reporting		✓	This will be included, as necessary, within our Controls, Themes and Observations Report which will be shared with you after the conclusion of our audit.
<b>Group audits</b>			
<ul style="list-style-type: none"> <li>▶ An overview of the type of work to be performed on the financial information of the components</li> <li>▶ An overview of the nature of the Group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components</li> <li>▶ Instances where the Group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work</li> </ul>		✓	Discussed within this report.
Any limitations on the Group audit, for example, where the Group engagement team's access to information may have been restricted			
Fraud or suspected fraud involving Group management, component management, employees who have significant roles in Group-wide controls or others where the fraud resulted in a material misstatement of the Group financial statements.	✓	✓	No such instances of fraud to communicate.



## Appendix C

## Required communications with the Audit and Risk Committee (cont'd)

	Communicate when event occurs	Communicate on a timely basis, at least annually	Reference
Audit and Risk Committee pre-approval of services, including specific pre-approval of internal control-related services and non-prohibited tax services		✓	Discussed within this report.
Critical accounting policies and practices. ISA 260 (UK and Ireland) requires the auditor to communicate the auditor's views on the qualitative aspects of the Company's accounting practices and financial reporting		✓	Discussed within this report.
All material alternative accounting treatments discussed with management		✓	Discussed within this report.
Fees		✓	Discussed in our planning report dated 12 November 2013 and in this report.
Other material written communications with management		✓	Discussed within this report.
Communication of independence matters		✓	Discussed within this report.
Other findings or issues regarding the oversight of the financial reporting process		✓	Discussed within this report.



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**POST OFFICE AUDIT, RISK AND COMPLIANCE COMMITTEE**

**Update on various Financial Services matters, including  
Bank of Ireland (UK) plc capital & liquidity**

**1. Purpose**

The purpose of this paper is to:

- 1.1 update the Committee on the Bank of Ireland (UK) plc's ("Bol") capital and liquidity position against its regulatory and Eagle contract requirements;
- 1.2 provide an update on the implementation of the Capital Requirements Directive IV (CRD IV) and its potential impact on the capital requirements on Bol;
- 1.3 update the Committee on Project Polo; and
- 1.4 update the Committee on the current Co-operative Bank plc situation and any potential impact on the Post Office.

**2. Bank of Ireland (UK) - Capital and Liquidity position**

- 2.1 A condition of the Financial Services Joint Venture Agreement ("FSJVA") is that Bol must attest bi-annually that it is meeting the capital and liquidity thresholds set out in the agreement.
- 2.2 The Bank's capital and liquidity reports are part of the early warning system that would enable the Post Office to take action in accordance with the termination provisions of the agreement, should this become necessary.
- 2.3 Bol has certified as at 31<sup>st</sup> December 2012 (Bol's year-end) that:
  - Bol's Core Tier 1 Capital Ratio exceeded the amount required under the FSJVA;
  - Bol was holding a surplus over its regulatory liquidity requirements;
  - Bol is meeting the Capital Planning Buffer as set by the regulator.
- 2.4 Bol also confirmed that at no stage in the six months to 31<sup>st</sup> December 2012 did it breach any of the termination thresholds.
- 2.5 On 30<sup>th</sup> January 2013 Post Office executives met with the tripartite regulators (Bank of England, HM Treasury and Financial Services Authority) to confirm the status of the Post Office's relationship with Bol and the termination structure and processes. No material issues were raised by any party.
- 2.6 Post Office is of the view that Bol remains well capitalised with surplus liquidity. The position has not deteriorated since the signing of Eagle.

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**3. CRD IV Update**

- 3.1 The European Parliament passed CRD IV on 16<sup>th</sup> April 2013 and it is now in legal drafting review ahead of formal adoption. The UK's Prudential Regulation Authority ("PRA") will seek to implement the requirements from 1<sup>st</sup> January 2014.
- In order to achieve this, the PRA intends to carry out two consultations on the changes. It is expected that the majority of existing capital requirement rules will be replaced by the new rules. The main consultation will begin in mid-2013.
- 3.2 Following implementation, the FSJVA requires Bol to certify to the Post Office that it is meeting the new standards.

**4. POLO update**

- 4.1 On 13<sup>th</sup> May 2013 Post Office and Bol launched the Polo current account in 29 branches in East Anglia.
- 4.2 To enable the launch the Parties concluded the first operational Product Note<sup>1</sup>.
- 4.3 Under Eagle all contracts in place at the time of signing were included in specific conditions relating to the sharing of any contract liability between the parties.
- 4.4 As part of the finalisation of the Polo Product Note, Bol requested that its contract with Affinion International Limited<sup>2</sup> should be included in these conditions. Bol's request was that, although the contract was not signed at the time of Eagle, Post Office was closely involved in the selection of Affinion, took part in the on-site operational reviews and made comments on the early draft of the contract. The potential liability risks potentially resulting from this contract are seen as slight.
- 4.5 To avoid a delay to the launch of Polo, Post Office agreed to Bol's request.
- 4.6 Post Office is working with Bol to establish a monitoring framework for this contract.

**5. Co-operative Bank plc update**

- 5.1 On 9<sup>th</sup> May Moody's downgraded the Co-operative Bank's credit rating from Baa1 to B1 ("junk" status), and continues to hold it on negative watch. Moody's has assessed that Co-Operative Bank has significantly lower levels of capital than its peers and is currently, by its own assessment below the Basle III CET 1 ratio of 7.0% at 6.7% (in January 2013).
- 5.2 The bank is in discussions with the PRA about improving its capital position, which could include selling its insurance business and potentially seeking more capital from the parent group.
- 5.3 The Post Office is monitoring the situation for the commercial opportunities this may present as well as any exposure we have to Co-operative Bank through our

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<sup>1</sup> The Product Note is the structure, established under Eagle, which establishes the product and distribution strategy, roles and responsibilities of each party, commission payments, withdrawal arrangements and other relevant matters and must be agreed prior to the launch of any product.

<sup>2</sup> The 3rd party that manages elements of the Package account.

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personal banking and bill payment business. Currently our overnight exposure to Co-operative Bank is very low (c£1 million owing from the bank and c£10m due from the Post Office).

**6. Recommendations**

The Committee is asked to:

- 6.1 note the update.

**Nicholas Kennett**  
**Director, Financial Services**  
**21 May 2013**