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required to make contributions to, or otherwise financially support, the Post Office Section (or any pension scheme to which the assets and liabilities of the Post Office Section are transferred in the future) if the Pensions Regulator considered that to be a reasonable exercise of its powers under the Pensions Act 2004 (as amended). The Pensions Regulator's powers will continue in respect of the Post Office Section for as long as RMG continues to be associated or connected with POL and for two years (in respect of a financial support direction) or six years (in respect of a contribution notice) after such association or connection has ceased. Such association or connection will cease on a change of control of RMG involving HM Government ceasing to hold, directly or indirectly, one third or more of the shares in RMG. However, the Post Office Section is estimated by the scheme actuary as at 31 March 2013 to not have a buy-out deficit.

1.18 The Group's relationship with POL exposes it to a number of material risks

Post Office branches serve as the Group's principal retail distribution network in the UK and the Group's distribution agreement with POL limits its ability to use other retail channels

The UK's network of more than 11,500 Post Office branches is a key sales channel for the Group's products in the UK and serves as the Group's principal retail distribution network in the UK. The Group's relationship with the Post Office is of material significance to the business and revenue of the Group. In FYE 2013, approximately £1.7 billion of the Group's revenue was generated through the sale of Royal Mail postage stamps and the Group's products by POL on the Group's behalf.

Under the Mails Distribution Agreement (further detail on which can be found in section 16.2(A) of Part XI (*Additional Information*)) between RMG and POL, POL sells Royal Mail postage stamps and the Group's letter and parcel products, under both the "Royal Mail" and the "Parcelforce Worldwide" brands. Part of the UK's Post Office network is used to satisfy part of RMG's obligation to provide access points for universal postal services under the designated universal service provider condition issued by Ofcom in March 2012. Post Office branches will continue to serve as points for the collection of letters and parcels by customers, including pursuant to the "click and collect" service announced by the Group in May 2013.

The Mails Distribution Agreement imposes limitations on the ability of the Group to use third party retail outlets in the UK for the sale or distribution of its products. The Group may be required to use POL's branch network as the retail outlet for any new products it wishes to introduce even if in the future there are circumstances in which POL may not be the Group's preferred retail partner, with the potential result that the Group is not able to realise all or part of the benefits that it expects from that new product. The Group is also reliant to an extent on POL to ensure that Post Office branches provide a physical estate and environment in which customers want to purchase the Group's products or ask for advice on sending items through the post. Furthermore, the Group's ability to introduce new products and services may be adversely affected by operational problems or limitations that may be encountered by POL. As an example, the Group is reliant on POL in connection with the successful implementation of its new "click and collect" service. Any limitations in POL's IT systems, or the ability of the Group's and POL's IT systems to interface with each other, may affect the ability of the Group to introduce new products or services (including Royal Mail's "click and collect" service) successfully through POL's branch network.

Although Royal Mail sells postage stamps through other sales channels, revenue generated for the Group under the Mails Distribution Agreement represents a significant proportion of the Group's total revenue and this, combined with the limitations accepted by RMG on its ability to use other retail outlets in addition to Post Office branches, means that the Group has a significant reliance on POL and POL's ability to meet its service obligations under the Mails Distribution Agreement.

Risk of material operational failure by POL

Any material failure by POL to meet its obligations under the Mails Distribution Agreement (including as a result of a failure of POL's IT systems or industrial action by POL's employees) could result in retail customers not being able to purchase the Group's products, or use the Group's services, at some or all Post Offices, which could have a material adverse effect on the Group's reputation, business, results of operations, financial position and prospects. POL is in the process of implementing its own modernisation programme in relation to its network of Post Office branches which may lead to localised service and quality disruptions, including as a result of industrial action, or lack of cooperation, affecting POL and/or all or part of the Post Office branch network.

The Group is also dependent on the effective operation of POL's IT and or other systems and processes for the successful provision of services by POL, including the sale of the Group's products in Post Office branches across the UK. Any material failures in POL's IT and or other systems and processes, including

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their interface with the Group's own IT systems, could cause material disruption to the operations of the Group and could affect the ability of POL to provide services for the Group, including the sale of the Group's products. Any such failures or disruption could have a material adverse effect on the Group's reputation, results of operations, financial condition and prospects.

Possible termination or expiry of the Mails Distribution Agreement

The provision of services under the Mails Distribution Agreement commenced on 26 March 2012, and the agreement will continue in force until at least the tenth anniversary of the date the agreement was signed (19 January 2012), subject to scheduled renegotiation events or termination in certain limited circumstances before the end of such period. Although the Group would have notice of POL's intention not to renew the agreement and would have the opportunity to develop alternative distribution arrangements, the termination or expiry of the agreement would result in the Group ceasing to have access to its principal retail distribution network in the UK which could have a material adverse effect on the business, results of operations, financial position and prospects of the Group. If the agreement were renewed or extended so that it did not expire in accordance with its terms, the new terms of any agreement with POL may be less favourable to the Group than the terms on which the current arrangements were concluded. Any deterioration in the terms on which the Group and POL contract could have a material adverse effect on the Group's results of operations, financial condition and prospects.

Further, the Mails Distribution Agreement provides for a number of renegotiation events whereby RMG and POL are to meet in good faith to enter into discussions with a view to agreeing amendments to the agreement. Under one such renegotiation event, the Mails Distribution Agreement and its operation will be reviewed by the parties within six weeks following the fifth anniversary of the commencement date to ensure that it continues to meet both parties' expectations and takes into account changing market dynamics over the first five years of the term. There is a risk that, following the occurrence of a renegotiation event under the Mails Distribution Agreement, the terms of any new agreement with POL may be less favourable to the Group than the terms of the current agreement. Any deterioration in the terms on which the Group and POL contract could have a material adverse effect on the Group's results of operations, financial condition and prospects.

Public perceptions that Royal Mail and POL are the same entity

There remains a perception on the part of some customers of the Group and some members of the general public in the UK that the "Post Office" and "Royal Mail" are the same entity. Any operational failure, disruption or industrial action affecting POL and/or the Post Office branch network, and/or any other business or commercial decisions taken by POL, could therefore be perceived as decisions taken by, or events relating directly to, the Group and adversely affect the reputation and brand of the Group. In particular given this perception on the part of some customers and members of the general public, any failure in POL's IT or other systems (including any failure which affects POL's ability to sell the Group's products and services) may lead to adverse publicity and adversely affect the reputation and brand of the Group.

The Group faces risks associated with the separation of POL's IT systems and infrastructure from those of the Group

Under the Master Services Agreement (further details on which can be found in section 16.2(B) of Part XI (*Additional Information*)), the Group provides certain services on a transitional basis to POL. POL is currently heavily dependent on the Group for the provision of IT services under the Master Services Agreement, including certain services provided through the Group's external IT suppliers. The IT services provided by the Group to POL are complex and cover a range of areas. Any failure in the Group's own IT systems, infrastructure or estate which affects the level of service which it is able to provide to POL may lead to adverse publicity and reputational damage for the Group. The Group and POL are undertaking a joint programme to deliver the required standalone IT capability for POL in order to facilitate the cessation of the provision of IT services by the Group to POL. The programme was originally intended to be completed by September 2014, when the provision of IT services to POL under the Master Services Agreement is due to terminate. However, as it is expected that some separation projects will go beyond September 2014, it is likely that POL will require certain ongoing IT services from the Group (and its external IT suppliers) after September 2014. Further details regarding the separation of POL's IT systems and infrastructure from those of the Group can be found in section 9.4 of Part II (*The Business*).

The ITST Programme (which is described further in section 1.15 of these Risk Factors) faces certain risks if the separation of POL's IT systems and infrastructure from those of the Group has not been completed by

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the time the Group transitions to its new IT arrangements as part of the ITST Programme. If this occurs, the Group could choose to delay the implementation of the ITST Programme. Alternatively, the scope of the ITST Programme, which does not currently include the provision of ongoing services to POL, may need to be changed to include the provision of services to POL. This could expose the Group to a challenge that the ITST Programme is not compliant with public procurement law, which, if successful, could have a number of material adverse consequences for the Group including the suspension of the ITST Programme or the award of a contract under the ITST Programme being deemed void and unenforceable. The ongoing provision of IT services to POL during the ITST Programme transition period would add considerable complexity to the transition, which would require the transition of additional services (or volumes of services) to the external suppliers selected as part of the ITST Programme. Such complexity may affect the level of service assurance which the Group could provide to POL during the ITST Programme transition period and would be likely to result in the need for the devotion of significant additional management time and other Group resources. In addition, the completion of the separation of POL's IT from that of the Group following the transition to the ITST Programme may adversely impact the Group's ability to execute its ongoing IT transformation activities. Any of the foregoing events could have a material adverse effect on the Group's business, prospects, results of operations and financial position.

The separation of POL's IT from that of the Group is a complex programme for both POL and the Group which requires significant management time and other Group and POL resources. Moreover, any failure or delay in completing the separation of POL's IT from that of the Group may lead to adverse publicity and reputational damage for the Group. Although the Group does not currently anticipate any material impediments in this regard, it may not, for technical reasons, be possible to achieve the entire separation of POL's IT systems and infrastructure from those of the Group as currently planned. As a result, POL may continue to be dependent on the Group for the provision of all or part of its IT systems and infrastructure in the future. The ongoing provision of IT systems and infrastructure by the Group to POL would be likely to require management time and other Group resources. Any of the foregoing events could have a material adverse effect on the Group's business, prospects, results of operations and financial position.

From Admission, the Group and POL will cease to be under common ownership

Prior to Admission, the Group and POL will be wholly-owned subsidiaries of the Selling Shareholder (and thereby, HM Government) but this will cease from Admission. Following Admission, POL will, subject to the PSA, remain under the ownership of the Selling Shareholder (and thereby, HM Government). There is therefore a risk that the Group's relationship with POL may change when they cease to be wholly-owned by, and under the control of, a common shareholder. Furthermore, it is possible that HM Government policy might change in the future in relation to the Post Office network, leading, in certain circumstances, to a reduction in the number of Post Office branches in the UK at which customers are able to purchase "Royal Mail" and "Parcelforce Worldwide" products and services. While, in the Mails Distribution Agreement, POL has agreed to use its reasonable endeavours to maintain a network of at least 11,500 Post Office branches until at least the end of March 2015, any material reduction in the size of the Post Office branch network could have a material adverse effect on the Group's results of operations, financial condition and prospects. Further information in relation to HM Government policy with respect to the Post Office can be found in Part V (*Relationship with HM Government*).

Draft European Directive relating to transactions in "vouchers"

In May 2012, the European Commission published a proposal for a Directive to change the VAT treatment of transactions in, or concerning, "vouchers" under the provisions of the Directive of 28 November 2006 on the Common System of Value Added Tax (Directive 2006/112/EC). The definition of a "voucher" in the draft Directive does not refer specifically to postage stamps but is expressed in terms which would be likely to encompass postage stamps.

It is uncertain whether this draft Directive will be adopted by the EU member states, either in its current form or in some amended form. Nor is it certain when the draft Directive, if so adopted, would be implemented in UK law. However, if the draft Directive were to be adopted in its current form, the resultant changes to the UK VAT treatment of transactions in postage stamps would potentially give rise to an increased cost for the Group. This is because the Mails Distribution Agreement between RMG and POL described in section 16.2(A) of Part XI (*Additional Information*) provides, as more fully explained in that section, for a substantial part of the remuneration earned by POL under that agreement to accrue to POL, once RMG and POL have ceased to be members of the same VAT group (which they will do if, upon implementation of the Offer, HM Government no longer has "control" of RMG and may do in other circumstances), as profit margin on the purchase and sale by POL of Royal Mail postage stamps (the "**POL Margin**"). It has been proposed to HMRC

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that the POL Margin should not, under current law, be liable to VAT and HMRC have accepted this in respect of part of the POL Margin. The implementation in UK law of the draft Directive in its current form would potentially change that treatment and require POL instead to account for VAT on the whole of the POL Margin. The resultant additional irrecoverable VAT cost to be borne by RMG in that event could have a material adverse effect on the Group's results of operations, financial condition and prospects.

1.19 The Group's IT systems are at risk of security breaches and attacks, including hacking and vandalism

As is the case with other entities that make material use of IT, security breaches or attacks on the Group's websites or IT systems could interrupt the Group's operations or materially impact its ability to conduct business or otherwise adversely affects its reputation. Repeated incidents could compromise the Group's ability to provide services to its customers and could result in the loss of business relationships. Any such incidents could have an adverse effect on the Group's results of operations, financial condition and future prospects. The Group cannot guarantee absolute protection against unauthorised attempts to access its websites and IT systems. Moreover, the risk of incidents regarding the Group's websites and IT systems may be increased as a result of the failure by the Group to properly and adequately maintain its IT infrastructure and systems. Viruses, worms and other malicious software programmes could, among other things, jeopardise the security of information stored in a user's computer or in the Group's computer systems or attempt to change the internet experience of customers by interfering with the Group's ability to connect with its customers. If any compromise in the Group's security measures were to occur and the Group's efforts to combat this breach were unsuccessful, the Group's reputation could be harmed leading to an adverse effect on the Group's results of operations, financial condition and future prospects. Further, the Group's insurance coverage might not adequately compensate it for material losses that could occur due to disruptions to its service as a result of failure of its websites or IT systems. The Group may also be subject to attempts to unlawfully obtain its data and other proprietary information through hacking, security attacks and other means. Any loss of data or information in this way may damage the reputation of the Group and lead to a material adverse effect on the Group's results of operations, financial condition and prospects. In addition, any such loss of data or information may lead to the imposition of sanctions, including fines and censure, against the Group, as further described in Risk Factor 1.35 below.

1.20 The Group's brands, reputation and goodwill are central to its customer and market perception and may be affected by a number of factors

The Group's brands and reputation are central to its customer and market perception (including by the general public in the UK). The Group operates in an industry where integrity, trust and confidence are paramount and is consequently exposed to risks, many of which are outside the control of the Group, including: failures or delays in the delivery of items to customers and other operational failures, including as a result of severe weather; failure or default by suppliers and sub-contractors; employee misconduct; adverse regulatory investigations, enquiries and actions; negative publicity; and press speculation (including widespread adverse social media commentary). Such eventualities could impact the Group's brands or reputation causing loss of consumer confidence and customers, which could in turn have a material adverse effect on the Group's results of operations, financial condition and prospects.

1.21 The Group may not be permitted to continue to use certain associations with the British Monarchy in the future

The Group is currently permitted to use the Royal Cypher (the *EIIR* symbol) and the Royal Crown emblem (together, the "**Royal Associations**"), which are associations connected with HM The Queen, pursuant to the terms of the Royal Associations Agreement. There can be no certainty that the Group will be able to use the Royal Associations indefinitely as consent to use them may be withdrawn in the circumstances set out in the Royal Associations Agreement. If the Group is required to cease using the Royal Associations in the future, it will incur significant costs as a result of the rebranding exercise it would be required to undertake to remove the Royal Associations from its branding. This may have a material adverse effect on the Group's financial condition and results of operations. Any such rebranding could also adversely impact the reputation and goodwill of the Group as a result of public and customer perception of the removal of the Royal Associations. Investors should also note that the rights granted to the Group under the Royal Associations Agreement will be reviewed upon the accession of a new Sovereign. See section 16.4(B) of Part XI (*Additional Information*) for further details of the Royal Associations Agreement.