

## **Royal Mail Holdings plc**

Control themes and observations  
for the year ended 27 March 2011





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**Private and confidential**

Mike Prince  
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15 November 2011

Dear Mike,

**Control themes and observations arising from the 2010-11 audit**

We have completed our procedures in relation to the audit of Royal Mail Holdings plc and substantially completed the audit of its subsidiary undertakings for the year ended 27 March 2011.

The key control themes and observations from our audit were discussed in the May 2011 Audit Results Report and are detailed in each section of this report. We have also noted a number of more routine observations in the report, which have been agreed with management.

Our review of the Group's systems of internal control is carried out to help us express an opinion on the accounts of the Group as a whole. This work is not primarily directed towards the discovery of weaknesses, the detection of fraud or other irregularities (other than those which would influence us in forming that opinion) and should not, therefore, be relied upon to show that no other weaknesses exist or areas require attention. Accordingly, the comments in this letter refer only to those matters that have come to our attention during the course of our normal audit work and do not attempt to indicate all possible improvements that a special review might develop. We would be happy to discuss any of the points contained within this letter in more detail with you.

We would like to take this opportunity to thank you, your colleagues and staff for their courtesy and assistance extended to us during the course of our audit.

Yours sincerely

The GRO logo, consisting of the letters 'GRO' in a bold, sans-serif font, enclosed within a dashed rectangular border.

Alison Duncan  
Partner, on behalf of Ernst & Young LLP

Enc

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## Overview

Our review of the Group's system of internal control is carried out to assist us in expressing an opinion on the accounts of the Group as a whole. This work focuses on the key processes that impact the financial statements, namely:

- ▶ Payroll
- ▶ Revenue
- ▶ IT

We selected key controls within these processes and performed testing to address the material financial statement risks in specific areas. We also revisited the recommendations that we made in 2010 and reviewed the status of management's agreed actions.

The key control themes and observations from our audit were discussed in the May 2011 Audit and Risk Committee and are detailed in each of the sections of this report. We have also noted a number of more routine observations in the report, which we have discussed with management and agreed actions.

We have split our report into the key areas where we perform our work, namely:

- ▶ UKLPI
- ▶ Post Office Limited
- ▶ GLS

## UKLPI

### Control observations

#### Financial statement close process

There have been changes to the Group's finance team as part of the business restructuring, a number occurring only a few months prior to the year end. The most significant change has been the merger of the previous Letters and Group teams. Despite the reduction in headcount and the uncertainty, we have not identified any significant impact on the control environment or noticed an impact on the quality and timeliness of the information provided to us as part of our audit either at the P11 hard close or the P12 year end.

This was achieved through re-engineering of roles and responsibilities within a very experienced team, a detailed handover from the 'Letters team' in P10, together with bringing forward as much work as possible to P11. This is evidenced by the number of accounting matters that were agreed prior to the year end.

#### Payroll process

Consistent with prior years, we were unable to rely on the IT general controls for the legacy Infinium payroll system due to developers having access to move programme changes into production, with no facility to log and review. Therefore, we have extended our sample testing in relation to application controls, have tested the source data for IT dependent manual controls and have recast any reports obtained from Infinium that we use as part of our audit.

We have tested manual and management level controls over the key elements of the payroll process, including joiner, leaver and payroll processing.

We noted that following the departure of a member of the leavers' team, a check of payments back to redundancy agreement for 100% of employees being made redundant was unintentionally discontinued. This was mitigated by higher level review controls during that period and management promptly reinstated the control following our finding.

All the other controls that we have sought to rely on for audit purposes were deemed to be operating effectively. Key management controls include the weekly and monthly 40X Reports whereby payroll amounts exceeding set thresholds in each payroll environment are investigated and resolved prior to the payroll run.

## **Revenue process**

Our work on the 'order to cash' revenue process focused on the most significant income streams. As in prior years, we performed controls testing over the Bulk Mail and Counter Stamps income streams. The controls we sought to rely on were tested as operating effectively.

A feature of the dockets and self billing OBA system is that a number of manual adjustments are required to correct errors, issue credit notes, or in some cases to record revenue for new products that cannot otherwise be recorded. One of the key controls tested is the review by the finance team of J-Dockets and support, prior to entries being uploaded into the system. This includes a hierarchy of approval limits and a review of the adjustments being proposed. We found this control to operate effectively but that it relied on operators' knowledge of other peoples' roles and titles in the organisation. For example, there is no formal updated authorisation list for refunds or other adjustments. In addition, we have reviewed J-Dockets with a value greater than £250,000 and noted no issues.

We have also reviewed the 'order to cash' revenue process for Wholesale and controls were deemed to operate effectively. J-Dockets were appropriately reviewed by finance prior to being uploaded into the system.

## **IT**

We test the IT general controls around the revenue systems and the SAP-ESFS general ledger in the Letters business. Where it is more efficient to do so, we place reliance on a SAS 70 report from CSC.

In prior years, we identified the fact that a large number of users were granted the powerful SAP\_ALL super user access and there was little formal review of their activities. The number of users with permanent SAP\_ALL access has decreased to six. The controls around granting temporary SAP\_ALL access are not sufficiently documented. We have performed alternative procedures to ensure that no entries were posted by super users to revenue and that no employee or supplier account had been set up. No issues were identified following these additional alternative procedures.

## **Taxation**

We have continued to see improvement in the tax control environment in the year. The improvements are reflected in regular meetings with HMRC and in the continued resolution of prior year items, and this is supported by feedback provided by HMRC in their recent risk review.

We have also had ongoing discussions with Royal Mail in respect of the Senior Accounting Officer certification obligation which for Royal Mail is due by September 2011. Management's progress on SAO certification is in line with what we see at UK plc as well as other organisations of similar size and complexity. Management is in the process of updating the documentation based on improvement suggestions from EY, and we will review again prior to submission in September.

## **VAT**

Following the legal challenge from TNT and the ruling from the European Court of Justice, Royal Mail was required to charge VAT on non-USO products from 31 January 2011. This was a complex project identifying which products would be subject to VAT, changing all impacted IT systems, updating the accounting and providing training to staff.



Our procedures included a high level review of both the VAT classification and interpretation of the legislation and our review of IT system changes focused on OBA. These were performed prior to the 'go live' date in order to be able to feedback on a timely basis any observations, and subsequently followed up post implementation.

Whilst our IT and VAT specialists suggested some minor improvement points around best practice, we were impressed by the governance of the project, ongoing collaboration with the HMRC, contingency planning and the delivery of the project to its timetable and budget. Our audit procedures at the year end did not identify any issues in relation to this new compliance obligation.

#### **Status on 2009-10 management letter points**

In the prior year we noted that a key payroll control in identifying any ghost employees, the human asset check, had been discontinued due to the significant level of change as a result of the Transformation. This control has been reinstated towards the end of the year.

We also highlighted the changes in VAT legislation as a significant risk. As noted above, this has been adequately managed and addressed in the current year.

### **Matters for the forthcoming year**

#### **Restructuring**

The finance restructuring started in 2010 is on track for completion in 2011-12 and some finance functions are yet to close down or be merged. These periods of change are always subject to risks of control breakdown. In the case of the Peterborough office, for example, the cash collection and processing team is currently in the process of moving to Bolton, with most of the employees being made redundant. We understand that management has identified dedicated resources to manage the transitions, with an interim move to Chesterfield being considered. We will continue to work closely with management to ensure that key controls are focused upon throughout this period.

#### **IT**

The new HR PSP payroll system has gone live at the end of May 2011 covering some of the employees of the Group. The system will be rolled out in phases, with the final phase being completed at the end next year. Management is required to replace the current system and has created new functionalities to create a more robust system that will, amongst other things, provide more detailed management information on the cost drivers in the business. Any new system carries a significant level of risk and this is deemed to be a business critical system. Other than the technical considerations, we believe it is important

that there is sufficient buy-in from the users of the system as the system places greater responsibilities on front line staff than the existing system.

We have started working with management in order to give our views on the control environment. We have agreed to test key controls over the coming months and intend to use our SAP Explorer technology to assist with maximising the efficiency and configuration of the SAP-HR system.

# Post Office Limited

## IT Control observations

### *Summary*

During 2010-11, Post Office Limited ('POL') made significant changes to its key financial systems environment. In September 2010 it completed the progressive replacement of Horizon with Horizon Next Generation (HNGX) across the branch estate, which had commenced in December 2009. In addition, the POLFS and SAP-ADS systems were consolidated into a single SAP system (POL-SAP) in August 2010.

HNGX is the main system used to process transactions from the counters/branches. It summarises transactions and uploads to POL-SAP, the primary back office system which underpins the production of the financial statements. In view of the volume of transactions flowing through the systems and the geographical spread of the branch network, they are critical to the ongoing operation of the business and financial reporting processes and hence our delivery of an efficient audit. In extremis, were we unable to place reliance on these systems it is arguable whether it would be possible to undertake the scale of substantive work necessary for us to form an opinion at all.

Our audit identified significant control weaknesses, which in our view reflects a need for improvement by the outsource provider Fujitsu but also a change in approach on the part of POL. Despite the outsourced IT environment, POL is responsible for the governance, risk and control framework over its business critical systems, and should have visibility and assurance over their design and operating effectiveness.

Management is acting on our recommendations and are remediating the existing IT controls framework to ensure that our findings and observations are taken into account as POL commences new contract negotiations with Fujitsu. We are satisfied that the recently joined POL IT Director has the right knowledge, attitude and experience to address these weaknesses and to ensure that POL takes ownership for the IT control environment and demands the appropriate service from Fujitsu.

Set out below are our observations and point of view on the audit process, controls findings and the contract with Fujitsu.

### *Audit process*

As in prior years, there was no SAS 70 independent audit report over the Fujitsu control environment. Consequently, it was agreed that Ernst & Young would undertake the necessary audit procedures to gain assurance over the IT general controls of logical access and programme change of POL-SAP and HNGX.

Ernst & Young had a new team this year, which unavoidably entailed a steep learning curve, but also highlighted that we had previously relied on knowledge within our team rather than the availability of documentation within Fujitsu. Despite the great support of POL's new IT Director, Lesley Sewell, and her team, which included securing from Fujitsu an audit liaison contact and the sponsorship of the Fujitsu account leader, the combination of: the degree of change in the IT environment; the change of EY team; and Fujitsu's approach in delivering audit requirements to POL and EY, resulted in an unduly lengthy, unpredictable and inefficient audit. Whilst we have found the audit process with Fujitsu challenging in prior years, we understand that the reason for additional problems in the current year is due to Fujitsu's delivery model for POL moving to a shared service model in conjunction with the rollout of HNGX. As a result, there is no one Fujitsu or POL person

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who has full knowledge of POL's end-to end processes or access to documentation and other evidence to support the operation of key controls which resulted in certain information we would consider routine not being available (such as listings of leavers) or requiring significant time to produce. This makes it very time-consuming for either POL or EY to gain assurance that adequate controls are in place and are operating as expected.

#### *Controls observations*

As noted above, our audit identified significant IT control weaknesses; however we ultimately obtained mitigating audit evidence to rely on the IT control environment. Details of our controls observations are included in the next section. In summary, however, our audit identified:

#### POL-SAP

- ▶ Accounts with access to both develop and deploy changes to the live environment
- ▶ Access to deploy changes for inappropriate individuals/leavers
- ▶ Lack of periodic review of and monitoring of changes deployed into production
- ▶ No evidence that program changes are approved, tested and authorised
- ▶ Lack of involvement of Post Office staff in testing most fixes and maintenance changes
- ▶ Multiple generic accounts with highly powerful privileges
- ▶ Users with permanent access to SAP\_ALL not being monitored
- ▶ Lack of periodic review of appropriateness of user access
- ▶ Lack of user administration procedures for Cash Centre users

#### HNGX

- ▶ Developers with access to migrate changes to live environment
- ▶ Leavers with access to promote changes to live environment not being removed
- ▶ Lack of periodic review and monitoring of changes deployed into production
- ▶ No evidence of Post Office approving specific HNGX releases following the pilot
- ▶ Evidence of POL testing on changes not being retained consistently
- ▶ Lack of periodic review of appropriateness of user access
- ▶ Leavers' access not being revoked in a timely manner
- ▶ Access requests being granted without evidence of approval from line managers
- ▶ Passwords for privileged generic accounts being shared by multiple users

Since the completion of our IT audit, we have discussed in detail the control observations and our expectations in addressing these with Fujitsu and POL. We have also held a de-brief session with Fujitsu and POL regarding the difficulties we faced during the audit. We have worked with Lesley Sewell in engaging with the Fujitsu account leader to highlight POL's desire to implement a required controls framework and explore options for the conduct of the audit in future. From these discussions we understand that Fujitsu has accepted that control improvements are required and has initiated a project to address the security issues; in addition, high-level action plans have been agreed by Fujitsu, POL and ourselves to improve the audit process for next year.

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*Recommendations – contract with Fujitsu*

In our opinion, POL currently relies on Fujitsu to act in its best interests, and will need to be more demanding in this contract relationship going forward. We have the following recommendations which should be addressed urgently:

- ▶ Fujitsu to undertake formally to address the control issues noted during the audit, whether relating to the POL account or to its shared service provision, and to accept a requirement to address issues arising in the future within a specified period
- ▶ POL to take ownership of the effectiveness of the control environment with Fujitsu and require Fujitsu to implement a control framework devised by POL (including standards and requirements) and to provide assurance (independent or otherwise) over its continued effective operation
- ▶ Metrics/service level agreements to be agreed for the timely provision of information in response to requests from Post Office itself or its auditors
- ▶ Whilst Fujitsu has indicated that the provision of an ISAE 3402 (formerly SAS70) would be excessively costly and the preference within POL at present is to focus on improving the existing audit process going forward, we recommend that POL keeps the ISAE 3402 option under consideration over time, as there are indications that Fujitsu will adopt an increasingly global approach to service provision, further complicating the process of gaining audit evidence

Whilst we do recognise that the current outsourcing model has been pursued to successfully deliver very significant commercial benefits to POL, there is a need to implement additional governance measures to reflect the shared service nature of Fujitsu's provision.

**Other Control observations****Financial statement close process**

The improvements made to the POL financial reporting and financial statement close process last year have continued. There was appropriate rigor over the P11 hard close with all reconciliations performed in a timely manner and supported by appropriate documentation.

**Payroll process**

The POL payroll process is independent of the process and systems that support the rest of RMG. It covers approximately 20,000 employees and agents, which primarily include front line workers and agents working at Post Offices around the country. The system supporting this process is a SAP-HR module.

We have had to take a fully substantive audit approach to POL payroll in recent years due to a number of control deficiencies over the review of joiners and leavers and a lack of documentation of a number of review controls. Following efforts in the prior year to improve the POL financial statement close process, the payroll process has received a high level of management focus and attention. The recommendations that we made last year have now been addressed. Although a number of small improvement points were identified (e.g. full human asset check, additional review of change request), we believe the controls have operated effectively during the year, and we relied on these controls for our audit.



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**OTHER CONTROL OBSERVATIONS**

Observation	Recommendation	Management comment
<p><b>Human Asset Check</b></p> <p>An employee asset check was completed for the first 6 months with a response rate of 75%. The remaining 25% was not completed given the upcoming organisational restructure. However, as all employees are expected to be put onto new online organisational chart before March 2011, Management believes this will allow for a more robust human asset check in the future.</p> <p>The agent asset check continues not to be in place. The design of an asset check for agents is still under discussion and the HR department have put forward a suggested process to senior management and are awaiting approval.</p> <p>As this control is not yet fully operational, there is a continued risk of either 'ghost' employees or agents, or that employees or agents who have left the business incorrectly remain on the payroll.</p>	<p>We recommend that HR reviews the results of the trial run of the employee asset check and ensure that 100% coverage is achieved.</p> <p>In addition, we await to see senior management's decision regarding implementation of the proposed agent's asset check but recommend that the proposed control is introduced at the earliest opportunity to migrate the inherent risks.</p>	<p>Agreed</p> <p>a) Employees – the final verification of our structure will in effect deliver the second 6 month review as per the agreed control.</p> <p>b) Agents – Currently we are performing a check of offices paid on HRSAP against office transacting basics products e.g. 1<sup>st</sup> class stamps (via Credence). We intend to continue with this check and await a decision on whether we require anything further to deliver an acceptable asset check.</p>

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**Review of Employee Change Request**

We noted a marked improvement in the maintenance and transparency of the employee changes log spreadsheet, however one month sampled identified that the 10% check had not been carried out in full, with only 8% of changes (contractual and non-contractual) being subject to review.

It was also noted that the log was not amended in cases where the information would suggest a contractual change but once processed this was not the case, however it is recorded by sign off if the change lead to a contractual change.

This control is important in ensuring that all changes are being reviewed and input onto SAP correctly. It was noted that this was done in the other months selected for testing apart from the exception noted above.

We recommend that the change from a “contractual” change request to a “non-contractual” change request be clearly documented on the spreadsheet in order to ensure transparency over what contractual changes have been made. In addition, we recommend that the level of secondary check each month (e.g. 10% of the full population) is adhered too in all cases.

Agreed – Now in place

a) Additional column has now been included on our spreadsheet to highlight where there is a change in status from the source document i.e. sent as contractual and processed as non-contractual or vice versa. This is already noted on the source document however this addition adds visibility.

b) 10% check as detailed in our Control Manual will be delivered. On the one month where only 8% was documented this has now been re-visited retrospectively and the team leader has checked a further sample to meet the agreed requirements.

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**Variance Report for Agents**

It was noted when testing the agents pay variance reports for April, August & September that there were a small number of exceptions per the generated exception reports that had not been brought forward and noted on the summary front sheet – which is in turn reviewed by the Service Team Leader (STL). There appear to be no guidelines in place which dictate which variances and follow ups require management review although those exceptions identified within the report had been investigated in the initial review but not included on the front sheet ready for STL review.

A lack of clear guidelines dictating which variances should be raised for management review leaves the potential for oversight of significant variances generated by the SAP report which are not included in the STL review

We recommend that there are clear process guidelines for the level of management checks to indicate which variances should be raised for management review, in order to ensure no significant variances and follow up actions are omitted. All items within the report meeting this threshold should then be included on the front sheet ready for management review.

Agreed – Fully implemented for P12 processing.

The check is 100% on the variances that are produced with those requiring action documented on a front facing sheet. Narrative detailing the guidelines to perform the check will accompany the front facing sheet. The sheet will also be updated to include a ‘balance’ of all variances identified that period which will form part of the team leader sign off.

# GLS

## Control observations

### Financial statement close process

In order to meet the Group reporting requirements at year end, GLS entities report eleven months of actual results together with one month of forecast results. GLS have a number of years of experience in this methodology and in 2010-11 there was minimal difference between the P12 forecast and P12 actual EBITA. This accurate forecasting allows GLS to meet the Group's fast timetable for consolidating results with a true-up performed once the actual results are finalised, and allows us to complete our audit procedures in line with the Group reporting deadlines.

The GLS business operates across a number of decentralised locations with reliance on a core management team that has a significant level of knowledge and experience. The control environment is complemented by the GLS ARC and the reviews performed by the GLS Internal Audit function.

The EY audit team attended the year end ARC meeting on 13 May and provided:

- ▶ An update on audit status
- ▶ A summary of the year end audit results
- ▶ Updates on significant litigation matters

EY performs audits at all of the significant GLS locations and an assessment is made, and agreed with GLS management, at the start of each year over the areas that will be covered by the external audit.

Overall, the only issues of Group audit importance noted in any of the GLS audits is the GLS LTIP item, the potential tax exposure in GLS Italy and the overprovision for damaged mail covered elsewhere in this report.

### Status on 2010-11 management letter points

A controls-based audit approach is taken at the significant GLS locations. Management is conscious of the recommendations that we raise and appropriate attention has been given to the points that we have made in previous years, including amendments to the IT control environment and intercompany confirmation process.



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## GLS Germany

Internal control/process issues

Observation	Recommendation	Management Response
<b>SAP_ALL Users (PR1)</b>  The profile SAP_ALL represents the status of a superuser and therefore provides unlimited access to the SAP R/3 systems. During our audit we observed that there is one external consultant in the SAP HR-System (PR1) with permanent SAP_ALL rights.	Permanent "SAP_ALL" rights should be limited to emergency users.  The use of the emergency user should be documented as well the temporary assignment of the SAP_ALL rights.	The SAP_ALL right for the external consultant (in fact it was an employee of the external consultant) has been cancelled.
<b>Several tools in place to support the Change Management process</b>  During our audit we observed that several independent tools are used to organise and document changes to IT systems within the change management processes. Each department used their own tool to manage the changes. No tool exists that covers the entire change management processes from the request to the deployment. Furthermore, no linkage to the incident and problem management exists.	The use of multiple tools is likely to create a management and documentation overhead. Furthermore, the likelihood of failures is increased. Due to the multiple tools it is difficult to track used times and to identify bottlenecks.  To increase efficiency, a single tool should be used to support the change management process. This will also ensure the traceability of a change, the complete process beginning with the request / defect (helpdesk call) and ending at the final deployment of the change.	The tools are based on our workflows for requests (LN teamroom), defects (testdirector) and support calls (LN helpdesk).  The tool for tracking defects (test director) will be at the end of its life in August 2011. Therefore we are evaluating a workflow tool that should cover all requirements in order to support the change management process as recommended. The first step will be then to replace the tool for the defect handling.

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**GLS Denmark A/S**

Internal control/process issues

Observation	Recommendation	Management Response
<p><b>IT – General controls - User rights – Segregation of duties</b></p> <p>A lack of segregation of duties was noted in relation to IT user rights.</p> <p>As such, there is an increased risk that unintentional or intentional errors in master data remain undetected. Specifically employees, who are in charge of creditor payments should not be allowed to change vendor master data or have super-user rights in Cap Nordic.</p> <p>During our walkthrough of approvals of costs we found several employees that had limits for approval above the normal level (not head of department employees approving more than DKK 10,000).</p>	<p>To ensure that the correct approval procedures are in place we recommend a periodical overview of the encoded authorizations to approve invoices in the Cap Nordic System - including which accounts the authorisation regards and a maximum amount, if any.</p>	<p>A new workflow system will be implemented as of 1 of June 2011, which, amongst other things, ensures a visible hierarchy structure for approval of invoices. This hierarchy will be build according to the implemented GLS Group Limits of Authority.</p>
<p><b>IT – General controls – Change Management</b></p> <p>Since October 2010, testing of the changes to the system have been confirmed by phone and not in recorded in written documentation, e.g. in an email. There is therefore no record that can be inspected to confirm that changes have been appropriately tested.</p>	<p>We recommend that the previous practice of maintaining written records is reinstated.</p>	<p>Monthly log showing all changes performed in the system will be reviewed and signed off by the Finance Director.</p>

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Observation	Recommendation	Management Response
<p><b>Payment of wages and salaries</b></p> <p>Wages and salaries are handled by a small team of individuals. Lack of segregation of duties weakens the internal controls and increases the potential risk of errors and fraud. According to the system "Personaleportalen", users with super-user rights can change master data. A change is performed by one person and another approves the change. The IT-system does not require that 2 different individuals perform this – in our test of control of changes of master data we found a small number of examples where there was no documentation for changes in employee's bank account number.</p>	<p>We recommend that the IT system is set up to secure that 2 different persons are always involved. Otherwise we recommend that the monthly approval is made by written documentation as an email or signing the paper profile. We furthermore recommend that for changes in master data made by users with super-user rights written documentation is archived.</p>	<p>We have no possibility to change super-user rights in "Personale-Portalen", as it is not our system. There are 3 super-users registered, Lone Koch (Payroll), Steen Kristensen (Finance Director) and Karsten Klitmøller (Regional Manager). They can individually prepare and approve changes in masterdata etc. Monthly white-collar payments are approved by the Finance Director and written documentation will in future be obtained. Furthermore we have implemented a procedure for documenting all changes in master data in written.</p>
<p><b>Transfer Pricing documentation</b></p> <p>We draw the attention to the Danish legislation on transfer pricing, which requires that written documentation must be prepared to document that the intra-group transactions are made at market prices. The documentation must also include all material transactions between Danish Group Companies, and e.g. GLS Express' transfer pricing documentation must also include transactions with Der Kurier.</p>	<p>We have been informed that GLS Group has prepared some documentation, e.g. documentation of corporate centre charge. However, we strongly recommend that GLS DK at least prepares documentation of all identified types of group internal transactions (with amounts and specification of countries involved) and a reference to the documentation that is supporting the pricing of the transaction.</p>	<p>Transfer pricing documentation for transactions between Danish Group companies and for Corporate center charge as well as loan in interest costs are updates and maintained in GLS Denmark. Transfer pricing documentation for international transactions (clearing) is maintained in GLS Germany.</p>

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**GLS France**

Internal control/process issues

<b>Observation</b>	<b>Recommendation</b>	<b>Management Response</b>
<p><b>Price sheets returned unsigned by the customer</b></p> <p>The price sheets provided with the customer agreements that serve as the basis for invoicing are not always returned duly signed by the customer.</p> <p>We put the stress on the following points:</p> <ul style="list-style-type: none"> <li>- The sales representatives and sales administration have set up improvement to keep on quality on this issue</li> <li>- Many agencies have set up follow-up of customers to have prices listing validated</li> <li>- Customers rarely contest the prices that GLS France charges to them</li> </ul>	<p>Actions plans have been implemented over the last 5 years; We recommended that the update of contracts and amendments has to be made in a more rigorous way.</p>	<p>Following action have been made by Sales Admin department to ease up the controlling of contracts updating by Sales Manager in region.</p> <ul style="list-style-type: none"> <li>- Selligent menu to have the list of each document not declared by sales service as validated in Selligent</li> </ul> <p>Moreover, to make the overview of contracts updating process more reliable, it has been decided to develop an IT program to enter data validation on Selligent based on the scanning of document. Each scan is available on a data base. The setting up of this process in region is in progress. A first statement will be made in June 2011.</p> <p>At least, to check controlling operation managed by region, Internal Audit team includes this guideline in their audit organisation</p>
<p><b>Price modification under Selligent or during the transfer between Alpha and Selligent</b></p> <p>During IT review we noticed that anyone in the agencies can modify the prices in the customer's data.</p>	<p>We recommend setting up an IT limitation so that only a few dedicated people can modify the client data in Selligent.</p>	<p>An analysis is planned. Solution will be proposed via a request and submitted for development.</p>
<b>Observation</b>	<b>Recommendation</b>	<b>Management Response</b>

GLS

<p><b>Subcontractors contracts</b></p> <p>During our audit, there were some cases for which we could not match some rates, per point or per round, applied in the invoices sent by subcontractors, with the contract.</p> <p>We had difficulties in obtaining the last price amendments for some subcontractors</p>	<p>We recommend updating the invoicing follow-up files set up in each agency. These files could include the reference of the last codicils corresponding to the updated price.</p> <p>Furthermore, we recommend keeping the last price amendments signed by the subcontractors in the subcontractor files in the agencies.</p>	<p>Action is still in progress in stressing by more internal audits of the subcontractor files :</p> <ul style="list-style-type: none"> <li>• Quality team audit on these files on the field.</li> <li>• Internal audit also systematically check and best practices spread.</li> </ul>
<p><b>Subcontractor file</b></p> <p>Some files selected during our audit did not include all the updated legal documents (copy of subcontractor insurances, copy of the driving licenses of the drivers)</p>	<p>Action plans have been set up over the last years. We recommend the agencies to be more rigorous.</p>	<p>Preventive actions: training of local correspondents and depot managers on the good recordkeeping, regular information on legal news and precise items.</p> <p>Corrective actions: annual checking of subcontractors' files sample by legal department with request of corrective actions, deadlines and checking of actions lead.</p>

GLS

## Internal control/process issues

Observation	Recommendation	Management Response
<p>During our audit procedures performed on the Claims process of both companies we noticed that both companies use an entirely different method for determining their monthly claims provision.</p> <p>The claims provision for GLS Belgium Distribution, mainly for freight activities, is calculated locally and is based on a formula taking into account:</p> <ul style="list-style-type: none"> <li>- Actual claim cost prior year</li> <li>- Ratio containing the claim cost trend over previous years</li> <li>- Actual weight (in kg) of prior year shipments</li> <li>- Actual number of shipments prior year</li> <li>- Estimated number of shipments current year</li> <li>- Risk factor</li> </ul> <p>We noted that no annual update of the data used in the formula is done.</p>	<p>First of all, we recommend GLS Belgium Distribution updating the date used in the formula each year in order to present a more up-to-date view of the actual claim costs in prior year.</p> <p>Furthermore, we recommend both companies to align the claims process in order to give a more transparent view and to facilitate the understanding of both provisions.</p>	<p>The claim departments of GBD and GBE have been centralised in Anderlecht since June 2010. Our first priority has been to cope with the extra volume of claims, since the staff that was formerly responsible for the GBE claims remained in Vilvoorde. We are currently engaged in the harmonisation of the claims procedures.</p> <p>The next priority in the ongoing harmonisation process, is the reporting format. This will include the provision building process as well as the provision reports. Obviously, GLS Belgium is expected to conform to the German template, but we will make sure the report is transparent and matches the templates we have been using for GBD in the past, so you can easily plug into the data of both companies at the next audit.</p> <p>The formula for the computation of the claim provisions for GBD is normally updated every year. However, since the FY2010 data were considered unrepresentative due to the perturbations of the protracted depot-splitting process, the computation basis of the previous financial year was upheld for one year. The financial year 2012 will be based on a fresh computation based on the FY2011 data.</p>
Observation	Recommendation	Management Response



GLS

<p>As from 2010-11, both companies report one consolidated MCP reporting package. Both companies are consolidated using the full consolidation method. The eliminations in the consolidation process are entirely based on intercompany codes which are automatically assigned in SAP at the moment intercompany invoices are encoded. SAP will eliminate these intercompany codes in a separate consolidation module. We noted that provisions and COD amounts which are built up between both companies at month end do not receive this intercompany code and are therefore not automatically eliminated in the consolidation. Furthermore we noted that no proper consolidation report is made on a regular basis in order to facilitate the review of the eliminations done on consolidation level.</p>	<p>We recommend both companies to use intercompany codes in SAP for all intercompany transactions encoded in order to avoid missing intercompany eliminations in the consolidation process.</p> <p>Furthermore we recommend to make a consolidation report on a monthly basis containing:</p> <ul style="list-style-type: none"> <li>- The separate trial balances of both companies with local accounting numbers</li> <li>- The separate eliminations done in both companies on accounting number level</li> <li>- One trial balance of both companies after eliminations on local accounting numbers</li> <li>- Mapping table between local accounting numbers and MCP classifications</li> </ul> <p>This, in order to facilitate the review of the eliminations and to assure reconciliation with the consolidated MCP reporting package.</p>	<p>With effect from April 2011 intercompany COD balances will be eliminated in the GLS Belgium MCP.</p> <p>An improved consolidation / elimination audit trail, as proposed by E&amp;Y, will also be put in place.</p>
<p>On a monthly basis General Logistic Systems Belgium extracts data from GEPARD and reconciles this data with the data available in SAP in order to assure the completeness between the two systems. Differences which come up during this reconciliation process are investigated and solved. During our review of this reconciliation process we noticed that neither the reconciliation nor the explanation of differences is documented or kept.</p>	<p>We recommend General Logistic Systems Belgium to formalise the documentation of this reconciliation process.</p>	<p>We will document the difference as of now.</p>

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