

Annex 2

Direction: new Regulatory Accounting Guidelines (RAG)

DIRECTION GIVEN BY OFCOM OF NEW REGULATORY ACCOUNTING GUIDELINES UNDER, AND FOR THE PURPOSES OF APPLYING, THE NEW USP ACCOUNTING CONDITION IN ACCORDANCE WITH SECTION 53 OF, AND PARAGRAPH 4 OF SCHEDULE 6 TO, THE POSTAL SERVICES ACT 2011

BACKGROUND

- (A) On 27 March 2012, following consultation, Ofcom published a statement entitled “*Securing the Universal Postal Service: Decision on the new regulatory framework*”¹ (the “**2012 Statement**”) setting out various decisions relating to the new regulatory framework for the postal sector, including the imposition on the universal service provider of a USP accounting condition to make provision about the matters set out in section 39 of the Act.
- (B) At Annex 11 to the 2012 Statement, Ofcom also gave a direction in accordance with section 53 of, and paragraph 4 of Schedule 6 to, the Act and pursuant to powers in the above-mentioned USP accounting condition that the condition shall have effect by reference to Regulatory Accounting Guidelines set out in the Schedule to the direction.
- (C) On 27 January 2014, following consultation, Ofcom published a statement entitled “*Updating the Regulatory Reporting Framework – Statement – USP Accounting Condition*”². Also on 27 January 2014, Ofcom separately published a notification entitled “*Updating the Regulatory Reporting Framework – Statutory Notification – USP accounting condition*”³ (the “**2014 Modification**”) in which Ofcom set out its decision to modify the USP accounting condition and the Regulatory Accounting Guidelines. The revised USP accounting condition and revised Regulatory Accounting Guidelines (clean copies as well as copies with tracked changes showing the updates) were set out in Annex 1 (the “**USPAC Condition**”) and Annex 2 (the “**RAG**”) to the 2014 Modification, respectively. The revisions took effect from the date of publication of the 2014 Modification.
- (D) On 31 March 2017, Ofcom published a consultation document entitled “*Review of Regulatory Financial Reporting for Royal Mail*”⁴ (the “**2017 Consultation**”) setting out in its Annex 5 a notification of Ofcom’s to revoke the existing USPAC Condition and impose on Royal Mail a new USP accounting condition to make provision about the matters set out in section 39 of the Act (the “**USPAC 2017 Notification**”). At Annex 6 to the 2017 Consultation, Ofcom published another notification proposing, in accordance with

¹ <http://stakeholders.ofcom.org.uk/binaries/consultations/review-of-regulatory-conditions/statement/statement.pdf>

² https://www.ofcom.org.uk/__data/assets/pdf_file/0020/71534/statement.pdf

³ https://www.ofcom.org.uk/__data/assets/pdf_file/0033/79863/statutory-notification.pdf

⁴ <https://www.ofcom.org.uk/consultations-and-statements/category-3/review-of-regulatory-financial-reporting-for-royal-mail-consultation>

section 53 of, and paragraph 4 of Schedule 6 to, the Act—and pursuant to anticipated powers under the new USP accounting condition proposed in Annex 5 to the 2017 Consultation—to withdraw the existing RAG and to give a new direction setting out specific requirements relating to that condition in a document to be known as the Regulatory Accounting Guidelines (the “**RAG 2017 Notification**”).

- (E) Having considered the responses, Ofcom has decided to give effect, with some modifications, to its proposals set out in the USPAC 2017 Notification. Accordingly, Ofcom has decided to revoke the existing USPAC Condition and impose on Royal Mail a new USP accounting condition to make provision about the matters set out in section 39 of the Act. The notification, together with the effective dates of that revocation and the imposition respectively, of the new USP accounting condition is set out in the accompanying statement.
- (F) A copy of the RAG 2017 Notification was sent to the Secretary of State in accordance with paragraph 5(1)(a) of Schedule 6 to the Act. Ofcom received responses to the RAG 2017 Notification and has considered every such representation. In accordance with paragraph 4(8) of Schedule 6 to the Act, Ofcom has made the decision set out below to give effect, with some modifications (the nature of which are explained in the accompanying statement), to its proposals set out in the RAG 2017 Notification. The Secretary of State has not notified Ofcom of any international obligation of the United Kingdom for the purposes of Ofcom giving effect to those proposals.

DECISION

- 1. Ofcom hereby, in accordance with section 53 of, and paragraph 4 of Schedule 6 to, the Act—and pursuant to its powers under the new USP accounting condition imposed by Ofcom under section 39 of the Act on Royal Mail (as specified in a separate notification in the accompanying statement)—
 - (a) withdraws the existing RAG with effect from 25 March 2018; and
 - (b) directs that the said new USP accounting condition shall have effect by reference to the specific requirements relating to that condition in a document to be known as the Regulatory Accounting Guidelines set out in the Schedule hereto, which shall take effect on 26 March 2018.
- 2. The effect of, and Ofcom’s reasons for making, this decision are set out in the accompanying statement.

OFCOM’S DUTIES AND LEGAL TESTS

- 4. Ofcom is satisfied that this decision satisfies the general test in paragraph 4(2) of Schedule 6 to the Act.
- 5. In making this decision, Ofcom has considered and acted in accordance with its principal duty in section 29 of the Act and its general duties in section 3 of the Communications Act 2003.

INTERPRETATION

- 9. Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them in this Direction and otherwise any word or expression shall have the same meaning as it has been ascribed for the purpose of Part 3 of the Act or for the purpose of the USP accounting condition (as relevant).

10. In this Direction—
- (a) “**2012 Statement**” has the meaning given to it in recital (A) to this Direction;
 - (b) “**2014 Modification**” has the meaning given to it in recital (C) to this Direction;
 - (c) “**2017 Consultation**” has the meaning given to it in recital (C) to this Direction;
 - (d) “**Act**” means the Postal Services Act 2011 (c.5);
 - (e) “**Ofcom**” means the Office of Communications;
 - (f) “**RAG**” has the meaning given to it in recital (C) to this Direction;
 - (g) “**RAG 2017 Notification**” has the meaning given to it in recital (D) to this Direction;
 - (h) “**Royal Mail**” means Royal Mail Group Ltd, whose registered company number in England and Wales is 04138203, which is the current universal service provider for the purposes of section 39 of the Act; and
 - (i) “**USPAC 2017 Notification**” has the meaning given to it in recital (D) to this Direction.
11. For the purpose of interpreting this Direction—
- (a) headings and titles shall be disregarded;
 - (b) expressions cognate with those referred to in this Direction shall be construed accordingly; and
 - (c) the Interpretation Act 1978 (c. 30) shall apply as if this Direction were an Act of Parliament.
12. The Schedule to this Direction shall form part of this Direction.

Signed by



David Brown

Director of Financial Economics, Ofcom

A person duly authorised by Ofcom under paragraph 18 of the Schedule to the Office of Communications Act 2002

18 December 2017

SCHEDULE

Regulatory Accounting Guidelines

Issue No. 3

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Section 1: Purpose

- 1.1** The USPAC Condition imposes on Royal Mail (as the universal service provider designated by OFCOM) various obligations under section 39 of the Act. Pursuant to powers in the USPAC Condition, OFCOM are empowered from time to time to give such directions as they consider appropriate in relation to Royal Mail—
- (a) maintaining a separation for accounting purposes between such different matters as OFCOM may direct for such purposes as they may direct, including separation in relation to different services, facilities or products or in relation to services, facilities or products provided in different areas as well as the accounting methods to be used in maintaining the separation;
 - (b) complying with rules made by OFCOM in relation to those matters about the identification of costs and cost orientation, including the application of presumptions in the fixing and determination of costs and charges for any purpose as well as the publication of such accounts and other information relating to anything required to be done by OFCOM in this regard;
 - (c) complying with rules made by OFCOM about the use of cost accounting systems in relation to those matters, including the application of presumptions in the fixing and determination of costs and charges for any purpose as well as the publication of such accounts and other information relating to anything required to be done by OFCOM in this regard;
 - (d) securing that Royal Mail's compliance with those systems is audited annually by a Qualified Independent Auditor, including Royal Mail meeting the costs of the audit; and
 - (e) otherwise in relation to Royal Mail's obligations under the USPAC Condition.
- 1.2** Pursuant to the obligation in USPAC 1.2.3 on Royal Mail to comply with any direction given by OFCOM from time to time under it, the regulatory requirements in any direction (including in these Guidelines) are enforceable via the USPAC Condition in accordance with the relevant procedures in the Act.
- 1.3** By definition in the USPAC Condition, the “Regulatory Accounting Guidelines” means the document so entitled and published by OFCOM (as amended from time to time) setting out such requirements as OFCOM may direct from time to time relating to the preparation, auditing, reporting and publication, of regulatory financial statements and other regulatory financial reports to be prepared and maintained by Royal Mail by or under the USPAC Condition. Additionally to the general direction-making power referred to in §1.1 above, the USPAC Condition makes express references to these Guidelines in prescribing specific requirements on Royal Mail imposed by means of a direction, such as those concerning the manner and form in which financial statements and information should be prepared and maintained, etc.
- 1.4** Accordingly, OFCOM has directed that the USPAC Condition shall have effect by reference to these Guidelines.

Section 2: Definitions & Interpretation

2.1 For the purpose of interpreting these Guidelines—

- (a) except in so far as the context otherwise requires (including where a term of art in postal sector or in accounting profession is used), words or expressions shall have the meaning assigned to them in **§2.2** and otherwise any word or expression in these Guidelines shall have the same meaning as it has been ascribed in, and for the purpose of, the USPAC Condition;
- (b) headings and titles shall be disregarded;
- (c) expressions cognate with those referred to in these Guidelines shall be construed accordingly;
- (d) the Interpretation Act 1978 (c. 30) shall apply as if these Guidelines were an Act of Parliament;
- (e) subject to **§2.1(f)**, references to “**material**”, and cognate expressions, are references to the meaning of materiality as prescribed by the Guiding Principle concerning materiality in USPAC 1.7.2(h);
- (f) in relation to the identification of material changes for the purpose of complying with the requirements set out in USPAC 1.6.3, materiality shall be determined as follows—
 - (i) for all items of the Regulatory Accounting Methodology, a change in any item (including revenues, costs, assets, liabilities, and cash flows) in any of the financial statements and/or information required by or under the USPAC Condition shall be deemed to be material if the resultant percentage difference (be it positive or negative) exceeds 5%. The resultant percentage difference shall be calculated by taking the value of the non-compliant item and subtracting from it the value of the same item if calculated under the compliant approach (“**Compliance Base Value**”), and then dividing this result by the Compliance Base Value;
 - (ii) for the purposes of the National Costing Methodology and the Zonal Costing Methodology only, a change in any reported item of product, SPHCC, or Activity Cost shall be deemed to be material if the resultant percentage difference (be it positive or negative) exceeds 1%, unless the change itself is smaller than £0.5 million. The resultant percentage difference shall be calculated by reference to the Compliance Base Value; and
 - (iii) any determination of materiality under **§2.1(f)(i) and (ii)** shall be measured by reference to the most recent quarterly or annual financial statements and/or information, as applicable.

2.2 In these Guidelines, the following words or expressions shall have the meaning assigned to them below—

Word or expression	Meaning
“ Activity Based Costing ”	A costing system used to allocate the costs recorded in the <u>General Ledger</u> , together with any sources of data (where necessary), to products, through an intermediate step of allocating <u>Activity Costs</u> .
“ ABC Model ”	‘Activity Based Costing Model’, which is the costing system that <u>Royal Mail</u> uses to allocate the costs recorded in the <u>General Ledger</u> , together with any sources of data (where necessary), to its products, through an intermediate step of allocating <u>Activity Costs</u> .
“ Activity ” or “ Activities ”	Activities, tasks or work (whether operational or non-operational) which are required to be carried out in order to complete a <u>Business Process</u> .
“ Activity Cost ”	Total or unit costs attributed to an <u>Activity</u> .
“ Activity Drivers ”	Numeric values which are used to assign <u>Activity Costs</u> to <u>SPHCCs</u> in accordance with <u>National Costing Rule 9</u> where they relate to the <u>National Costing Methodology</u> or in accordance with <u>Zonal Costing Rule 9</u> where they relate to the <u>Zonal Costing Methodology</u> .
“ Aggregate Costs ”	Has the meaning given to it by <u>National Costing Rule 8</u> where it relates to the <u>National Costing Methodology</u> or by <u>Zonal Costing Rule 8</u> where it relates to the <u>Zonal Costing Methodology</u> .
“ Attributable Non-operational Costs ”	Has the meaning given to it by §8.24(b) .
“ Attributable Operational Costs ”	Has the meaning given to it by §8.24(a) .
“ Avoidable First Class Costs ”	Has the meaning given to it by <u>National Costing Rule 3</u> where it relates to the <u>National Costing Methodology</u> or by <u>Zonal Costing Rule 8</u> where it relates to the <u>Zonal Costing Methodology</u> .
“ Avoidable Second Class Costs ”	Has the meaning given to it by <u>National Costing Rule 3</u> where it relates to the <u>National Costing Methodology</u> or by <u>Zonal Costing Rule 3</u> where it relates to the <u>Zonal Costing Methodology</u> .
“ Bulk Mail ”	A retail service offered at a price which is subject to discounts related to volume of mail per mailing or presentation of mail, typically involving conveyance of more than 250 items per mailing.
“ Business Process ”	<u>Operational Business Processes</u> and <u>Non-operational Business Processes</u> .
“ Class Costing ”	The methodologies applied in the <u>National Costing Methodology</u> and the <u>Zonal Costing Methodology</u> to quantify the additional costs of processing certain classes of mail

relative to other classes of mail.

“Compliance Base Value”	Has the meaning given to it under §2.1(f)(i) of these Guidelines.
“Cost Centre”	The basic unit of responsibility in an organisation for which costs are accumulated, such as a production or service location, function, <u>Activity</u> or item of equipment.
“Cost Element”	A cost recorded in the <u>General Ledger</u> , such as basic pay, overtime pay and National Insurance payments.
“Cost Matrix”	A breakdown of the costs of the <u>Reported Business</u> included in the calculation of the <u>Financeability EBIT</u> as shown in Figure 7 of Appendix 1 of these Guidelines.
“Cost Type”	Cost figures obtained after rearranging the relevant categories of costs recorded in <u>Royal Mail’s</u> financial information, including the <u>General Ledger</u> , including aggregating or separating some of those costs.
“CPI”	Consumer Price Index, which means the index of consumer prices compiled by an agency or a public body on behalf of Her Majesty’s Government or a governmental department (which is the Office for National Statistics at the time of publication of these Guidelines) from time to time in respect of all items.
“CVE”	‘Cost Volume Elasticity’, which is the ratio of the variable amount of time needed to process items of mail within a given <u>Operational Business Process</u> to the total amount of time needed to process those items of mail within that <u>Operational Business Process</u> , where variable time needed to process mail items is the time which varies in direct proportion to the volume of the mail items being processed.
“DB Pension Service Costs”	Costs of service contributions <u>Royal Mail</u> makes to its defined benefits pension plans in any given period.
“Delivery Office”	Part of <u>Royal Mail’s</u> <u>postal network</u> (as defined by section 38(3) of the <u>Act</u>) that is responsible for the final sortation, preparation and delivery of mail items to delivery points.
“Downstream Services”	The group of <u>Activities</u> related to the processes of final sorting in <u>Inward Mail Centres</u> , subsequent conveying, sequencing and delivery of mail to its final destination.
“Financeability EBIT”	‘Earnings Before Interest and Tax’ calculated as revenue less all the costs of products and services provided and <u>Transformation Costs</u> , before the deduction of interest and tax.
“EPMU”	‘Equi-Proportional Mark-Up’, which has the meaning given to it in <u>National Costing Rule 12</u> where it relates to the <u>National Costing Methodology</u> or by <u>Zonal Costing Rule 12</u> where it relates to the <u>Zonal Costing Methodology</u> .
“FAC”	‘Fully Allocated Cost’, which is a costing methodology in

which all costs (including Overheads but excluding any form of return, such as return on sales) are allocated to the outputs of the business.

“First Class”	A product and/or service that aims to deliver the next working day (including Saturday) after collection.
“Fixed Asset Register”	A register or list of assets held for the purpose of production of goods or rendering of services that are not held for the purpose of sale in the ordinary course of business. The list allows a company to keep track of details of each fixed asset, ensuring control and preventing misappropriation of assets. It also keeps track of the correct value of assets, which allows for computation of depreciation and for tax and insurance purposes.
“FTE”	Full Time Equivalent which means staff headcount for a period which is calculated by dividing total frontline staff hours worked in that period (including temporary and agency staff hours but excluding contractors’ hours, and including overtime and scheduled attendance) by the total standard full time hours for that period; and adding the result to the average headcount of the rest of the staff in that period.
“GDP”	Gross Domestic Product, which means a measure of economic activity that captures the value of goods and services that the UK produces during a given period.
“General Ledger”	The accounting ledger that contains the financial accounts used by <u>Royal Mail</u> for the application of the <u>National Costing Methodology</u> and the <u>Zonal Costing Methodology</u> for the <u>Reported Business</u> .
“General Overheads”	Has the meaning given to it by <u>National Costing Rule 8</u> where it relates to the <u>National Costing Methodology</u> or by <u>Zonal Costing Rule 8</u> where it relates to the <u>Zonal Costing Methodology</u> .
“Gross Hours”	Total paid hours of frontline staff working in a given <u>Operational Business Process</u> or <u>Operational Business Processes</u> in a given period.
“Gross Hours Reduction”	Reduction in <u>Gross Hours</u> in a given period compared with the period prior to that period.
“IAS 19”	International Accounting Standard 19 - Employee Benefits (2011), which outlines the accounting requirements for employee benefits, including short-term benefits (e.g. wages and salaries, annual leave), post-employment benefits such as retirement benefits, other long-term benefits (e.g. long service leave) and termination benefits.
“Inward Mail Centre”	The part of <u>Royal Mail</u> ’s mail centres in which the activities relating to the processes of final sorting of inward mail for delivery to the final addresses take place.
“MCS”	‘Mails Characteristics Survey’, which is a survey conducted by <u>Royal Mail</u> of the mail product types and volumes within the mail traffic of the <u>Reported Business</u> .

“National Costing Rule(s)”	The requirements in these Guidelines, in paragraphs 8.11 to 8.43, for the purpose of the <u>National Costing Methodology</u> .
“NBV”	‘Net Book Value’, which is the historical cost of an asset less the associated accumulated depreciation.
“Non-operational Business Processes”	The following business processes of the <u>Reported Business</u> as defined in the <u>Costing Manual</u> — <ol style="list-style-type: none">1. commercial;2. support;3. wholesale; and4. business sustaining activities.
“Operational Business Processes”	The following business processes of the <u>Reported Business</u> as defined in the <u>Costing Manual</u> — <ol style="list-style-type: none">1. access (collections);2. outward processing;3. network distribution;4. regional distribution centres processing;5. inward processing;6. local distribution;7. delivery – indoor;8. delivery – outdoor;9. walk bundling centre;10. perform mailroom management; and11. international mail.

“Operational Volumes”	Volume of a product going through the <u>Pipeline</u> measured by the <u>Operational Volumes Method</u> .
“Operational Volumes Method”	A method of measuring the volume of a product going through the <u>Pipeline</u> , by counting or sampling.
“Other Drivers”	Has the meaning given to it by §8.26(b) , read together with <u>National Costing Rule 11</u> where it relates to the <u>National Costing Methodology</u> or by §8.26(b) , read together with <u>Zonal Costing Rule 11</u> where it relates to the <u>Zonal Costing Methodology</u> .
“Overheads”	Costs which are either <u>General Overheads</u> or <u>Pipeline Overheads</u> have the meanings given to them by <u>National Costing Rule 8</u> where they relate to the <u>National Costing Methodology</u> or by <u>Zonal Costing Rule 8</u> where they relate to the <u>Zonal Costing Methodology</u> .
“Pipeline”	All the <u>Operational Business Processes</u> involved in <u>Royal Mail</u> ’s provision of its products and/or services from collection to final delivery of the products and/or services.
“Pipeline Overheads”	Has the meaning given to it by <u>National Costing Rule 8</u> where it relates to the <u>National Costing Methodology</u> or by <u>Zonal Costing Rule 8</u> where it relates to the <u>Zonal Costing Methodology</u> .
“Planning Values”	Number of minutes needed to process 1000 items of mail within a given <u>Operational Business Process</u> , as derived from industrial engineering methods.
“POL”	‘Post Office Limited’ whose registered company number in England and Wales is 02154540, and any of its subsidiaries (as defined by section 1159 of the Companies Act 2006) or any of its subsidiary undertakings (as defined by section 1162 of the Companies Act 2006 and for which section Post Office Limited shall be treated as the parent undertaking).
“PPI”	‘Printed Postage Impressions’, which is pre-printed postage.
“PPIA”	‘Properly Prepared In Accordance’ with these Guidelines and the <u>Guiding Principles</u> set out under <u>USPAC 1.7.2</u> ’, which is an audit opinion that provides reasonable assurance that a financial statement and information, taken as a whole, have been prepared, in all material respects, in accordance with the detailed requirements prescribed by these Guidelines.
“Productivity”	The ratio of the <u>Workload</u> of a given <u>Operational Business Process</u> or <u>Operational Business Processes</u> in a given period to the <u>Gross Hours</u> of that <u>Operational Business Process</u> or those <u>Operational Business Processes</u> in that period.
“Proportional Factors”	Factors representing the proportion of the total volume of each <u>SPHCC</u> which uses the related <u>Activity</u> and determined in accordance with the <u>National Costing Rule 10</u> where they relate to the <u>National Costing Methodology</u> or in accordance with <u>Zonal Costing Rule 10</u> where they relate to the <u>Zonal Costing Methodology</u> .

“PVEO Analysis”	An analysis of the changes in a <u>Financial Year</u> , from the prior <u>Financial Year</u> , of all the costs of the <u>Reported Business</u> included in the calculation of the <u>Financeability EBIT</u> , between the effects of price, volume, efficiency and other factors, as shown in Figure 8 of Appendix 1 of these Guidelines.
“Resource Drivers”	Numeric values which are used to attribute <u>Cost Types</u> to <u>Activities</u> and determined in accordance with <u>National Costing Rule 6</u> where they relate to the <u>National Costing Methodology</u> or in accordance with <u>Zonal Costing Rule 6</u> where they relate to the <u>Zonal Costing Methodology</u> .
“Revenue Derived Volumes”	Volume of a product going through the <u>Pipeline</u> measured by the <u>Revenue Derived Method</u> .
“Revenue Derived Method”	A method of deriving the volume of a product going through the <u>Pipeline</u> , by dividing the revenue received for that product by the average unit price of that product, which is estimated by sampling.
“Second Class”	A product and/or service that aims to deliver by the second or third working day (including Saturday) after collection.
“Short SPHCC”	‘Short Sales Product Handling Characteristic Combinations’, which are products and/or services sub-divided based on the relevant measured characteristics as prescribed by these Guidelines, apart from the characteristic referred to in paragraph 8.22(d) of these Guidelines.
“SPHCC”	‘Sales Product Handling Characteristic Combinations’, which are products and/or services sub-divided based on the relevant measured characteristics as prescribed by these Guidelines.
“Third Class”	A product and/or service that aims to deliver by later than the third working day (including Saturday) after collection.
“Transformation Costs”	Annually recurring costs which <u>Royal Mail</u> incurs in order to restructure its business and/or operations, including redundancy costs.
“Transfer Charge(s)” or “Transfer Price(s)”	The charge or price that one part of a business may charge to another part of the same business, for the products and/or services which the former provides to the latter.
“UKPIL”	‘UK Parcels, International and Letters’, which is an operating unit of <u>Royal Mail</u> .
“Upstream Services”	The group of <u>Activities</u> related to the collection, sorting and conveying of mail to the point where <u>Downstream Services</u> begin.
“USPAC Condition”	The USP accounting condition imposed on <u>Royal Mail</u> as set out in the notification published by <u>OFCOM</u> at Annex 10 to the statement entitled ‘Securing the Universal Postal Service’ dated 27 March 2012, and as modified by <u>OFCOM</u> from time to time.
“V4 Format”	Categorisation of products and/or services into a single billing

code or a group of similar billing codes.

“Weighting Factors”

Factors representing the relative proportions of resources that units of each SPHCC require from the related Activity and determined in accordance with the National Costing Rule 10 where they relate to the National Costing Methodology or in accordance with Zonal Costing Rule 10 where they relate to the Zonal Costing Methodology.

“Weighted Volume Drivers”

Has the meaning given to it by National Costing Rule 10 where it relates to the National Costing Methodology or by Zonal Costing Rule 10 where it relates to the Zonal Costing Methodology.

“Workload”

A measure of weighted volume calculated by using weights derived from the amount of time required for frontline staff to carry out the tasks, identified and measured by industrial engineering methods, in order to process the mail volumes presented in a given Operational Business Process in a given period, expressed relative to the time taken to process 1000 sequenced letters in all relevant Operational Business Processes.

“Zone”

A part of the United Kingdom (based on postcode sectors) for which Royal Mail is using the same price for products and/or services falling within the Reported Business.

“Zonal Costing Rule(s)”

The requirements in these Guidelines for the purpose of the Zonal Costing Methodology.

Section 3: Obligations relating to the Relevant Group under USPAC 1.3

3.1 For the purpose of USPAC 1.3.2, Royal Mail must prepare the financial statements and information specified in **Column 1 of Table 1** by using the pro-forma corresponding to the statement or information as specified in **Column 2 of that Table** (including notes disclosing a breakdown and explanations of any material items).

Table 1: Pro-formas for the financial statements and information for the Relevant Group

<i>Column 1: Financial statement/information referred to in USPAC 1.3.1</i>		<i>Column 2: Pro-forma specified in Appendix 1 of these Guidelines</i>
USPAC 1.3.1(a)	<u>consolidated</u> cash flow projection statement	<i>Not applicable</i>
USPAC 1.3.1(b)	<u>Strategic Business Plan</u>	Figures 7 and 8 of Appendix 1
USPAC 1.3.1(c)	<u>Annual Budget</u>	Figures 7 and 8 of Appendix 1

3.2 For the purpose of USPAC 1.3.3, Royal Mail must prepare each of the financial statements and information specified in **Column 1 of Table 2** in accordance with the additional requirements corresponding to the statement or information as prescribed by **Column 2 of that Table**.

Table 2: Additional requirements for the financial statements and information for the Relevant Group

<i>Column 1: Financial statement/information referred to in USPAC 1.3.1</i>		<i>Column 2: Additional requirements in these Guidelines</i>
USPAC 1.3.1(a)	<u>consolidated</u> cash flow projection statement	<p>The rules in Section 8 of the Guidelines shall apply.</p> <p>The <u>consolidated</u> cash flow projection statement shall include the following—</p> <ul style="list-style-type: none"> a) figures projected for the <u>Financial Quarter</u> for which the statement must be prepared together with the five <u>Financial Quarters</u> that follow that <u>Financial Quarter</u> showing the cash flows and the cash position for the <u>Relevant Group</u>; b) an explanation of the key assumptions underpinning the scenarios prepared in (a) above; c) if <u>Royal Mail</u> changes its projections from one <u>Financial Quarter</u> to another, a reconciliation of the new projections to the previous projections, together with an

		<p>explanation of the material changes;</p> <p>d) figures showing the actual cash position of the <u>Relevant Group</u> at the beginning of the <u>Financial Quarter</u> in question, including a breakdown of material balances and movements in those balances since the beginning of the preceding <u>Financial Quarter</u>, together with an explanation of those material movements and differences with the projections for that preceding <u>Financial Quarter</u>;</p> <p>e) <u>Royal Mail</u>'s assessment of the financial sustainability of the <u>Relevant Group</u>, including its identification of key risks that may affect that sustainability;</p> <p>f) a statement of financing facilities available to the <u>Relevant Group</u> as at the beginning of the <u>Financial Quarter</u> in question, together with information on the extent to which these facilities have been utilised;</p> <p>g) the cash flows referred to in (a) above shall include at least the following—</p> <ol style="list-style-type: none"> 1) 'EBITDA', namely revenue less all the costs of products and services provided before interest, tax, depreciation and amortisation; 2) pension costs including <u>DB Pension Service Costs</u>; 3) working capital; 4) dividends; 5) investments; 6) capital expenditure and proceeds from disposals; and 7) <u>Transformation Costs</u> and any other operating and non-operating specific items; and <p>h) if there are material presentational or methodological changes in the cash flow projections between the <u>Financial Quarter</u> in question and the preceding <u>Financial Quarter</u>, <u>Royal Mail</u> must restate the information relating to the latter together with explanatory notes. This additional requirement shall apply for the second <u>Financial Quarter</u> of the first <u>Financial Year</u> and subsequent <u>Financial Quarters</u>.</p>
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USPAC 1.3.1(b)	<u>Strategic Business Plan</u>	<p>The rules in Section 8 of the Guidelines shall apply.</p> <p>The <u>Strategic Business Plan</u> shall include the following information in relation to the <u>Relevant Group</u> for each <u>Financial Year</u> forecast by <u>Royal Mail</u>—</p> <ul style="list-style-type: none"> a) income statement, balance sheet and cash flow statement; and b) financial health metrics, including the metrics required by the covenants of loans and borrowing facilities, and the metrics considered in assessing and monitoring credit rating. <p>The <u>Strategic Business Plan</u> shall include a reconciliation of the income statement set out in (a) above to the income statements of <u>UKPIL</u> and the <u>Reported Business</u>. The reconciliation must include a reconciliation of the <u>DB Pension Service Costs</u> of the <u>Relevant Group</u>, <u>UKPIL</u>, and the <u>Reported Business</u> calculated on both the cash paid basis and in accordance with <u>IAS 19</u>.</p> <p>The <u>Strategic Business Plan</u> shall include the information set out in (a) and (b) above, and the above-mentioned reconciliation, for the two <u>Financial Years</u> immediately preceding the first <u>Financial Year</u> forecast by <u>Royal Mail</u>.</p> <p>The <u>Strategic Business Plan</u> shall include the following information forecast by <u>Royal Mail</u> in relation to the <u>Reported Business</u> for each of the same <u>Financial Years</u> forecast by <u>Royal Mail</u> in relation to the <u>Relevant Group</u>—</p> <ul style="list-style-type: none"> c) revenues and costs of the <u>Reported Business</u> showing how the <u>Financeability EBIT</u> is calculated; d) breakdown of revenues and volumes in <u>V4 Format</u> and showing separately any contingencies provided against the revenues of any products or product groups; e) <u>Cost Matrix</u> as shown in Figure 7 of Appendix 1 of these Guidelines; f) <u>PVEO Analysis</u> as shown in Figure 8 of Appendix 1 of these Guidelines; g) <u>Workload</u> calculations for all relevant <u>Operational Business Processes</u> including— <ul style="list-style-type: none"> 1) reconciliation of <u>Operational Volumes</u> to <u>Revenue Derived Volumes</u> for each relevant <u>Operational Business Processes</u>
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		<p>and each relevant format;</p> <ol style="list-style-type: none"> 2) mapping of <u>Revenue Derived Volumes</u> used in (g)(1) above to <u>Revenue Derived Volumes</u> provided under (d) above; 3) mapping of the <u>Operational Volumes recorded to the Operational Volumes</u> in (g)(1) above; 4) breakdown of the recorded <u>Operational Volumes</u> in (g)(3) above by the <u>Workload</u> weighting categories, together with the calculations carried out and the assumptions made in preparing the <u>Workload</u> weighting category breakdown; 5) calculation of fixed and variable <u>Workload</u> for each <u>Workload</u> weighting category, setting out the following: <ol style="list-style-type: none"> i. fixed and variable <u>Workload</u> weights for each <u>Operational Business Process</u>; ii. fixed and variable <u>Planning Values</u> for each <u>Operational Business Process</u>; iii. base overall <u>Planning Value</u> for a sequenced letter; iv. <u>CVEs</u> for each <u>Operational Business Process</u>; and v. number of working days; h) <u>Gross Hours Reduction</u>, and <u>Productivity</u> calculations, broken down by the relevant <u>Operational Business Processes</u> and format; i) Headcount and <u>FTEs</u> broken down between frontline, management and other staff; j) explanation of the main assumptions and the key drivers used by <u>Royal Mail</u> in its forecasts of volumes, the <u>Workload</u>, revenues, costs, and <u>Productivities</u> of the <u>Reported Business</u>, including but not limited to economic growth (including <u>GDP</u>), inflation (including <u>CPI</u>), market developments, competition, pricing, sales and marketing initiatives, efficiency initiatives, <u>Gross Hours Reduction</u>, pay and pension arrangements, taxation, legislation, depreciation, and contingencies; and k) a statement of changes in the forecast revenues and costs between the <u>Strategic Business Plan</u> submitted by <u>Royal Mail</u> to
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		<p><u>OFCOM</u> in the Financial Year in question and the most recent <u>Strategic Business Plan</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> prior to that; breaking down the changes in forecast revenues between key revenue streams, and breaking down the changes in forecast costs into key cost categories; and explaining and quantifying the impact of the main drivers of the changes including but not limited to the changes in assumptions with regard to economic growth (including <u>GDP</u>), inflation (including <u>CPI</u>), market developments, competition, pricing, sales and marketing initiatives, efficiency initiatives, <u>Workload</u>, <u>Gross Hours Reduction</u>, <u>Productivity</u>, pay and pension arrangements, taxation, legislation, depreciation, and contingencies.</p> <p>The <u>Strategic Business Plan</u> shall include the information set out in (c), (d), (e), and (g) above in relation to the <u>Reported Business</u> for the two <u>Financial Years</u> immediately preceding the first <u>Financial Year</u> forecast by <u>Royal Mail</u>.</p> <p>The <u>Strategic Business Plan</u> must include sensitivity analyses of the key inputs which have a significant risk of deviating from the values assumed in the <u>Strategic Business Plan</u>. These analyses must include a restatement of the relevant calculations and outputs of the <u>Strategic Business Plan</u> assuming those risks materialise.</p>
<p>USPAC 1.3.1(c)</p>	<p><u>Annual Budget</u></p>	<p>The rules in Section 8 of the Guidelines shall apply.</p> <p>The <u>Annual Budget</u> shall include the following information in relation to the <u>Relevant Group</u>—</p> <ul style="list-style-type: none"> a) income statement, balance sheet and cash flow statement; and b) financial health metrics, including the metrics required by the covenants of loans and borrowing facilities, and the metrics considered in assessing and monitoring credit rating. <p>The <u>Annual Budget</u> shall include a reconciliation of the income statement set out in (a) above to the income statements of <u>UKPIL</u> and the <u>Reported Business</u>. The reconciliation must include a reconciliation of the <u>DB Pension Service Costs</u> of the <u>Relevant Group</u>, <u>UKPIL</u>, and the <u>Reported Business</u> calculated on both the cash paid basis and in accordance with <u>IAS 19</u>.</p> <p>The <u>Annual Budget</u> shall include the following</p>

		<p>information forecast by <u>Royal Mail</u> in relation to the <u>Reported Business</u>—</p> <ul style="list-style-type: none"> c) revenues and costs of the <u>Reported Business</u> showing how the <u>Financeability EBIT</u> is calculated; d) breakdown of revenues and volumes in <u>V4 Format</u> and showing separately any contingencies provided against the revenues of any products or product groups; e) <u>Cost Matrix</u> as shown in Figure 7 of Appendix 1 of these Guidelines; f) <u>PVEO Analysis</u> as shown in Figure 8 of Appendix 1 of these Guidelines; g) <u>Workload</u> calculations for all relevant <u>Operational Business Processes</u> including— <ul style="list-style-type: none"> 1) reconciliation of <u>Operational Volumes</u> to <u>Revenue Derived Volumes</u> for each relevant <u>Operational Business Processes</u> and each relevant format; 2) mapping of <u>Revenue Derived Volumes</u> used in (g)(1) above to <u>Revenue Derived Volumes</u> provided under (d) above; 3) mapping of the <u>Operational Volumes recorded to the Operational Volumes</u> in (g)(1) above; 4) breakdown of the recorded <u>Operational Volumes</u> in (g)(3) above by the <u>Workload</u> weighting categories, together with the calculations carried out and the assumptions made in preparing the <u>Workload</u> weighting category breakdown; 5) calculation of fixed and variable <u>Workload</u> for each <u>Workload</u> weighting category, setting out the following: <ul style="list-style-type: none"> i. fixed and variable <u>Workload</u> weights for each <u>Operational Business Process</u>; ii. fixed and variable <u>Planning Values</u> for each <u>Operational Business Process</u>; iii. base overall <u>Planning Value</u> for a sequenced letter; iv. <u>CVEs</u> for each <u>Operational Business Process</u>; and v. number of working days;
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		<p>6) information in (g)(3) to (g)(5) above recalculated using the assumptions and categories adopted in the <u>Strategic Business Plan</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> on 14 May 2015, together with a mapping of the categories of the recorded <u>Operational Volumes</u> in (g)(3) above to the categories of the recorded <u>Operational Volumes</u> used in the <u>Strategic Business Plan</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> on 14 May 2015; and</p> <p>7) a reconciliation of the total <u>Workload</u> calculated in accordance with (g)(1) to (g)(5) above to the total <u>Workload</u> calculated in accordance with (6) above, breaking down the difference into the differences caused by the following changes:</p> <ul style="list-style-type: none"> i. changes in the <u>Workload</u> calculation methodology including changes in measurement and sampling methodology; ii. changes in the <u>Activities</u> within the <u>Operational Business Processes</u> and <u>Non-operational Business Processes</u>; iii. changes in the standing data (eg container fills and distances) as a result of new measurements carried out using current measurement methodologies; and iv. changes in the scope of the <u>Workload</u> calculation with respect to the <u>Operational Business Processes</u> which are included in the calculation; <p>h) <u>Gross Hours Reduction</u>, and <u>Productivity</u> calculations, broken down by the relevant <u>Operational Business Processes</u> and format;</p> <p>i) <u>Gross Hours Reduction</u>, and <u>Productivity</u> calculations provided under (h) above restated based on the definitions in the <u>Strategic Business Plan</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> on 14 May 2015;</p> <p>j) Headcount and <u>FTEs</u> broken down between frontline, management and other staff;</p> <p>k) explanation of the main assumptions and the key drivers used by <u>Royal Mail</u> in its</p>
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		<p>forecasts of volumes, the <u>Workload</u>, revenues, costs, and <u>Productivities</u> of the <u>Reported Business</u>, including but not limited to economic growth (including <u>GDP</u>), inflation (including <u>CPI</u>), market developments, competition, pricing, sales and marketing initiatives, efficiency initiatives, <u>Gross Hours Reduction</u>, pay and pension arrangements, taxation, legislation, depreciation, and contingencies; and</p> <p>l) a statement of changes in the forecast revenues and costs between the <u>Annual Budget</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> in the <u>Financial Year</u> in question and the most recent <u>Annual Budget</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> prior to that; breaking down the changes in forecast revenues between key revenue streams, and breaking down the changes in forecast costs into key cost categories; and explaining and quantifying the impact of the main drivers of the changes including but not limited to the changes in assumptions with regard to economic growth (including <u>GDP</u>), inflation (including <u>CPI</u>), market developments, competition, pricing, sales and marketing initiatives, efficiency initiatives, <u>Workload</u>, <u>Gross Hours Reduction</u>, <u>Productivity</u>, pay and pension arrangements, taxation, legislation, depreciation, and contingencies.</p> <p>The <u>Annual Budget</u> must include sensitivity analyses of the key inputs which have a significant risk of deviating from the values assumed in the <u>Annual Budget</u>. These analyses must include a restatement of the relevant calculations and outputs of the <u>Annual Budget</u> assuming those risks materialise.</p>
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Section 4: Obligations relating to the Reported Business under USPAC 1.4

4.1 For the purpose of USPAC 1.4.2, Royal Mail must prepare the financial statements and information specified in **Column 1 of Table 3** by using the pro-forma corresponding to the statement or information as specified in **Column 2 of that Table** (including notes disclosing a breakdown and explanations of any material items).

Table 3: Pro-formas for the financial statements and information for the Reported Business

Column 1: Financial statement/information referred to in USPAC 1.4.1		Column 2: Pro-forma specified in Appendix 1 of these Guidelines
USPAC 1.4.1(a)	Annual income statement	Figure 1, 2, 7 and 8, Appendix 1
USPAC 1.4.1(b)	Quarterly income statement	Figure 2 and 7, Appendix 1
USPAC 1.4.1(c)	Annual reconciliation of statements/information specified in USPAC 1.4.1(c)	<i>Not applicable</i>
USPAC 1.4.1(d)	Annual reconciliation of statements/information specified in USPAC 1.4.1(d)	Figure 3, Appendix 1
USPAC 1.4.1(e)	Annual capital employed statement	Figure 4, Appendix 1
USPAC 1.4.1(f)	Annual reconciliation of statements/information specified in USPAC 1.4.1(f)	Figure 4, Appendix 1
USPAC 1.4.1(g)	Annual cash flow statement	Figure 5, Appendix 1
USPAC 1.4.1(h)	Annual reconciliation of statements/information specified in USPAC 1.4.1(h)	Figure 5, Appendix 1
USPAC 1.4.1(i)	Annual product profitability statement	Figure 6, Appendix 1
USPAC 1.4.1(j)	Quarterly product profitability statement	Figure 6, Appendix 1
USPAC 1.4.1(k)	Monthly revenue and volume information statement	<i>Not applicable</i>
USPAC 1.4.1(l)	Quarterly revenue, cost and volume information statements	Figures 9, 10 and 11, Appendix 1

4.2 For the purpose of USPAC 1.4.3, Royal Mail must prepare the financial statements and information specified in **Column 1 of Table 4** in accordance with the additional requirements corresponding to the statement or information as prescribed by **Column 2 of that Table**.

Table 4: Additional requirements for the financial statements and information for the separated Reported Business

Column 1: Financial statement/information referred to in USPAC 1.4.1		Column 2: Additional requirements in these Guidelines
USPAC 1.4.1(a) and (b)	Annual income statement and quarterly income statement	<p>The rules in Section 8 of the Guidelines concerning income statements and product profitability statements shall apply.</p> <p>The annual and quarterly income statements shall include—</p> <p>a) <u>Cost Matrix</u> as shown in Figure 7 of Appendix 1 of these Guidelines;</p> <p>b) a breakdown of items of revenue or cost in these statements, which <u>Royal Mail</u> categorises as other operating and non-operating specific items not included in the calculation of the <u>Financeability EBIT</u>; together with explanations as to the nature of each item and the reasons why each item arose; and</p> <p>c) adjustments made to re-state the <u>DB Pension Service Costs</u> from the basis in accordance with <u>IAS 19</u> to a cash paid basis.</p> <p>The annual income statement shall include—</p> <p>d) <u>PVEO Analysis</u> as shown in Figure 8 of Appendix 1 of these Guidelines; and</p> <p>e) a reconciliation of the total costs included in the following statements and information:</p> <ol style="list-style-type: none"> 1) annual income statements set out in Figures 2 and 3 of Appendix 1 of these Guidelines; 2) annual <u>Cost Matrix</u> as shown in Figure 7 of Appendix 1 of these Guidelines; 3) <u>PVEO Analysis</u> as shown in Figure 8 of Appendix 1 of these Guidelines; and 4) Technical appendices cost data as shown in Appendix 4 of these Guidelines. <p>The quarterly income statement shall include the revenues and costs of the <u>Reported Business</u> forecast by <u>Royal Mail</u> in accordance with the <u>Strategic Business Plan</u>, showing how the forecast <u>Financeability EBIT</u> is calculated.</p> <p>For the avoidance of doubt, items (a) (<u>Cost Matrix</u>) and (d) (<u>PVEO Analysis</u>) above are not</p>

		required for the publicly available annual income statement.
USPAC 1.4.1(c)	Annual reconciliation of statements/information specified in USPAC 1.4.1(c)	<p>The rules in Section 8 of the Guidelines concerning income statements and product profitability statements shall apply.</p> <p>The annual reconciliation shall set out each of the quarterly financial statements and information to be prepared for USPAC 1.4.1(b) and then reconcile the combined total of these four statements with the financial statement and information to be prepared for USPAC 1.4.1(a). Where there are any reconciling differences, <u>Royal Mail</u> must provide accompanying notes and explanations to describe these reconciling differences.</p>
USPAC 1.4.1(d)	Annual reconciliation of statements/information specified in USPAC 1.4.1(d)	<p>The rules in Section 8 of the Guidelines concerning income statements and product profitability statements shall apply.</p> <p>The annual reconciliation shall be reconciled giving appropriate detail and explanation of any reconciling items. Each reconciliation shall include the following two steps as shown in Figure 3 of Appendix 1 of these Guidelines—</p> <ul style="list-style-type: none"> a) a reconciliation between the <u>Reported Business</u> and <u>UKPIL</u>; and b) a reconciliation between <u>UKPIL</u> and the <u>Relevant Group</u>. <p>In addition, <u>Royal Mail</u> must provide in the accompanying notes the detail of the material reconciling differences in the annual reconciliation.</p>

USPAC 1.4.1(e)	Annual capital employed statement	<p>The rules in Section 8 of the Guidelines concerning capital employed statements shall apply.</p> <p><u>Royal Mail</u> shall provide a breakdown of the total fixed asset <u>NBV</u> allocated to the <u>Reported Business</u> as a whole, by main asset classes.</p>
USPAC 1.4.1(f)	Annual reconciliation of statements/information specified in USPAC 1.4.1(f)	<p>The rules in Section 8 of the Guidelines concerning capital employed statements shall apply.</p> <p>The annual reconciliation shall be reconciled giving appropriate detail and explanation of any reconciling items. Each reconciliation shall include the following two steps as shown in Figure 4 of Appendix 1 of these Guidelines—</p> <ul style="list-style-type: none"> a) a reconciliation between the <u>Reported Business</u> and <u>UKPIL</u>; and b) a reconciliation between <u>UKPIL</u> and the <u>Relevant Group</u>. <p>In addition, <u>Royal Mail</u> must provide in the accompanying notes the detail of the material reconciling differences in the annual reconciliation.</p>
USPAC 1.4.1(g)	Annual cash flow statement	<p>The rules in Section 8 of the Guidelines concerning cash flow statements shall apply.</p>
USPAC 1.4.1(h)	Annual reconciliation of statements/information specified in USPAC 1.4.1(h)	<p>The rules in Section 8 of the Guidelines concerning cash flow statements shall apply.</p> <p>The annual reconciliation shall be reconciled giving appropriate detail and explanation of any reconciling items. Each reconciliation shall include the following two steps as shown in Figure 5 of Appendix 1 of these Guidelines—</p> <ul style="list-style-type: none"> a) a reconciliation between the <u>Reported Business</u> and <u>UKPIL</u>; and b) a reconciliation between <u>UKPIL</u> and the <u>Relevant Group</u>. <p>In addition, <u>Royal Mail</u> must provide in the accompanying notes the detail of the material reconciling differences in the annual reconciliation.</p>

USPAC 1.4.1(i)	Annual product profitability statement	<p>The rules in Section 8 of the Guidelines concerning income statements and product profitability statements shall apply.</p> <p><u>Royal Mail</u> must prepare and maintain separate annual product profitability statements for each of the products specified in Column 3 of Table 5.</p> <p>Each of these statements shall only include the costs covered in the <u>National Costing Methodology</u>.</p>
USPAC 1.4.1(j)	Quarterly product profitability statement	<p>The rules in Section 8 of the Guidelines concerning income statements and product profitability statements shall apply.</p> <p><u>Royal Mail</u> must prepare and maintain separate quarterly product profitability statements for each of the products specified in Column 2 of Table 5.</p> <p>Each of these statements shall only include the costs covered in the <u>National Costing Methodology</u>.</p>
USPAC 1.4.1(k)	Monthly revenue and volume information statement	<i>Not applicable</i>
USPAC 1.4.1(l)	Quarterly revenue, cost and volume information statements	<p>The rules in Sections 8 and 9 of the Guidelines shall apply.</p> <p>Quarterly revenue, volume and cost information statement shall include (except for items (c)(6), (c)(7), and (c)(9) which are only required to be included in the statement for the last <u>Financial Quarter</u> of each <u>Financial Year</u>)—</p> <ul style="list-style-type: none"> a) actual and budgeted revenue and volume information for groups of products sold in each <u>Financial Quarter</u>, in the form set out in Figure 9 of Appendix 1 of these Guidelines; b) actual and budgeted cost metrics information for each <u>Financial Quarter</u>, in the form set out in Figure 10 of Appendix 1 of these Guidelines. <u>Royal Mail</u> shall provide an explanation of the variances included in the cost metrics report; c) <u>Workload</u> calculations for all relevant <u>Operational Business Processes</u> including— <ul style="list-style-type: none"> 1) reconciliation of <u>Operational Volumes</u> to <u>Revenue Derived Volumes</u> for each relevant <u>Operational Business Processes</u> and each relevant format; 2) mapping of <u>Revenue Derived Volumes</u> used in (c)(1) above to <u>Revenue Derived Volumes</u> provided under (a) above and (d) below;

		<p>3) mapping of the <u>Operational Volumes recorded to the Operational Volumes</u> in (c)(1) above;</p> <p>4) breakdown of the recorded <u>Operational Volumes</u> in (c)(3) above by the <u>Workload weighting categories</u>, together with the calculations carried out and the assumptions made in preparing the <u>Workload weighting category breakdown</u>;</p> <p>5) calculation of fixed and variable <u>Workload</u> for each <u>Workload weighting category</u>, setting out the following:</p> <ul style="list-style-type: none"> i. fixed and variable <u>Workload weights</u> for each <u>Operational Business Process</u>; ii. fixed and variable <u>Planning Values</u> for each <u>Operational Business Process</u>; iii. base overall <u>Planning Value</u> for a sequenced letter; iv. <u>CVEs</u> for each <u>Operational Business Process</u>; and v. number of working days; <p>6) information in (c)(3) to (c)(5) above covering the results for the <u>Financial Year</u> as a whole, recalculated using the assumptions and categories adopted in the <u>Strategic Business Plan</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> on 14 May 2015, together with a mapping of the categories of the recorded <u>Operational Volumes</u> in (c)(3) above to the categories of the recorded <u>Operational Volumes</u> used in the <u>Strategic Business Plan</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> on 14 May 2015;</p> <p>7) a reconciliation of the total <u>Workload</u> calculated in accordance with (c)(1) to (c)(5) above to the total <u>Workload</u> calculated in accordance with (6) above, covering the results for the <u>Financial Year</u> as a whole, breaking down the difference into the differences caused by the following changes:</p> <ul style="list-style-type: none"> i. changes in the <u>Workload calculation methodology</u> including changes in measurement and sampling methodology; ii. changes in the <u>Activities</u> within the
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		<p><u>Operational Business Processes and Non-operational Business Processes</u>;</p> <p>iii. changes in the standing data (eg container fills and distances) as a result of new measurements carried out using current measurement methodologies; and</p> <p>iv. changes in the scope of the <u>Workload</u> calculation with respect to the <u>Operational Business Processes</u> which are included in the calculation;</p> <p>8) <u>Gross Hours Reduction</u>, and <u>Productivity</u> calculations, broken down by the relevant <u>Operational Business Processes</u> and format; and</p> <p>9) <u>Gross Hours Reduction</u>, and <u>Productivity</u> calculations provided under (8) above, covering the results for the <u>Financial Year</u> as a whole, restated based on the definitions in the <u>Strategic Business Plan</u> submitted by <u>Royal Mail</u> to <u>OFCOM</u> on 14 May 2015;</p> <p>d) actual revenue, cost, and volume information for <u>Short SPHCCs</u>, and <u>Transfer Prices</u> between <u>Upstream Services</u> and <u>Downstream Services</u> for the products set out in Appendix 2 to these Guidelines, for each <u>Financial Quarter</u>, in the form set out in Figure 11 of Appendix 1 of these Guidelines;</p> <p>e) reconciliations of the total revenues and volumes included in the following statements and information—</p> <p>1) quarterly income statement set out in Figure 2 of Appendix 1 of these Guidelines;</p> <p>2) quarterly revenues and volumes information set out in Figure 9 of Appendix 1 of these Guidelines; and</p> <p>3) quarterly revenue, cost, and volume information for <u>Short SPHCCs</u>, in the form set out in Figure 11 of Appendix 1 of these Guidelines; and</p> <p>f) reconciliations of the total costs included in the following statements and information—</p> <p>1) quarterly income statement set out in Figure 2 of Appendix 1 of these</p>
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		<p>Guidelines;</p> <p>2) quarterly <u>Cost Matrix</u> set out in Figure 7 of Appendix 1 of these Guidelines; and</p> <p>3) quarterly revenue, cost, and volume information for <u>Short SPHCCs</u>, in the form set out in Figure 11 of Appendix 1 of these Guidelines.</p>
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Table 5: Product profitability statements

<i>Column 1: Statement number</i>	<i>Column 2: Products specified by <u>OFCOM</u> to be contained in the quarterly product profitability statement</i>	<i>Column 3: Products specified by <u>OFCOM</u> to be contained in the annual product profitability statement</i>
1	<u>Access</u> products D+2 and later letters and large letters	
2	Other <u>Access</u> products	
3		<u>Access</u> products
4		<u>PAF</u>

4.3 For the purpose of interpreting the full meaning of the products specified in **Columns 2 and 3** of **Table 5**, words or expressions shall be interpreted in accordance with **Section 2** of these Guidelines.

Section 5: Obligations relating to the separated Reported Business under USPAC 1.5

5.1 For the purpose of USPAC 1.5.3, Royal Mail must prepare the financial statements and information specified in **Column 1 of Table 6** by using the pro-forma corresponding to the statement or information as specified in **Column 2 of that Table** (including notes disclosing a breakdown and explanations of any material items).

Table 6: Pro-formas for the financial statements and information for the separated Reported Business

<i>Column 1: Financial statement/information referred to in USPAC 1.5.2</i>		<i>Column 2: Pro-forma specified in Appendix 1 of these Guidelines</i>
USPAC 1.5.2(a)	Annual end to end income statement in respect of <u>USO</u> , <u>non-USO</u> and <u>non-Mails</u>	Figure 1, Appendix 1 (for statements to be published by USPAC 1.5.8); and Figure 2, Appendix 1 (for statements to be delivered to <u>OFCOM</u> by USPAC 1.5.10).
USPAC 1.5.2(b)	Quarterly end to end income statement in respect of <u>USO</u> , <u>non-USO</u> and <u>non-Mails</u>	Figure 2, Appendix 1

5.2 For the purpose of USPAC 1.5.4 and USPAC 1.6.1, Royal Mail must prepare the financial statements and information specified in **Column 1 of Table 7** in accordance with the additional requirements corresponding to the statement or information as prescribed by **Column 2 of that Table**.

Table 7: Additional requirements for the financial statements and information for the separated Reported Business

<i>Column 1: Financial statement/information referred to in USPAC 1.5.2</i>		<i>Column 2: Additional requirements in these Guidelines</i>
USPAC 1.5.2(a)	Annual end to end income statement in respect of <u>USO</u> , <u>non-USO</u> and <u>non-Mails</u>	The rules in Section 8 of the Guidelines concerning income statements and product profitability statements and the rules in Section 9 of the Guidelines shall apply.
USPAC 1.5.2(b)	Quarterly end to end income statement in respect of <u>USO</u> , <u>non-USO</u> and <u>non-Mails</u>	The rules in Section 8 of the Guidelines concerning income statements and product profitability statements and the rules in Section 9 of the Guidelines shall apply.

Section 6: Obligations relating to the Costing Manual and the Accounting Methodology Manual under USPAC 1.6

- 6.1 For the purpose of USPAC 1.6.1, Royal Mail must prepare, maintain and keep up-to-date the Costing Manual and the Accounting Methodology Manual in accordance with the general requirements set out in this **Section 6** concerning the Costing Manual and the Accounting Methodology Manual, respectively.

The Costing Manual

General requirements

- 6.2 Royal Mail must comply with the rules in **Section 8** of the Guidelines concerning the National Costing Rules and the Zonal Costing Rules.
- 6.3 Subject to **§6.4**, Royal Mail must prepare, maintain and keep up-to-date the Costing Manual to a comprehensive level of detail to demonstrate compliance with the rules referred to in **§6.2**.
- 6.4 Royal Mail must prepare and present the Costing Manual in a manner that contains the level of detail necessary to allow a competent user of the Costing Manual with a reasonable degree of professional skill to reproduce the results of the National Costing Methodology and the Zonal Costing Methodology without the need for further instruction or interpretation.
- 6.5 Royal Mail must provide information to OFCOM for each separate material change to the Costing Manual in a format that is clear and transparent using the pro-formas set out in **Appendix 3** of these Guidelines.

Technical appendices

- 6.6 OFCOM hereby direct that—
- (a) for the purpose of USPAC 1.6.1, Royal Mail must include in the technical appendices of the Costing Manual the information prescribed in, and the manner required by the pro-forma specified in, **Appendix 4** of these Guidelines; and
 - (b) for the purpose of USPAC 1.6.6, the technical appendices of the Costing Manual that contain commercially confidential information to Royal Mail is prescribed as confidential for that purpose.

The Accounting Methodology Manual

- 6.7 Royal Mail must in the Accounting Methodology Manual include all the detailed documentation of the Regulatory Accounting Methodology that Royal Mail is not required to document in the Costing Manual.
- 6.8 Royal Mail must prepare, maintain and keep up-to-date the Accounting Methodology Manual in accordance with **§6.9** and to a comprehensive level of detail to demonstrate compliance with its obligation referred to in **§6.7**. Without prejudice to the generality of that obligation to include a comprehensive level of detail in the Accounting Methodology Manual, Royal Mail must include—
- (a) a detailed description of the methodology followed in the identification of the relevant

Royal Mail costs for the Relevant Group and the Reported Business; and

(b) separate descriptions of the detailed Regulatory Accounting Methodology used by Royal Mail shall be provided for all the main items in the income statements, capital employed statement and cash flow statements, and including—

(i) a description of the data sources used to calculate inputs and allocations; and

(ii) the methodology and calculations used by Royal Mail to determine that the Transfer Charges are presented in sufficient detail to enable OFCOM to ensure that the calculated Transfer Charges follow the requirements in these Guidelines.

6.9 Royal Mail must prepare and present the Accounting Methodology Manual in a manner that contains the level of detail necessary to allow a competent user of the Accounting Methodology Manual with a reasonable degree of professional accounting skill, and when used in conjunction with the Costing Manual, to gain a clear understanding of how the financial statements and information required by or under the USPAC Condition have been prepared without the need for further instruction or interpretation.

6.10 Royal Mail must provide information to OFCOM for each separate material change to the Accounting Methodology Manual in a format that is clear and transparent using the pro-formas as set out in **Appendix 3** of these Guidelines.

Section 7: Product Allocations for Accounting Separation

- 7.1 For the purpose of USPAC 1.4.7, OFCOM hereby direct that, in relation to product profitability statements in **Column 1** of **Table 5** in **Section 4** of these Guidelines, Royal Mail is only required to publish the combined figures for Access products < 2kg and Access products > 2kg.
- 7.2 Royal Mail must specify in the Accounting Methodology Manual every product and service that falls into each product profitability statement in **Column 1** of **Table 5** in **Section 4** of these Guidelines and every product and service that falls into each product group required by USPAC 1.5.2(a) and 1.5.2(b).
- 7.3 For the avoidance of doubt, any changes Royal Mail may make to the product and service allocations referred to in **§7.2**, for any Financial Quarter or Financial Year to which the USPAC Conditions apply, shall be treated as a change subject to the obligation referred to in **§6.10**.

Section 8: Regulatory Accounting Methodology

- 8.1** Royal Mail must ensure that the Regulatory Accounting Methodology complies with the detailed rules set out in this **Section 8**, which relate to the allocation and apportionment of costs, revenues, assets and cash flows for the Reported Business.

Income statements and product profitability statements

Introduction

- 8.2** Royal Mail must ensure that its preparation of any income statement or product profitability statement for the Reported Business required by or under the USPAC Condition complies with the rules set out below.

Levels of preparation

- 8.3** Royal Mail must ensure, for the purposes of USPAC 1.4.1(a), (d), and (i), that annual income statements, annual reconciliations of such income statements, and annual product profitability statements are prepared to the level of Financeability EBIT, and EBIT as defined in the statutory financial statements of RM plc.
- 8.4** Royal Mail must ensure, for the purposes of USPAC 1.4.1(b), (c), and (j) that quarterly income statements, annual reconciliations of such income statements, and quarterly product profitability statements are prepared to the level of Financeability EBIT, and EBIT as defined in the statutory financial statements of RM plc.

Revenue Accounting

- 8.5** References to “revenue” in this **Section 8** are references to external and internal turnover used in the preparation of any income statement or product profitability statement. External and internal turnover shall consist of income for products and/or services arising from the fair value of the consideration received or receivable for products and/or services provided as part of the operational trading of the Reported Business.
- 8.6** To recognise revenue, Royal Mail must follow the revenue recognition accounting policies adopted by Royal Mail as part of their compliance with the accounting standards used in producing its audited annual statutory accounts.
- 8.7** Revenue shall be assigned directly to the appropriate products and/or services using the relevant information in Royal Mail's billing systems, and shall be consistently applied across all products and/or services, including stamped and metered mail.
- 8.8** Where it is not possible to directly allocate revenue to products and/or services, Royal Mail must use its best endeavours to find the most appropriate and objective driver to apportion the revenue to product and to document this apportionment of revenue in the Accounting Methodology Manual.
- 8.9** Royal Mail must report the revenue by showing the following separately—
- (a) external revenues relating to the sales of any product or service outside of the Relevant Group; and

- (b) internal revenues (resulting from Transfer Charges) relating to the sales of any product or service within the Relevant Group.

Volumes

- 8.10** Royal Mail must follow National Costing Rule 13 as the sole basis for traffic measurement used in the financial statements and information.

Costing

National Costing Methodology

- 8.11** Royal Mail must—

- (a) ensure that the National Costing Methodology complies with the National Costing Rules set out in this **Section 8**;
- (b) document the National Costing Methodology in the Costing Manual; and
- (c) apply the National Costing Methodology to all the costs of the products and/or services of the Reported Business.

National Costing Rules

National Costing Rule 1: Activity Based Costing ('ABC')

- 8.12** The National Costing Methodology shall—

- (a) be based on Activity Based Costing;
- (b) identify—
 - (i) all the Activities that the Reported Business performs as part of its Operational Business Processes and Non-operational Business Processes;
 - (ii) all the products and/or services and SPHCCs which the Reported Business provides;
- (c) calculate Activity Costs, using appropriate Resource Drivers, and ensure that the costs of the resources which each Activity consumes are attributed to that Activity; and
- (d) assign Activity Costs, using appropriate Activity Drivers, to all the products and/or services and SPHCCs which are provided as a result of, or are supported by, that particular Activity. The assignment of Activity Costs shall be undertaken in one of the following two ways—
 - (i) attributing, where a direct causal link between an Activity and the relevant products and/or services and SPHCCs can be identified and used as the basis for assigning costs; or
 - (ii) allocating, where no direct causal link can be identified between an Activity and the relevant products and/or services and SPHCCs, and instead a reasonable assumption shall be made to assign the Activity Costs to the relevant products

and/or services and SPHCCs.

National Costing Rule 2: Operational reality

8.13 As far as is practicable, the National Costing Methodology shall reflect the trading operations of Royal Mail as they are undertaken with the exception of National Costing Rule 3 below concerning Class Costing, but subject to the additional requirements of the Zonal Costing Rules.

National Costing Rule 3: Class Costing

First Class mail

8.14 Class Costing shall be applied to all Avoidable First Class Costs which meet the following criteria—

- (a) the costs would be avoided, if Royal Mail were not to offer First Class, but the current operational specifications of all other products and/or services were to remain unchanged⁵; and
- (b) the costs exclude any incremental costs which would be incurred, if all Second Class using the First Class Activities were to be processed alongside other Second Class.

Avoidable First Class Costs

8.15 All Avoidable First Class Costs shall be attributed only to First Class. Avoidable First Class Costs may include, but is not limited to, the following Cost Types—

- (a) accommodation;
- (b) shift pay allowance; and
- (c) plant and machinery non-running time costs.

Second Class mail

8.16 Class Costing shall be applied to all Avoidable Second Class Costs which meet the following criteria—

- (a) the costs would be avoided, if Royal Mail were not to offer First Class or Second Class, but the current operational specifications of Third Class were to remain unchanged; and
- (b) the costs exclude any incremental costs which would be incurred, if all Third Class using First Class or Second Class Activities were to be processed alongside other Third Class.

Avoidable Second Class Costs

8.17 All Avoidable Second Class Costs shall be attributed only to Second Class. Avoidable Second Class Costs may include, but is not limited to, the following Cost Types—

- (a) accommodation;

⁵ For example, that Second Class mail would continue to be collected and delivered six days a week.

- (b) shift pay allowance; and
- (c) plant and machinery non-running time costs.

National Costing Rule 4: General Ledger costs and Cost Types

8.18 The relevant categories of costs recorded in Royal Mail's financial records (including the financial statements and information required by or under the USPAC Condition), including in the General Ledger, may be aggregated into a set of Cost Types before attributing those costs to Activities. Cost Types shall be selected such that each represents the costs of a single key resource being utilised (e.g. staff, machines, accommodation, vehicles).

National Costing Rule 5: Activities

8.19 Where appropriate (and to the extent possible), Business Processes shall be divided into Activities.

National Costing Rule 6: Resource Drivers

8.20 All costs aggregated into Cost Types shall be attributed to the Activities which cause those costs to be incurred. Where a Cost Type is incurred as a result of more than one Activity, Resource Drivers shall be used to attribute an appropriate share of the Cost Type to each Activity.

8.21 The Resource Driver for each Cost Type shall be—

- (a) based on the resource consumption giving rise to the Cost Type (e.g. staff hours, machine hours, accommodation footprint, vehicle hours); and
- (b) quantified based on appropriate operational and financial data.

National Costing Rule 7: Products and SPHCCs

8.22 Where applicable, each product and/or service, or a group of similar products and/or services, shall be divided into a range of SPHCCs which identifies, and differentiates between, all the applicable and relevant measured characteristics which affect how processing an item of that product and/or service, or group of products and/or services, incurs costs. The measuring characteristics shall, as a minimum, include the following—

- (a) format (e.g. letter, large letter, packet, etc.);
- (b) class (e.g. First Class, Second Class, Third Class, etc.);
- (c) payment method (e.g. stamped, metered, account, PPI, etc.); and
- (d) handling (e.g. mechanised versus manual, etc.).

8.23 The National Costing Methodology shall apply a cost to the whole range of SPHCCs. For the avoidance of doubt, Royal Mail may use additional measuring characteristics.

National Costing Rule 8: Activity Costs

8.24 The National Costing Methodology shall assign an appropriate share of each Activity Cost to each of the relevant SPHCCs as set out below. To determine how an Activity Cost shall be assigned to the relevant SPHCCs, it shall first be determined into which one of the following categories the Activity Cost falls—

- (a) **Attributable Operational Costs:** Activity Costs within a single Operational Business Process which have a direct causal link to the processing of some or all of the SPHCCs;
- (b) **Attributable Non-operational Costs:** Activity Costs which are directly related to certain products and/or services, but are not part of the Operational Business Processes; and
- (c) **Aggregate Costs:** Activity Costs, or a proportion of an Activity Cost, which are assigned in aggregate to notional SPHCCs and not incorporated into the unit costs of other SPHCCs, for the following reasons—
 - (i) the costs do not follow the handling characteristics which are used to define SPHCCs (see National Costing Rule 7); or
 - (ii) the costs relate to Activities carried out on behalf of other Royal Mail business units for products and/or services that do not result in external revenues attributed to the Reported Business, and do not relate to any of the products and/or services of the Reported Business. These costs shall be included in the costing covered by the National Costing Methodology to ensure reconciliation of costs and data integrity.
- (d) Overheads, which shall be classed either—
 - (i) if the Activity Costs relate to one or more Operational Business Processes which do not have a direct causal link to any of the SPHCCs being processed, as Pipeline Overheads; or
 - (ii) if the Activity Costs relate to Non-operational Business Processes, as General Overheads.

National Costing Rule 9: Activity Drivers

8.25 The assignment of Activity Costs to SPHCCs shall be undertaken using appropriate Activity Drivers which shall be identified and quantified based on the following rules—

- (a) each Activity Cost shall be assigned to all the SPHCCs which that Activity directly contributes to, or indirectly supports; and
- (b) Activity Drivers shall reflect the relative proportions of the amount of work which the totality of all the units of each SPHCC creates for the related Activity.

8.26 Three types of Activity Drivers shall be used—

- (a) **Weighted Volume Drivers** (see National Costing Rule 10): These drivers represent the relative amount of work of processing all the units of each SPHCC taking into account the proportion of the total number of units which consume the relevant Activity.
- (b) **Other Drivers** (see National Costing Rule 11): These drivers shall be used for costs which are directly linked to a factor other than mail traffic in the Pipeline (e.g. certain network distribution costs which depend on vehicle runs).

- (c) **EPMU** (see National Costing Rule 12): EPMU methods which allocate costs based on the relative proportions of the costs which have already been assigned to the relevant SPHCCs.

8.27 **Table 8** below shows how each type of Activity Cost shall be assigned to SPHCC (which is illustrated by a tick in the Table).

Table 8: Activity Cost assignment to SPHCC

	<u>Attributable Operational Costs and Attributable Non-operational Costs</u>	Overheads	Aggregate Costs
Weighted Volume Drivers	✓		
Other Drivers	✓		✓
EPMU		✓	

National Costing Rule 10: Weighted Volume Drivers

8.28 Weighted Volume Drivers shall incorporate two types of factors for each relevant attributable Activity Cost, namely—

- (a) Proportional Factors, which represent the proportion of the total volume of each SPHCC which uses the related Activity; and
- (b) Weighting Factors, which represent the relative proportions of amount of work that units of each SPHCC require from the related Activity.

8.29 Proportional Factors referred to in **§8.28(a)** shall be based on operational data collected using representative measurements of total volumes (including statistical sampling techniques where necessary).

8.30 Depending on the nature of the Activity, one or more of the following variables may be used as a determinant of the amount of work to calculate the Weighting Factors—

- (a) time (needed to carry out the Activity): where appropriate, industrial engineering studies must be carried out in accordance with relevant ISO standards;
- (b) weight: appropriate operational data must be used; and
- (c) size: appropriate operational data must be used.

8.31 Royal Mail must carry out for each Financial Year a review to ascertain which Proportional Factors and Weighting Factors need to be reviewed and, if necessary, must update them to ensure that they continue to reflect operational reality accurately.

8.32 To identify the Proportional Factors and the Weighting Factors which may need adjusting

referred to in **§8.31**, Royal Mail must consider what (if any) changes have occurred during the Financial Year in question in the following areas—

- (a) working practices;
- (b) technology; and
- (c) SPHCCs mix (relative volumes).

8.33 Royal Mail may carry out ad hoc event-driven reviews and updates if necessary.

National Costing Rule 11: Other Drivers

8.34 Other Drivers shall be used for costs (certain Attributable Operational Costs and all Attributable Non-operational Costs and Aggregate Costs) which are directly linked to a factor other than mail traffic in the Pipeline.

8.35 Other Drivers shall be defined in a way which appropriately reflects the causal link with that factor.

National Costing Rule 12: Equi-Proportional Mark-Up ('EPMU')

8.36 EPMU shall be used for allocating Overheads by treating them in the following manner—

- (a) Pipeline Overheads shall be allocated to all, and only, those SPHCCs which are processed by that element of the Pipeline; and
- (b) General Overheads shall be allocated to all SPHCCs which are processed through the Pipeline.

8.37 EPMU shall be applied for each of the Activity Costs within Overheads separately, and be based only on the proportions of the Attributable Operational Costs and the Attributable Non-operational Costs, once they have been attributed. EPMU applications shall not take account of any other costs already allocated using EPMU (“non-nested” approach).

National Costing Rule 13: Traffic measurement

8.38 Royal Mail must use the Revenue Derived Method of traffic measurement, whereby the traffic volume for products and/or services is calculated by dividing the total revenue of the products and/or services by the average unit price of them, in the National Costing Methodology.

8.39 The measurement method used for each SPHCC shall be applied consistently within the National Costing Methodology and over time.

National Costing Rule 14: Operational data and sampling

8.40 All operational data used by the National Costing Methodology shall be regularly reviewed and, where necessary, updated to ensure the accuracy of costing and its consistency with the operational reality (see National Costing Rule 2).

8.41 Royal Mail must ensure that all sampling used by the National Costing Methodology is applied by a qualified professional statistician as such sampling must be based on statistical techniques regarded as appropriate for such purposes. The reference to a “qualified professional statistician” is a reference to a person with the relevant statistical knowledge

and expertise, who shall have a qualification in statistics from a recognised professional body, such as the Royal Statistical Society in the United Kingdom.

National Costing Rule 15: Data integrity

- 8.42** The integrity of financial and operational data used for the National Costing Methodology shall be preserved by adequate checks and controls, which shall include reconciliation of total cost data at appropriate points in the National Costing Methodology.
- 8.43** The total amount of input costs relating to any element of the National Costing Methodology shall be equal to the total amount of output costs relating to that element. In particular, the following total figures shall be reconciled to each other—
- (a) the total costs in the General Ledger;
 - (b) the total Activity Costs; and
 - (c) the total costs of all SPHCCs.

Zonal Costing Methodology

- 8.44** Royal Mail must—
- (a) ensure that the Zonal Costing Methodology complies with the Zonal Costing Rules set out in this **Section 8**;
 - (b) document the Zonal Costing Methodology in the Costing Manual; and
 - (c) apply the Zonal Costing Methodology where Royal Mail uses different prices for products and/or services falling within the Reported Business for different parts of the United Kingdom, but only where the provision of such products and/or services are subject to obligations under regulatory conditions (as defined by section 28(2) of the Act).

Zonal Costing Rules

Zonal Costing Rule 1: Activity Based Costing ('ABC')

- 8.45** The National Costing Rule 1 shall apply and the reference in that Rule to the National Costing Methodology is to be read as a reference to Zonal Costing Methodology.

Zonal Costing Rule 2: Operational reality

- 8.46** The National Costing Rule 2 shall apply and references in that Rule to—
- (a) the National Costing Methodology is to be read as a reference to Zonal Costing Methodology; and
 - (b) National Costing Rule 3 is to be read as a reference to Zonal Costing Rule 3.

Zonal Costing Rule 3: Class costing

- 8.47** The National Costing Rule 3 shall apply.

Zonal Costing Rule 4: Zonal General Ledger costs and Cost Types

- 8.48** Non-staff costs attributed to the Delivery Office shall be broken down by Cost Type. (For the avoidance of doubt, any differences relating to a geographic area in these Cost Types shall be included in the Zonal Costing Methodology in accordance with Zonal Costing Rule 16.) Subject to that qualification, the National Costing Rule 4 shall apply.

Zonal Costing Rule 5: Activities

- 8.49** The National Costing Rule 5 shall apply.

Zonal Costing Rule 6: Resource Drivers

- 8.50** The National Costing Rule 6 shall apply.

Zonal Costing Rule 7: Zonal Products and SPHCCs

- 8.51** Royal Mail must attribute costs to products and/or services falling within the Reported Business referred to in **§8.44(c)** by sub-dividing them into SPHCCs in accordance with the following measured characteristics—

- (a) format (e.g. letter, flat, packet, etc.);
- (b) class (e.g. First Class, Second Class, Third Class, etc.); and
- (c) payment method (e.g. stamped, metered, account, PPI, etc.); and
- (d) handling (e.g. mechanised versus manual, etc.).

- 8.52** For the avoidance of doubt, Royal Mail may use additional measuring characteristics, provided that the measured characteristics referred to in **§8.51** are used.

Zonal Costing Rule 8: Activity Costs

- 8.53** The National Costing Rule 8 shall apply and references in that Rule to—

- (a) the National Costing Methodology is to be read as a reference to Zonal Costing Methodology; and
- (b) National Costing Rule 3 is to be read as a reference to Zonal Costing Rule 7.

Zonal Costing Rule 9: Activity Drivers

- 8.54** The National Costing Rule 9 shall apply and references in that Rule to—

- (a) the National Costing Methodology is to be read as a reference to Zonal Costing Methodology;
- (b) National Costing Rule 10 is to be read as a reference to Zonal Costing Rule 10;
- (c) National Costing Rule 11 is to be read as a reference to Zonal Costing Rule 11; and
- (d) National Costing Rule 12 is to be read as a reference to Zonal Costing Rule 12.

Zonal Costing Rule 10: Weighted Volume Drivers

8.55 The National Costing Rule 10 shall apply.

Zonal Costing Rule 11: Other Drivers

8.56 The National Costing Rule 11 shall apply.

Zonal Costing Rule 12: Equi-proportional Mark-up ('EPMU')

8.57 The National Costing Rule 12 shall apply.

Zonal Costing Rule 13: Zonal Traffic measurement

8.58 The National Costing Rule 13 shall apply and references in that Rule to the National Costing Methodology are to be read as references to Zonal Costing Methodology.

8.59 With the commencement of the second Financial Quarter of the first Financial Year, Royal Mail must ensure that any MCS sampling used for estimating costs in relation to Zones for downstream services must include all volumes associated with the downstream services. References to downstream services for that purpose are references to services relating to the final sortation conducted at the Inward Mail Centre and Delivery Offices, and the conveyance of mail items from the Inward Mail Centre to final delivery destination.

Zonal Costing Rule 14: Zonal Operational data and sampling

8.60 Subject to **§§8.61-8.63**, the National Costing Rule 14 shall apply and references in that Rule to—

- (a) the National Costing Methodology is to be read as a reference to Zonal Costing Methodology; and
- (b) National Costing Rule 2 is to be read as a reference to Zonal Costing Rule 2.

8.61 Royal Mail must review its operational data for the estimation of costs of products and/or services falling within the Reported Business referred to in **§8.44(c)**. In addition, Royal Mail must update its estimation of such costs to ensure that it is consistent with—

- (a) the updated values of the explanatory variables⁶ of the relevant cost functions (e.g. postcode sector volumes, number of delivery points, area, volume delivered per delivery point and proportion of business delivery);
- (b) the updated variable coefficients⁷ of the relevant cost functions (updated variable coefficients⁸);
- (c) the updated mapping of postcode sectors, Delivery Offices, and Inward Mail Centres to Zones; and

⁶ The reference to an explanatory variable is a reference to a variable which is used to explain or to predict changes in the value of another variable.

⁷ The reference to a variable coefficient is a reference to figure multiplied with a variable or an unknown quantity in an algebraic formula.

⁸ *Ibid.*

- (d) the updated differentials in costs for each Zone arising from geographic differentials in pay rates and other input costs.

Except for the first Financial Year, Royal Mail must comply with these obligations before the start of every Financial Year. In relation to the first Financial Year, Royal Mail must comply with these obligations by the end of that Financial Year.

- 8.62** Where regressions⁹ are used to estimate the costs referred to in **§8.61**, Royal Mail must include in the Costing Manual information demonstrating that the regressions¹⁰ are statistically valid. Royal Mail must ensure that such regressions are derived by a qualified professional econometrician using data in accordance with the Zonal Costing Rules. The reference to a “qualified professional econometrician” is a reference to a person with the relevant knowledge and expertise in econometrics, who is qualified in the application of mathematics and statistical methods to economic data.
- 8.63** Royal Mail must ensure that all sampling used for the estimation of costs referred to in **§8.61** is applied by a qualified professional statistician as such sampling must be based on statistical techniques regarded as appropriate for such purposes. The reference to a “qualified professional statistician” is a reference to a person with the relevant statistical knowledge and expertise, who shall have a qualification in statistics from a recognised professional body, such as the Royal Statistical Society in the United Kingdom. Royal Mail must include in the Costing Manual information demonstrating that the sampling is statistically valid.

Zonal Costing Rule 15: Zonal Data consistency

- 8.64** The National Costing Rule 15 shall apply and references in that Rule to the National Costing Methodology are to be read as references to Zonal Costing Methodology.
- 8.65** Royal Mail must also ensure that the following figures are reconciled to each other—
- (a) any estimated costs for the postcode sectors served by each Delivery Office shall be reconciled with the total relevant costs of that Delivery Office; and
 - (b) geographically de-averaged costs used for estimating costs in relation to Zones shall be reconciled with the corresponding costs to be derived under National Costing Rule 15.

Zonal Costing Rule 16: Geographic cost reflectivity

- 8.66** Royal Mail must ensure that its estimation of costs in relation to Zones includes all material differences between costs that vary by each geographical area encompassed by the Zone in question.

Zonal Costing Rule 17: Postcode sector cost estimation

- 8.67** Royal Mail must, where it uses estimates of costs in relation to postcode sectors as inputs for estimating costs in relation to Zones, use actual postcode sector data.

Zonal Costing Rule 18: Amendment of Zones

⁹ The reference to a regression is a reference to a relationship between the mean value of a random variable and the corresponding values of one or more independent variables.

¹⁰ *Ibid.*

8.68 Royal Mail must comply with the following rules in relation to defining and amending Zones—

- (a) for the first Financial Year, the total number of Zones shall not exceed four; and
- (b) Royal Mail must review the boundaries of Zones and Royal Mail may define new or additional Zones, provided that Zones having the similarly estimated unit costs shall always be treated as part of the same Zone.

Except for the first Financial Year, Royal Mail must comply with the obligation in **§8.68(b)** before the start of every Financial Year. In relation to the first Financial Year, Royal Mail must comply with that obligation by the end of that Financial Year.

Zonal Costing Rule 19: Reconciliation of zonal and national cost estimates

8.69 Royal Mail must review changes in its estimation of costs in relation to Zones to ensure that—

- (a) in deriving each unit cost estimate, the estimated total postcode sector volumes and estimated total volumes in relation to Zones both equal the total national volumes derived under National Costing Rule 15, and
- (b) the average unit costs in relation to Zones derived from the volumes referred to in **§8.69(a)** remains equal to the corresponding average unit costs derived under the National Costing Methodology.

Except for the first Financial Year, Royal Mail must comply with these obligations before the start of every Financial Year. In relation to the first Financial Year, Royal Mail must comply with these obligations by the end of that Financial Year.

Transformation Costs

8.70 Royal Mail must account for all Transformation Costs arising from the trading operations of Royal Mail relevant to the Reported Business which are not already included in the National Costing Methodology. Royal Mail must account for Transformation Costs in the income statements and product profitability statements for the Reported Business.

8.71 Royal Mail must allocate the Transformation Costs referred to in **§8.70** to the Reported Business by using an appropriate cost driver. The basis of the allocation concerned shall be set out in the Accounting Methodology Manual.

Transfer Charges

8.72 Royal Mail must ensure that Transfer Charges between the Reported Business and the rest of the Relevant Group are applied in compliance with the rules set out in **§8.73-§8.80**.

8.73 For **§8.72**, a Transfer Charge shall be calculated on an arm's length basis for each product and/or service provided.

8.74 Royal Mail must set a Transfer Charge for the provision of each product and/or service between the Reported Business and the rest of the Relevant Group.

- 8.75** All income statements for the Reported Business shall include the Transfer Charges between the Reported Business and the rest of Relevant Group.
- 8.76** Subject to **§§8.77-78**, Royal Mail must calculate a Transfer Charge on an arm's length basis in accordance with **§8.72** by securing that—
- (a) if the product and/or service provided is provided to persons other than the Relevant Group, the Transfer Price shall be equivalent to the price charged to those persons;
 - (b) if the product and/or service is provided to the Relevant Group by other persons, the Transfer Price shall be equivalent to the price charged by those persons; and
 - (c) if the product and/or service does not fall within **§8.76(a) or (b)**, the Transfer Price shall be equal to the FAC of that product and/or service plus a mark up of 10% on FAC.
- 8.77** Royal Mail is not required to set a Transfer Price for the services provided by central finance, human resources, and purchasing and customer management services which are used by UKPIL and are managed centrally.
- 8.78** Royal Mail must apply the rule referred to in **§8.76(c)** in relation to any use of its vehicles, where the use of vehicles is shared between the Reported Business and the rest of the Relevant Group.
- 8.79** Royal Mail must provide a statement setting out all Transfer Charges as part of the notes to the annual and quarterly income statements.
- 8.80** Royal Mail must include in the Accounting Methodology Manual a detailed description of the approach and the assumptions used for the calculation of the Transfer Charges.

Cost Matrix

- 8.81** The cost lines included in the Cost Matrix must be based on the mapping to the General Ledger which was applied in the Cost Matrix prepared as part of Royal Mail's Strategic Business Plan submitted by Royal Mail to OFCOM on 14 May 2015, with the exception of the guidance given in notes 2, 3 and 4 to **Figure 7 of Appendix 1** of these Guidelines.
- 8.82** When changes to the mapping of the Cost Matrix to the General Ledger are necessary, the Cost Matrix shall include the details and the impact of those changes and the reasons for those changes.

PVEO Analysis

- 8.83** The PVEO Analysis for a Financial Year in question shall be prepared in compliance with the following rules:
- (a) Price related cost changes in the Financial Year in question from the prior Financial Year must be calculated by multiplying the costs in the prior Financial Year (excluding all non-recurring items captured by **§8.83(c)**) by the percentage change in an appropriate inflation index during the Financial Year in question from the prior Financial Year.

- (b) Volume related cost changes in the Financial Year in question from the prior Financial Year must be calculated as the sum of the following changes:
- (i) the cost changes related to the changes in the Workload in the Financial Year in question from the prior Financial Year, calculated by multiplying the percentage change in the Workload in the Financial Year in question from the prior Financial Year by the relevant costs in the prior Financial Year excluding non-recurring items (captured by **§8.83(c)**) and subsequently inflated using the inflation index used in **§8.83(a)**;
 - (ii) the changes in the Financial Year in question from the prior Financial Year in all the costs related to POL and international terminal dues; and
 - (iii) any other cost changes in the Financial Year in question from the prior Financial Year related to changes in mail volume.
- (c) Other cost changes must encompass all the cost changes in excess of £5 million related to non-recurring items in the Financial Year in question and the prior Financial Year.
- (d) Efficiency related cost changes shall be the remaining change in the cost in the Financial Year in question from the prior Financial Year, after all the cost changes in **§§8.83(a), (b) and (c)** have been deducted from the total change in costs in the Financial Year in question from the prior Financial Year.

Pension costs

- 8.84** Any pension contributions made by Royal Mail to its pension schemes, including DB Pension Service Costs, which is included in the income statement, the PVEO Analysis, and Cost Matrix shall be measured on a cash paid basis.

Capital employed statements

Introduction

- 8.85** Royal Mail must ensure that the preparation of the annual capital employed financial statement for the Reported Business complies with the rules set out in **§§8.86-8.124**.
- 8.86** The annual capital employed statement shall include operational assets and net working capital (net value of current assets and current liabilities).
- 8.87** The annual capital employed statement shall represent the closing balances of the items as at the end of the Financial Year to which the annual capital employed statement relates.
- 8.88** All the assets and liabilities which are wholly related to the operations and trading of products and services of the Reported Business shall be included in the annual capital employed statement.
- 8.89** Those assets and liabilities which are partly related to the operations and trading of products

and services of the Reported Business shall be apportioned to the Reported Business in compliance with the rules set out in **§§8.90-8.124**.

Non-current assets

8.90 Royal Mail must include in the annual capital employed statement the non-current assets specified in (and in the manner prescribed in) **§§8.91-8.101**.

Fixed assets (property, plant and equipment)

8.91 The value of the fixed assets shall be based on the historical costs and depreciation records kept in the Fixed Asset Register.

8.92 The value of the fixed assets shall be consistent with the values reported in the statutory accounts and the depreciation costs calculated by the National Costing Methodology.

8.93 Royal Mail must include a note to the annual capital employed statement setting out the main asset categories together with their associated NBV, costs and depreciations.

8.94 The allocation of fixed assets which are wholly or partly used by the products and/or services of the Reported Business shall be based on the relative extent to which those assets are used by the products and/or services concerned, where applicable consistent with the allocation of corresponding depreciation charges in the National Costing Methodology.

8.95 If a Transfer Price is charged to the Reported Business by the rest of the Relevant Group for the use of a fixed asset, that fixed asset shall be excluded from the annual capital employed statement of the Reported Business.

8.96 Any internal transfer of fixed assets shall be disclosed in the notes to the annual capital employed statement.

Intangible assets

8.97 The categorisation of intangible assets for the Reported Business shall be consistent with the categorisation in the RM plc's statutory accounts.

8.98 Royal Mail is not required to include goodwill in intangible assets.

8.99 The allocation of software, master franchise licences and customer listing assets shall be based on the relative extent to which such assets are used by the products and/or services of the Reported Business.

Other non-current assets

8.100 Subject to **§8.101**, Royal Mail may include in aggregate other non-current assets.

8.101 Royal Mail must include a note to the annual capital employed statement setting out the main items included in other non-current assets.

Current assets

8.102 Royal Mail must include in the annual capital employed statement the current assets specified in (and in the manner prescribed in) **§§8.103-8.114**.

Trade and other receivables

- 8.103 Trade and other receivables shall include prepayments.
- 8.104 Prepayments shall be allocated based on the allocation of the costs of the associated products and/or services.
- 8.105 Trade receivables shall be allocated based on the revenues of the products and/or services to which they relate.
- 8.106 Royal Mail must include a note to the annual capital employed statement setting out details of the amount of any bad debt provisions allocated to trade receivables.
- 8.107 Royal Mail may include in aggregate other receivables, but Royal Mail must include a note to the annual capital employed statement setting out the main items included in other receivables.

Cash and cash equivalent

- 8.108 The categorisation of cash and cash equivalents for the Reported Business shall include items that are maintained for the purpose of financing business operations and to enable trading of the products and/or services in the Reported Business.
- 8.109 Overdrafts shall be netted off against cash and cash equivalents.
- 8.110 Cash and cash equivalents that are managed centrally within the Relevant Group shall be allocated to the Reported Business to identify the cash requirements for the purpose of financing the operations and trading of the products and/or services of the Reported Business.
- 8.111 The cash requirements of the Reported Business shall be determined based on the operating cash flows and capital expenditure commitments identified to the Reported Business by the rules in these Guidelines.
- 8.112 The cash requirements of the Reported Business may be estimated based on the actual operating and capital expenditures.
- 8.113 Royal Mail must include a note to the annual capital employed statement setting out the main items included in cash and cash equivalents.

Other current assets

- 8.114 Royal Mail may include in aggregate other items in other current assets, but Royal Mail must include a note to the annual capital employed statement setting out the main items included in other current assets.

Current liabilities

- 8.115 Royal Mail must include in the annual capital employed statement at least the current liabilities specified in (and in the manner prescribed in) **§§8.116-8.124**.

Trade and other payables

- 8.116** The allocation of trade payables between the Reported Business and the rest of Royal Mail shall be based on the allocation of the costs of the Activities, products and/or services to which they relate.
- 8.117** Trade and other payables shall include deferred income. The allocation of deferred income between the Reported Business and the rest of Royal Mail shall be based on the allocation of the corresponding income.
- 8.118** Royal Mail may include in aggregate other items in other payables, but Royal Mail must include a note to the annual capital employed statement setting out the main items included in other payables.

Financial liabilities

- 8.119** Financial liabilities shall include interest bearing loans (with less than a year maturity), leases and derivative financial liabilities.
- 8.120** The allocation of financial liabilities between the Reported Business and the rest of the Relevant Group shall be carried out as follows—
- (a) An analysis of the loans shall be undertaken to identify whether the loans have been obtained in relation to a specific asset or group of assets, in which case, the loan shall be allocated based on the allocation of the corresponding asset or group of assets. If the loan does not relate to a specific asset or group of assets, it must be allocated to the Reported Business using the same basis used for the allocation of cash and cash equivalents.
 - (b) The allocation of lease liabilities to the Reported Business shall be based on the allocation of the assets to which the associated leases relate.
- 8.121** Royal Mail must include a note to the annual capital employed statement setting out the details of the facilities (for example, due date, interest rates, etc.).

Provisions and other current liabilities

- 8.122** The allocation of provisions and other current liabilities to the Reported Business shall be based on the costs and Activities to which those provisions and other current liabilities relate.
- 8.123** Where possible, allocation of provisions and other current liabilities to the Reported Business shall be based on the allocation of related costs and activities to the Reported Business.
- 8.124** Royal Mail may include in aggregate provisions and other current liabilities, but Royal Mail must include a note to the annual capital employed statement setting out the main items included in provisions and other current liabilities.

Cash flow statements

- 8.125** Royal Mail must ensure that the preparation of the annual cash flow statement for the Reported Business complies with the rules set out in **§§8.126-8.127**.
- 8.126** The annual cash flow statement shall include all operational cash flows of the Reported Business.

8.127 The allocation of cash flow items to the Reported Business shall be consistent with the allocation of costs and revenues in the corresponding income statements, or the allocation of assets and liabilities in the corresponding capital employed statements.

Section 9: Separation Methodology

Introduction

- 9.1 Royal Mail must ensure that the Regulatory Accounting Methodology complies with the detailed rules set out in this **Section 9**, which relate to the separation, allocation and apportionment of costs, revenues, assets and cash flows between any product groups within the Reported Business.

Income statements

- 9.2 Royal Mail must ensure that its preparation of any income statement for any product groups complies with the rules set out in **§§9.3-9.13**.

Levels of preparation

- 9.3 Royal Mail must ensure, for the purposes of USPAC 1.5.2(a), that annual end to end income statements in respect of USO, non-USO and non-Mails are prepared to the level of Financeability EBIT.
- 9.4 Royal Mail must ensure, for the purposes of USPAC 1.5.2(b), that quarterly end to end income statements in respect of USO, non-USO and non-Mails are prepared to the level of Financeability EBIT.

Apportionment of revenues

- 9.5 References to “revenue” in this **Section 9** are references to external and internal turnover used in the preparation of any income statement. External and internal turnover shall consist of income for products and/or services arising from the fair value of the consideration received or receivable for products and/or services provided as part of the operational trading of the Reported Business.
- 9.6 Revenues shall be allocated to products and/or services in accordance with **Section 7** of these Guidelines.

Apportionment of costs

- 9.7 Costs shall be allocated across any product groups within the Reported Business as follows—
- (a) The costs which are within the scope of the National Costing Methodology shall be allocated to product groups in accordance with the National Costing Methodology. Where SPHCCs are mapped to more than one product group, the basis of the allocation of the SPHCC costs concerned shall be included in the National Costing Methodology and set out in the Costing Manual.
 - (b) Transformation Costs referred to in **§8.70** shall be allocated to product groups using an appropriate underlying driver. The basis of the allocation concerned shall be set out in the Accounting Methodology Manual.

Transfer Pricing between Upstream Services and Downstream Services

- 9.8** Transfer Prices between the Upstream Services and the Downstream Services shall be determined in compliance with the rules set out in **§§9.9-9.13**.

Equivalence pricing

- 9.9** Where there are appropriate comparable Access products and/or services provided by Royal Mail to external customers, Royal Mail must apply the equivalence pricing approach referred to **§9.10** in determining Transfer Prices.

- 9.10** The equivalence pricing approach means—

- (a) An appropriate comparable Access product and/or service shall be identified for the internal product and/or service for which the Transfer Price is to be determined.
- (b) The operational and Activity differences between the internal product and/or service for which the Transfer Price is to be determined, and the appropriate comparable product or service shall be identified.
- (c) The FAC differences of the operational and Activity differences referred to in **§9.10(b)** above shall be identified in a manner consistent with the National Costing Methodology.
- (d) The Transfer Price shall be determined as the sum of the price of the appropriate comparable Access product and/or service, the FAC differences referred to in **§9.10(c)** plus a mark up of 10% on those FAC differences.

- 9.11** Royal Mail may use prices for First Class Access products and/or services, provided that the equivalence pricing approach referred to **§9.10** is followed and that they have—

- (a) sufficient sales volumes to form a statistically valid basis for the calculation of the FAC of the product and/or service in question; and
- (b) material sales volumes.

Where Royal Mail wishes to use prices for First Class Access products and/or services but is unable to satisfy **§9.11(a) and (b)**, Royal Mail must use the price for the most comparable Second Class Access products and/or services.

Cost-plus pricing

- 9.12** Where there are no appropriate comparable Access products and/or services, Royal Mail must set the Transfer Price as equal to the FAC of the product and/or service in question plus a mark up of 10% on that FAC.

Grouping

- 9.13** Single Transfer Prices may be applied to groups of products and/or services, provided that all of the following requirements are met—

- (a) in determining such groups, Royal Mail must only include products and/or services

in a group that fall within the same market definition as out in the following market studies—

- (i) Market study decisions on wholesale & packets markets published in November 2010¹¹.
 - (ii) Market study proposals on retail markets published in March 2011¹².
 - (iii) Market study proposals on international outbound mail market published in May 2011¹³.
- (b) in determining such groups, Royal Mail must not include in a group products and/or services that have materially different handling characteristics as defined in the Costing Manual.
- (c) in determining such groups, Royal Mail must not include in a group products and/or services that are subject to different obligations under regulatory conditions (as defined by section 28(2) of the Act).

¹¹ <http://www.nationalarchives.gov.uk/webarchive/communications-media.htm>

¹² [ibid](#)

¹³ [ibid](#)

Section 10: Auditing

10.1 For the purpose of USPAC 1.4.4, Royal Mail must secure an appropriate audit opinion by a Qualified Independent Auditor in respect of the financial statements and information specified in **Column 1 of Table 10** on the basis specified in **Column 2 of that Table**.

Table 10: Auditing bases directed for the purpose of USPAC 1.4.4

Column 1: Financial statement/information referred to in USPAC 1.4.1		Column 2: Auditing basis
USPAC 1.4.1(a)	Annual income statement (excluding <u>Cost Matrix</u> and <u>PVEO Analysis</u>)	<u>PPIA</u>
USPAC 1.4.1(b)	Quarterly income statement	<i>Not applicable</i>
USPAC 1.4.1(c)	Annual reconciliation of statements/information specified in USPAC 1.4.1(c)	<i>Not applicable</i>
USPAC 1.4.1(d)	Annual reconciliation of statements/information specified in USPAC 1.4.1(d)	<u>PPIA</u>
USPAC 1.4.1(e)	Annual capital employed statement	<u>PPIA</u>
USPAC 1.4.1(f)	Annual reconciliation of statements/information specified in USPAC 1.4.1(f)	<u>PPIA</u>
USPAC 1.4.1(g)	Annual cash flow statement	<u>PPIA</u>
USPAC 1.4.1(h)	Annual reconciliation of statements/information specified in USPAC 1.4.1(h)	<i>Not applicable</i>
USPAC 1.4.1(i)	Annual product profitability statement	<u>PPIA</u>
USPAC 1.4.1(j)	Quarterly product profitability statement	<i>Not applicable</i>
USPAC 1.4.1(k)	Monthly revenue and volume information statement	<i>Not applicable</i>
USPAC 1.4.1(l)	Quarterly revenue, cost and volume information statements	<i>Not applicable</i>

10.2 For the purpose of USPAC 1.5.5, Royal Mail must secure an appropriate audit opinion by a Qualified Independent Auditor in respect of the financial statements and information specified

in **Column 1 of Table 11** on the basis specified in **Column 2 of that Table**.

Table 11: Auditing bases directed for the purpose of USPAC 1.5.5

<i>Column 1: Financial statement/information referred to in USPAC 1.5.2</i>		<i>Column 2: Auditing basis</i>
USPAC 1.5.2(a)	Annual end to end income statement in respect of <u>USO</u> , <u>non-USO</u> and <u>non-Mails</u>	<u>PPIA</u>
USPAC 1.5.2(b)	Quarterly end to end income statement in respect of <u>USO</u> , <u>non-USO</u> and <u>non-Mails</u>	<i>Not applicable</i>

Appendix 1

Pro-formas

Figure 1: Reported Business annual income statement - For publication

	USO Mail	Other	Total Reported Business
	£m	£m	£m
Revenues	xx	xx	xx
Operating costs	xx	xx	xx
People costs (with DB Pension Service Costs on cash paid basis)	xx	xx	xx
Depreciation, amortisation and impairments	xx	xx	xx
Other operating cost	xx	xx	xx
Operating profit/(loss)	xx	xx	xx
Transformation costs	xx	xx	xx
Financeability EBIT	xx	xx	xx
Other operating specific items			xx
Non-operating specific items			xx
EBIT			xx
Financeability EBIT as % of total revenues	x%	x%	x%
Volumes (million items)	xx	xx	xx

Figure 2: Reported Business quarterly and annual income statement - Confidential

	USO Mail	Non USO Mail	Non Mails	Total Reported Business	Total Reported Business
	Actual	Actual	Actual	Actual	Budget
	£m	£m	£m	£m	£m
Revenues	xx	xx	xx	xx	xx
Operating costs	xx	xx	xx	xx	xx
People costs (with DB Pension Service Costs on cash paid basis)	xx	xx	xx	xx	xx
Depreciation, amortisation and impairments	xx	xx	xx	xx	xx
Other operating cost	xx	xx	xx	xx	xx
Operating profit/(loss)	xx	xx	xx	xx	xx
Transformation costs	xx	xx	xx	xx	xx
Financeability EBIT	xx	xx	xx	xx	xx
Other operating specific items				xx	xx
Non-operating specific items				xx	xx
EBIT				xx	xx
Financeability EBIT as % of total revenues	x%	x%	x%	x%	x%
Volumes (million items)	xx	xx	xx	xx	xx

Guidance

The 'Total Reported Business Budget' figures in **Figure 2** above are not within the scope of the PPIA audit requirement under USPAC 1.4.4 set out in **Table 10** of these Guidelines with respect to USPAC 1.4.1(a).

Figure 3: Reconciliation of the annual income statement of the Reported Business to the Relevant Group

	Reported Business	Other operations and adjustments	UKPIL	Other units, eliminations and recharges	Relevant Group
	£m	£m	£m	£m	£m
Revenues	xx	xx	xx	xx	xx
Operating costs	xx	xx	xx	xx	xx
People costs (with DB Pension Service Costs on cash paid basis)	xx	xx	xx	xx	xx
Depreciation, amortisation and impairments	xx	xx	xx	xx	xx
Other operating cost	xx	xx	xx	xx	xx
Operating profit/(loss)	xx	xx	xx	xx	xx
Transformation costs	xx	xx	xx	xx	xx
Financeability EBIT	xx	xx	xx	xx	xx
Other operating specific items	xx	xx	xx	xx	xx
Non-operating specific items	xx	xx	xx	xx	xx
EBIT	xx	xx	xx	xx	xx
Financeability EBIT as % of total revenues	x%	x%	x%	x%	x%
Volumes (million items)	xx	xx	xx	xx	xx

Figure 4: Reported Business capital employed statement and reconciliation to the Relevant Group

	Reported Business	Other operations / Adjustments	UKPIL	Other operations / Adjustments	Relevant Group
	£m	£m	£m	£m	£m
Non-current assets	xx	xx	xx	xx	xx
Tangible assets	xx	xx	xx	xx	xx
Goodwill and Intangible assets	xx	xx	xx	xx	xx
Other non current assets	xx	xx	xx	xx	xx
Current assets	xx	xx	xx	xx	xx
Inventories	xx	xx	xx	xx	xx
Trade and other receivables	xx	xx	xx	xx	xx
Cash and cash equivalents	xx	xx	xx	xx	xx
Other current assets	xx	xx	xx	xx	xx
Total assets	xx	xx	xx	xx	xx
Current liabilities	xx	xx	xx	xx	xx
Trade and other payables	xx	xx	xx	xx	xx
Financial liabilities	xx	xx	xx	xx	xx
Provisions and other current liabilities	xx	xx	xx	xx	xx
Capital employed (total assets less current liabilities)	xx	xx	xx	xx	xx
Non-current liabilities					xx
Financial liabilities					xx
Retirement benefit obligation – pension deficit					xx
Provisions and other non-current liabilities					xx
Total liabilities					xx
Net assets (total assets less total liabilities)					xx
Total equity					xx

Figure 5: Reported Business cash flow statement and reconciliation to the Relevant Group

	Reported Business	Other operations / Adjustments	UKPIL	Other operations / Adjustments	Relevant Group
	£m	£m	£m	£m	£m
EBIT before Transformation Costs with pension costs on IFRS basis	xx	xx	xx	xx	xx
Pension cost adjustment from IFRS to cash basis	xx	xx	xx	xx	xx
EBIT before Transformation Costs with pension costs on cash paid basis	xx	xx	xx	xx	xx
Adjustment for:					
Depreciation and amortisation	xx	xx	xx	xx	xx
Share of post-tax profit from associates	xx	xx	xx	xx	xx
Other	xx	xx	xx	xx	xx
EBITDA before Transformation Costs	xx	xx	xx	xx	xx
Adjustment for working capital movements:					
Inventories	xx	xx	xx	xx	xx
Receivables	xx	xx	xx	xx	xx
Payables	xx	xx	xx	xx	xx
Other	xx	xx	xx	xx	xx
Transformation Costs cash flow	xx	xx	xx	xx	xx
Tax	xx	xx	xx	xx	xx
Other operating activities	xx	xx	xx	xx	xx
Cash flow from operating activities	xx	xx	xx	xx	xx
Investment income	xx	xx	xx	xx	xx
Purchase of assets	xx	xx	xx	xx	xx
Purchase of business interests	xx	xx	xx	xx	xx
Disposals of assets	xx	xx	xx	xx	xx
Disposals of business interests	xx	xx	xx	xx	xx
Other investing activities	xx	xx	xx	xx	xx
Cash flow from investing activities	xx	xx	xx	xx	xx
Finance costs	xx	xx	xx	xx	xx
Repayment of capital element of finance leases	xx	xx	xx	xx	xx
Sale and leaseback	xx	xx	xx	xx	xx
New loan and borrowings proceeds	xx	xx	xx	xx	xx
Repayment of loans and borrowings	xx	xx	xx	xx	xx
Dividends paid to equity holders of parent company	xx	xx	xx	xx	xx
Other dividends	xx	xx	xx	xx	xx
Other financing activities	xx	xx	xx	xx	xx
Cash flow from financing activities	xx	xx	xx	xx	xx
Net increase/(decrease) in cash and cash equivalents	xx	xx	xx	xx	xx
Effect of exchange rates on cash and cash equivalents	xx	xx	xx	xx	xx
Cash and cash equivalents at start of the year	xx	xx	xx	xx	xx
Cash and cash equivalents at end of the year	xx	xx	xx	xx	xx

Figure 6: Annual and quarterly product profitability statements

	Product group 1	Product group 2	...	Product group n
	£m	£m		£m
Revenues	xx	xx		xx
Operating costs	xx	xx		xx
People costs (with DB Pension Service Costs on cash paid basis)	xx	xx		xx
Depreciation, amortisation and impairments	xx	xx		xx
Other operating cost	xx	xx		xx
Operating profit/(loss)	xx	xx		xx
Transformation costs	xx	xx		xx
Financeability EBIT	xx	xx		xx
Financeability EBIT as % of total revenues	x%	x%		x%
Volumes (million items)	xx	xx		xx

Figure 7: Cost Matrix

	Prior Financial Quarter or Year (DB Pension Service Costs on IAS 19 basis)	Prior Financial Quarter or Year (DB Pension Service Costs on cash paid basis)	Current Financial Quarter or Year (DB Pension Service Costs on cash paid basis)	Current Financial Quarter or Year (DB Pension Service Costs on IAS 19 basis)
	£m	£m	£m	£m
Processing & Regional Logistics	xx	xx	xx	xx
Delivery	xx	xx	xx	xx
Network Road Operations	xx	xx	xx	xx
RDC Operation	xx	xx	xx	xx
Frontline people costs	xx	xx	xx	xx
Other/Managers	xx	xx	xx	xx
Operations	xx	xx	xx	xx
Commercial	xx	xx	xx	xx
Technology	xx	xx	xx	xx
Property	xx	xx	xx	xx
Central Admin	xx	xx	xx	xx
Centrally Held (see Note 2)	xx	xx	xx	xx
Total people costs	xx	xx	xx	xx
Collection Delivery & Conveyance Charges (see Note 3)	xx	xx	xx	xx
International Terminal Dues (see Note 4)	xx	xx	xx	xx
Vehicle Fleet & Fuel	xx	xx	xx	xx
Total Distribution & Conveyance Costs	xx	xx	xx	xx
Property	xx	xx	xx	xx
Romec FM Costs	xx	xx	xx	xx
IT & Communication	xx	xx	xx	xx
Depreciation & Amortisation	xx	xx	xx	xx
Total Infrastructure Costs	xx	xx	xx	xx
Audit, Assurance, Consulting, Marketing & Legal	xx	xx	xx	xx
Compensation	xx	xx	xx	xx
Staff & Agents Related Costs & Consumables	xx	xx	xx	xx
Bad Debts and Bank Charges	xx	xx	xx	xx
Low Value Assets, Other Outsourcing, Stamp Production	xx	xx	xx	xx
POL costs	xx	xx	xx	xx
Other External Costs	xx	xx	xx	xx
Internal Charges	xx	xx	xx	xx
Budget Contingency	xx	xx	xx	xx
Total Other Operating Costs	xx	xx	xx	xx
Unallocated non-people costs	xx	xx	xx	xx
Total non-people costs	xx	xx	xx	xx
Total costs before Transformation Costs	xx	xx	xx	xx
Project specific costs	xx	xx	xx	xx
Voluntary redundancy - Frontline	xx	xx	xx	xx
Voluntary redundancy - Management	xx	xx	xx	xx
Voluntary redundancy - Other staff	xx	xx	xx	xx
Business transformation payments	xx	xx	xx	xx
Other Transformation Costs	xx	xx	xx	xx
Transformation Costs	xx	xx	xx	xx
Total costs after Transformation Costs	xx	xx	xx	xx

Guidance

1. The cost lines included in the Cost Matrix must be based on the mapping to the General Ledger which was applied in the Cost Matrix prepared as part of Royal Mail's 2015 Strategic Business Plan submitted to OFCOM on 14 May 2015, with the exception of the following items in notes 2, 3 and 4 below.
2. All pay related costs in this category, including pension costs, must be re-allocated to pay cost categories above it.
3. This must exclude 'International Terminal Dues' shown separately in the line below it.
4. This shall comprise delivery charges from foreign postal and delivery companies for delivery of mail exported from the UK.

Figure 8: PVEO Analysis

	Prior Financial Year (DB Pension Service Costs on cash paid basis)	Prior Financial Year non-recurring items	Prior Financial Year underlying costs (DB Pension Service Costs on cash paid basis)	Price related changes	Prior Financial Year inc. Price related changes	Volume related changes	Efficiency related changes	Current Financial Year non-recurring items	Current Financial Year (DB Pension Service Costs on cash paid basis)	Inflation rate used for Price related changes (see note 5)
	£m	£m	£m	£m	£m	£m	£m	£m	£m	%
Processing & Regional Logistics (Frontline)	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Delivery (Frontline)	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Network Road Operations (Frontline)	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
RDC Operation (Frontline)	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Other/Managers	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Operations	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Commercial	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Technology	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Property	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Central Admin	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Centrally Held (see Note 2)	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Total people costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	
Collection Delivery & Conveyance Charges (see Note 3)	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
International Terminal Dues (see Note 4)	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Vehicle Fleet & Fuel	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Total Distribution & Conveyance Costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	
Property	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Romec FM Costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
IT & Communication	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Depreciation & Amortisation	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Total Infrastructure Costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	
Audit, Assurance, Consulting, Marketing & Legal	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Compensation	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Staff & Agents Related Costs & Consumables	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Bad Debts and Bank Charges	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Low Value Assets, Other Outsourcing, Stamp Production	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
POL costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Other External Costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Internal Charges	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Budget Contingency	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Total Other Operating Costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	
Unallocated non-people costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Total Non People costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	
Total costs before Transformation Costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	
Transformation Costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	x
Total costs after Transformation Costs	xx	xx	xx	xx	xx	xx	xx	xx	xx	

Guidance

1. The cost lines included in the PVEO Analysis must be based on the mapping to the General Ledger which was applied in the Cost Matrix prepared as part of Royal Mail's 2015 Strategic Business Plan submitted to OFCOM on 14 May 2015, with the exception of the following items in notes 2, 3 and 4 below.
2. All pay related costs in this category, including pension costs, must be re-allocated to pay cost categories above it.
3. This must exclude 'International Terminal Dues' shown separately in the line below it.
4. This shall comprise delivery charges from foreign postal and delivery companies for delivery of mail exported from the UK.
5. Royal Mail must provide a description, including the source, of the inflation rates used.

Figure 9: Quarterly revenues and volumes summary

	Revenue - Financial Year to date					Volume - Financial Year to date				
		Prior	%		%		Prior	%		%
	Actual	Financial Year	Variance	Budget	Variance	Actual	Financial Year	Variance	Budget	Variance
A. Letters & Large Letters										
Single Piece	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Bulk Mail (RM24 & 48)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Bulk Mail (Other)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Tracked	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Tracked Returns	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Special Delivery	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Elections	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Other	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total End to End Inland	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total Access	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
International Export	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
International Import	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total International	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Unaddressed	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
TOTAL Letters & Large Letters	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
B. Parcels										
Single Piece	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Bulk Mail (RM24 & 48)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Bulk Mail (Other)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Tracked	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Tracked Returns	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Special Delivery	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Other	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total End to End Inland	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total Access	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
International Export	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
International Import	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total International	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
TOTAL Parcels	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
C = A + B. Total Reported Business										
Single Piece	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Bulk Mail (RM24 & 48)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Bulk Mail (Other)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Tracked	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Tracked Returns	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Special Delivery	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Elections	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Other	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total End to End Inland	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total Access	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
International Export	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
International Import	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total International	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Unaddressed	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
TOTAL Reported Business	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
D. Outside Reported Business and within UKPIL										
Parcelforce Worldwide	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
TOTAL Outside Reported Business and within UKPIL	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
E. = C + D. UKPIL										
TOTAL UKPIL	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx

Figure 10: Quarterly cost metrics

	Financial Quarter					Financial Year to date				
	Actual	Prior year	% Variance	Budget	% Variance	Actual	Prior year	% Variance	Budget	% Variance
Delivery										
Volumes (operational) (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross Hours (k)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross hours % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Productivity % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Processing										
Volumes (operational) (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross Hours (k)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross hours % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Productivity % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Subtotal (Delivery & Processing)										
Volumes (operational) (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross Hours (k)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross hours % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Productivity % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
RDCs										
Volumes (operational) (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross Hours (k)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross hours % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Productivity % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Regional Logistics										
Volumes (operational) (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross Hours (k)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross hours % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Productivity % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Other										
Volumes (operational) (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross Hours (k)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross hours % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Productivity % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total										
Volumes (operational) (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload (m)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross Hours (k)	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Workload % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Gross hours % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Productivity % change	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Number of working days										
	xx	xx				xx	xx			
Cost Savings from Initiatives (£m)										
Hours Reduction Cost Savings	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Other Cost Savings	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Reported Business Headcount Bridge for the Financial Quarter (no. of people)										
	Joiners	Leavers; VR	Leavers; Retirement	Leavers; Attrition	Other (inc. timing, transfers)	Actual Headcount	Prior Year	%Var	Budget	%Var
Fixed Term Full Time	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Fixed Term Part Time	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Permanent Full Time	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Permanent Part Time	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Timing	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx
Total	xx	xx	xx	xx	xx	xx	xx	xx	xx	xx

Figure 11: Short SPHCC revenue, cost and volume data extract file

	Short SPHCC 1		Short SPHCC 2		...	Short SPHCC n	
	YTD Actual	YTD Prior Year	YTD Actual	YTD Prior Year		YTD Actual	YTD Prior Year
Format	xx	xx	xx	xx		xx	xx
Weight Step	xx	xx	xx	xx		xx	xx
Class	xx	xx	xx	xx		xx	xx
Payment method	xx	xx	xx	xx		xx	xx
Scorecard category	xx	xx	xx	xx		xx	xx
Product group	xx	xx	xx	xx		xx	xx
Sales product	xx	xx	xx	xx		xx	xx
V4 category	xx	xx	xx	xx		xx	xx
Volume	xx	xx	xx	xx		xx	xx
Revenue, £	xx	xx	xx	xx		xx	xx
People costs, £	xx	xx	xx	xx		xx	xx
Depreciation, amortisation & impairments, £	xx	xx	xx	xx		xx	xx
Other operating costs, £	xx	xx	xx	xx		xx	xx
Total operating costs, £	xx	xx	xx	xx		xx	xx
Transformation costs, £	xx	xx	xx	xx		xx	xx
Total operating costs inc. Transformation Costs, £	xx	xx	xx	xx		xx	xx
Separated/Non-Separated (see Appendix 2 for Short SPHCCs to be separated)	xx	xx	xx	xx		xx	xx
Transfer price (from Downstream Services to Upstream Services), £	xx	xx	xx	xx		xx	xx
Upstream revenue, £	xx	xx	xx	xx		xx	xx
Upstream total operating costs, £	xx	xx	xx	xx		xx	xx
Upstream total operating costs inc. Transformation Costs, £	xx	xx	xx	xx		xx	xx
Downstream revenue, £	xx	xx	xx	xx		xx	xx
Downstream total operating costs, £	xx	xx	xx	xx		xx	xx
Downstream total operating costs inc. Transformation Costs, £	xx	xx	xx	xx		xx	xx

Appendix 2: Products subject to upstream/downstream separation

<ul style="list-style-type: none"> Business Collections Mailrooms Bespoke Collection Swapshot Mail Collect Safebox Special Delivery Return to Sender Non USO Sales Agents Response Services 1st Sales Agents Response Services 2nd Sales Agents Royal Mail 24 Sales Agents Royal Mail 48 Sales Agents Royal Mail 24 (sort 8) Sales Agents Royal Mail 48 (sort 8) Sales Agents Royal Mail 48 Presort Flat Rate Sales Agents Misc ABB Services Sales Agents Advertising Mail High Sort 1st Sales Agents Advertising Mail High Sort 2nd Sales Agents Advertising Mail High Sort Economy Sales Agents Sustainable Advertising Mail Intermediate Low Sort 2C Sales Agents Advertising Mail Low Sort Economy Sales Agents Business Mail High Sort 1st Sales Agents Business Mail High Sort 2nd Sales Agents Business Mail High Sort Economy Sales Agents Business Mail Low Sort 1st Sales Agents Business Mail Low Sort 2nd Sales Agents Business Mail Low Sort Economy Sales Agents Business Mail Unsorbed 1st Sales Agents Business Mail Unsorbed 2nd Sales Agents Publishing Mail High Sort 1st Sales Agents Publishing Mail High Sort 2nd Sales Agents Sustainable Advertising Mail Low Sort Economy Sales Agents Advertising Mail Low Sort OCR 1st Sales Agents Advertising Mail Low Sort CBC 2nd Sales Agents Business Mail Unsorbed Advance OCR 1st Sales Agents Advertising Mail Unsorbed 1st Sales Agents Advertising Mail Unsorbed 2nd Sales Agents Advertising Catalogue Mail Advertising Mail High Sort 1st Direct Advertising Mail High Sort 1st Residue Advertising Mail High Sort 2nd Direct Advertising Mail High Sort 2nd Residue Advertising Mail High Sort Economy Direct Advertising Mail High Sort Economy Residue Advertising Mail Low Sort BC 1st Advertising Mail Low Sort BC 2nd Advertising Mail Low Sort BC Economy Advertising Mail Low Sort OCR 1st Advertising Mail Low Sort OCR 2nd Advertising Mail Low Sort OCR Economy Advertising Mail Multi Stage Advertising Mail Unsorbed 1st Advertising Mail Unsorbed 2nd Advertising Mail Unsorbed OCR 1st Advertising Mail Unsorbed OCR 2nd Advertising Mail Unsorbed Barcode 1st Advertising Mail Unsorbed Barcode 2nd 	<ul style="list-style-type: none"> Advertising Mail Unsorbed Plus Barcode 1st Advertising Mail Unsorbed Plus Barcode 2nd Advertising Mail Unsorbed Plus OCR 1st Advertising Mail Unsorbed Plus OCR 2nd Advertising with Response Advertising Mail High Sort With Response Economy Direct Advertising Mail Response Business Mail High Sort 1st Direct Business Mail High Sort 1st Residue Business Mail High Sort 2nd Direct Business Mail High Sort 2nd Residue Business Mail High Sort Economy Direct Business Mail High Sort Economy Residue Business Mail Low Sort BC 1st Business Mail Low Sort BC 2nd Business Mail Low Sort BC Economy Business Mail Low Sort OCR 1st Business Mail Low Sort OCR 2nd Business Mail Low Sort OCR Economy Business Mail Unsorbed OCR 1st Business Mail Unsorbed OCR 2nd Business Mail Unsorbed BC 1st Business Mail Unsorbed BC 2nd Business Mail Unsorbed Plus Barcode 1st Business Mail Unsorbed Plus Barcode 2nd Business Mail Unsorbed Plus OCR 1st Business Mail Unsorbed Plus OCR 2nd Business Mail Unsorbed 1st Business Mail Unsorbed 2nd Business Mail Unsorbed Advance OCR 1st Business Mail Unsorbed Advance OCR 2nd Publishing Mail High Sort 1st Direct Publishing Mail High Sort 1st Residue Publishing Mail High Sort 2nd Direct Publishing Mail High Sort 2nd Residue Publishing Mail Low Sort 1st Publishing Mail Low Sort 2nd Publishing Premium Sustainable Advertising Mail High Sort Entry 1st Direct Sustainable Advertising Mail High Sort Entry 1st Residue Sustainable Advertising Mail High Sort Entry 2nd Direct Sustainable Advertising Mail High Sort Entry 2nd Residue Sustainable Advertising Mail High Sort Entry Economy Direct Sustainable Advertising Mail High Sort Entry Economy Residue Sustainable Advertising Mail High Sort Intermediate 1st Direct Sustainable Advertising Mail High Sort Intermediate 1st Residue Sustainable Advertising Mail High Sort Intermediate 2nd Direct Sustainable Advertising Mail High Sort Intermediate 2nd Residue Sustainable Advertising Mail High Sort Intermediate Economy Direct Sustainable Advertising Mail High Sort Intermediate Economy Residue Sustainable Advertising Mail Low Sort Entry BC 1st Sustainable Advertising Mail Low Sort Entry BC 2nd Sustainable Advertising Mail Low Sort Entry BC Economy Sustainable Advertising Mail Low Sort Entry OCR 1st Sustainable Advertising Mail Low Sort Entry OCR 2nd 	<ul style="list-style-type: none"> Sustainable Advertising Mail Low Sort Entry OCR Economy Sustainable Advertising Mail Low Sort Intermediate BC 1st Sustainable Advertising Mail Low Sort Intermediate BC 2nd Sustainable Advertising Mail Low Sort Intermediate BC Economy Sustainable Advertising Mail Low Sort Intermediate OCR 1st Sustainable Advertising Mail Low Sort Intermediate OCR 2nd Sustainable Advertising Mail Low Sort Intermediate OCR Economy Business Sorted Bespoke Advertising Mail Low Sort EIB 1c Advertising Mail Low Sort Mailmark 2nd Business Mail Low Sort Mailmark 1st Business Mail Unsorbed Mailmark 1st Business Mail Unsorbed Mailmark 2nd Advertising Mail Unsorbed Mailmark 2nd Business Mail Low Sort Mailmark 2nd Business Mail Low Sort Mailmark Economy Sustainable Advertising Mail Low Sort Intermediate Mailmark 1c Sustainable Advertising Mail Low Sort Intermediate EIB 2C Sustainable Advertising Mail Low Sort Intermediate Mailmark Economy Publishing Mail Low Sort Mailmark 1c Direct Publishing Mail Low Sort Mailmark 1c EIB Publishing Mail Low Sort Mailmark 2nd Advertising Mail Unsorbed Mailmark 1st Sustainable Advertising Mail Low Sort Entry EIB 1c Sustainable Advertising Mail Low Sort Entry Mailmark 2nd Sustainable Advertising Mail Low Sort Entry Mailmark Economy Advertising Mail Low Sort Mailmark Economy Business Mail 1st Class Advanced Mailmark Letters Business Mail 2nd Class Advanced Mailmark Letters Advertising Mail Unsorbed 1C Advertising Mail Unsorbed 2C Business Mail Low Sort 2C Mailmark ND Advertising Mail Catalogue High Sort Economy Advertising Mail Catalogue High Sort Economy Residues Admail Bespokes Calling for Priority Mail Diversion (Del at Another Address) Freepost Name Government Postage General Election Election Streetsort Election Sort Large User Priority Response Services Large User Response Barcode Large User Response Services ilroom Management Royal Mail 24 Daily Rate Royal Mail 48 Royal Mail 24 Flat Rate Royal Mail 48 Flat Rate Floor Fees Pouch Services Priority Response Services Private Boxes Delivery to Normal Address 12 Months Private Boxes Delivery to Normal Address 6 Months 	<ul style="list-style-type: none"> Private Boxes Early Collection 12 Months Private Boxes Locked 12 Months Private Boxes Standard Service 12 Months Private Boxes Standard Service 6 Months Private Boxes Transfer to PO Box 12 Months Private Boxes Transfer to PO Box 6 Months Private Boxes Standard Service Monthly Private Boxes Delivery to Normal Address Monthly Private Boxes Transfer to PO Box Monthly Response Service Barcode Response Services Standard Retention of Mail (Business only) Rural Carriage of Goods Rural Newspaper Delivery Service Rural Roadside Locked P Letter Boxes Selectapost Surcharges (Business) Surcharges (Mailmark) Timed Delivery Poll Card Mailing Option Do Not Redirect Courier Service (Bespoke) Royal Mail 24 (sort 8) Flat Rate Royal Mail 48 (sort 8) Flat Rate Royal Mail 24 (sort 8) Daily Rate Royal Mail 48 (sort 8) Daily Rate Priority Response Services Licence Freepost Name Licence Priority Services Registered Plus Licence 1500 Large Priority Response Licence Royal Mail 24 (presorted) Royal Mail 48 (presorted) Santa Mail Collection from Private PO Box Safebox Royal Mail Tracked Returns 24 Royal Mail Tracked Returns 48 Tracked Returns Enhancements 1c Tracked Returns Enhancements 2c Postal Voting Pre Sorted Delivery Early Extraction Early Collect Response Services Plus Business Mail Secure Sales Related Fees Response Service Licence Market Reach
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Guidance

For the avoidance of doubt, all the Short SPHCCs within the products included in the above table are subject to the requirements for upstream/downstream separation.

Appendix 3

Material change pro-formas

Royal Mail must—

- (a) in relation to any material change to the Costing Manual, use the pro-forma set out in **Table A** of this **Appendix 3**;
- (b) in relation to any material change to the Accounting Methodology Manual, use the pro-forma set out in **Table B** of this **Appendix 3**;
- (c) in relation to the combined effect of all the material changes made in the Financial Year to the Costing Manual and the Accounting Methodology Manual on Short SPHCCs, use the pro forma set out in **Table C** of this **Appendix 3**; and
- (d) in relation to the combined effect of all the material changes to the Costing Manual and the Accounting Methodology Manual on the Reported Business annual income statements, use the pro forma set out in **Figure 2 of Appendix 1** of these Guidelines.

In using these pro-formas, Royal Mail must ensure that—

- (e) the description of the change is explained in a manner that can be easily understood by a reader who does not have a detailed technical knowledge of Royal Mail's operations and systems (e.g. avoiding acronyms and technical jargon to the greatest extent possible);
- (f) in giving reasons for the change, a brief explanation of the available options for change and Royal Mail's assessment of those options are provided; and
- (g) in stating the compliance with these Guidelines, a reference to the relevant obligations in these Guidelines and an explanation of how Royal Mail considers that the change complies with these obligations.

For the avoidance of doubt, the pro-formas referred to in (a) and (b) above must be notified to OFCOM within 7 days prior to making the changes in question (USPAC 1.6.3). In contrast, by way of exception to USPAC 1.6.3, the pro-forma referred to in (c) above must be notified to OFCOM within 54 days after the end of the last Financial Quarter of the Financial Year, and the pro-forma referred to in (d) above must, be notified to OFCOM within 90 days after the end of the Financial Year.

Table A: Material changes to the Costing Manual

Description of change:						
Date change effective from:						
Area of the National Costing Methodology or Zonal Costing Methodology affected:						
Area of the Pipeline affected:						
Reasons for change:						
Compliance with the Regulatory Accounting Guidelines:						
		(a)	(b)	(c)	(c) / (a)	
Items affected		Value before change	Value after change	Difference	% difference	Comments
Total costs of the Reported Business						
Activity Costs	Activity 1					
	Activity 2					
	...					
	Activity x					
SPHCC Costs	SPHCC 1					
	SPHCC 2					
	...					
	SPHCC x					
Costs of products and/or services	USO products					
	Access products					
	non-USO products (remainder)					
Pipeline costs	Upstream Services					
	Downstream Services					

Table B: Material changes to the Accounting Methodology Manual

Description of change:
Date change effective from:
Reasons for change:
Compliance with the Regulatory Accounting Guidelines:

Income statement: material changes					
	(a)	(b)	(c)	(c) / (a)	
Reported Item	Value before change	Value after change	Difference	% difference	Comments
Item 1					
Item 2					
....					
Item x					

Capital employed statement: material changes					
	(a)	(b)	(c)	(c) / (a)	
Reported Item	Value before change	Value after change	Difference	% difference	Comments
Item 1					
Item 2					
....					
Item x					

Cash flow statement: material changes					
	(a)	(b)	(c)	(c) / (a)	
Reported Item	Value before change	Value after change	Difference	% difference	Comments
Item 1					
Item 2					
....					
Item x					

Notes to the statements: material changes	
Reported Item	Notes
Item 1	
Item 2	
....	
Item x	

Table C: Annual statement of combined effect of all material changes in the Financial Year to the Costing Manual and the Accounting Methodology Manual

		(a)	(b)	(c)	(c) / (a)	
		Value before change	Value after change	Difference	% difference	Comments
Revenues	Short SPHCC 1					
	Short SPHCC 2					
	...					
	Short SPHCC x					
	Total					
Costs	Short SPHCC 1					
	Short SPHCC 2					
	...					
	Short SPHCC x					
	Total					

Appendix 4: Annual information to be included in the pro-formas for the technical appendices of the Costing Manual for the Financial Year

Data Template A

Scope: all SPHCCs with a non-zero FAC or traffic volume in the year

Significant digits: to minimise the impact of rounding errors please provide all data to the maximum number of significant figures allowed by the RM system

					RDT Volume	Total FAC (£)	Unit FAC (p)
SPHCC Group	SPHCC Code	SPHCC Description	Sales Product Code Description	Mon-mails Flag	FY	FY	FY

Data Template B

Scope: all Activities with a non-zero value in the year

Significant digits: to minimise the impact of rounding errors please provide all data to the maximum number of significant figures allowed by the RM system

				Cost (£)
Activity Code	Activity Description	Pipeline Segment	Attribute Description	FY

Data Template C

Scope: all Activities whose cost is allocated by the application of PFs and WFs (excluding "class activities")

Significant digits: to minimise the impact of rounding errors please provide all data to the maximum number of significant figures allowed by the RM system

		PF %	WF
Activity Code	SPHCC Code	FY	FY

Data Template D

Scope: all "class activities" whose PFs and WFs are assigned by reference to another "source activity" on the basis of class

Significant digits: to minimise the impact of rounding errors please provide all data to the maximum number of significant figures allowed by the RM system

			Should Class adopt PF of source Activity	Should Class adopt WF of source Activity
Activity Code of Class Activity	Activity Code of Source Activity	Class	Yes = 1, No = 1	Yes = 1, No = 1

Data Template E

Scope: list all activities whose cost is allocated on an EPMU basis

Activity Code
e.g. HD0104XX

Data Template F

Scope: all SPHCC x Activity combinations with a non-zero total FAC in any quarter

Significant digits: to minimise the impact of rounding errors please provide all data to the maximum number of significant figures allowed by the RM system

		FAC (£)
Activity Code	SPHCC Code	FY