

Registered Number 04138203

Royal Mail Group plc

Accounts

2005-2006



Royal Mail Group plc

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Royal Mail Group plc

Directors' Report

The Directors present the accounts of Royal Mail Group plc (the Company). These accounts relate to the 52 weeks ended 26 March 2006 (2005 52 weeks ended 27 March 2005).

Principal activities

The Company continues to provide a nationwide and international distribution service, principally of mails and parcels.

Review of the business and future developments

Royal Mail collects and delivers over 84 million letters and packages to 27 million addresses every working day, in line with its unique Universal Service Obligation. It is also responsible for designing and producing the UK's stamps and philatelic products. Parcelforce Worldwide is a leading provider of collection and delivery services for urgent packages and parcels within the UK and throughout the world, providing both business and private addresses with a range of timed delivery options.

Over the past year, the postal market in the UK changed forever – since 1 January 2006, Royal Mail has been facing full competition. Our future success now depends on competing effectively in a market where customers have real choice. The mail market opened to full competition and bulk mailers, already active, have in the last 12 months handled more than one billion letters under access agreements with Royal Mail. Our postmen and postwomen are still delivering this mail but we've lost revenue as it is transported directly into our mail centres. We face the prospect of access volumes climbing to three billion items per annum within the next two years, which would amount to around one in seven of the letters we currently handle.

Competition changes everything but we cannot afford to lose the momentum we built up over our three-year Renewal Plan and have sustained over the last year. Improving service to customers has continued to be the number one priority of everyone in the Company during 2005-06. Quality of service performance for both First Class and Second Class mail has been above target levels for over a year – with 94.1% of First Class mail arriving the day after posting. Second Class mail was ahead of target too with a 98.8% performance and the large bulk of business mail services also hit or exceeded their targets.

There was a decline in inland addressed mail with the impact exacerbated by some bulk mail customers switching to lower-priced services. Royal Mail also continues to make losses in fulfilling its Universal Service 'one-price goes anywhere' Obligation as we continue to lose money on First and Second Class stamped letters.

With competition intensifying and clear signs that the letters market may well decline further, the need for Royal Mail to drive efficiency changes is unmistakable. Improving efficiency in a declining market is much tougher than making productivity gains in a growing one. A key challenge we face is to make rapid progress by investing in new technology and modernising the way we work.

In Royal Mail we have introduced a number of initiatives giving high priority to ensuring the integrity of the mail. We have introduced this year new management processes, appointed a director who is specifically responsible for mails integrity and revised and updated our policies. Last year was the first full year that we applied the vetting powers, that Royal Mail sought and was granted, to check if applicants were attempting to conceal any past criminal convictions. It has armed us with an additional layer of security. We have also reduced the number of casual employees to around 500 – in marked contrast to the almost 20,000 employed in the autumn of 2004 and have deployed a new quarterly audit of the security of the mail in all our mail centres and delivery offices. Our policy remains – zero tolerance to any form of wrongdoing.

In the parcels market, Parcelforce Worldwide has continued to establish itself as a key player in the competitive, non-regulated express parcels delivery service. It delivers some 45 million parcels a year, to customers in 239 countries and territories across the world. Parcelforce Worldwide made a full year operating profit for the first time ever – the result of a long haul involving a focus on business customers, exiting from loss-making contracts and cutting costs, while all the time focusing on delivering quality service by well-motivated people. It's a fantastic achievement but we are in no way complacent as maintaining profitability in an intensely competitive market is a further tough challenge faced by the business.

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Directors' Report (continued)

Providing a consistent high quality service to customers and giving them value-for-money will continue to be the top priorities for all our business segments in the current year as these are key to keeping customers, and winning new ones, in a competitive marketplace. Our parcels business is expected to grow, albeit at lower rates than experienced in the past, due in part to the industry-wide consolidation that is taking place. Royal Mail has recently accepted Postcomm's proposals for the third price control for the next four years, but finds itself further burdened by restrictions on its ability to change its non-price terms at a time when markets are being opened and flexibility will be key. It also expects to see further volume loss to Downstream Access over and above the 1 billion loss in 2005-06. However, Royal Mail continues to drive efficiencies, but must now significantly invest in its network to ensure it can continue to do so and compete with domestic and European rivals.

Results and dividends

The profit after taxation for the year was £740m (2005 restated £165m). The Directors do not recommend a dividend (2005 nil dividend). The movements in reserves are shown in note 24 to the accounts.

Pensions

Royal Mail Group plc's pension assets and liabilities are materially larger than its other operating assets and it is one of the most exposed UK corporates to pension scheme volatility, particularly with respect to movements in equity values and bond rates.

Royal Mail Group plc is the sponsoring employer for the Royal Mail Pension Plan, the Royal Mail Senior Executive Pension Plan and the Royal Mail Retirement Savings Plan. These plans together constitute the sixth largest pension scheme in the UK.

The Company has legal liability for the pension scheme but has an agreement to second employees to its subsidiary, Post Office Limited, under which Post Office Limited bears the cost of employment of these employees and is responsible for the funding of the pension deficit for these employees. Consequently, the deficit has been allocated based on the share of employee numbers over the past 12 years.

The Company recognises the remaining share of the RMPP and RMSEPP total deficit. This approximated to 93% of the total deficit. The Group's current service cost and future service contributions are applied to the Company's payroll. Curtailments are charged and paid by the Company. The finance income, deficiency payments and actuarial gains or losses are allocated on the same basis as the original deficit giving the Company approximately 93% of the Group totals.

The last full triennial valuation of the pension schemes as at March 2003 confirmed a substantial funding deficit due principally to changes in asset valuations, lower discount rates, a fall in the expected long-term investment returns and increased life expectancy of employees and pensioners. The FRS 17 deficit has increased this year from a liability of £3,678m in 2005 to £5,156m. The increase in the deficit of £1,478m during the year mainly relates to an actuarial loss of £1,509m, which principally arose from the lower discount rate assumption and revised mortality assumptions. Full pension disclosures are made in note 25 to the accounts.

Political and charitable contributions

During the year, the Company made charitable contributions amounting to £1m (2005 £2m). No political contributions were made in the year (2005 £nil).

Research and development

Research and development expenditure during the year amounted to £1m (2005 £1m).

Policy on the payment of suppliers

The Company's policy is to use its purchasing power fairly. Payment terms are agreed in advance for all major contracts. For lower value transactions, the standard payment terms, printed on the purchase order apply. It is Company policy to abide with the agreed terms. The Company has sought to comply with the DTI's Better Payment Practice Code. Copies of this can be obtained from the DTI.

The number of days' purchases in creditors at the balance sheet date was 16 (2005 16 days).

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Directors' Report (continued)

Land and buildings

In the opinion of the Directors, the aggregate market value of the Company's land and buildings exceeds the net book value, based upon a historic cost accounting policy, of £1,029m (2005 £1,066m) by £594m (2005 £405m).

Directors and their interests

The following have served as Directors of the Company during the year ended 26 March 2006 and up to the date of approval of these accounts:

Allan Leighton (Chairman)

David Burden

Alan Cook

Appointed 1 March 2006

Adam Crozier

Ian Griffiths

Appointed 6 February 2006

Tony McCarthy

Marisa Cassoni

Resigned 17 November 2005

David Mills

Resigned 31 December 2005

No Director has a beneficial interest in the share capital of the Company.

Qualifying third party indemnity provisions for Directors

At the time the Directors' Report was approved under s234A, a partial qualifying third party indemnity provision was and remains in force for the benefit of all Directors of Royal Mail Group plc was and remains in force for the benefit of one or more persons who were then Directors of the Company. The indemnity is granted under article 129 of the Company's Articles of Association. The indemnity is partial in that it does not allow the Company to cover the costs of an unsuccessful defence of a third party claim.

Financial risk management objectives and policies

The Company's principal financial instruments, other than derivatives, comprise short-term deposits, money market liquidity investments, Government gilt edged securities, loans, finance leases and hire purchase contracts and cash. The main purposes of these financial instruments are to raise finance and manage the liquidity needs of the business operations. The Company has various other financial instruments such as trade debtors and trade creditors, which arise directly from operations.

The Company also enters into derivative transactions, principally commodity swaps and forward currency contracts. The purpose is to manage the commodity and currency risks arising from the Company's operations. It is, and has been throughout the year under review, the Company's policy that no speculative trading in financial instruments shall be undertaken.

Further details of the Company's treasury risk management policies can be found in note 28 and in the Operating and Financial Review within the Royal Mail Holdings plc Group accounts.

People

Royal Mail Group plc employs approximately 193,000 people (2005 196,000) in our wholly owned UK subsidiaries. Our people are our strategic strength and competitive advantage.

The Company's policy is to encourage effective communication and consultation between our people, particularly on matters relating to strategy, financial and economic factors that may influence the Company's performance. This is achieved through the use of an extensive range of communication channels, including magazines, briefings, open forums and an intranet website. Our people have various bonus schemes, significant elements of which are based on business-related targets.

We actively encourage continuous training and skill development for all our people to ensure achievement of corporate and individual objectives. Management development and training programmes have been designed to attract and retain the best. The Company has worked with the unions to introduce several innovative working practices to improve efficiency.

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Directors' Report (continued)

An Equal Opportunities policy is maintained in all respects including disability, age, religion, colour, sex, nationality, ethnic origin, sexual orientation, race, creed and marital status.

In 2002, the Chairman created a programme to make Royal Mail Group a 'Great Place to Work' and made it a priority for everyone across the business. The purpose of the programme is to encourage people to contribute to improving their working environment, to equip our people with the skills they need, to develop pride in and understanding of the business and to drive respect for colleagues - in short, to ensure people considerations are at the heart of all major business decisions. The programme is ongoing and will remain an integral part of our people strategy. Royal Mail's people are our greatest asset and we are committed to making the Royal Mail a great place to work. Engaging and involving our people is the key to this and that is why we want them to have a stake in the Company. We hold regular Worktime Listening and Learning sessions to hear and discuss how we are tackling the challenges we face and the direction in which the Company is moving as well as raising issues of concern to our people.

Corporate Social Responsibility

Royal Mail is committed to carrying out its activities in a socially responsible manner in respect of the environment, employees, customers and local communities. A Corporate and Social Responsibility (CSR) Governance Committee reports to the Board, which publishes an annual report of its activities. Further details of our CSR governance structure and activities will be available in our 2006 CSR Report, due to be published in September 2006.

Disabled employees

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


Going concern

After analysis of the financial resources available and on the basis of careful consideration of the cash flow projections for the Company, the Directors have concluded that it is appropriate that the financial statements have been prepared on a going concern basis. Further information regarding going concern has been disclosed in the Fundamental accounting concept policy (note 1 to the accounts).

Auditors

A resolution to reappoint Ernst & Young LLP as auditors will be put to the Annual General Meeting.

By Order of the Board



Jonathan Evans
Secretary
London
2 August 2006

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Statement of Directors' responsibilities in respect of the accounts

Company law requires the Directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing those accounts Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent; and
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts.

Directors are responsible for ensuring that proper accounting records are kept which disclose with reasonable accuracy, at any time, the financial position of the Company, and which enable them to ensure that the accounts comply with the Companies Act 1985. Directors are also responsible for ensuring that the assets of the Company are safeguarded and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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Independent Auditors' Report to the members of Royal Mail Group plc

We have audited the Company's financial statements for the year ended 26 March 2006 which comprise the profit and loss account, the statement of total recognised gains and losses, the reconciliation of movements in shareholders' funds, the balance sheet and the related notes 1 to 31. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

The Directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and Accounting Standards (United Kingdom Generally Accepted Accounting Practice) as set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 26 March 2006 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young LLP

Ernst & Young LLP
Registered auditor
London
2 August 2006

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Profit and loss account

for the years ended 26 March 2006 and 27 March 2005

		2006			2005 As restated*		
	Notes	Before exceptional items £m	Exceptional items (note 5) £m	Total £m	Before exceptional items £m	Exceptional items (note 5) £m	Total £m
Turnover	2	7,195	-	7,195	7,083	-	7,083
Costs:		(6,851)	172	(6,679)	(6,739)	(242)	(6,981)
Staff costs	3/5	(4,842)	(141)	(4,983)	(4,761)	(237)	(4,998)
Depreciation and amortisation	4	(149)	-	(149)	(135)	-	(135)
Impairment	4/5	-	(5)	(5)	-	(3)	(3)
Other operating charges	4/5	(1,860)	318	(1,542)	(1,843)	(2)	(1,845)
Operating profit	4	344	172	516	344	(242)	102
Net profit on disposal of tangible fixed assets	5	-	53	53	-	56	56
Profit/(loss) on disposal of subsidiary undertaking	5	-	5	5	-	(1)	(1)
Profit on ordinary activities		344	230	574	344	(187)	157
Income from investments	7	7	-	7	3	-	3
Finance income - net pensions interest	8	94	-	94	55	-	55
Other net interest receivable	9	29	-	29	31	-	31
Profit on ordinary activities before taxation		474	230	704	433	(187)	246
Taxation	10			36			(81)
Profit retained for the financial year	24			740			165

*see note 1 for information about the restatements.

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Statement of total recognised gains and losses for the years ended 26 March 2006 and 27 March 2005

	Notes	2006 £m	2005 As restated* £m
Profit for the financial year		740	165
Actuarial (loss)/gain on defined benefit schemes	24/25	(1,509)	382
Gains on cash flow hedges taken to equity during the year	24	3	-
Transfers to profit and loss account on cash flow hedges	24	(10)	-
Transfers to the balance sheet – on the carrying amount of non financial assets and liabilities	24	(1)	-
Taxation on items taken directly to equity	10/24	(33)	364
Total recognised (loss)/gain for the financial year		(810)	911

Note on prior period adjustment

Total recognised gains and losses related to the year (as above)	(810)
Loss on first time adoption of FRS 25 and FRS 26 (see accounting policy note on page 11 – Basis of preparation)	(3)
Prior period adjustment (as explained in note 24)	(4,222)
Total recognised gains and losses since last Annual Report	(5,035)

Reconciliation of movements in shareholders' funds

	Notes	2006 £m	2005 As restated* £m
Opening shareholders' funds as previously reported	24	2,329	2,146
Prior period adjustment	24	(4,222)	(4,950)
Restated opening shareholders' funds	24	(1,893)	(2,804)
Restatement for the effect of FRS 25 and FRS 26		(3)	-
Total recognised losses related to the year (see above)		(810)	911
Closing shareholders' funds	24	(2,706)	(1,893)

*see note 1 for information about the restatements.

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

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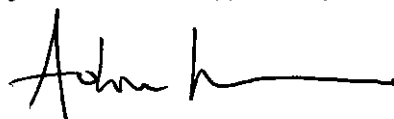
Balance sheet

at 26 March 2006 and 27 March 2005

	Notes	2006 £m	2005 As restated* £m
Fixed assets			
Intangible assets	11	27	-
Tangible assets	12	1,454	1,464
Financial assets - investments	13	42	42
Total fixed assets		1,523	1,506
Current assets			
Stocks		13	15
Debtors - receivable within one year	14	1,061	918
Debtors - receivable beyond one year	14	626	623
Financial assets - derivatives	15	3	-
Financial assets - investments	16	953	1,056
Cash at bank and in hand		11	12
		2,667	2,624
Amounts falling due within one year:			
Creditors	17	(1,308)	(1,587)
Financial liabilities - derivatives	18	(3)	-
Net current assets		1,356	1,037
Total assets less current liabilities		2,879	2,543
Retirement benefit obligation	19/25	(4,893)	(3,352)
Other creditors - amounts falling due after more than one year	20	(583)	(904)
Provisions for liabilities and charges	22	(109)	(180)
Net assets		(2,706)	(1,893)
Shareholder's equity			
Called up share capital	23	-	-
Share premium	24	3,784	3,784
Revaluation reserve	24	-	-
Profit and loss account	24	(7,326)	(6,478)
Mails reserve	24	836	801
Hedging reserve	24	-	-
Equity shareholders' funds		(2,706)	(1,893)

*see note 1 for information about the restatements.

The accounts on pages 8 to 33 were approved by the Board of Directors on 2 August 2006 and signed on its behalf by:


Adam Crozier

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Notes to the accounts

1 Accounting policies

The following accounting policies apply throughout the Company:

Financial year

The financial year ends on the last Sunday in March and accordingly, these accounts are made up to the 52 weeks ended 26 March 2006 (2005 52 weeks ended 27 March 2005).

Basis of preparation

The accounts on pages 8 to 33 have been prepared in accordance with applicable accounting standards under the historic cost accounting convention and the requirements of the Companies Act 1985, except for comparative disclosures relating to investments in Government gilt-edged securities as described in the Financial instruments accounting policy note on page 15.

The accounts present information about the Company as an individual undertaking and not as a Group. The Company has taken advantage of section 228 of the Companies Act 1985 not to prepare Group accounts on the grounds that its ultimate parent undertaking makes its Group accounts publicly available.

In preparing the financial statements for the current year, the Company has adopted the following new Financial Reporting Standards that have been issued by the Accounting Standards Board:

FRS 17 – Retirement benefits. The standard prescribes how to measure the assets and liabilities of the defined benefit schemes. It also prescribes the basis for determining the profit and loss charge. The impact at 28 March 2005 of full implementation has been to write-off the SSAP 24 debtor of £835m and its associated deferred tax liability of £76m and to recognise a liability of £3,678m and an associated deferred tax asset of £326m (resulting in a reduction in net assets of £4,111m). The effect of this change was to reduce the prior year profit by £90m.

FRS 23 – Effects of changes in Foreign Exchange Rates. In the context of these accounts, the standard prescribes how to include foreign currency transactions in financial statements. These accounts comply with the requirements of the standard. The 'Foreign currencies' accounting policy note below details the Company's approach to foreign currency translation. There is no additional impact on the results of the Company through the adoption of this standard.

FRS 25 – Financial Instruments: Disclosure and Presentation and FRS 26 – Financial Instruments: Measurement. These standards contain requirements regarding the measurement and presentation and classification of financial instruments and the relevant information that should be disclosed. The accounting policy notes 'Financial instruments' and 'Derivative financial instruments' below set out the Company's approach to the application of these standards. The impact of these standards is as follows:

- derivative instruments of £9m assets and £1m liabilities have been recognised in the balance sheet at fair value at 28 March 2005; and
- under the previous standard FRS 13, foreign exchange gains and losses on an unsettled hedge programme were carried in the balance sheet. On introducing FRS 25 and FRS 26 at 28 March 2005, losses amounting to £11m have been written off against retained earnings.

FRS 21 – Events after the balance sheet date. This standard has also been adopted but as the Company already complies with its requirements, there is no additional impact on the reported results.

No financial instrument disclosures have been presented as the Company is a wholly-owned subsidiary of a company which has presented such disclosures in its Group accounts.

In accordance with FRS 1 (revised) 'Cash flow statements', no cash flow statement has been presented as the Company is a wholly-owned subsidiary of a company which has presented a consolidated cash flow statement within its Group accounts.

Royal Mail Group plc

1 Accounting policies (continued)

Royal Mail Group plc is exposed to the risk of being fined by its industry Regulator and of being required to pay compensation to certain customers, as a result of failing to meet operational targets set by the Regulator in the Company's licence. The amount of such fines and compensation will be determined by the Regulator after further representations from the Company and no further information is being disclosed on the grounds that it can be expected to prejudice the outcome of that process.

Change in accounting policies

In accordance with FRS 18 'Accounting policies' the Company's accounting policies are reviewed regularly and changed when a new policy becomes more appropriate. Accordingly, the following changes in policy have been adopted in the 2005-06 financial year to provide a more relevant and reliable presentation of results:

Financial assets – investments (fixed assets)

Previously, investments in internally formed companies were recognised at the net asset value of the internally formed company. The adoption of the current accounting policy, disclosed in the Financial assets – investments policy note below, has resulted in a prior year adjustment, reducing investments by £65m. This reduction has had no profit or loss impact as the adjustment affects only the investment value and revaluation reserve. There is no impact of this change of policy on the current year results.

Annual leave entitlement liability

Following improvements in the reporting of annual leave information, an accrual is recognised for all short-term accumulating compensated absences, such as holiday entitlement earned but not taken at the balance sheet date. The impact of this change of policy on the prior year results is that the retained profit of the Company was reduced by £39m. The effect of this adjustment was to decrease profit in the prior year by £2m. In the current year the accrual was reduced by £3m and the retained profit of the Company therefore increased by £3m.

Operating leases – incentives

Due to improved information the aggregate benefit of incentives, received as part of the agreement of a new or renewed operating lease, is now being recognised as a reduction of rental expense over the lease term, on a straight-line basis. As a result, the Company recognised lease incentives of £8m in the prior year of which £1m was amortised. The impact of this change of policy on the prior year results of the Company is therefore a reduction of £7m retained profit. A further £2m of new lease incentives were recognised in the balance sheet for the current year and this amount, although offset by a relatively small amortisation credit relating to existing lease incentives, has resulted in an additional £2m charge to the profit and loss account in the current year.

Fundamental accounting concept

Royal Mail Group plc has net liabilities at 26 March 2006, primarily because of the pension deficit within its main pension plan, the Royal Mail Pension Plan. Consequently, Royal Mail Group plc is in default of its borrowing facilities with Government, but has received formal waivers from the Department of Trade and Industry, in its capacity as lender.

Royal Mail Group plc is profitable, even though it has to bear losses relating to stamped mail and the carrying out of its Universal Service Obligations, but it now faces considerable cash requirements with respect to its proposed investment in plant and equipment and the funding of its pension deficit at a time when the market has been opened up to full competition.

It is, therefore, currently in discussion with its Shareholder around a new funding package that will enable the transformation of the Company to take place and permit appropriate discussion with its pension schemes' Trustee with respect to the funding of its pension deficits. The Directors of Royal Mail Group plc believe that the financing package will be delivered this year. If new financing is not made available, the Directors will have to review the cash requirements of its strategic plan that will result in a delay to the

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planned benefits. On the basis of careful consideration of cash flow projections the Directors have concluded that it is appropriate that the accounts have been prepared on a going concern basis.

Interbusiness trading

The Company operates through business units that make use of the services of other companies within the Group in order to take advantage of Group synergies, having regard to the mutual dependencies that exist. The interbusiness charges recognise these dependencies and are reached through negotiation between the respective businesses.

Turnover

Mails

Account revenue is derived from specific contracts and recognised when the mail delivery is substantially complete. Prepaid revenue mainly relating to stamp and meter income is recognised when the sale is made, adjusted to reflect a value of stamp and meter credits held but not used by the customer.

Parcels

Account revenue is derived from specific contracts and recognised when the delivery of an item is substantially complete.

Intangible assets

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

Finite lives of intangible assets are in the range of 1–6 years. Amortisation of intangible assets with finite lives is taken annually to the profit and loss account.

Tangible fixed assets

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

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

	Average remaining lives	Range of asset lives
Land and buildings:		
Freehold land	Not depreciated	Not depreciated
Freehold buildings	14 years	Up to 50 years
Leasehold land and buildings	9 years	The shorter of the period of the lease, 50 years or the estimated remaining useful life
Plant and machinery	5 years	3 – 15 years
Motor vehicles and trailers	3 years	1 – 12 years
Fixtures and equipment	2 years	2 – 15 years

Impairment reviews of fixed assets are performed where there is an indication of impairment as defined by FRS 11 'Impairment of fixed assets and goodwill'. Further details on tangible fixed assets can be found in note 12 to the accounts.

Royal Mail Group plc

1 Accounting policies (continued)

Leases

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

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

Leases where substantially all the risks and rewards of ownership of the asset are retained by the lessor, are classified as operating leases and rentals are charged to the profit and loss account over the lease term.

Financial assets – investments (fixed assets)

Investments in subsidiaries and associates within the Company's accounts are stated at cost less any accumulated impairment losses.

Stocks

Stocks, which include uniforms, bicycles and stationery are carried at the lower of cost and net realisable value.

Deferred tax

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

Deferred tax is not recognised in the following instances:

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

Deferred tax assets and liabilities are not discounted. Deferred tax is charged or credited directly to reserves if it relates to items that are credited or charged to reserves. Otherwise it is recognised in the profit and loss account. Further details of deferred tax can be found in notes 10 and 14 of the accounts.

Pensions and other post-retirement benefits

Membership of occupational pension schemes is open to most permanent UK employees of the Company. All members of defined benefit schemes are contracted out of the earnings-related part of the State pension scheme. Overseas subsidiaries make separate arrangements for the provision of pensions and other post-retirement benefits.

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

Royal Mail Group plc

1 Accounting policies (continued)

For defined benefit schemes, the amounts charged to operating profit and included as part of people costs are the current service costs and any gains and losses due on settlements and curtailments. Past service costs are charged to operating profit immediately if benefits have vested. If the benefits have not vested immediately, the costs are recognised by equal annual instalments over the period until vesting occurs. The net difference between the interest costs and the expected return on plan assets is recognised as net pensions interest. Actuarial gains and losses are recognised immediately in the statement of total recognised gains and losses (STRGL). Any deferred tax movement associated with the actuarial gains and losses is also recognised in the STRGL.

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

Research and development

Expenditure on research and development is written off in the year in which it is incurred. Further details can be found in note 4 to the accounts.

Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction (or at the contracted rate if the transaction is covered by a forward foreign currency contract). Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date (or the appropriate forward contract rate). All differences are taken to the profit and loss account with the exception of differences on foreign currency borrowings, which are used to finance or provide a hedge against foreign equity investments. These are taken directly to reserves together with the exchange difference on the carrying amount of the related investments. Tax charges and credits attributable to exchange differences on those borrowings are also dealt with in reserves.

Financial instruments

Financial assets within the scope of FRS 26 'Financial Instruments: Measurement' are classified as: financial assets at fair value through the profit and loss account; loans, and receivables; held to maturity investments; or as available for sale financial assets, as appropriate. The Company determines the classification of its financial assets at initial recognition and re-evaluates this designation at each financial year end. When financial assets are recognised initially, they are measured at fair value, being the transaction price plus, in the case of financial assets not at 'fair value through the profit and loss account', any directly attributable transactional costs.

The subsequent measurement of financial assets depends on their classification as follows:

Financial assets at fair value through the profit and loss account (held for trading)

Financial assets are classified as held for trading if they are acquired for sale in the short term. Derivatives are also classified as held for trading unless they are designated as hedging instruments. Assets are carried in the balance sheet at fair value with gains or losses on 'financial assets at fair value through the profit and loss account', recognised in the profit and loss account.

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as 'held to maturity' when the Company has the positive intention and ability to hold to maturity. Held to maturity investments are carried at amortised cost using the effective interest rate method. Gains and losses are recognised in the profit and loss account when the investments are derecognised or impaired, as well as through the amortisation process. Investments intended to be held for an undefined period are not included in this classification. Prior to 28 March 2005, the Company held such investments at historic cost less any provision for impairment, except Government gilt-edged securities, which were stated at market value and will now be categorised as 'held for trading'.

Royal Mail Group plc

1 Accounting policies (continued)

Loans and receivables

Non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, do not qualify as trading assets and have not been designated as either 'fair value through the profit and loss account' or available for sale. Such assets are carried at amortised cost using the effective interest rate method if the time value of money is significant. Gains and losses are recognised in the profit and loss account when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available for sale financial assets

'Available for sale financial assets' are non-derivative financial assets that are designated as such or are not classified in any of the three preceding categories. After initial recognition, available for sale financial assets are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised, or until the investment is deemed to be impaired at which time the cumulative gain or loss previously reported in equity is included in the profit and loss account. The fair value of quoted investments is determined by reference to bid prices at the close of business on the balance sheet date. Where there is no active market, fair value is determined using valuation techniques. These include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; and discounted cash flow analysis and pricing models. Otherwise assets will be carried at cost.

The Company has followed the transitional provisions of FRS 25 'Financial Instruments: Disclosure and Presentation' and FRS 26 'Financial Instruments: Measurement', to adopt these standards from 28 March 2005, the first day of the 2005-06 financial year, and not restate comparative amounts on first applying FRS 25 and FRS 26. Under previous UK GAAP, the Company held financial instruments at historic cost less provision for impairment, except for Government gilt-edged securities, which were stated at market value and are now categorised as 'held for trading'.

Derivative financial instruments

The Company uses derivative instruments such as foreign currency contracts in order to manage the risk profile of any underlying risk exposure of the Company, in line with the Group's treasury management policies. Such derivative financial instruments are initially stated at fair value.

For the purpose of hedge accounting, hedges are classified as cash flow hedges where they hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecasted transaction.

In relation to cash flow hedges to hedge the foreign exchange risk of firm commitments that meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity and the ineffective portion is recognised in the profit and loss account.

When the hedged firm commitment results in the recognition of a non financial asset or non financial liability, then, at the time the asset or liability is recognised, the associated gains or losses that had previously been recognised in equity are included in the initial measurement of the acquisition cost or other carrying amount of the asset or liability. For all other cash flow hedges, the gains or losses that are recognised in equity are transferred to the profit and loss account in the same year in which the hedged firm commitment affects the net profit/loss, for example when the future sale actually occurs.

Royal Mail Group plc

1 Accounting policies (continued)

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the profit and loss account in the period.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity is kept in equity until the forecast transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the profit and loss account for the year.

In accordance with the exemption under FRS 26, comparative information has been prepared under the previous UK GAAP and not FRS 25 and FRS 26. The comparative information in the financial statements is presented as follows:

- forward foreign currency contracts are used to reduce exposure to foreign exchange rates. The Company's policy is that its derivative instruments qualify for hedge accounting when the following criteria are met:
 - the instrument must be related to a foreign currency asset or liability that is probable and whose characteristics have been identified;
 - it must involve the same currency risk as the hedged item; and
 - it must reduce the risk of foreign currency movements on the Company's operations.
- contracted rates are used to record the hedged item. As a result, gains and losses are offset against the foreign exchange gains and losses on the related financial assets and liabilities. Where the instrument is used to hedge a committed or probable future transaction, gains or losses are not recognised until the transaction occurs; and
- over-the-counter derivative products are used to manage both the commodity and foreign exchange risks associated with the fuel procurement policy.

No financial instrument disclosures have been presented as the Company is a wholly-owned subsidiary of a company which has presented such disclosures within its Group accounts.

2 Turnover

Turnover, all from continuing operations, comprises the value of services provided, excluding VAT, from the Company's principal area of activity of providing a nationwide and international distribution service, principally of mails and parcels. The Company operates wholly within the United Kingdom.

Royal Mail Group plc

3 Staff costs

	2006	2005 As restated
	£m	£m
Wages and salaries	4,094	4,056
Social security costs	309	319
Pension costs (see note 25)	508	470
Temporary resource	72	153
Total	4,983	4,998

Staff costs include £141m (£112m wages and salaries, £8m social security costs and £21m pension costs), which are operating exceptional items (2005 £237m, £197m, £22m and £18m respectively).

Temporary resource costs were included in 'other operating charges' in the 2004-05 accounts.

Staff numbers, calculated on a headcount basis and including part-time employees were:

	Period end employees		Average employees	
	2006	2005	2006	2005
Mails and Parcels	181,642	184,299	184,186	183,442
Counter Services	11,327	12,145	11,774	12,510
Total Employees	192,969	196,444	195,960	195,952

Included in the average number of employees are 11,774 (2005 12,510) who are seconded to subsidiary undertakings and whose costs are borne by those companies.

4 Operating profit

	2006	2005
	£m	£m

Operating profit is stated after charging:

Depreciation:	149	135
Depreciation of owned tangible fixed assets	131	114
Depreciation of tangible fixed assets held under finance leases and hire purchase agreements	18	21
Exceptional impairment write-down: tangible fixed assets	5	3
Research and development expenditure	1	1
Operating lease charges:	172	195
Land and buildings	111	111
Vehicles and equipment	61	84
Regulatory body costs:	20	20
Postcomm	9	10
Postwatch	11	10

Auditors' remuneration amounted to £1,178,000 (2005 £1,065,000) for the audit of the statutory accounts and £303,000 (2005 £287,000) for the audit of the regulatory accounts. Remuneration for non-audit services amounted to £868,000 (2005 £614,000). These amounts include the costs incurred in respect of all subsidiaries of Royal Mail Holdings plc, with the exception of the overseas' subsidiaries and Post Office Limited, as these costs were incurred centrally and not recharged.

Royal Mail Group plc

5 Exceptional Items

The operating profit includes a credit in respect of operating exceptional items of £172m (2005 £242m charge). This comprises a credit of £318m (2005 £nil) on the reversal of a bad debt provision relating to an intercompany loan to Royal Mail Investments Limited, offset by Share in Success costs of £81m (2005 £203m), provision for restructuring of £60m (2005 £36m) and impairments of tangible and intangible fixed assets of £5m (2005 £3m). The £60m provision for restructuring charge (2005 £36m charge) above is all in respect of employee-related costs (2005 £34m in respect of employee-related costs and £2m in respect of other operating costs).

The £58m of non-operating exceptional profit (2005 £55m) comprises £53m profit associated with the sale of a number of properties (2005 £56m) and a £5m profit relating to the disposal (2005 £1m loss) of a subsidiary company.

6 Directors emoluments

The emoluments of all Directors of the Company, who were also Directors of Royal Mail Holdings plc, are disclosed in the Royal Mail Holdings plc Group accounts.

During 2004-05, there were four Directors of the Company who were not also Directors of Royal Mail Holdings plc. The total emoluments for these Directors up to the date of their resignation were £287,000 (excluding pension contributions), of which £77,000 was in respect of the highest paid Director. Company contributions to the defined benefit schemes for which all four Directors were members amounted to £41,000. The Company contributions to the defined benefit schemes for the highest paid Director amounted to £18,000 and the transfer value of accrued pension benefits for the highest paid Director amounted to £639,000.

7 Income from investments

	2006 £m	2005 £m
Total income from investments	7	3

Dividends received were from Quadrant £4m (2005 £2m), Romec £2m (£nil), and NDC £1m (£1m).

8. Finance income - net pensions interest

	2006 £m	2005 £m
Total net pensions interest	94	55

9 Other net interest receivable

	2006 £m	2005 £m
Interest receivable on investments	59	60
Interest payable on bank loans and overdrafts	(30)	(29)
Total other net interest receivable	29	31

Royal Mail Group plc

10 Taxation

(a) Tax on profit on ordinary activities

The tax (credit)/charge is made up as follows:

	2006 £m	2005 As restated £m
Corporation tax charge for year	46	52
Tax (over)/under provided in previous years	(10)	10
Total current tax (see table below)	36	62
Total deferred tax	(72)	19
Total tax (credit)/charge	(36)	81

(b) Factors affecting the current tax charge

The tax assessed for the year differs from the standard rate of corporation tax in the UK of 30% (2005 30%). The differences are explained below:

	2006 £m	2005 As restated £m
Profit on ordinary activities before tax	704	246
Profit on ordinary activities multiplied by the standard rate of corporation tax in the UK of 30% (2005 30%)	211	74
Deferred relief for asset depreciation and impairment	21	21
Expenditure disallowable for tax	7	10
Transitional relief for holiday pay accrual	(12)	-
(Accelerated)/Deferred relief for pension contributions	(24)	101
Provisions not deductible until incurred	(13)	(73)
Provision movement non-taxable	(95)	-
Adjustment in respect of prior period	(10)	10
Utilisation of prior year losses	-	(34)
Effect of group relief surrenders from other companies	(48)	(47)
Dividend not taxable	(1)	-
Total current tax (see table above)	36	62

Pensions contributions paid in the year exceeded charges to the profit and loss account.

(c) Tax charged/(credited) directly in reserves

	2006 £m	2005 As restated £m
Current tax	(31)	(38)
Deferred tax	64	(326)
Tax charge/(credit) reported in reserves	33	(364)

Royal Mail Group plc

10 Taxation (continued)

(d) Factors that may affect future tax charges

The Company has access to capital losses carried forward, the tax effect of which is approximately £11m (2005 £10m). Most of these losses reside in Royal Mail Holdings plc but they may be set-off in future years against the capital gains of the Company. The Company has rolled over capital gains, the tax effect of which totals £62m (2005 £70m). It is expected that gains on tangible fixed assets sold in the year will be fully rolled over in due course.

(e) Tax credit on non-operating exceptional items

The tax credit on non-operating exceptional items was:

	2006 £m	2005 £m
Disposal of tangible fixed asset	-	(1)
Total tax credit on non-operating exceptional items	-	(1)

11 Intangible fixed assets

	Cost at 28 March 2005 £m	Additions £m	Amortisation £m	Net book value 26 March 2006 £m
Software	-	27	-	27

The intangible software assets recognised in the Company's balance sheet are written down on a straight-line basis over their remaining economic lives of between 1 and 6 years. During the year the company incurred software costs of £27m.

Royal Mail Group plc

12 Tangible fixed assets

Land and Buildings							
	Freehold £m	Long leasehold £m	Short leasehold £m	Motor Vehicles £m	Plant and machinery £m	Fixtures and equipment £m	Total £m
COST							
At 28 March 2005	1,346	231	404	142	677	115	2,915
Reclassification	(10)	3	7	-	-	-	-
Additions	41	6	17	56	44	7	171
Disposals	(25)	-	(2)	(21)	(1)	(6)	(55)
Transfers to subsidiary	(5)	-	(5)	-	-	-	(10)
At 26 March 2006	1,347	240	421	177	720	116	3,021
DEPRECIATION							
At 28 March 2005	635	131	149	58	377	101	1,451
Reclassification	-	-	-	-	-	-	-
Charge for the year	39	6	25	29	46	4	149
Impairment	4	-	1	-	-	-	5
Disposals	(9)	-	(2)	(20)	(1)	(6)	(38)
At 26 March 2006	669	137	173	67	422	99	1,567
NET BOOK VALUE							
At 26 March 2006	678	103	248	110	298	17	1,454
At 28 March 2005	711	100	255	84	300	14	1,464

Depreciation rates are disclosed within the accounting policies. No depreciation is provided on freehold land, which represents £126m (2005 £139m) of the total cost of freehold properties. The net book value of the Company's tangible fixed assets held under hire purchase contracts and finance leases amount to £54m (2005 £72m).

13 Financial assets – investments

	Investment in subsidiary undertakings £m	Associates/ joint ventures £m	2006 Total £m	2005 As restated Total £m
Cost				
At 28 March 2005:				
As reported	81	26	107	107
Prior period adjustment (see accounting policy note 1)	(65)	-	(65)	(65)
As restated at 26 March 2006	16	26	42	42

Royal Mail Group plc

13 Financial assets - investments (continued)

The prior year adjustment results from the change in accounting policy (note 1) valuing investments in subsidiaries at cost less cumulative impairment losses. Details of principal subsidiary undertakings, joint ventures and associates are given in note 29.

14 Debtors

	2006 £m	2005 As restated £m
Receivable within one year:		
Trade debtors	609	563
Amounts owed by subsidiary undertakings	344	264
Other prepayments and accrued income	108	90
Loan to associate	-	1
Total	1,061	918

	2006 £m	2005 As restated £m
Receivable beyond one year:		
Amounts owed by subsidiary undertakings	567	608
Deferred tax asset	53	-
Other	6	15
Total	626	623

Other long-term debtors mainly represent amounts payable from employees in respect of the home computing initiative launched in November 2003.

	2006 £m
The deferred tax asset comprises:	
Deferred capital allowances	6
Pension timing differences	45
Provisions	2
Total	53

15 Financial assets - derivatives

	2006 £m	2005 £m
Total	3	-

Royal Mail Group plc

16 Financial assets – investments

	2006 £m	2005 £m
Government gilt-edged securities	133	134
Government short-term deposits (National Loans Fund)	549	576
Other deposits	271	346
Total	953	1,056

Within current asset investments, a total of £836m investments relate to the Mails Reserve and are restricted in their use to that permissible by the section 72 order which created the Mails Reserve (note 24). These investments include deposits of £549m, which are subject to a charge as security against the loan facilities from the Department of Trade and Industry (DTI).

17 Creditors – amounts falling due within one year

	2006 £m	2005 As restated £m
Loans (note 21)	–	14
Trade creditors and accruals	928	1,199
Advanced customer payments	213	198
Other taxation and social security	78	77
Annual leave entitlement accrual	36	39
Amounts due to subsidiary undertakings	26	25
Corporation tax	15	24
Lease incentives	1	1
Other creditors	11	10
Total	1,308	1,587

18 Financial liabilities – derivatives

	2006 £m	2005 £m
Total	3	–

19 Retirement benefit obligation

	2006 £m	2005 £m
Total	4,893	3,352

The retirement benefit obligation of £4,893m (2005 £3,352m) comprises the deficit in Plans at the end of the period of £5,156m (2005 £3,678m), offset by a related deferred tax asset of £263m (2005 £326m).

Royal Mail Group plc

20 Other creditors – amounts falling due after more than one year

	2006 £m	2005 As restated £m
Loans (note 21)	500	500
Amounts due to subsidiary undertakings	68	385
Lease incentives	8	6
Other	7	13
Total	583	904

Other long-term creditors represent amounts payable to the leasing company in respect of the home computing initiative, launched in November 2003.

21 Loans

	2006 £m	2005 £m
Amounts falling due in:		
One year or less	-	14
More than 5 years	500	500
Total	500	514

Analysis of loans and facilities

	Loan £m	Further facility £m	Total facility £m	Average interest %	Average maturity date Year
DTI loans to Royal Mail Group plc	500	844	1,344	5.8	2023

The Company has various borrowing facilities available to it. The undrawn committed facilities available at 26 March 2006, in respect of which all conditions precedent had been met at that date, are as follows:

	2006 £m	2005 £m
Expiring in one year or less	200	-
Expiring in more than one year but not more than two years	150	200
Expiring in more than two years	494	644
Total	844	844

The undrawn amounts comprise multiple loan facilities amounting to £844m. £500m of the committed facilities had been utilised at 26 March 2006. The £500m loan is secured by way of a fixed and floating charge on various assets of the Company.

Royal Mail Group plc

22 Provisions for liabilities and charges

	At 28 March 2005 as restated £m	Charged/ (released) in the year £m	Utilised Non- cash £m	Utilised cash £m	At 26 March 2006 £m
Mails and Parcels	161	71	(40)	(83)	109
Deferred tax	19	(19)	-	-	-
Total	180	52	(40)	(83)	109

The cash utilisation of £83m includes £80m of spend relating to exceptional rationalisation and £3m relating to other operating costs. Included within provisions is £51m (2005 £67m) relating to onerous property contracts.

The Mails and Parcels provision includes amounts relating to redundancy and other non-redundancy items (onerous property contracts and decommissioning costs), which relate to restructuring programmes. During the year £60m (2005 £36m) was charged to exceptional items and £11m (2005 £11m) to other operating costs. £39m was transferred to creditors due within one year mainly relating to amounts due to the pension scheme for redundancies with early retirement. £58m of this provision is expected to be utilised in 2006-07 and the remainder over the following two to three years, except for £12m relating to decommissioning costs and £31m relating to onerous property contracts, which are expected to be utilised over a longer period. The timing of cash flows for these provisions are by their nature uncertain and dependent upon the outcome of related events. The best estimates of the amounts are shown in the table above.

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

The deferred tax provision of £19m was credited against the profit and loss tax charge during the year.

23 Called up share capital

	2006 £000	2005 £000
Authorised		
100,000 ordinary shares of £1 each	100	100
Total	100	100
Allotted and fully paid		
50,000 ordinary shares of £1 each	50	50
Total	50	50

Royal Mail Group plc

24 Capital and reserves

	Share premium £m	Retained earnings £m	Mails reserve £m	Revaluation reserve £m	Hedging reserve £m	2006 Total £m	2005 As restated Total £m
At previously reported	3,784	(2,321)	801	65	-	2,329	2,146
Prior period adjustment ⁽¹⁾	-	(4,157)	-	(65)	-	(4,222)	(4,950)
Restated balance at 27 March 2005	3,784	(6,478)	801	-	-	(1,893)	(2,804)
Restatement for the effect of FRS 25 and FRS 26 at 28 March 2005	-	(11)	-	-	8	(3)	-
Restated balance at 28 March 2005	3,784	(6,489)	801	-	8	(1,896)	(2,804)
Profit for the financial year	-	740	-	-	-	740	165
Actuarial (loss)/gain on defined benefit schemes	-	(1,509)	-	-	-	(1,509)	382
Taxation on items taken directly to reserves	-	(33)	-	-	-	(33)	364
Interest added to reserves	-	(35)	35	-	-	-	-
Gain on cash flow hedge deferred into equity	-	-	-	-	3	3	-
Gain transferred from equity to profit and loss during the year	-	-	-	-	(10)	(10)	-
Gain transferred from equity to the initial carrying value of non financial asset	-	-	-	-	(1)	(1)	-
At 26 March 2006	3,784	(7,326)	836	-	-	(2,706)	(1,893)

⁽¹⁾ The prior period adjustment of £4,222m (2005 £4,950m) relates to the adoption of FRS 17 Retirement benefits £4,111m (2005 £4,764m), reversal of revaluation reserve £65m (2005 £141m), see accounting policy note 1, and adjustments made for the recognition of the liability in respect of annual leave entitlement liability £39m (2005 £37m) and lease incentives £7m (2005 £8m).

The Mails Reserve was created in Royal Mail Group plc on 3 February 2003, following directions issued by the Secretary of State for Trade and Industry under section 72 of the Postal Services Act 2000. The amounts allocated to the reserve are to be applied as if they were profits available for distribution and they are to be principally used to provide financial assistance to Post Office Limited and security for loans to the Company.

During the period, none of the Mails Reserve has been utilised for the provision of financial assistance to Post Office Limited (2005 £nil).

The £35m interest relates to income recorded in the profit and loss account, which has been earned on the assets that support the Mails Reserve.

Royal Mail Group plc

25 Pensions

The Company participates in pension schemes as detailed below.

Name	Eligibility	Type
Royal Mail Pension Plan (RMPP)	UK employees	Defined benefit
Royal Mail Senior Executive Pension Plan (RMSEPP)	UK senior executives	Defined benefit
Royal Mail Retirement Savings Plan (RMRSP)	UK employees	Defined contribution

Note: All references to the Group in this note refer to the combined totals of the defined benefit plans as noted above.

Defined contribution

A charge for the defined contribution schemes of £2m (2005 £1m) was recognised in operating profit before exceptional items within the profit and loss account. The Company contributions to these schemes was £1m (2005 £1m).

Defined benefit

Both RMPP and RMSEPP are funded by the payment of contributions to separate trustee administered funds. The latest full actuarial valuations of both schemes were carried out as at 31 March 2003 using the projected unit method. The next full valuations are due to be carried out as at 31 March 2006.

The regular future service contributions for RMPP, expressed as a percentage of pensionable pay, are expected to increase from 12.6% to 20%. For RMSEPP, contributions are at 20.9% and future rates will be discussed with the Trustee during the 2006 actuarial valuation. Payment of £108m (2005 £127m) was made during the year to fund the deficit in the schemes. It is anticipated that further such payments will be made in future as required. A current liability of £38m (2005 £185m) has been recognised for payments to the pension schemes relating to redundancy. During the year, payments of £186m (2005 £4m) relating to redundancy were made.

The Company has legal liability for the pension scheme but has an agreement to second employees to its subsidiary, Post Office Limited, under which Post Office Limited bears the cost of employment of these employees and is responsible for the funding of the pension deficit for these employees. Consequently, the deficit has been allocated based on the share of employee numbers over the past 12 years.

The Company recognises the remaining share of the RMPP and RMSEPP total deficit. This approximated to 93% of the total deficit. The Group's current service cost and future service contributions are applied to the Company's payroll. Curtailments are charged and paid by the Company. The finance income, deficiency payments and actuarial gains or losses are allocated on the same basis as the original deficit giving the Company approximately 93% of the Group totals.

Royal Mail Group plc

The following disclosures relate to the RMPP and RMSEPP defined benefit scheme plans for the Company:

a) Major assumptions

	At 26 March 2006 % pa	At 27 March 2005 % pa
Rate of increase in salaries	3.8	4.2
Rate of increase in pensions and deferred pensions	2.8	2.7
Discount rate	4.9	5.5
Inflation assumption	2.8	2.7
Expected average rate of return on assets	7.1	7.4

Mortality

Over recent months the Company and the RMPP Trustee have discussed potential changes to the mortality assumptions to be adopted for the 2006 actuarial valuation. These discussions have been based on an analysis carried out by the Trustee of the experience of the plan's pensioner population up to 31 March 2005. The Trustee has proposed a particular mortality basis - based on the 1992 series mortality tables allowing for 'medium cohort' projections of future improvements - and this has been applied to RMPP at the current year end. For consistency, the same improvement has been assumed for RMSEPP. This differs from the prior year, when assumptions consistent with the latest full actuarial valuations were used. The table below illustrates how these assumptions have changed.

Average expected life expectancy from age 60:	2006	2005
For a current 60 year old male RMPP member	26 years	22 years
For a current 60 year old female RMPP member	29 years	25 years
For a current 40 year old male RMPP member	28 years	24 years
For a current 40 year old female RMPP member	30 years	27 years

b) Plans' assets and expected rates of return

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

At 26 March 2006

	Market value £m	Long-term rate of return expected % pa
Equities	17,227	7.7
Bonds	2,682	4.2
Property	1,835	5.9
Other assets	140	3.8
Fair value of plans' assets	21,884	
Present value of plans' liabilities	(27,435)	
Deficit in schemes	(5,551)	

Royal Mail Group plc

25 Pensions (continued)

At 27 March 2005

	Market value £m	Long-term rate of return expected % pa
Equities	13,376	8.0
Bonds	2,006	4.8
Property	1,639	6.4
Other assets	336	3.7
Fair value of plans' assets	17,357	
Present value of plans' liabilities	(21,315)	
Deficit in schemes	(3,958)	

c) Components of defined benefit costs in Royal Mail Group plc

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

	2006 £m	2005 £m
Analysis of amounts charged to operating profit before exceptional items:		
Current service cost	485	445
Loss due on settlements	-	6
Total charge to operating profit before exceptional items	485	451
Analysis of amounts charged to operating exceptional items:		
Loss due to curtailments	21	18
Total charge to operating profit	506	469
Analysis of amounts charged/(credited) to net pensions interest:		
Interest on plans' liabilities for the Group	1,162	1,068
Expected return on plans' assets for the Group	(1,263)	(1,127)
Total net pensions interest for the Group	(101)	(59)
Total net pensions interest for the Company (at approximately 93%)	(94)	(55)
Total charge to profit and loss account before deduction for tax	412	414
Analysis of amounts recognised in the statement of total recognised gains and losses (STRGL)		
Actual return on plans' assets for the Group	4,721	2,170
Less: expected return on plans' assets for the Group	(1,263)	(1,127)
	3,458	1,043
Other actuarial losses for the Group	(5,080)	(632)
Actuarial (losses)/gains recognised in STRGL for the Group	(1,622)	411
Actuarial (losses)/gains recognised in STRGL for the Company (at approximately 93%)	(1,509)	382

Royal Mail Group plc

25. Pensions (continued)

d) Company's share of movement in (deficit)/surplus in the Plans during the period

The deficit in the schemes in the Company is approximately 93% of the total deficit in the Group.

	2006 £m	2005 £m
Company share of deficit in Plans at beginning of period	(3,678)	(4,086)
Company contributions paid	605	296
Movement in company contributions accrued	(146)	316
Current service cost	(485)	(445)
Adjustments arising on settlements	-	(14)
Costs recharged	2	3
Curtailment costs*	(39)	(185)
Net pensions interest	94	55
Actuarial (loss)/gain (recognised in STRGL)	(1,509)	382
Company share of deficit in Plans at end of period before impact of deferred tax	(5,156)	(3,678)
Related deferred tax asset	263	326
Company share of deficit in Plans at end of period net of deferred tax	(4,893)	(3,352)

*The curtailment costs in the profit and loss account are recognised on a consistent basis with the associated compensation costs. Estimates of both are included, for example, in any redundancy provisions raised. The curtailment costs above represent the costs associated with those people paid compensation in respect of redundancy in 2005-06. This may occur in an accounting period subsequent to the recognition of costs in the profit and loss account.

e) History of experience gains and losses

	2006 £m	2005 £m	2004 £m
Fair value of assets for the Group	21,884	17,357	15,200
Present value of liabilities for the Group	(27,435)	(21,315)	(19,594)
Deficit in schemes in the Group	(5,551)	(3,958)	(4,394)
Deficit in schemes in the Company (at approximately 93%)	(5,156)	(3,678)	(4,086)

	2006 £m	2005 £m
Actuarial gains arising on assets for the Group	3,458	1,043
Experience losses on Plan liabilities	(162)	(301)
Loss on change in assumptions (financial and demographic)	(4,918)	(331)
Total actuarial gains and losses for the Group	(1,622)	411
Total actuarial gains and losses (recognised in STRGL) in the Company (at approximately 93%)	(1,509)	382

Royal Mail Group plc

25. Pensions (continued)

	2006 %	2005 %
For the Group:		
Gain/loss between actual and expected return on Plan assets as % of assets at end of period	15.8	6.0
Experience gain/loss as % of liabilities at end of period	0.6	1.4
Total actuarial gains and losses as % of liabilities at end of period	5.9	1.9

26 Commitments

Capital commitments contracted for but not provided in the accounts amount to £49m (2005 £84m). The Company is committed to the following payments on operating leases during the next twelve months:

	Land and buildings		Vehicles and equipment		IT equipment	
	2006 £m	2005 £m	2006 £m	2005 As restated £m	2006 £m	2005 £m
Within one year	4	7	6	10	-	-
Between one and five years	15	14	36	37	-	-
Beyond five years	66	69	3	2	46	46
Total	85	90	45	49	46	46

27 Contingent liabilities and guarantees

The Company has guaranteed the performance of a third party in relation to lease payments payable over the 15-year term of a lease entered into on the 21 December 2000, and has given certain tax indemnities to the US lessors. In the opinion of the Directors, no loss will result to the Company as a result of these guarantees.

As required by the Notes Sorting Facility rules, notes in transit to cash handling centres and those processed overnight, for which the Company has received credit, are secured by gilts deposited with the Bank of England. On default, the estimated maximum liability would be £104m.

The Company has given a guarantee to the Secretary of State for Work and Pensions, the Department for Social Development (Northern Ireland) and the Commissioners of Inland Revenue, to underwrite the performance of Post Office Limited of its obligations under the Universal Banking Contract (Post Office Card Account).

The Company has also given a guarantee to Electronic Data Systems Limited to underwrite Post Office Limited's performance of its obligations under the Universal Banking Contract (Post Office Card Account).

28 Related party transactions

The Company has taken advantage of one of the exemptions conferred by FRS 8 'Related party transactions', whereby certain details regarding transactions with Group companies do not have to be disclosed where Group accounts are publicly available.

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29 Principal subsidiary undertakings, joint ventures and associates

	Country of incorporation	Percentage holding %	Principal activities
Subsidiary undertakings			
Post Office Limited	UK	100	Counter Services
Royal Mail Investments Limited ¹	UK	100	Holding company
General Logistics Systems International Holdings B.V. ¹	Netherlands	100	Holding company
Romec Limited	UK	51	Facilities management
NDC 2000 Limited	UK	51	Design consultancy
Associates			
Camelot Group plc	UK	20	Lottery operations
Quadrant Catering Limited ²	UK	51	Catering services
G3 Worldwide Mail N.V. (trade name 'Spring')	Netherlands	25	Mail services
Midasgrange Limited	UK	50	Financial services
Joint ventures			
First Rate Exchange Services Holdings Limited (Previously known as First Rate Travel Services Limited until its name change on 23 February 2006)	UK	50	Bureau de Change

¹ These are non-trading holding companies, which have investments in other operational companies that are based in Europe.

² The Company holds 51% of the share capital of Quadrant Catering Limited. However, the voting rights attached to the various classes of shares give the other investor operational control. Quadrant is therefore treated as an associate in the Company accounts.

All these principal subsidiary, joint venture and associate companies have a 31 March year end date with the exception of Quadrant Catering Limited which has a 30 September year end date and G3 Worldwide Mail N.V. and Romec Limited which both have a 31 December year end date.

A full list of subsidiary undertakings, joint ventures and associates is available from the Company's Registered Office. All shareholdings are equity shares.

30 Immediate and ultimate parent undertaking

At 26 March 2006, the Directors regarded Royal Mail Holdings plc as the immediate and ultimate parent company. The results of the Company form part of the Royal Mail Holdings plc Group accounts, which are available from the Company's website (www.royalmailgroup.com).

31 Events after the balance sheet date

The Company has made two payments of £37.5m to Post Office Limited as part of the Social Network Payment for 2006-07.