



Introduction

1. This report sets out the Compliance Officer's activities for the year 2004/05 pursuant to the reporting requirements set out in Licence condition 13.5. The report also sets out in outline the overall business procedures, which were in place in 2004/05 to mitigate against the risk of failure to comply with requirements set out in part 4 of the Licence and licence conditions 16 & 17 and how these interact with the activities of the Compliance Officer.
2. It is Royal Mail policy to comply with Regulatory and Legislative requirements and as such over the last 12 months Royal Mail has continued to take steps to improve the processes and procedures that facilitate compliance with the Royal Mail Group Licence in general and Part 4 of the licence in particular.

General points

3. Throughout 2004/05 the focus on compliance within Royal Mail Group has increased culminating in the appointment of a new Compliance Director in February 2005.
4. In Financial Year 2003/04 and beginning of 2004/05 the Royal Mail Company Secretary supported by a Deputy Compliance Officer discharged the function of the Compliance Officer under part 4 of the Licence.
5. The procedures in place for achievement of requirements set out in the licence conditions were based on existing processes and procedures such as Internal Audit and Risk Management monitoring key corporate risks as well as validating procedures in place to mitigate such risks.

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6. The risk identification was based on Business Unit self-assessment and reporting through the risk management process through to the Audit and Risk Committee.
7. Throughout 2004/05 the Compliance Officer relied on existing procedures and structures with regards to compliance with part 4 of the Licence, and a review was initiated as to the best way in which to manage the risk of non-compliance with licence conditions.
8. This review culminated in a recommendation put to the Royal Mail Holdings Board by the Chief Executive recommending a new proactive compliance unit is set up. This recommendation was adopted and a recruitment process commenced to externally appoint a Compliance Director with significant regulatory and compliance experience at senior levels of comparative organisations.
9. In February 2005 Luke March was appointed as Royal Mail Group Compliance Director and has since commenced work on a revised compliance policy for Royal Mail Group plc.
10. The sections below set out, in outline, the procedures in place throughout 2004/05 to ensure the requirements of each condition making up Part 4 of the Licence as well as conditions 16 and 17 were met.

Condition 9 Access to the Licensee's postal facilities and Condition 10 Prohibition of obtaining unfair commercial Advantage.

11. Negotiation with third parties with regards to condition 9 Access is handled centrally. To ensure boundaries are in place between the negotiation of access agreement and other Trading Businesses within Royal Mail Holdings plc all such

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negotiation are led by the Regulatory Affairs and Wholesale team within Royal Mail Group.

12. When an Access agreement has been finalised this becomes a “standard” Downstream Access (DSA) contract that can be offered to any other operator or customer wishing to gain access to the Royal Mail Delivery network.
13. To minimise the risk of undue discrimination between persons having access each new agreement is negotiated centrally with a lead from the Regulatory Affairs and Wholesale team.

Condition 11 – Promotion of effective competition

14. The procedures for ensuring compliance with condition 11 of the Licence have been strengthened throughout 2004/05.
15. In April 2004 Royal Mail submitted to Postcomm a revised process for the approval of Sales Promotions in Royal Mail, setting out the need for each promotion to go through a four stage approval process with senior level sign off for the final design of the promotion.
16. This was reconfirmed when Royal Mail issued a set of assurances on 18 January 2005, jointly signed by the Chief Executive and the Compliance Officer. In these assurances Royal Mail also committed to training all Sales and Marketing Staff on the requirements of condition 11 of the licence, Chapter II of the Competition Act 1998 and Article 82 of the EC Treaty. This training was completed by the end of April 2005 (except for some individual staff on long term sickness and maternity leave). In excess of 1000 staff have been trained, with a follow up e-

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learning package for new entrants and masterclass training for senior personnel currently under development.

17. In the Approval Procedure set out in the Assurances the formal requirement for Regulatory and Competition Law assessments was established for all such activities with a requirement to refer to the Compliance Officer any proposal that may contain compliance risks. In 2004/05 two such assessments were referred to and reviewed by the Compliance Director.

Condition 11 and 12 Notification requirements

18. Condition 11.6 requires Royal Mail to furnish Postcomm with copies of any notifications made under section 13 or 14 of the Competition Act 1998, including any request for an individual exemption, any notification for guidance under section 21 of the Competition Act or any notification for a decision under section 22 of the Competition Act 1998, and any application to the European Commission for any form of clearance in relation to Articles 81 and 82 of the Treaty of Rome.
19. Condition 12 requires Royal Mail to give Postcomm copies of notices given under section 75a of the Fair Trading Act 1973, and any notification for the purpose of Council Regulation EEC 4064/89.
20. No such notifications were made in 2004/05. The Royal Mail teams dealing with such matters that may involve submissions to the competition authorities are fully aware of the requirement of these licence conditions and they are required to provide copies of any relevant submissions to the Compliance Officer who will forward them to Postcomm.

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Condition 13 – Appointment of Compliance Officer

21. As part of the Royal Mail focus on compliance throughout 2004/05 an appointment process was commenced in December 2004 and a new Royal Mail Group Compliance Director was appointed in February 2005 to head up a new Compliance Unit. The Compliance Director has direct access to the Chief Executive. The Compliance Unit is empowered to meet its remit by having the ability to raise matters directly with the Board, the Audit Committee and business unit management teams.
22. Upon commencement of his employment the Compliance Director initiated a search within Royal Mail to fill a further 3 roles which he viewed as necessary to staff his unit.
23. The initial task of the new Compliance Unit was to start work on developing an overall compliance policy for the mails business.
24. The compliance policy will be discharged through:
 - a. Setting up a framework of compliance champions across Royal Mail who will be empowered to drive compliance activities throughout each part of the business and ensure the requirements of the overall framework is met.
 - b. The development of regular and comprehensive monitoring and audit programme to ensure the continuing effective deployment of the Policy.

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- c. Deployment of a training, Knowledge and Awareness programme to include face to face training and communications through all key internal communications vehicles.
 - d. The establishment of a comprehensive compliance programme which incorporates training, communication and a programme of audit and monitoring, taking into account the requirements set out in the Assurances and the Royal Mail Group plc Licence.
25. Throughout 2004/05 the procedure for dealing with Condition 16 information requests was led via Regulatory Affairs. Following the reviews referred to above and the appointment of a Compliance Director in February 2005 this approach has been revised and, although the management of the information requests is still carried out via Regulatory Affairs, the Compliance Unit has taken on a more proactive role in ensuring that any requirement made on Royal Mail Group Plc with regards to conditions 16 and 17 are effectively complied with as set out in condition 13.4.
26. Royal Mail have noted Postcomm's criticism in its decision with regards to the investigation into Royal Mail sales promotions resulting in the Assurances signed by Royal Mail on 18 January 2005. As a consequence the internal procedures have been revised to ensure that any investigation under Part 4 of the Licence are to be referred to the Compliance Unit under condition 13.

Conditions 16 & 17 Provision of Information to Postcomm and the Council

27. Under Condition 16 Postcomm have the power to request from Royal Mail such information as Postcomm may require or may be necessary for the purpose of

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performing the functions assigned to Postcomm under the Postal Services Act 2000.

28. Under Condition 17 Postwatch have the power to request from Royal Mail information that may reasonably be required to fulfil Postwatch's functions assigned to it under the Postal Services Act 2000.
29. It is Royal Mail Group Policy to fully cooperate with each such information request and when collating information to respond the Regulatory Affairs team have access to all necessary personnel and resource to ensure comprehensive, accurate and timely response to such information requests.
30. The procedure in place for 2004/05 ensured that each such information request was managed centrally via the Regulatory Affairs and Wholesale Team, with the responsibility for the response being within the remit of the Director Regulatory Affairs and Wholesale. The procedures require that for all such requests the Regulatory affairs lead facilitates the provision and collection of information in accordance with the requirements set out in the information request.

Risk Management

In addition to the specific licence condition controls outlined above Royal Mail operate a comprehensive risk management approach. This framework also contributes towards the achievement of the requirements of Part 4 of the Royal Mail Group Licence

31. A summary of the key elements of the Royal Mail Risk Management and Control programme is set out below.

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- a. It is line management's responsibility to ensure that business activities are conducted in an appropriately controlled manner and that business risks are identified and mitigated in a timely manner.
- b. Business units are responsible for the training and awareness (with input from specialists) with regards to competition law and regulatory requirements, including use of CD Rom, E-learning and Face to Face training sessions, as well as the maintenance of training records.
- c. The risk management structure provides a structure of independent oversight of business unit risk management actions.
- d. At the corporate level the Corporate Risk Management Committee oversees Royal Mail's overall risk environment. This committee is a sub committee of the Audit and Risk Committee, which consist of Royal Mail Group Holdings Board Non Executive Directors.

Group Audit Function

32. In addition to the risk programme Royal Mail has an established, properly resourced and independent Internal Audit process. Responsibility for Internal Audit activity within the Company lies with the Internal Audit and Risk Management Department (IA & RM). The department has a remit to conduct Internal Audit activity throughout the business and reports its findings to the Audit & Risk Committee and the Board of Directors. The Director of the Department is accountable to the Chair of the Audit & Risk Committee and reports to the Chief Executive of the Company.

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33. The Internal Audit function within Royal Mail Group looks at how the Company is managing its risks. It provides the Audit & Risk Committee, the Board of Directors and other key stakeholders (including the Compliance Officer) with information on risks in the business and provides assurance on the control environment in place to mitigate those risks. Internal Audit also works with senior management (including the Compliance Officer) within the Company to develop recommendations for improvements to the control environment.
34. IA&RM work to an annual audit plan that is approved by the Audit & Risk Committee. The plan covers all major business units and processes within the Company and focuses on areas of significant risk. The content of the plan is developed through a formal process that reviews corporate risk information from various sources such as the risk management structure, Royal Mail Compliance Officer, Board of Directors and Senior Management.
35. Inherently, as a regulated business, non-compliance with regulatory and statutory obligations is classed as a significant risk and receives appropriate coverage in the audit plan.
36. The Audit & Risk Committee on an ongoing basis reviews the adequacy and effectiveness of the IA&RM department. The department itself is committed to a process of continual improvement and reviews its own performance and capability against professional and industry best practice. The management team within IA&RM are all professionally qualified with extensive Internal Audit experience.

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Next steps

37. As set out above 2004/05 has been a year of transition with regards to compliance culminating with the appointment of a Compliance Director. The initial focus of the new Compliance Unit (end 04/05 and beginning of 05/06) has been the development of an overall compliance plan to include
- a. Knowledge and awareness requirements including both training and communication.
 - b. Monitoring programme incorporating the use of the existing Internal Audit and Risk Management structures set out above.
 - c. Promote a culture of compliance with the rules of Fair Trading including appropriate recognition and reward structures.
 - d. Compliance management throughout the organisation (through the line) and reporting requirements both internally and externally.
38. The Compliance Policy re-iterates that the responsibility for compliance sits within the business line management and that the Compliance Unit is an advisory function specifying the appropriate levels of compliance to be observed in Royal Mail.
39. For subsequent years the compliance annual plan will be an integral part of the overall business planning process to ensure compliance requirements are acknowledged in the core planning activity.

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Summary

The report period 2004 / 05 financial year has been a period of transition within Royal Mail's ongoing focus on compliance. A risk management programme as well as internal business procedures ensured that throughout 2004/05 a structure was in place for risk management including the risk of non-compliance with licence conditions. Royal Mail is aware and acknowledges that during the year Postcomm was concerned with some of the historic activity undertaken by Royal Mail. Royal Mail hopes that Postcomm acknowledges the hard work and commitment within Royal Mail to resolve these concerns and that the recent change in structure with the appointment of a Compliance Director with a dedicated Compliance Unit is a proactive step to ensure compliance issues receive greater attention in the future. Royal Mail believes that through the assurances signed on 18 January 2005 and following the review of internal processes as well as the planned activity for 2005/06, it is in a better position to avoid such concerns in the future.

Luke March

Compliance Director

June 2005