Independent Auditor's Report to the members of Royal Mail plc

Opinions and conclusions arising from our audit

1 Our opinion on the financial statements is unmodified

We have audited the financial statements of Royal Mail plc for the 52 weeks ended 27 March 2016 set out on pages 89-150. In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 27 March 2016 and of the Group's profit for the 52 weeks then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union;
- the parent Company financial statements have been properly prepared in accordance with UK Accounting Standards, including FRS 101 Reduced Disclosure Framework; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006; and, as regards the Group financial statements, Article 4 of the IAS Regulation.

2 Our assessment of risks of material misstatement

In arriving at our audit opinion above on the financial statements the risks of material misstatement that had the greatest effect on our audit in decreasing order of significance were as follows:

The determination of deferred revenue associated with advance customer payments arising from stamps and meter credits sold £252 million (2014-15: £259 million)

Refer to page 53 (Audit and Risk Committee report), page 138 (accounting policy) and page 118 (financial disclosures).

Risk

Advance payments are made by households, retailers and businesses who purchase stamps and meter credits in advance of actual usage. The Group estimates the amounts that have been sold but not used at year end and defers revenue to reflect that the service will need to be provided by the Group during future accounting periods for pre-purchased stamps and meter credits.

As no unique identification of the stamps and meter credits unused is possible, the calculation and methodology of the advance customer payments balance is inherently subjective by nature and is based on inputs including third party surveys, Group sales data and internal survey data on meter usage. The methodology adjusts for stamp holdings which are considered to be abnormal.

Our response

Our procedures included:

- Assessing the methodology and assumptions used to determine the number of stamps and meter credits held at the balance sheet date and its consistency of application year on year. We used our own statistical specialists and held discussions with the independent third party specialist to assist us in evaluating the methodologies used by the Group.
- Evaluating the methodology and results of the external surveys (including consideration of survey size, household adjustment and caps in place to address the impact of abnormal holdings) using our own specialists to assist us in this evaluation.
- Assessing the competence, independence and integrity of the Group's third party survey specialist which provides the survey data.
- Independently testing the revenue data in the calculation.

Independent Auditor's Report to the members of Royal Mail plc (continued)

The carrying valuation of pension scheme surplus (£3,430m asset) (2014-15: £3,367m asset)

Refer to page 54 (Audit and Risk Committee report), page 145 (accounting policy) and page 105 (financial disclosures).

Risk
Significant estimates are made in valuing the Group's post-retirement defined benefit plan's obligations, including in particular the discount rate, the inflation assumptions and the mortality assumptions used to calculate the retirement benefit obligation. Small changes in the assumptions used in the valuation could have a significant effect on the financial position of the Group.

Our response
Our procedures included:

- Challenging the key assumptions applied being the discount rate, inflation rate, mortality and salary growth with the support of our own actuarial specialists. This included a comparison of these key assumptions against externally derived data.
- Assessing the competence, independence and integrity of the Group's actuarial expert.
- Considering the adequacy of the Group's disclosures in respect of the sensitivity of the surplus to these assumptions.

The recognition, measurement and disclosure of the Group's provisions and contingent liabilities associated with the potential industrial diseases and the Ofcom investigation under its competition authority powers

Refer to page 53 and 54 (Audit and Risk Committee report), page 139 (accounting policy) and page 131 and 133 (financial disclosures).

Risk
A number of significant judgments are made by the Group in the accounting for the industrial diseases provision and in assessing whether any contingent liability or provision arises from the ongoing Ofcom regulatory investigation. The assessment of the likelihood and quantum of any liability in respect of legal and regulatory matters can be judgmental due to the uncertainty inherent in their nature.

Response
Our procedures included:

- Challenging the estimates and ranges underlying the Group's independent adviser's reports on the industrial disease provision by assessing the methodology used to calculate the provision and independently assessing the inputs into the report including the discount rate and the historical incidence of claims. We used our own valuation specialists to assist us in evaluating the assumptions and methodologies used by the Group.
- Assessing the competence, independence and integrity of the Group's third party independent adviser.
- Examining the latest correspondence and other evidence used by the Group in assessing whether a contingent liability or provision arises in relation to the ongoing Ofcom investigation.
- Inspecting correspondence and holding discussions with the Group's legal advisers on all significant legal cases.
- Considering the adequacy of the Group's disclosures in respect of these claims

3 Our application of materiality and an overview of the scope of our audit
The materiality for the Group financial statements as a whole was set at £18 million. This was determined with reference to a benchmark of five per cent of Group profit before tax adjusted to add back the IFRS 2 charge for employee free shares issues and to deduct the profit on disposal of DPD assets. We consider adjusted profit to be one of the principal considerations for members of the company in assessing the financial performance of the Group. The specific items not included in the benchmark were all subject to audit procedures.

We agreed with the Audit and Risk Committee to report to it all corrected and uncorrected misstatements we identified through our audit with a value in excess of £0.9 million, in addition to other audit misstatements below that threshold that we consider warranted reporting on qualitative grounds.

Audits for Group reporting purposes were performed at the key reporting components being, UKPIL (the core UK and international parcels and letter delivery business) and GLS (the Group's European parcels business). The Group engagement team performed the audit of UKPIL and instructed component auditors to perform the audit of GLS. These Group procedures covered 99.9 per cent of total Group revenue; 87 per cent of Group profit before taxation; and 99.5 per cent of total Group assets. For the remaining components, we performed analysis at an aggregated Group level to re-examine our assessment that there were no significant risks of material misstatement within these.

The audits undertaken for Group reporting purposes at the key reporting components of the Group were all performed to materiality levels set by, or agreed with, the Group audit team.

The Group team instructed component auditors as to the significant areas to be covered, including the relevant risks detailed above and the information to be reported back. The Group team visited the GLS component during the planning, execution and finalisation phases of the GLS audit.

Independent Auditor's Report to the members of Royal Mail plc (continued)

The Group team also held regular telephone conference meetings with this component team. At these visits and meetings, the findings reported to the Group team were discussed in more detail, and any further work required by the Group team was then performed by the component auditor.

4 Our opinion on other matters prescribed by the Companies Act 2006 is unmodified

In our opinion:

- the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Strategic report and the Directors' report for the financial reporting year for which the financial statements are prepared is consistent with the financial statements.

5 We have nothing to report on the disclosures of principal risks

Based on the knowledge we acquired during our audit, we have nothing material to add or draw attention to in relation to:

- the Directors' statement of viability on page 35, concerning the principal risks, their management, and, based on that, the Directors' assessment and expectations of the Group's continuing in operation over the three years to 2019; or
- the disclosures in Note 1 of the financial statements concerning the use of the going concern basis of accounting.

6 We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the Annual Report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our audit and the Directors' statement that they consider that the Annual Report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy; or
- the Audit and Risk Committee report does not appropriately address matters communicated by us to the Audit and Risk Committee.

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' remuneration report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the Directors' statements, set out on page 84, in relation to going concern and longer-term viability; and
- the part of the Corporate Governance Statement on page 42 relating to the Company's compliance with the eleven provisions of the 2014 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

Scope and responsibilities

As explained more fully in the Directors' responsibilities statement set out on page 84, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate. This report is made solely to the company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at www.kpmg.com/uk/auditscopeukco2014a, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

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18 May 2016