



Commission for
Communications Regulation

Submissions to Consultation

Regulation of Universal Postal Services – Accounting Separation & Costing Methodology

Accounting Direction to An Post

Submissions received from respondents

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An Post Response to

Regulation of Universal Postal Services – Accounting Separation & Costing Methodology New Accounting Direction to An Post (06/55)

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1. Introduction

An Post welcomes the opportunity to respond to ComReg's consultation paper - Regulation of Universal Postal Services Accounting Separation & Costing Methodology - New Accounting Direction to An Post (document 06/55).

An Post strongly values the production of high quality financial statements and is proud of its track record in the production of both annual financial statements and regulatory accounts.

The An Post response consists of two main sections. Section 2 provides the An Post general comments on the key issues surrounding the consultation paper. Section 3 provides answers to the specific questions raised in the consultation paper. A letter from KPMG, An Post's auditors, setting out their comments on the LECG Report is attached as an appendix to the An Post response.

2. General Comments

An Post agrees with the objective that ComReg should have assurance through the form of an audit opinion that the An Post regulatory accounts fairly present the results attributable to the USO. As in the past, An Post remains committed to on-going improvement in the collection of statistics underpinning the accounts and is receptive to providing a more detailed narrative explanation in the submission of the regulatory accounts to ComReg.

In these regards, the general thrust of the proposed revised Accounting Direction is largely acceptable to An Post. An Post has made every effort to engage constructively with ComReg, LECG and with the current consultation process. An Post would make the following observations with regard to the process.

- In many areas, ComReg's proposals remain largely unclear in the absence of defined structures and templates. An Post continues to emphasise the absolute importance of discussion and agreement between An Post and ComReg in these areas of detail. This is imperative for the successful implementation of the new Accounting Direction. An Post would be concerned should ComReg finalise its proposals before such discussion takes place.
- In any regulatory change, as per Ministerial Direction, there is a requirement to assess the impact of the changes. Wherever the proposed new Accounting Direction creates additional workload for An Post, it is important the change is validated by reference to consideration of the benefits arising from the change relative to the costs imposed. In short, accounting and reporting requirements should not be unnecessarily onerous. In discussions with ComReg, An Post will seek to ensure that this principle is observed.
- The process has been carried out within an expedited timeframe. An Post would have sought more consultation with ComReg in advance of the LECG project. This issue was itself a delaying factor. LECG has commented that it did not have sufficient time to interact with An Post.
- An Post was provided with a copy of the LECG report in advance of its publication. An Post outlined by submission (28 September 2006) a number of areas in the report where corrections were necessary. Not all of these corrections were addressed by LECG in finalising the report for publication.

An Post views the key components of the consultation paper as falling within the following core areas:

1.1 Reporting and Transparency

An Post finds the outlined additional reporting requirements of the proposed revised Accounting Direction generally acceptable.

The precise format of the regulatory accounting templates however is not included in the consultation paper. An Post views this as critical to the production of future regulatory accounts and considers it imperative that working parties are established with ComReg to determine the exact structure of the templates.

1.2 Accounting Manual

The fundamental objective of the Accounting Manual is to document the policies and procedures used in the production of regulatory accounts

An Post finds the majority of the additional information requirements to be included in the Accounting Manual as generally acceptable and appropriate.

An Post will provide an Accounting Manual on an annual basis at the start of the relevant period. In practice, changes to the nature of the business may well take place during the year. For example if new operational pay or non pay activities are established during the current regulatory period, these will not be reflected in any Accounting Manual submitted at the start of the relevant period. Details of such changes to the manual will be made available to ComReg.

1.3 Mail Volume and Revenue Identification

The proposed revised Accounting Direction requests detailed information regarding the volumes of individual services derived from both revenue based methodology and operational based methodology.

An Post can provide data along these lines. However, there needs to be recognition of the structural challenge which faces all postal companies in the reconciliation of volume figures derived from different sources. This is an issue which must be addressed over a period of time, and An Post believes that it will be necessary to engage with ComReg on the dimensions of this issue and the initiatives required to address it. In particular, it would be unworkable to have a situation in which there were alternative versions of the regulatory accounts based on different methods of calculating volumes. In the view of An Post, the current revenue-derived basis for calculating volumes must remain the basis for financial reporting and the preparation of the regulatory accounts into the future, with on-going improvements to the collection of information (including operational information) on which this method relies. Ultimately, the project to understand and minimise the difference between results from different volume measurement/estimation techniques will lead to increased accuracy in all methods and convergence between the results. The experience of other postal operators indicates that this process cannot be accomplished quickly and that while the extent of the difference can be reduced, it will never be entirely eliminated. In the meantime, it is necessary to have clarity and certainty about the regulatory accounts.

1.4 Cost Allocation

The underlying principles concerning cost allocation to individual services remains largely unchanged from the 2001 Accounting Direction.

An Post currently classifies both operational pay and non pay costs across the various parts of the pipeline. The proposed revised Accounting Direction proposes to increase the reporting requirements in this area to distinguishing between directly allocated costs, common costs which have been allocated on the basis of the analysis of the origin of the cost themselves and common costs which have been allocated on the basis of a general allocator. An Post can fulfil this requirement.

1.5 Audit

An Post views an audit of the regulatory accounts as a valuable exercise as it would provide assurance to readers that the An Post regulatory accounts fairly present the results attributable to services within the USO.

An Post agrees that it would be appropriate to consult with ComReg prior to the appointment of the auditor of the regulatory accounts.

An Post believes that the audit engagement should be between the company and the auditor. The auditing profession has extensive literature and standards in respect of audit opinions and An Post considers the task of designing the audit opinion should be left to the auditing profession.

1.6 Timelines

This timetable remains unchanged from the 2001 Accounting Direction.

The level of detail and the auditing of the regulatory accounts will add to the amount of work involved with regulatory reporting. Until there is clarity about the practicalities involved it would be unwise for An Post to commit to an exact deadline.

An Post however is determined to work constructively with the Regulator, the auditor and others to establish a timetable that is reasonable, practical and means that the financial information is relevant and timely. The details of this should be worked out by the parties involved.

3. An Post responses to the specific questions posed

Q.1. Do you consider that the current Accounting Direction should be revised at this time?

An Post recognises the importance of an agreed approach to regulatory reporting requirements.

An Post fully understands the need to ensure that the rules and regulations utilised in the production of regulatory accounts take into consideration market developments and the evolving requirements of ComReg.

An Post looks forward to the opportunity of meeting with ComReg to discuss and agree the rules and procedures which shall be utilised in the production of future regulatory accounts.

Q.2. Do you consider that the changes recommended by LECG are warranted and appropriate?

An Post comments regarding the LECG recommendations are set out below:

2.1 Fundamental Requirements

The proposed revised Accounting Direction states that *“The financial and accounting information shall be maintained in sufficient detail to facilitate a detailed analysis on a geographic and/or category of customer and/payment method basis, for the purpose of calculating the cost of complying with obligations in respect of Universal Service and cross subsidisation and ensuring that tariffs are geared to cost, affordable, transparent, non-discriminatory and where appropriate, take account of the avoided costs, as compared to services utilising all features of the public postal network.”*

An Post welcomes the opportunity to meet with ComReg and discuss its exact requirements in greater detail.

2.2 Reporting and transparency

The proposed revised Accounting Direction outlines the reporting requirements to be contained in the regulatory accounts. These include the following:

(a) “A commentary on the regulatory performance. The commentary shall explain at a minimum:

- trends relating to products, expected significant future events and how these might impact the business;*
- trends relating to revenue by service;*
- trends relating to mail volumes, by service, recorded separately from (i) revenue data recorded at the point of sale; and (ii) operational data recorded in the outward phase of the postal pipeline;*
- the reasons for any divergence between mail volumes, by service, recorded separately from (i) revenue data recorded at the point of sale; and (ii) operational data recorded in the outward phase of the postal pipeline;*

- *significant year on year movements in the reported performance and balances;*
 - *one-off or exceptional events in the year;*
 - *large adjustments made to produce the accounts; and*
 - *the impact of changes in accounting policies, methodologies and estimation techniques;”*

An Post agrees in principle to the provision of a commentary on the regulatory accounts along the lines proposed by ComReg, but would need to have further discussion with ComReg with regard to the appropriate level of detail (see comments concerning volumes in Section 1.3 of this response).

(b) “A comprehensive explanation of the basis of preparation of the regulatory accounts, including an explanation of the key regulatory policies adopted by An Post.”

An Post considers this provision appropriate.

(c) “Profit and loss accounts and balance sheets for each business segment as defined in IAS14 or as agreed by ComReg, and prepared in accordance with IAS14.”

An Post has no objection in principle to the provision of profit and loss accounts and a statement of net assets for the mails business segment (fully reconciled to the company balance sheet), but would require the opportunity to agree with ComReg the level and depth of information to be provided, balancing information requirements with cost effectiveness.

(d) “Profit and loss accounts for the business segments providing services within the scope of universal service as defined in the Regulations and clarified by ComReg in any document issued following a public consultation, distinguishing between services wholly within the Reserved Sector and those wholly within the Non-Reserved Sector. These accounts shall also include profit and loss accounts for each service. They are also required to be fully reconciled to the published financial accounts of An Post, identifying all items not relevant to the accounting period that have been excluded from the regulatory accounts.”

The precise structure of the data required would need to be agreed with ComReg

(e) The information relating to the first regulatory reporting period to which the Direction applies shall be presented in the formats and the level of detail shown in the template schedules to be prescribed by ComReg, in this Direction or a subsequent Direction.”

As outlined in (d) above, An Post views the structure of the template schedules as critical to the production of future regulatory accounts and therefore believes that working parties should be established between ComReg and An Post to produce these templates as soon as possible.

(f) “The regulatory accounts shall include volume information that shows mail volume by service, recorded separately from (i) revenue data recorded at the point of sale; and (ii) operational data recorded in the outward phase of the postal pipeline.”

An Post can provide volume data from these sources. This information can be provided in tandem with the regulatory accounts. However, for the reasons outlined in Section 1.3 of this response, the information should not be included as part of the regulatory accounts as such.

(g) "The regulatory accounts shall include details of expenditure by pipeline process distinguishing between costs which have been directly allocated to specific services, common costs which have been allocated on the basis of the origin of the costs themselves, and common costs which have been allocated or apportioned on the basis of a general allocator."

An Post will work with ComReg to ensure that the cost allocation drivers are fully understood.

(h) "The regulatory accounts shall include details of revenues distinguishing between revenues which have been directly allocated to specific services and other revenues which have been allocated or apportioned on the basis of a general allocator."

An Post will work with ComReg to ensure that the revenue allocators are fully understood.

(i) "A signed statement from the Directors of An Post acknowledging their responsibilities for the preparation of the regulatory accounts and confirming their compliance with the requirements of the Direction."

An Post foresees no difficulty in the provision of this statement, though as this is a new requirement, the precise format will need to be established. An Post envisages this being of a similar nature to the regulatory Statement of Directors already included in the annual financial statements.

(j) "An auditor's reports and opinions on the regulatory accounts and An Post's compliance with the requirements of the Direction."

An Post is of the view that an audit would add significant value to the regulatory accounts as it would provide assurance that the An Post regulatory accounts fairly present the results attributable to services within the USO. Section 2.5 of this response provides greater insight into audit related issues.

(k) "The results of the annual audit of any statistical sampling process undertaken to identify revenue or mail volumes."

The audit process surrounding the regulatory accounts is dealt with in greater detail in Section 2.5 of this response.

The remainder of this section deals specifically with:

(l) Cost of service information

(m) Ad hoc reporting

(n) Publication

An Post believes it is appropriate to provide ComReg with a detailed report outlining cost of service information whenever An Post seeks concurrence with proposals to increase prices of services in the reserved area. This report will compare the existing and proposed price with a detailed estimate of the cost of providing the service.

It is important to state that An Post does not agree that information of the same kind would be provided to ComReg in advance of non-reserved price increases. ComReg does not have *ex ante* jurisdiction over non-reserved price increases, and An Post cannot accept requirements in the Accounting Direction that would seek to give ComReg *de facto* power of prior approval over non-reserved prices. This is an important principle for An Post. ComReg's powers in respect of the *ex-post* nature of non-reserved investigations are clearly set out in the governing legislation (European Communities (Postal Services) Regulations S.I. 616 of 2002 'the Regulations').

An Post can provide ad hoc reports that may be required from time to time to enable ComReg to perform its regulatory functions as outlined in the Regulations. However, any requests should be proportionate and reasonable, having regard to the cost of preparing them and the purpose for which they are required.

Whilst there is no legal requirement for An Post to publish regulatory accounting data on its website, An Post is willing to meet with ComReg to discuss the structure of the data which they would wish to see published. An Post believes however, that it would be inappropriate to publish the full regulatory accounts as doing so would involve the disclosure of commercially sensitive information.

2.3 Accounting Manual

The proposed revised Accounting Direction states that *“An Post must:*

- (a) document in an Accounting Manual the procedures and policies being used in the preparation of its regulatory accounts;*
- (b) document in the Accounting Manual the procedures undertaken to establish the processes used to identify revenues and mail volumes; by service;*
- (c) review the Accounting Manual annually;*
- (d) make the Accounting Manual subject to periodic review by an independent reviewer; and*
- (e) obtain ComReg’s approval for each annual edition of the Accounting Manual in advance of the start of the relevant regulatory period.”*

An Post views the regulatory Accounting Manual as an extremely important document and is proud of the Accounting Manual it has produced annually since 2001. An Post fully understands that the Accounting Manual must document the procedures and policies adopted in the production of the regulatory accounts and is of the opinion that the provisions contained in points (a) – (c) above are appropriate.

In relation to point (d) above, like other professional documents in use within the business, An Post recognises the benefit of a periodic review by outside professionals. It would not be necessary or proportionate for this to be carried out annually and An Post would like to agree with ComReg reasonable conditions with regard to independent review.

In relation to point (e) above, An Post finds it appropriate to provide an Accounting Manual to ComReg each year. In practice, changes to the nature of the business may well take place during the year. For example if new operational pay or non pay activities are established during the current regulatory period, these will not be reflected in any Accounting Manual submitted at the start of the relevant period. Details of such changes to the manual will be made available to ComReg.

The proposed revised Accounting Direction also states that *“The Accounting Manual shall contain a schedule showing how each individual cost category is treated. The Accounting Manual shall, at a minimum, provide an overview of:*

(a) An Post’s business, explaining the main activities and functions performed by An Post to deliver postal services to customers, clearly indicating which businesses and services are regulated;

(b) An Post’s management structure;

(c) how the underlying financial transactions supporting the business activities and functions are recorded in the financial ledgers, and how the transactions are grouped to provide the starting costs, revenues, assets and liabilities used within the internal costing systems to allocate costs;

(d) the accounting systems, in terms of the underlying costing principles and the conceptual flow of costs and revenues from source financial systems to the separated businesses;

(e) what the regulatory accounts comprise and the regulatory accounting process (including the basis of preparation for the regulatory accounts);

(f) year on year changes to regulatory accounts and changes to cost allocations, together with an assessment of the impact of these changes;

(g) how the regulatory accounts differ from the statutory accounts;

(h) the internal safeguards that are incorporated to ensure that the cost allocation system is free from material error; and

(i) the audit of the regulatory accounts in terms of scope of the audit and the process to appoint auditors.”

An Post in principle does not foresee any difficulty with the provision of information along these lines, though would welcome an opportunity to discuss with ComReg the level of detail envisaged.

2.4 The apportionment of income and costs between services

2.4.1 Business Segments

The proposed revised Direction states that *“Revenue and costs shall initially be directly assigned to business segments in accordance with the principles set out in IAS14. Fixed assets (buildings, vehicles, sorting equipment etc.) shall be shown in the balance sheet of the “prime user”, with use by other business segments charged on an arms length basis”.*

An Post is committed to providing professional segmented accounts and looks forward to addressing the detail with ComReg (see comments in Section 2.2 (c)).

2.4.2 Inter-company / inter-segment transactions

The proposed revised Accounting Direction states that *“payments/charges shall be calculated on an arms length basis, and in a transparent and non-discriminatory manner, with the proviso that this transfer “charge” shall equal the price An Post would charge to any competitor who wished to use its network or pay to any external supplier”*.

The An Post regulatory accounting systems ensure that inter-company transactions are accounted for on an arms length basis and will continue to do so.

2.4.3 Mail volume and Revenue Identification

The proposed revised Accounting Direction states *“Within the business segments, as defined by IAS14, mail volumes and revenue shall be allocated to each of the Reserved and to the Non-Reserved services respectively in the following manner:*

(a) mail volumes and revenue which can be directly assigned to a particular services shall be so assigned;

(b) mail volumes, by service, shall be recorded separately, from (i) revenue data recorded at the point of sale; and (ii) operational data recorded in the outward phase of the postal pipeline;

(c) mail volumes, by service, separately recorded, from (i) revenue data recorded at the point of sale; and (ii) operational data recorded in the outward phase of the postal pipeline, shall be compared. An Post shall understand and shall be able to report the reasons for any divergence between the two measures;

(d) revenue, by service, shall be recorded at the point of sale;

(e) mail volumes and revenue recorded at the point of sale that cannot be directly assigned to their use of specific services or retention by users for later use (e.g. postage stamps sold and franking machine credits) shall be apportioned to services on the basis of statistical sampling accurate to +/-1% at the 95% Confidence Level;

(f) for mail volumes recorded at the outward phase of the postal pipeline, which cannot be directly assigned to their specific services (e.g. manually sorted mail items), mail volumes shall be apportioned on the basis of statistical sampling, by service, with a margin of error agreed with ComReg; and

A list of services (as defined in this Direction) provided by the An Post shall be included in the Accounting Manual, and may be published by ComReg.”

Please see comments under Sections 1.3 and 2.2(f).

2.4.4 Cost allocation and Apportionment Principles

The proposed revised Accounting Direction states *“Within the business segments, as defined by IAS14, costs shall be allocated to each of the Reserved and to the Non-Reserved services respectively, in the following manner:*

(a) costs which can be directly assigned to a particular service shall be so assigned;

(b) common costs, which are costs that cannot be directly assigned to a particular service, shall be allocated as follows:

- (i) whenever possible, common costs shall be allocated on the basis of direct analysis of the origin of the costs themselves;*
- (ii) when direct analysis is not possible, common cost categories shall be allocated on the basis of the indirect linkage to another cost category or group of cost categories for which a direct assignment or allocation is possible; the indirect linkage shall be based on comparable cost structures;*
- (iii) when neither direct nor indirect measures of cost allocation can be found, the cost category shall be allocated on the basis of a general allocator computed by using the ratio of all expenses directly or indirectly assigned or allocated, on the one hand, to each of the Reserved services and, on the other hand, to the other services."*

The An Post regulatory accounting systems adhere to these cost allocation principles and will continue to do so.

2.4.5 Cost allocation and Apportionment Rules

The proposed revised Accounting Direction states *"The Accounting Manual shall set out how the operating cost of the various aspects of the public postal network, as defined in the Regulations, shall be identified.*

It shall set out the basis on which the costs of particular activities are to be apportioned between services. Costs shall be apportioned between the various services that use each aspect of the network on the basis of volumes, "weighted" by factors which reflect the different impact of each item on the cost of the activity. The weighting factors shall be specific to each operational process, as well as the range of services that use that process, and shall be updated annually.

As a minimum, the hierarchy of costs to be applied to each service shall enable the cost of the following activities to be calculated;

- (a) Revenue Collection;*
- (b) Collection;*
- (c) Outbound sorting;*
- (d) Transport;*
- (e) Inbound sorting; and*
- (f) Preparation and Delivery.*

The hierarchy of accounts shall also distinguish between directly allocated costs, common costs which have been allocated on the basis of the analysis of the origin of the cost themselves, and common costs which have been allocated on the basis of a general allocator. Accounting items not involving the movement of funds (e.g. depreciation) shall also be identified separately.

The Accounting Manual shall specify in technical detail the range and scope of the data to be collected and the basis on which it is to be allocated / apportioned between services. The Accounting Manual shall also provide, at a minimum detail of:

- *the process by which An Post identifies how costs are found to be directly or indirectly attributable, joint or common;*
- *the process by which An Post identifies how avoidable, variable and fixed costs are defined;*
- *how equivalent volume drivers are derived;*
- *how costs are allocated to products with different weight, format and payment characteristics; and*
- *how cost allocation drivers are reviewed, updated and verified.”*

The An Post regulatory accounts classify operational pay and non pay costs into the hierarchy outlined in (a)-(f) above. The regulatory accounts have one additional cost classification (other), which consists fundamentally of indirect administration costs which cannot be classified directly into any of the other categories.

An Post can modify the regulatory accounting systems to ensure that under each classification of costs, distinction can be made between directly allocated costs, common costs which have been allocated on the basis of the analysis of the origin of the cost themselves and common costs which have been allocated on the basis of a general allocator.

The regulatory accounting systems can also be modified to ensure that accounting items not involving the movement of funds are identified separately.

An Post believes that it is appropriate for an explanation for each of the five bullet points above to be included in the Accounting Manual.

2.5 Audit and Confirmation of Compliance

The proposed revised Accounting Direction states “*An Post shall:*

(a) engage an independent auditor(s) to verify compliance with the Direction and to perform an audit of the regulatory accounts in accordance with the principles and guidance of the Auditing Practices Board;

(b) publish the auditor’s report and opinions on An Post’s compliance with the requirements of the Direction in its annual report submitted to the Minister under section 33 of the 1983 Act; and

(c) publish the auditor’s report and opinions on the regulatory accounts and on An Post’s compliance with the requirements of the Direction within the regulatory accounts. The auditor’s report and opinions shall be addressed to both An Post and to ComReg. The precise form of the audit opinion shall be developed by ComReg after consultation with An Post’s auditors and the Irish accountancy profession, amongst others and with regard to international best practice. ComReg will issue a separate Direction containing the form of the opinions.

An Post shall consult with ComReg before appointing or reappointing auditors for this purpose. ComReg shall be party to the auditor’s terms of engagement and agree to the scope of the audit of the regulatory accounts.

In addition An Post shall make:

(a) the Accounting Manual subject to periodic review by an independent reviewer;

(b) the processes used to identify revenue and mail volumes subject to periodic review by an independent reviewer; and

(c) any statistical sampling conducted to identify mail volumes subject to (i) annual statistical audit; and (ii) annual procedural review, taking into account changes to the population size of each service or other significant market changes. The audit and procedural review shall be conducted either by a statistical expert, ComReg or as part of the regulatory auditing process. Any alterations to the procedure resulting from the review shall be stated in the Accounting Manual.

An Post views an audit of the regulatory accounts as a valuable exercise. An audit would provide ComReg with assurance that the An Post regulatory accounts fairly present the results attributable to the services.

There are however, certain aspects on which An Post has further comment. These are as outlined as follows:

2.5.1. The auditors report and opinions shall be addressed to both An Post and ComReg.

Whilst An Post is of the opinion that it is appropriate to consult with ComReg before the appointing or reappointing of the auditor of the regulatory accounts, An Post believes that it is inappropriate for:

- (a) ComReg being a party to the auditor's terms of engagement; or
- (b) ComReg determining the precise form of the audit opinion

In relation to (a), it is standard practice in an audit of postal industry regulatory accounts, that the engagement letter be entered into directly between the auditor and the client. This is an approach which is adopted by Royal Mail. An Post will of course consult with ComReg in respect of the engagement letter but considers that the formal engagement should be between An Post and the auditor.

In relation to (b), it does not appear to be a core competency of the Regulator to design audit reports and An Post expects that this professional exercise should be left in the hands of the accountancy profession through professional auditors and their institute, the Institute of Chartered Accountants in Ireland.

2.5.2. An Post shall make the Accounting Manual subject to periodic review by an independent reviewer

As outlined in Section 2.3, it would not be necessary or proportionate for this to be carried out annually and An Post would like to agree with ComReg reasonable conditions with regard to independent review.

2.5.3 An Post shall make any statistical sampling conducted to identify mail volumes subject to (i) annual statistical audit; and (ii) annual procedural review, taking into account changes to the population size of each service or other significant market changes

An Post sampling is performed in accordance with a detailed statistical sampling plan established in conjunction with PwC. This sampling plan is adhered to rigorously. An Post believes that a periodic review of the statistical basis is appropriate, however having to perform a full statistical audit annually would be of limited benefit and leads to an unnecessary increase in the cost of regulation.

2.6 Timetable for the production of regulatory accounts

The proposed revised Accounting Direction states *“In accordance with Regulation 11(7) and 18(2), An Post shall provide to ComReg regulatory accounts disaggregated to the level of services within 19 weeks of the end of each financial year”*.

This timetable remains unchanged from the 2001 Accounting Direction.

The level of detail and the auditing of the regulatory accounts will add to the amount of work involved with regulatory reporting. Until there is clarity about the practicalities involved it would be unwise for An Post to commit to an exact deadline.

An Post however is determined to work constructively with the Regulator, the auditor and others to establish a timetable that is reasonable, practical and means that the financial information is relevant and timely. The details of this should be worked out by the parties involved.

Q.3. What is your view on the practicalities, timelines, cost etc. of implementing the changes recommended by LECG?

The proposed revised Accounting Direction states *“The above Direction will apply to accounting periods beginning on or after 1 January 2007. An Post is required to submit for approval by ComReg, no later than 1 February 2007, its timed programme for compliance with this Direction, including preparation of the Accounting Manual. In the same document, An Post shall indicate the extent to which it can comply with the Direction for accounting periods ending on or before 31 December 2006, and the reasons why they cannot comply with any specific item.”*

Arising from the consultation process, it is envisaged that An Post will engage directly with ComReg at a working level to agree a process and timeline to resolve any outstanding issues between the parties. Given that a number of issues remain to be clarified, it would be premature to commit to particular dates at this stage, but An Post is committed to actively engage with ComReg on all issues at its earliest convenience and progress this on an expedited basis.

Q.4. Are there any additional changes that you would recommend?

There are no additional changes that An Post would recommend.

4. Appendix – KPMG Letter to ComReg



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Our ref 00501/cf

26 October 2006

Dear Sir

Consultation on Regulation of Universal Postal Services – Accounting separation and costing methodology (Doc No. 06/55)

We have considered the proposals for financial reporting contained in the paper above together with LECG report “Revised Accounting Direction and Related Issues” (ComReg document 06/55a) and set out below a number of observations and comments, that we believe require consideration by the Commission for Communications Regulation (ComReg) before concluding on a new Accounting Direction to An Post (the company).

Our observations below are numbered for clarity in accordance with the structure of the LECG Report. We have not responded to all consultation questions but have restricted our comments to areas where we have direct knowledge through our audit of An Post, other regulated entities and the accounting profession in Ireland.

Q1. Do you consider that the current Accounting Direction should be revised at this time?

In broad terms, we agree that the current Direction should be revised to provide greater clarity both to the company, its regulator and the auditor as to the required format of the regulated accounts, the agreed accounting framework on which such accounts are prepared and ensure better understanding of the audit process and resulting audit opinion.

Denis O'Connor • Darina Barrett • Alan Boyne • Gary Britton • Keith Browne • Sharon Burke • Niall Campbell • Brian Clavin
Jim Clery • Colm Clifford • Mark Collins • Ivor Conlon • Michele Connolly • Adrian Crawford • William Cunningham • Brian Daly
Jon D'Arcy • Robert Dix • Paul Doherty • Eamonn Donaghy • Michael Farrell • Michael Flaherty • Gerard Flood • Caroline Flynn
Michael Gaffney • Laura Gallagher • Donall Gannon • Ruaidhri Gibbons • Roger Gillespie • Seamus Hand • Michael Hayes • Paul Holloway
Ray Jackson • Declan Keane • David Kennedy • Jonathan Lew • Liam Lynch • Olivia Lynch • Tom McEvoy • Pat McDaid • Paul McGowan
Niamh Marshall • David Meagher • James Menton • Cliona Mullen • Shaun Murphy • Arthur O'Brien • Colin O'Brien • Conor O'Brien
Pat O'Brien • Kevin O'Donovan • Conall O'Halloran • Sean O'Keefe • Garrett O'Neill • Terence O'Neill • Terence O'Rourke
Conor O'Sullivan • Vincent Reilly • Colm Rogers • Eamonn Russell • Anna Scally • Seamus Taaffe • Eric Wallace • Kieran Wallace
Richard Whelan • David Wilkinson

Consultants (qualifications other than Chartered Accountant): John Bradley • Robert Dowley • Colm Gorman • Ken Hardy • John McGlone
Sean Mooney

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Form and content of financial information

12.5 to

12.13 This section of the report deals with the current format and content of regulatory accounts and the differing views of ComReg and An Post with respect to the transparency and level of information provided in regulatory information. Irish companies preparing statutory financial statements, either in accordance with Irish Generally Accepted Accounting Practice (GAAP) or International Financial Reporting Standards (IFRS), have a clearly prescribed set of schedules to prepare and disclosure information to provide. This guidance is supplemented by Irish Company Law which requires further specific disclosure information. Little scope for misunderstanding as to the nature and content exists between preparers, users and auditors.

Guidance on regulated accounts in Ireland is limited and reporting to regulators has evolved according to the requirements of particular regulators.

The LECG report comments on the lack of transparency of the regulatory information and notes the absence of financial commentary and narrative explanation. Such treatment is consistent with current GAAP. Paragraph 12.7 sites FRS 18 as a standard requiring disclosure; however, this is only one of 29 such standards underpinning the financial reporting framework in Irish GAAP, all of which require disclosure of specific items. GAAP does not contain any requirement to disclose general commentary on trends or movements with the exception of published guidance relating to operating and financial reviews. That guidance (intended to be persuasive and not mandatory) was written by the Accounting Standards Board, with quoted companies in mind and was designed to assist companies in setting out business analysis matters.

We would strongly concur that there is a requirement for far greater agreement between An Post and ComReg as to the required content of regulatory accounts to remove ambiguity for preparers, users and auditors of such information.

Accounting framework

1.27 We concur with the comments noted that the company should apply GAAP in preparing regulatory accounts. The current Direction does not specify the basis on which the regulatory accounts are to be prepared. All statutory financial statements are required to state the basis on which the information is presented and the directors acknowledge their responsibility for same. We consider that regulated accounts should be prepared in a similar manner. An agreed accounting framework is essential to ensure that any audit will fulfil its function and provide a meaningful audit opinion.

9.14 The report notes that Regulation 11(2) requires An Post to maintain financial records and systems to ensure that "separate accounts can be maintained for each of the services

within the reserved sector on the one hand and each of the services within the non-reserved sector on the other”. In our experience it is not common practice for Irish regulated entities to provide non-regulated financial information to regulators in the same level of detail as regulated information. Our experience indicates that typical regulated accounts would provide the regulated financial information to specified levels of detail and include non-regulated information as a whole without disaggregation into constituent activities.

We would concur that the form of GAAP should be agreed between An Post and ComReg and that an agreed basis is fundamental to proper preparation of the regulated accounts. An Post maintains its statutory accounting information and prepares its statutory financial information in accordance with Irish GAAP. Irish GAAP requires disclosure of segmental information in accordance with SSAP 25 “Segmental Reporting”. SSAP 25 does however permit companies to omit disclosure of specified information if such disclosure would be seriously prejudicial to the interests of the company. We understand that the company, in line with other Irish regulated entities, does not provide full analysis of non-regulated activities on grounds that such information is competitively sensitive.

- 12.15 Paragraphs 12.15 to 12.21 discuss the basis of regulatory accounts preparation on a consistent and comparable basis and, specifically, when financial information should be restated for a prior year to reflect current year practices. GAAP requires restatements to be made to prior year financial information only in the event of discovery of a fundamental error in such information or on a change in accounting policy. A change in accounting estimate does not require restatement of financial information. Accounting policies define the process whereby transactions and other events are reflected in the financial statements. Estimation techniques on the other hand implement the measurement aspect of accounting policies. GAAP requires entities to disclose material accounting policies and describe significant estimation techniques. GAAP also requires where the effect of a change to an estimation technique is material, a description of the change and, where practicable, the effect of the results on the current period. Note that it does not require a restatement of the prior year financial information when an estimation technique has changed in the current year.
- 12.19 This paragraph suggests alternative treatments for restatements of financial information. As noted above, current GAAP would require restatement to financial information in the event of a change in accounting policy and would require disclosure only of the impact of a change in an estimation technique, where such impact is significant. This is likely to be a more cost-effective option than requiring a full restatement in every event.

Audit matters

9.19 &

- 9.20 The consultation paper notes that the Direction does not require audit of the cost allocation system. Paragraph 9.20 notes that the Regulations have primacy over the Direction. The Regulations currently require that the company’s cost allocation systems

should be “verified by auditors engaged by the provider and shall publish a statement to that effect in its annual report”. The paper then goes on to recommend that the cost allocation system should be audited rather than “verified” as required by the Regulation. In normal statutory financial reporting, it is required practice for auditors to assess the information system from which the financial information is derived to ensure the system can provide complete and accurate information which is then subject to audit.

Regulated accounts are typically prepared in accordance with a clearly specified basis of preparation and audit and other reports thereon are generally designed to ensure that the resulting regulated accounts have been prepared in accordance with that specified basis of preparation. Agreement between preparers and users as to the appropriateness of the basis of preparation is therefore essential to ensure the information meets user needs. The basis of preparation would normally detail how all significant costs are allocated between activities. The requirement to issue an audit opinion on these financial statements would, by definition, include the requirement to design audit procedures to assess the underlying cost allocation system.

12.22 to

12.32 These paragraphs deal with audit interpretation issues. Since the introduction of the Direction, the Directors of An Post have furnished a statement of compliance with the Regulations within the main statutory annual report and KPMG, as auditors of An Post, have reported on that statement without qualification within the statutory annual report. We have not performed an audit of the regulatory accounts as we are not required to under the current Regulations or Direction, nor have we performed an audit of the cost allocation system. As noted in the consultation paper, our audit report is dated prior to the issuance of the regulatory accounts and therefore our audit report could not be inferred to cover an audit of those regulated accounts. We agree that the current Direction does not provide sufficient or clear guidance on the precise nature of the audit requirement and concur that clarification of such matters would be welcome.

Q2. Do you consider that the changes recommended by LECG are warranted and appropriate?

We consider that a number of proposals advanced by LECG relating to clarity of financial information and basis of preparation are appropriate. We have included certain comments pertaining to audit matters for Irish entities as we consider that a number of comments raised by LECG are more appropriate in the context of UK entities where more prescriptive guidance exists that has not been reflected by the Irish accountancy profession.

Form and content of financial statements

14.8 to

14.11 We consider that the proposals to standardise the format and content of regulatory accounts are broadly positive and would reiterate the necessity for ComReg and An Post

to agree on the specific schedules to be presented in the regulatory accounts, the level of disclosures to be provided and, fundamentally, the underlying GAAP to be used.

It is common practice in GAAP that companies are afforded sufficient time to comply with new requirements when initially introduced. We consider that ComReg should consult with An Post in determining an appropriate timeframe for preparing and auditing the regulated accounts in addition to agreeing on treatment of comparative information in the year of initial adoption of the new Direction.

Accounting framework

13.17 We would support the recommendation for ComReg and An Post to agree a common definition of materiality in relation to the regulatory accounts. Such agreement would facilitate a clearer accounting methodology and auditing process.

14.2 To facilitate consistent and coherent preparation and presentation of the financial statements we consider that Irish GAAP is the most relevant starting point, with any deviations therefrom being agreed in advance between An Post and ComReg. Such basis of preparation should then be clearly disclosed in the financial statements as is normal practice in statutory financial statements. We concur that it may be more appropriate to include the allocation details and mechanisms thereof in the Accounting Manual.

Our view is that agreement of the basis of preparation between An Post and ComReg is critical prior to actual preparation of the regulatory information.

14.3 We agree that the regulatory accounts should be reconciled to the statutory financial statements. The consultation paper suggests that each reconciling item should be properly explained. We consider that this may not be practical or cost-efficient for the company and it may be more appropriate for ComReg and An Post to agree a qualitative and/or quantitative basis as a framework for guidance on required explanations of reconciling amounts.

14.7 We consider that restatement of prior year accounts should follow Irish GAAP which currently requires financial information to be restated when a company adopts a change in accounting policy or discovers a fundamental error in such financial information. A change in accounting estimate does not warrant a restatement of the prior year numbers. However, changes in estimates that are material in the current period results should be measured and disclosed.

Audit matters

11.14 We concur that An Post should properly document its controls over its cost allocation systems. Such system provides the basis on which financial information, subsequently subject to audit, is derived.

11.15 The paper recommends that the cost allocation system “should be audited by an external auditor. This review should not just be a review of the process, but should also seek to comment on the principles used, the appropriateness of selected cost drivers, etc.” In our view, this requirement would be more appropriately addressed by ComReg and An Post agreeing, in advance of any audit process, the basis on which costs are allocated and the appropriate format and content of regulatory information. An independent audit of regulated accounts is intended to provide an opinion on the financial information; specifically, that the financial information has been properly prepared in accordance with the stated basis of preparation. A normal audit process would require the independent auditor to assess the systems and processes used to capture and report financial information on which the audit opinion is provided.

Paragraph 11.17 suggests that an option for reviewing the method of allocation costs is for ComReg to “designate a second auditor to review the audit activities”. This would be inappropriate as it would appear to negate the independent audit process conducted in accordance with Auditing Standards and would involve significant additional cost burden for the company.

13.38 to

13.41 The consultation paper sites guidance from ICAEW in discussing a proposed form of audit opinion. Such guidance however has been prepared for use in the UK market and no such equivalent guidance currently exists from the Institute of Chartered Accountants in Ireland with respect to Irish registered companies. Notwithstanding this, we would agree that an appropriate form of opinion for the regulatory audit is one that would state that the financial information had been properly prepared in accordance with the basis of preparation as specified within the financial statements. Therefore, it is of the utmost importance that the basis of preparation is agreed by ComReg and An Post in advance of any audit process.

14.21 We would concur with LECG’s opinion that it is more appropriate, on grounds of efficiency, to include an auditor opinion on the regulatory audit with the regulatory accounts rather than in An Post’s Annual Report. If the company chooses to publish summarised regulatory accounts rather than the full regulatory accounts, then we agree that this information should have an auditor opinion confirming that the opinion has been properly extracted from the full regulatory accounts and should also confirm the nature of the opinion issued upon those regulatory accounts.

14.23 &

14.24 Our experience indicates that it is common practice for Regulated Entities to appoint the same auditor for the both the financial statement and regulatory audits, principally on grounds of efficiency. The consultation paper requires ComReg to be consulted before the appointment and re-appointment of the auditor. The proposals however do not appear to take into account, the arrangements in Company Law for appointment of auditors. Reports for regulatory purposes are commonly sought from a company’s auditor

appointed by the shareholders in General Meeting and it is they and the company's directors who have the power relating to appointment and removal of the auditor. Appointment of a second auditor to "perform a quality review of the work performed by the first auditor" as suggested in paragraph 14.27 would be wholly inappropriate as it would appear to ignore auditing standards, auditor independence and objectivity and would involve additional cost burden for the company.

- 14.29 ICAEW Guidance has been cited as providing the most appropriate form of wording for the regulatory audit opinion. Such guidance, as indicated under comments on paragraph 13.38 -13.41 above, applies solely to UK registered companies and the Institute of Chartered Accountants in Ireland has not adopted any such form of guidance. In broad terms we would agree that an appropriate form of opinion is one that would state that the regulated financial statements have been properly prepared in accordance with the stated basis of preparation and with specified sections of the Direction. We would welcome the opportunity of agreeing the precise form of opinion with the company. .

If you would find it helpful to obtain further information or discuss our comments in more detail, please contact Caroline Flynn. We would be happy to provide ComReg with further details in relation to any matters raised in this letter and to contribute to development of appropriate structures to meet your requirements.

Yours faithfully


KPMG