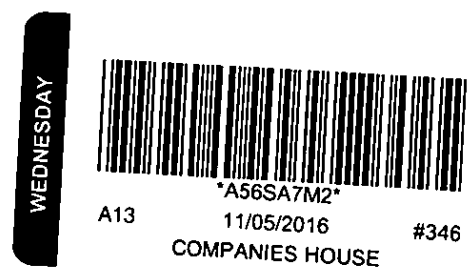


To be filed with the financial statements for  
Pearson Dollar Finance plc, company number  
5111013.

PARENT ACCOUNTS

# Pearson plc

## Annual Report and Accounts 2015



80 Strand  
London WC2R 0RL

Registered Number 53723 (England)

IMAGE REMOVED

# Focused on delivery

Pearson Annual report and accounts 2015

IMAGE REMOVED

IMAGE REMOVED

---

## Pearson at a glance

### Financial highlights

---

Sales

£4.5bn

-5%

IMAGE REMOVED

---

Adjusted operating profit

£723m

-3%

IMAGE REMOVED

---

Average annual growth in  
headline terms 2010–2015

Adjusted earnings per share

-1.9%

Operating cash flow

-16.3%

IMAGE REMOVED

IMAGE REMOVED

Dividend

+6.1%

➔ To read about our KPIs go to p14

Throughout this report growth rates are stated on a constant exchange rate (CER) basis unless otherwise stated. Where quoted, underlying growth rates exclude both currency movements and portfolio changes

## About Pearson

Pearson is the world's learning company, with global capabilities in educational courseware and assessment, based on a strong portfolio of products and services, powered by technology.

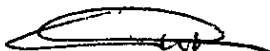
We believe that our strategy of combining these core capabilities with services enable our partners to scale online, reach more people and ensure better learning outcomes, providing Pearson with a larger market opportunity, a sharper focus on the fastest-growing education markets and stronger financial returns.

Our mission is to help people make progress through access to better learning. We believe that learning opens up opportunities, creating fulfilling careers and better lives.

This strategic report is formed of three sections 'Our business', 'Our performance' and 'Social impact', (p02-67), and was approved for issue by the board on 4 March 2016 and signed on its behalf by:

IMAGE REMOVED

Coram Williams  
Chief financial officer



## Strategic report

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## Chairman's introduction

Sidney Taurel  
Chairman

IMAGE REMOVED

**“My focus will be on helping guide Pearson back to growth, supporting the management team and all of our employees in our mission: to help more people make progress in their lives through learning.”**

Dear shareholders,  
I am proud to introduce our annual report for the first time as Pearson's chairman

My predecessor, Glen Moreno, made a major contribution to Pearson during his long and successful tenure as chairman. I am sure my fellow shareholders will join me in thanking Glen and wishing him all the best for the future

This is an important time to be joining Pearson. Our 2015 performance was not what we would have wanted, and we now have a plan in place to return the company to growth

The company has a strong purpose at its heart, and has made great strides in focusing on education. My own focus will be on helping guide Pearson back to growth, supporting the management team and all of our employees in our mission: to help more people make progress in their lives through learning

### Our immediate priorities

This is a challenging time for businesses in global education, with rapid changes taking place in the sector. Digital technology is revolutionising education just as it has all other aspects of the way we work, communicate and do business. In an era of constrained spending, there is a big productivity challenge, as governments and education leaders seek to achieve better outcomes

at the same or lower cost. The value of a university degree continues to grow, but many students and institutions face cost pressures. These changes offer big opportunities for Pearson, but also present risks and transitions that we will need to manage in some of our traditionally strong businesses

With these factors in mind, my immediate priorities are clear

- › I will be supporting our management team to ensure that we stay focused on our biggest strategic growth objectives
- › I will offer guidance to help them to make further progress on simplifying and integrating the business. We need to make sure that Pearson is better able to leverage our assets, skills, and technology platforms in order to deploy our products globally
- › I will be supporting the team to ensure that capital is allocated in a way that provides better returns for shareholders, ultimately creating a better, more sustainable company for the future

We will engage transparently with shareholders on our capital allocation plans and progress against our strategic goals, as well as on all important issues

We plan to hold our dividend at the 2015 level while we rebuild cover, reflecting the board's confidence in the medium-term outlook for our business, and we are committed to increasing total shareholder returns

These priorities require strong leadership, dedication and hard work from me, the board, and the management team

### Our leadership team

We have continued to enhance the strength and depth of our board, including the appointment of Coram Williams as our chief financial officer. Coram has a decade's experience working directly for Pearson and helped to lead our joint venture, Penguin Random House, through a successful company integration as its first CFO

Like me, Lincoln Wallen joined the board on 1 January 2016. Lincoln is chief technology officer for DreamWorks Animation, and his appointment further strengthens our digital capabilities. Like thousands of Pearson employees across the globe, he also has a background in education and teaching

We have an experienced executive team, and committed employees around the world. I look forward to working with John Fallon and the executive team to deliver our agenda

Read more about our board on pages 72-73 ➔

## Share price performance

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

Source Datastream to 31 December 2015

## Total shareholder return (TSR)

See p14 ➔

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

Source Datastream to 31 December 2015

## Building a company for the future

I led Eli Lilly, a business in the global health sector, as CEO and Chair for ten years. I see some clear parallels between health and education that I believe provide opportunities for Pearson.

Like health, education affects every citizen of the world in a deep and personal way. Both sectors have seen dramatic increases in the use of digital technologies for the benefit of users – in our case, teachers and students. For us, this means personalised, adaptive learning, with the ability to measure and improve outcomes at an individual level.

So we are continuing at pace on our mission to become more digital and service-driven, and a simpler, better integrated business, with efficacy at the heart of everything we do. Read more on our ongoing commitment to efficacy on pages 46-53 ➔

## Pearson's future

I would like to thank you for your continued support of Pearson. It has been a tough 2015, and there are undoubtedly challenges ahead. Pearson is a company with strong market positions, real competitive advantage and a significant medium-term market opportunity. The board believes that the plans we are enacting will help to build on these strengths and enjoy sustained growth.

I see an exciting future ahead for Pearson – as with my experience in the health sector, I am inspired by working in a company with a strong sense of purpose. As chairman I am fully focused on helping the management team develop our strategy and deliver long-term value for our students, customers and you, our shareholders.

IMAGE REMOVED

**Sidney Taurel**  
Chairman

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## Chief executive's strategic overview

John Fallon  
Chief executive

IMAGE REMOVED

“2015 was a year of change and challenge at Pearson, which ultimately will leave us better placed to meet the huge unmet demands in global education.”

Dear shareholders,  
2015 was a year of change and challenge at Pearson, which ultimately will leave us better placed to meet the huge unmet demands in global education

The biggest change was that, with the sale of the Financial Times Group and our stake in The Economist, we completed Pearson's exit from the financial news and information market. We thought long and hard about these disposals. It is not easy to part with such globally respected brands, which have been an important part of Pearson for many years. After careful consideration, the board concluded that these transactions made strategic sense, achieved a good financial return for shareholders, and were in the best long-term interest of both The Economist and the Financial Times.

The pace of disruptive change in new technology – in particular, the growth of mobile and social media – poses a direct challenge to how leading news organisations produce and sell their journalism. The best way to ensure continuing success is to be part of a global, digital news organisation that is completely focused on the business of journalism. We concluded that new owners with strong track records in media would help grow the FT and The Economist's global reach and reputation in a digital age, just as we secured Penguin's creative and commercial future by combining it with Random House to create the world's largest consumer publisher, Penguin Random House. That business, of which we own a 47% stake, continues to perform well, as you can read on page 33.

### Our strategy

#### Short-term priorities

- Deliver transformation
- Simplify our business
- Stronger cash generation
- A growing company

#### Strategic growth drivers

- Digital & services**  
Build on our global strength in educational courseware and assessment with leading digital products and services, where we see the greatest potential for growth, scalability and impact on learner progress
- Market presence.**  
Our strategy to build on our leading presence in developed markets, and the opportunity to meet growing global demand for education

### Challenges in 2015

These disposals enable us to focus more fully on our education business, which was where we faced our biggest challenge last year. The cyclical and policy related headwinds we face in our major education markets – which we have described in previous years and which we cover later in this report – are persisting for longer than we anticipated. They are also having a more pronounced impact on our profitability than we expected, reducing our annual operating profit by approximately £230m from its peak. These headwinds are largely cyclical and, over the next two years, they should finally abate.

This means that, although operating profit and earnings per share were only down marginally in underlying terms on the previous year, they fell short of the goals we set at the start of the year.

### Our strong competitive performance

Pearson's competitive performance remains strong. We held or increased our market share in higher education courseware, school courseware, and in UK general qualifications. In professional testing, virtual schooling, online higher education and other areas we increased our capabilities, our reach and our commercial success substantially. You can read more about our operating performance on pages 16-33.

We are also confident that education remains an attractive investment opportunity with the growth potential to enable us to serve more students around the world and deliver good, sustainable returns to our shareholders.

### A clear strategy

Our strategy to capitalise on this opportunity is clear. As the world's learning company, Pearson has world-class capabilities and products in educational courseware and assessment, powered by learning technology. By combining these capabilities with teaching and learning services, we help schools, universities and others to scale online, reach more people and ensure better learning outcomes. As we do so, we provide Pearson with a larger market opportunity, a sharper focus on the fastest-growing education markets and stronger financial returns.

This approach recognises that education is undergoing a number of structural changes. The economic value of an education remains large. In the US, for example, the earnings premium of a university degree has never been higher. However, the cost of education is going up faster than inflation – and public funding for education is under real pressure. This presents our customers – university presidents, school superintendents, teachers and faculty, students and their parents – with a real challenge.

It is compounded by the fact that rising costs have not brought any real increases in learning outcomes – which remain uneven and variable – and there is an alarming mismatch between the expectations of educators and employers. For example, according to Gallup research from 2014, 96% of chief academic officers in the US rate their institution as somewhat or very effective at preparing students for the world of work. Yet only 11% of business leaders agree.

## 3 Measurable outcomes

Our efficacy programme is our long term commitment to delivering measurable impact. It informs all strategic decision making across Pearson, including our product and services strategy. We will begin reporting formally on this impact from 2018.

### Our constant goals

#### Generate sustainable returns by

Delivering long-term growth

Extending our global presence and reach

Building on our leading education position

To deliver measurable impact

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## Chief executive's strategic overview continued

### Helping teachers to be more effective and students more successful

We know that technology can help to address these challenges, by making learning more accessible, flexible, personal and affordable. For example, we are drawing on the latest digital advances to develop products which further customise and personalise learning. So we are embedding learning analytics in our new courseware offerings, such as Revel, to help teachers use data to teach students more effectively.

For students themselves, we are using adaptive learning technologies to focus their studies on concepts which require more time and attention.

We are developing new qualifications and certifications that help students to translate education into employment by assessing career-relevant knowledge and skills, providing quality assurance to schools, universities and employers. For example, last year we ran nearly 50 million practice or actual assessments for students on digital devices in the US using our TestNav application, aligning these new tests to higher standards for career and college readiness.

Online degree and virtual online school programmes represent 10% of Pearson today, from nothing five years ago – and are growing at double-digit rates each year. With a solid platform and market position in the US, we are now growing these businesses globally. With the global online programme management market set to double in the next five years, there will be many more opportunities for Pearson to partner with universities to improve learning.

This opportunity is highlighted through our long-standing partnership with Arizona State University, where we are helping to recruit, retain and teach several thousand online students. As more and more universities and students embrace the possibilities for improving access and success in education using technology, there will be many more opportunities for Pearson to partner with institutions on course design, student recruitment and online tuition.

All of our new products and services are underpinned by our efficacy approach, launched three years ago, which is designed to ensure that we help teachers to be more effective, and students to be more successful. We are committed to reporting on the learning impact of our individual products from 2018 onwards, through independently audited evidence and reports. We are making good progress towards this target, as you can read later in this report (pages 46-53).

Our success in helping our customers address these structural changes in education should enable Pearson to increase our average revenue per customer, and access larger markets as we provide educational services far broader than just stand-alone content or assessment. To make the most of the opportunity, we are making Pearson a simpler, better integrated, more cost-efficient company.

### Sharpening the future

In January we announced a series of actions that will help us to achieve this goal.

We are creating a single global product organisation, combining our three previously separate lines of business. We are integrating our school, clinical and professional assessment operations in North America. We are reducing our exposure to large, direct delivery operations to focus on online, virtual, and blended services in a much more scalable, and profitable way. Each of these changes will help us invest in fewer, bigger opportunities, and ensure that our world-class capabilities can be scaled to customers around the globe.

We are also making productivity improvements across all our enabling functions like Technology, HR and Finance – as our product offering and customer and employee support becomes more digital. We plan to rationalise our property portfolio and consolidate major supplier agreements to drive greater cost efficiency.

As a result of these changes, we expect to reduce Pearson's global workforce by around 4,000 roles, 10% of our headcount. These are decisions that we never take lightly and we are committed to supporting our colleagues during the transition. These actions will be complete by the end of 2016, and will reduce our annual running costs by around £350m. Importantly, they will also create a more focused, integrated business, better able to create and sell products across our markets to improve learning outcomes. This restructuring will give us the improved operational and financial flexibility to invest in growth areas and underpin shareholder returns.

### Our reach and impact

Big changes in the education landscape will create big opportunities for Pearson to grow our reach and impact.

There are huge unmet demands in global education that need to be addressed.

In higher education, the number of students going to university worldwide is expected to increase by more than 50 million to 260 million by 2025. Every one of those students wants a degree that is more affordable, more accessible and more likely to lead to a good job. One billion people will soon be learning English worldwide. School students and teachers increasingly expect to learn digitally.

So we plan to increase access to high quality education, ensure the success of all our learners against measurable outcomes, and to help more people around the world make progress in their lives – giving them the ability to secure a better job and a better life

As well as measuring the impact of individual products, we should also be measuring Pearson's total impact on learning. We are committed to ambitious goals to expand our reach and impact over the next decade. We currently reach around 75 million learners each year. By 2025, our aspiration is to reach 200 million learners each year – more than doubling our reach. These ambitious goals will contribute not only to Pearson's success, but to the societies of which we are a part.

In 2015 Pearson joined other businesses and world leaders in committing to the UN's Sustainable Development Goals (SDGs). The SDGs represent global challenges, many of which can be alleviated through better literacy and better education. In particular, Goal 4 of the SDGs, to '*ensure inclusive and equitable quality education and promote lifelong opportunities for all*', is central to the work of every Pearson employee and the millions of teachers and students we work with around the world each year.

To help maximise our contribution towards these goals, in 2015 we continued our strong commitment to sustainability, built new relationships with partners like Save the Children and supported a new coalition called Project Literacy. (Read more about Pearson's social impact on pages 54-67.)

We also invested in the Pearson brand in 2015 and it continues as an area of focus in the year ahead. Building a stronger brand will give us a better platform to reach more students and teachers, and act as a mark of quality as we develop and deliver new services across education. We have introduced a new visual brand capturing the curiosity and excitement of learning, which will unify Pearson's portfolio of products and services over time. The new brand is represented in this annual report for the first time.

### Our long-term opportunity

It's clear that 2016 will be a tough year as we work through the substantial change programme outlined above. Our plan focuses on operational execution, tight cost management and a sharper strategy to return to growth. We will be faster, leaner and more agile as a result of the changes we are making. We expect our business to stabilise into 2017 and return to growth in 2018.

We remain committed to the long-term opportunity for Pearson to provide high quality, affordable and accessible education that leads to a better job and a better life. For many people, learning is the route to a job to support their family or to acquiring the skills to help them progress in their career. For others, it's simply a passion for discovery that enriches their lives. All over the world, we hear parents say the same thing: they want to see a greater return on their investment in education, so that their children can gain skills, get better jobs and succeed in their lives. That remains a very compelling and exciting opportunity.

This powerful motivating purpose is what drives Pearson's business, which carries with it great responsibilities to learners as well as to you, our shareholders. In 2016, we are focused on delivering these responsibilities, and the plans laid out in this report explain how they will be achieved. We are confident that they will ultimately make Pearson a simpler, stronger company, and that they set the company up for a sustained period of growth. We'll keep you updated on our progress.

Thank you for your ongoing support

IMAGE REMOVED

John Fallon  
Chief executive

### My executive team

Coram Williams Chief Financial Officer

Michael Barber Chief Education Advisor

Tim Bozik President Global Product

Rod Bristow President Core Markets

Giovanni Giovannelli President Growth Markets

Albert Hitchcock Chief Technology and Operations Officer

Kate James Chief Corporate Affairs Officer

Don Kilburn President North America

Bob Whelan President Pearson Assessments

Melinda Wolfe Chief Human Resources Officer

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## Our business model

**Creating value** by developing products and services that meet learner needs most effectively

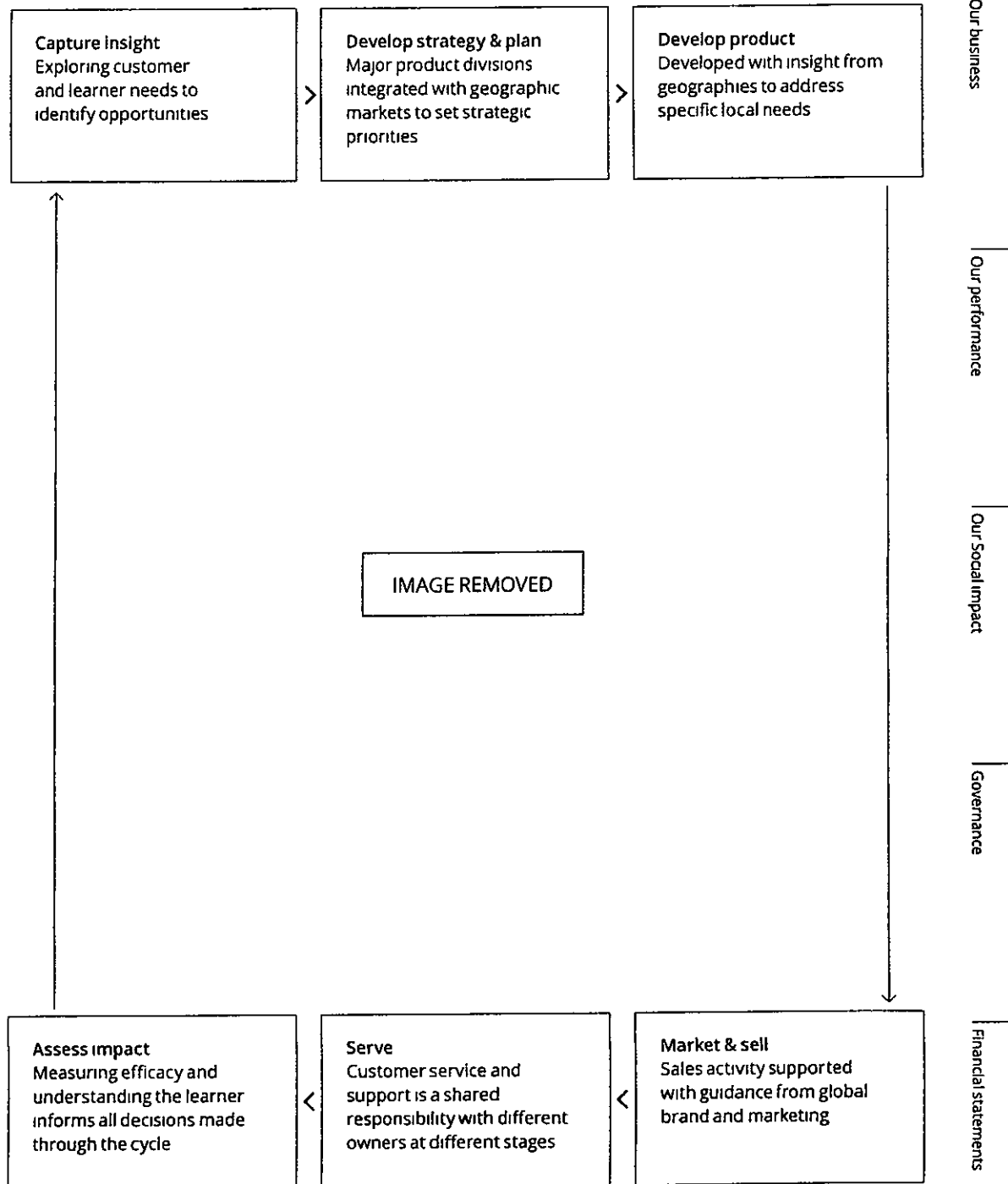
At the heart of this is our efficacy strategy which over the long-term provides insight and data on the full impact of our products and services.

From 2018 our efficacy programme will be reporting on this.

### How our strategy aligns with value creation

<b>1 Digital &amp; services</b> <b>Plan and develop</b> We combine our insights into market need with our global education expertise. This perspective informs the planning and development of all our teaching and learning products and services, driven by technology, and shapes those where we place the greatest investment.	<b>2 Market presence</b> <b>Market, sell and serve</b> Our leading position in educational courseware and assessment enables us to build our capabilities in fast-growing related services. We use our experience and expertise across the business to develop scalable, successful products and services, always meeting learner needs.	<b>3 Measurable outcomes</b> <b>Assess and provide insight</b> We measure and assess the impact of our products and services on learner outcomes. This feeds into our global insights capabilities, enabling us to build a deep understanding of learners' and customers' needs, and develop world-class products and services.
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See a summary of our strategy on p04-05 ➔



## Financial overview

Coram Williams  
Chief financial officer

IMAGE REMOVED

“In 2015, Pearson’s sales decreased by £72m in headline terms to £4.5bn. Total adjusted operating profit rose £1m to £723m.”

Sales (at CER)

-5%

Adjusted earnings per share

+5%

Operating cash flow

-33%

Dividend per share

+2%

### Business performance

£ millions	2015	2014	Headline growth	CER growth	Underlying growth
Sales	4,468	4,540	(2)%	(5)%	(2)%
Adjusted operating profit	723	722	-	(3)%	(2)%
Adjusted earnings per share	70 3p	66 7p	5%		
Operating cash flow	435	649	(33)%		
Net debt	(654)	(1,639)	60%		

### Statutory results

£ millions	2015	2014	Headline growth	CER growth	Underlying growth
Sales	4,468	4,540	(2)%		
Operating (loss)/profit	(404)	348			
(Loss)/profit before tax	(433)	255			
Profit for the year	823	470	75%		
Basic earnings per share	101 2p	58 1p	74%		
Cash generated from operations	518	704	(26)%		
Dividend per share	52p	51p	2%		

a) Growth rates are stated on a constant exchange rate (CER) basis unless otherwise stated. Where quoted, underlying growth rates exclude both currency movements and portfolio changes. Unless otherwise stated, sales exclude FT Group, while total adjusted operating profits include FT Group. Continuing operations exclude FT Group.

b) The 'business performance' measures are non-GAAP measures and reconciliations to the equivalent statutory heading under IFRS are included in notes to the consolidated financial statements 2, 6, 7, 8 and 32, and the corporate and operating measures.

### Profit and loss statement

In 2015, Pearson's sales decreased by £72m in headline terms to £4.5bn. Total adjusted operating profit rose £1m to £723m (2014: £722m).

Currency movements, primarily from the depreciation of sterling against the US dollar during the period, increased sales by £137m and operating profits by £22m.

At constant exchange rates (i.e. stripping out the impact of those currency movements), our sales fell by 5% primarily due to a change in revenue model at Connections Education which now records revenues charged at cost on a net basis, and adjusted operating profit fell by 3% due to revenue mix and an operating loss in our Growth segment.

The net effect of acquisitions, disposals and revenue model adjustments reduced sales by £129m and operating profits by £9m.

Stripping out the impact of portfolio changes and currency movements, revenues were down 2% in underlying terms while adjusted operating profit fell 2%.

Net interest payable in 2015 was £46m, compared to £64m in 2014. Our tax rate in 2015 was 15.5% compared to 17.9% in 2014. The decrease in both interest and tax was primarily due to agreement on historical tax positions and the release of associated accrued interest.

Adjusted earnings per share were 70.3p (2014: 66.7p).

### Cash generation

Headline operating cash flow decreased by £214m to £435m as a result of challenging trading and disposals. Operating cash conversion fell from 90% in 2014 to 60% in 2015 due to a mismatch between cash and accrued incentive compensation as a result of lower incentive compensation awards for 2015 when compared to 2014, capital expenditure greater than depreciation due to investments in our enabling function technology designed to lower administrative costs, an increase in US Higher Education textbook returns, and pension top up payments as a result of a triennial valuation. These factors were partly offset by an increased dividend payment from Penguin Random House.

### Return on invested capital

Our return on average invested capital was 5.8% (2014: 5.6%) primarily due to lower operating cash tax paid.

### Statutory results

Our statutory results showed a profit for the year after tax of £823m, including gains on the disposal of the Financial Times Group, The Economist Group and PowerSchool of £1,214m and an impairment of goodwill and intangibles of £849m, primarily reflecting trading pressures in our Growth and North America businesses. Included within the net gain on disposal is a £70m balance sheet write down on the disposal of PowerSchool, related to the reduced market opportunity for software (such as Pearson System of Courses and Schoolnet) which was to be integrated with PowerSchool and the recognition that adoption of such software in US Schools is now unlikely to occur at the rate originally envisaged.

### Balance sheet

Our net debt decreased to £654m (2014: £1,639m) primarily reflecting the disposals of the Financial Times, The Economist Group and PowerSchool and an increased dividend from Penguin Random House, offset by the strengthening of the US dollar relative to sterling, a higher group dividend and higher working capital. Pearson's net debt/EBITDA ratio decreased from 1.9x in 2014 to 0.8x in 2015 and our interest cover increased from 11.3x to 15.7x.

### Dividend

The Board is proposing a flat final dividend of 34p, which results in a 2% increase in the overall 2015 dividend to 52p, subject to shareholder approval.

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## Financial overview continued

### 2016 outlook

In 2016, we expect to report adjusted operating profit before restructuring costs of between £580m and £620m. This reflects the impact of the in-year benefits from restructuring offset by the loss of operating profit from disposals made in 2015, ongoing challenging conditions in our largest markets, the reinstatement of the employee incentive pool and other operational factors (including dual running costs as we rationalise our technology infrastructure, cost inflation and increased pre-publication amortisation relating to new product launches).

We expect adjusted earnings per share to be between 50p and 55p, after a normalised interest charge of approximately £60m and a tax rate of approximately 19%. In 2016, we are excluding the one-off cost of our major restructuring from adjusted operating profit and earnings per share to better reflect the underlying earnings potential of the business. Operating profit after restructuring charges is expected to be in the £260m to £300m range. This guidance is based on our current portfolio of businesses and exchange rates on 31 December 2015.

The major factors behind this guidance are as follows

#### Trading conditions

While we expect to achieve continued good growth in areas such as virtual schools and online programme management, we anticipate trading conditions to remain challenging in our major markets in 2016.

#### North America

In North America, our largest market, we anticipate US college enrolments will be flat given forecast modest improvements in US employment, a smaller adoption market in K-12 learning services and lower participation rate partially offset by growth in open territories driven by new products, reduced testing revenues in North America reflecting State and National Assessment contract losses worth approximately £100m announced in 2015, and growth in clinical assessments and professional certification.

#### Core

In our Core markets (which include the UK, Italy and Australia), we expect declines in vocational course registrations in UK schools, ongoing pressure in our various learning services businesses, partially offset by growth in managed services in Australia and the UK. At VUE, we will cease to deliver the contract to administer the UK Driving Theory test for the DVSA in September 2016.

#### Growth

In our Growth markets (which include Brazil, China, India and South Africa), we expect continued pressure in South Africa on government spending on textbooks and lower enrolments in CTI, macro-economic pressures in emerging markets, specifically China and Brazil, offset by growth from new products such as our Wall Street English new student experience.

#### Penguin Random House

In Penguin Random House, we anticipate that additional benefits from the ongoing integration of the business will be broadly offset by reduced demand for ebooks, following industry-wide changes in terms in 2015.

### Portfolio changes

We completed the sale of PowerSchool on 31 July 2015 for £222m, the sale of the Financial Times on 30 November 2015 for £858m, and substantially completed the sale of our 50% stake in The Economist Group on 16 October 2015 for £469m. In addition we disposed of Fronter and a number of print textbook lists in the US. Total disposals contributed approximately £90m to 2015 operating profit which will not recur in 2016.

### Other operational factors

Dual running costs from technology implementations, increased investment amortisation from new product launches and cost inflation will increase costs by approximately £90m in 2016 when compared to 2015.

### Incentive compensation

Group incentive compensation was zero in 2015 reflecting the weakness of performance versus budget. The incentive pool will be reinstated to £110m in 2016 to ensure our workforce is incentivised to sustain its strong competitive performance and to implement a significant programme of change within the company.

### Restructuring

Building on the work we have done over the last three years, we are taking further action to simplify our business, reduce our costs and position Pearson for growth in our major markets. We will create a single courseware product organisation, integrate our North America assessment operations, reduce our exposure to large scale direct delivery and focus on more scalable online, virtual, and blended services, implement major efficiency improvements across all our enabling functions - technology, finance, HR, and rationalise our property portfolio and renegotiate and consolidate major supplier agreements.

To implement this programme, we will incur costs of approximately £320m in 2016 and expect to generate annualised savings of approximately £350m, with approximately £250m of savings in 2016 and a further £100m of savings in 2017. We have already implemented a number of significant associated actions since announcing the programme in January.

### Currency movements

In 2015, Pearson generated approximately 63% of its sales in the US, 6% in Greater China, 5% in the Eurozone, 3% in Brazil, 2% in Canada, 2% in Australia, 2% in South Africa and 1% in India and our guidance is based on exchange rates at 31 December 2015.

### Interest and tax

We expect our interest charge to be approximately £60m, with lower average net debt levels offset by the absence of released accrued interest payments following agreement on historical tax positions. We expect a tax rate of approximately 19% on our total profit before tax (which includes the post-tax contribution from Penguin Random House).

IMAGE REMOVED

Coram Williams  
Chief financial officer

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## Key performance indicators

### Five-year performance

Financial objectives	KPI	Performance
Maintain long-term growth	<b>Sales</b> Sales fell 5% at CER in 2015 and have grown over the last five years at an average annual rate of over 1%, reflecting good long-term growth in digital and services businesses and acquisitions in the global education market, partially offset by a shift to subscription revenues, recent cyclical and policy factors and adverse exchange rate movements in emerging markets	+1.2%
	<b>Total adjusted operating profit</b> Total adjusted operating profit fell 3% in 2015 at CER and has fallen at a compound annual rate of 5.1% since 2010 reflecting good long-term growth in digital and services offset by the sale of businesses, recent cyclical and policy factors and adverse exchange rate movements in emerging markets	-5.1%
Deliver sustainable returns	<b>Total adjusted earnings</b> Total adjusted earnings per share is up 5% year-on-year in 2015, reflecting portfolio changes, exchange rate movements and a lower tax rate. Over five years EPS has declined at an average annual rate of 1.9% reflecting good long-term growth in our digital and services businesses offset by declines in print, portfolio changes, cyclical and policy factors and adverse exchange rate movements in emerging markets	-1.9%
	<b>Return on invested capital</b> ROIC grew 0.2% to 5.8% in 2015 and was affected by a lower tax charge. ROIC has fallen from 10.2% in 2010. We expect ROIC to improve as we deliver the plans for simplification and growth that we announced in January and make progress towards our 2018 goals	-4.4 percentage points
	<b>Total shareholder return</b> TSR in 2015 was -36% which compares to a -1% return on the FTSE 100 Index of large UK listed companies. Over five years, Pearson has returned approximately -11%, well behind the return on the FTSE 100 Index of 27% over the same period. Our recent shareprice performance has been disappointing but we are confident that the plans and strategy laid out in this report will make Pearson a simpler, stronger company, and that they set the company up for a sustained period of growth and value creation	-11.2%
	<b>Dividends per share</b> We increased dividends in comparison to 2014 by 2% to 52p, our 24th straight year of increasing our dividend above the rate of inflation. Pearson plans to hold its dividend at the 2015 level whilst it rebuilds cover, reflecting the Board's confidence in the medium term outlook	+6.1%
Manage our cash position effectively	<b>Operating cash flow</b> Operating cash flow fell to £435m in 2015, reflecting an increase in capital investment in new simplified systems, higher returns in our US higher education business due to de-stocking at one major retailer, weaker trading and pension top-ups partly offset by an increased dividend from Penguin Random House. Over five years operating cash flow has declined at an average annual rate of over 16% per annum, reflecting good long-term growth in our digital and services businesses offset by declines in print, portfolio changes, recent cyclical and policy factors and adverse exchange rate movements	-16.3%

## Data/Progress

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

## Strategic objectives

## Data/Progress

Transform  
to digital and  
services

Digital and services revenue share  
2010 46.5% 2015 65.0%

£2.1bn £2.9bn

Grow presence  
in emerging  
markets

Emerging markets revenue share  
2010 11.3% 2015 16.4%

£475m £734m

Deliver  
measurable  
impact  
(Efficacy)

- › Reporting programme on track for 2018
- › Growth and impact goals set for 2025
- Product improvements identified by efficacy reviews are being implemented on track with plans

95%

See strategic growth drivers on p04-05 ➔

## Non-financial measures

Deliver  
gender balance

## Gender diversity

	Men		Women	
Board	7	70%	3	30%
Senior managers (excl executive board directors)	68	66%	35	34%
All employees	16,781	41%	24,260	59%

Reduce our  
carbon footprint

Global Greenhouse Gas (GHG) emissions  
Metric tonnes CO<sub>2</sub>e

2015

110,724 -15%

2014

129,742

Maintain  
community  
investment

IMAGE REMOVED

See Our social impact section on p54-67 ➔

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# Operating performance overview

## Developing for access, delivering for outcomes

IMAGE REMOVED

Education is a sector with large growth opportunities for Pearson. The rise of digital and the need for effective learning which better equips students for their future careers are trends which will benefit us in the long term.

Pearson has world class capabilities and products in educational courseware and assessment, powered by learning technology. By combining these capabilities with digital teaching and learning services, we help schools, universities and others to scale online, reach more people and ensure better learning outcomes.

Our primary segments for management reporting are Geographies (North America, Core and Growth), as this is how we drive business performance. This is how we reach learners, through content and digital services in individual classrooms, through broad partnerships with public and private education institutions and, in certain markets, by directly expanding capacity through our own schools and colleges.

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Geography

# North America

Sales

£2.9bn

Adjusted operating profit

£480m

IMAGE REMOVED

Revenues grew 1% in headline terms, due to the depreciation of sterling against the US dollar, but fell by 5% at CER and 1% in underlying terms

In School, strong enrolment growth in Connections Education, good growth in clinical assessment and market share gains in courseware were offset by the impact of a smaller textbook adoptions market and weakness in the open territories in K-12 courseware, and a change in revenue model at Connections Education which records revenue for services charged at cost on a net basis

In Higher Education, market share gains in courseware were offset by lower enrolments (total US college enrolments fell 1.7%, with combined two-year public and four-year for-profit enrolments declining 4.4%, affected by a rising employment rate and regulatory change affecting the for-profit and developmental learning sectors), higher textbook returns and list sales. Strong enrolment growth at Pearson online services was offset by lower revenues from Learning Studio, a higher education learning management system that we are retiring, and the impact of a change in revenue model

In Professional, revenues grew strongly at VUE due to higher volumes of professional certification assessments. Adjusted operating profits rose 8% in headline terms due to currency movements, fell 1% at CER and were up 1% in underlying terms, with contract losses in school assessment and an adverse revenue mix offset by tight cost control and the profit on sale of lists

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## Operating performance continued

North America  
continued

## School

Connections Education, our virtual school business served over 68,000 full time equivalent students through full-time virtual and blended school programmes in 2015, up 11% from 2014 as a result of underlying growth and a new statewide school in North Carolina. Connections manages 30 virtual public schools with three new, full-time state-wide virtual public schools approved for the 2016-17 school year to serve students in Arkansas, Washington and New Mexico. In its annual Parent Satisfaction Survey, 93% of parents of students enrolled in full-time online partner schools "recommend" Connections to other families.

In courseware, revenue declined year-on-year despite strong market share performance, primarily due to a smaller overall adoption market as compared to 2014. Overall market share increased slightly driven by a strong performance in new adoption markets where we won 31% (2014: 25%) of new adoptions competed for, or 29% (2014: 25%) of the total new adoption market

of \$730m in 2015 (2014: \$910m), led by a strong performance in Grades K-6 Social Studies in Texas and Indiana, and in Grades K-6 Science in Oklahoma. We expanded iLit, our digital reading intervention programme, covering a broader range of students including English language learners. Research studies show that students using iLit gain two or more years of reading growth in a year using this tablet-based programme (<http://pearson/PERhf>). We launched ReadyGEN, a K-6 reading series and enVisionMATH2.0, the newest offering in the highly successful enVisionMATH K-6 maths programme.

In State and National Assessments, revenues for the full year declined due to contract losses. High-stakes online test volumes grew strongly, up 130% on 2014 to 26.4 million, as customers transitioned to computer-based testing. Paper-based high-stakes test volumes grew 3% to 32.7 million. Pearson successfully delivered English Language, Arts and Math PARCC assessments to 5.1 million students across ten states and the District of

IMAGE REMOVED

IMAGE REMOVED

Tremayne, General Education Degree graduate, US

Living in Maryland in the United States, Tremayne was 19 years old when he realised that dropping out of high school was a big mistake. "I realised that without a high school diploma or GED no one would hire me." He knew he needed a change, so he turned to the GED Testing Service to help him and found the MyGED portal fit well with his lifestyle, "having the GED portal online was very convenient, very quick. I used to access it on my phone."

Tremayne successfully passed the test and is looking forward to exciting new opportunities, "when I received my diploma, I was so proud of myself."

"I wasn't used to accomplishing much in life and I realised that I could do anything I put my mind to."

He's been accepted into a local community college in Maryland and plans to transfer to a four-year school to study engineering. He hopes one day to start his own construction business.

Columbia ACT Aspire delivered Common Core aligned college and career readiness assessments to 1.3 million students up 67% from 2014 and was chosen for three new state-wide deployments in 2016. The states of Arkansas, Mississippi and Ohio will discontinue PARCC assessments in 2016. We were awarded contracts to deliver the Indiana Statewide Test of Educational Progress (ISTEP), renewed the Puerto Rican Tests of Academic Achievement (PPAA) and parts of the assessments contract awarded by the Texas Education Agency, and extended our contracts to administer the Mississippi Science Test and Mississippi Subject Area Testing Program. We ceased to administer the majority of the current Texas STAAR contract in September 2015. Pearson extended its partnership with the College Board for the SAT assessment with the award of a five-year contract for processing of the redesigned SAT and PSAT assessments. Pearson will continue to provide the essay-scoring component for the SAT until March 2016.

Clinical assessment grew well, benefiting from continued growth of the fifth edition of the *Wechsler Intelligence Scale for Children (WISC-V)*, strong growth in *Behavior Assessment for Children 3e (BASC)* and rapid growth in Q-Interactive, Pearson's digital solution for clinical assessment administration with geographic expansion and continued strong growth in active users to over 9,000 from 4,000 in 2014 with test administrations up over 400% to 1.3 million sub-tests.



Bradford, High school student, US

Bradford attends Hart-Ransom Academic Charter High School, an independent-study high school, which uses Connections Learning for its online learning curriculum. Now in the 11th grade, Bradford likes the online curriculum's rigour, and has taken advantage of Connections Learning's flexibility and self-paced learning to accelerate his education.

"It definitely challenges me academically, and thanks to the online learning, I can pace myself exactly how I need to be paced."

Bradford appreciates the personal attention he's received from his online learning teachers, like his Spanish teacher, who he talks to on the phone, and his Maths teacher, who meets him virtually in the LiveLesson room. "I really like how involved the teachers are with the students."



+11%

Connections Education served over 68,000 Full Time Equivalent students through full time virtual and blended school programmes in 2015, up 11% from 2014.

## Operating performance continued

North America  
continuedIMAGE  
REMOVED

Sterling, University student, US

Sterling is currently a junior in the business school at Texas A & M University and is majoring in marketing. To fulfil a prerequisite for upper-level business classes, Sterling took a State government course online last summer, using REVEL, Pearson's interactive learning programme for the humanities and social sciences. "I learned so much in the course because it wasn't the same thing every time you flipped the page," Sterling explained. "There would be a graph, then a video, and then a picture. And you could get involved with some of the animations."

"I really loved that it was so interactive, because it influenced how well I learned and how quickly I picked up the material."

IMAGE REMOVED

## Higher Education

Gross courseware revenues fell 1.5% (compared to industry gross revenue declines of 2.7%), due to lower college enrolments offset by market share gains. Net revenues declined 5.7% (compared to industry net declines of 7.5%) reflecting the impact of higher returns. Our market share in courseware benefited from strong performance from key titles including *Hubbard Economics 5e*, *Hibbeler Engineering Mechanics 14e* and *Marieb Human Anatomy & Physiology 10e*.

Global digital registrations of MyLab and related products grew 3% to nearly 13 million. In North America, digital registrations grew 3% to almost 11 million with good growth in Science, Business & Economics, Statistics, REVEL and skills applications like Pearson Writer, offset by softness in developmental Mathematics. Faculty-generated case studies indicate that the use of MyLab programmes, as part of a broader course redesign, can support improvements in student test scores and lower institutional cost (<http://pearson/IZxLE>). We launched a suite of features that include Adaptive Practice in our MyLabs to personalise subjects including Mathematics and Nursing practice, Predictive Analytics Early Alerts in Mastering to help science instructors support at-risk students, gamification features in Business and rich learning analytics dashboards in numerous products that offer deep insight into students' progress, performance and engagement.

11m

In North America, digital registrations grew 3% to almost 11 million with good growth in Science, Business & Economics, Statistics, REVEL and skills applications like Pearson Writer.

IMAGE  
REMOVED

In Pearson online services, our higher education Online Program Management (OPM) business, course enrolments grew strongly, up 25% to over 265,000, boosted by strong growth in Arizona State University Online where we renewed our partnership at the start of 2015. We extended our collaboration with Maryville University to launch a Bachelor and Master's in Cybersecurity and a Doctorate in Leadership. Ohio University is partnering with Pearson to launch a Master's in Financial Economics and Public Relations. University of Nevada Reno is partnering to increase access to the Master of Social Work degree programme online. Pearson launched a new managed programmes service model with Cincinnati State Technical and Community College, adapting traditional OPM services to the Community College market signing a landmark ten-year agreement to provide marketing, recruiting, admission and retention services both to online and ground-based programmes.

In enterprise solutions, Pearson signed significant large-scale, enterprise adoptions of cross-discipline digital content, where content is purchased via an upfront course fee and integrated with university IT systems, with Jones County College, National University, Algonquin College and the University of Missouri system. We signed an expanded strategic partnership agreement with Southern New Hampshire University's (SNHU) College of Online and Continuing Education (COCE). Pearson will support curriculum development, online tutoring, enterprise-wide content and data integration, ebooks with a print-on-demand option and data and analytics services, which will provide greater visibility into students' achievement of learning outcomes.

The Charles A. Dana Center at The University of Texas at Austin is collaborating with Pearson to provide webbased course resources to community colleges across Texas that dramatically shorten the time it takes for students to earn college credit in mathematics as part of the New Mathways Project. Three courses were launched in 2015: Foundations Mathematical Reasoning, Statistics Reasoning and Quantitative Reasoning, with more planned in 2016.

Pearson was named as the premier US Green Building Council Education Partner and will offer curriculum and course services to universities, associations, training companies, corporations, and workforce education and apprenticeship programmes. We are partnering with Broward College to launch new competency-based workforce certification pathways focused on IT and Healthcare. Pearson will support Broward's strategy by providing 12 industry certifications with existing workforce education courseware, as well as curriculum development services to build new courses towards certification and the Acclaim badging platform.

#### Professional

In professional certification, VUE global test volumes grew 11% year-on-year to 14.2 million, boosted by continued growth in IT, Professional and GED, with increased volumes from Microsoft Certified Professional (MCP) Program globally, National Council of State Boards of Nursing and US teacher certification programmes. VUE renewed the Certipoint Microsoft Office Specialists and Microsoft Technology Associate programmes for an additional year and extended our partnership with Cisco Systems for three and a half years.



## Operating performance continued

### Geography

# Core

Sales

£836m

Adjusted operating profit

£114m

Revenues declined by 8% in headline terms, 5% at CER and in underlying terms

Growth in Pearson online services in Australia, Wall Street English in Italy, Clinical Assessment in Germany and the Pearson Test of English in Australia was more than offset by revenue declines in UK qualifications as the business nears the end of a period of policy change, revenue declines at VUE, phasing and market weakness in Australian higher education courseware and the focusing of our UK school courseware on products that directly support Pearson Qualifications. Adjusted operating profit (excluding the FT, The Economist and Mergermarket) declined 2% in underlying terms due to lower revenue offset by tight cost control.

IMAGE REMOVED

Read about Sarah and Pearson College on p26 ➔

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IMAGE REMOVED

## Operating performance continued

### Core continued

#### School

In assessment, UK qualifications have been impacted by government policy, where changes to accountability measures have led to a further 20% decline in BTEC registrations in 2015. GCSE and GCE entries for summer 2015 grew modestly compared with 2014, resulting from increases in GCSE registrations in Sport, ICT and Business and strength in iGCSE entries. We successfully delivered the National Curriculum Test for 2015, marking 4 million scripts from 1.7 million students and successfully transitioned the marking of the test to an online-only model.

In courseware, UK School revenue fell with growth in primary school more than offset by declines in secondary, as the vocational market contracted and our upper secondary revenues were impacted by lower market participation as we focus on products

that directly support our qualifications. More than 5,400 UK schools now subscribe to at least one Bug Club service, our primary school blended reading programme, representing growth of nearly 16% in the year. There are over 1.8 million pupils, more than 9,000 schools and 152,000 teachers currently using a service on ActiveLearn Primary. Italy revenues declined slightly with market share gains in primary offset by market weakness and a lower share in upper secondary. Australia revenues declined, with growth and increased market share in primary more than offset by a weaker secondary market.

Clinical assessment grew well with Germany benefiting from strong growth in *Kaufman Assessment Battery for Children* (K-ABC), partly offset by declines in Australia, after a strong year in 2014 driven by the release of Wechsler Primary and Preschool Scale of Intelligence IV.

IMAGE  
REMOVED

IMAGE  
REMOVED

Sarah, Pearson College London student, UK

Sarah works in the marketing team at Nestlé, having graduated from Pearson College London last September. She says "Education gave me the confidence to take a step back from a career path that I was unhappy with and find a new direction. It gave me the flexibility to study a full degree in two years which enabled me to get back on my career ladder as soon as possible."

"Pearson College London gave me the skills to impress at interview, the knowledge to succeed in my new role and the confidence to apply in the first place."

"Through the degree, and the environment, I was able to understand what I wanted from a career and find the right move for me."

IMAGE  
REMOVED

IMAGE  
REMOVED

Noel, Pearson VUE customer, UK

The Chartered Institute of Management Accountants (CIMA) has worked in partnership with Pearson VUE to transform its portfolio of professional-level exams from pen and paper to computer-based testing. Noel Tagoe, Executive Director of CIMA, says "By maximising the opportunities offered through technological advances in computerised assessment, we can access a wide range of testing methods, assess a variety of skills and competencies at different levels, and offer much greater flexibility for where and when examinations are taken. All of which will be of tremendous benefit to both students and, importantly, employers. These changes will take full advantage of the role that technology plays in the lives of the younger generation, and reflect the evolution in the workplace."

### Higher Education

In courseware, UK revenues declined, primarily due to a weak market. In Australia, revenues declined significantly due to phasing and market weakness.

In online services, our Australian University Partnerships business grew strongly with combined course enrolments of nearly 4,000, up 380% from 2014. The growth of our partnership with Monash University was led by the Graduate Diploma in Psychology, which is now one of Monash's largest postgraduate courses. Our new partnership with Griffith University started very strongly, seeing consistent demand for the MBA programme and the launch of two further courses. Kings College London partnered with Pearson to launch online postgraduate degree programmes in Psychology and Law.

Total enrolled students at Pearson College doubled to 232.

### Professional

The Pearson Test of English Academic (PTEA) saw strong growth in test volumes and revenues after gaining approval from the Australian Department of Immigration and Border Protection to administer a broad range of language tests linked to visa applications.

Wall Street English revenues fell slightly with strong growth in Italy offset by declines in Germany.

IMAGE  
REMOVED

**Stephanie, Winner of Outstanding BTEC Student of the Year Award 2015, UK**

Stephanie studied a Level 3 Diploma in Health and Social Care at Penwith College in the UK. She is passionate about helping others and her outstanding achievements in college and in the local community marked her out to the BTEC Award judges as truly outstanding.

Stephanie supported herself financially with paid employment as a community carer alongside her BTEC. She juggled long working hours with her studies, yet still far exceeded the 100-hour work experience requirements of her course, completing a range of placements in hospital wards, care homes and day care centres. She also participated in many local voluntary projects working with individuals in her community who are isolated and lonely.

IMAGE  
REMOVED

## Operating performance continued

## Geography

# Growth

Sales

£692m

Adjusted operating loss

-£12m

Revenues fell 4% in headline terms, were flat at CER and fell 1% in underlying terms

In China, revenues grew modestly reflecting strong sales of premium services in our direct delivery English Language Learning businesses offset by list disposals. In Brazil, revenues were stable with good growth in private sistemas and language schools, offset by declines in government funded sistemas and language schools. In South Africa, revenues declined significantly due to a smaller textbook adoption cycle and lower enrolments at CTI, due to a reduction in the number of qualified students graduating from high school and tightening consumer credit affecting re-enrolment rates. In the Middle East, our business was impacted by the withdrawal from the Saudi Arabian Colleges of Excellence.

Adjusted operating profit decreased £44m to a loss of £12m due to the strengthening of Sterling against key Emerging Market currencies, revenue declines in South Africa, a contract termination charge arising from the transition of our three Saudi Colleges to new providers, cost inflation and additional investment in China, partially offset by the benefits of restructuring and integration in Brazil.

IMAGE REMOVED

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## Operating performance continued

### Growth continued

#### School

In South Africa, there was continued pressure on Government spending on textbooks due to budget pressures, which resulted in the value of the textbook market falling 60% from a peak of R2.9bn in 2013 to an estimated R1.15bn in 2015. We continued to perform well competitively and maintained a leading market share.

In Brazil, sistemas revenues grew well with strong growth in private sistemas partly offset by declines in NAME, our public sistema, following the cancellation of a large contract as a result of government spending cuts. Overall sistema enrolments fell 7% to nearly 449,000 with declines in NAME partly offset by growth in our three private sistemas, led by our largest sistema, COC. More than half of COC schools that participated in the High School National Exam (ENEM) ranked among the top three schools in their municipalities.

In India, enrolments at our managed schools grew 14% to nearly 27,000 students and we launched a pilot in more than 60 schools of MyPedia, an inside service 'sistema' solution for schools comprising print and digital content, assessment and academic support services.

Middle East school courseware and professional development revenues grew strongly on improved distribution.

#### Higher Education

In South Africa, after strong growth over a number of years, student enrolments at CTI universities fell by 16% to 11,300 driven by a 13% decline in qualified graduating high school students and tightening consumer credit affecting re-enrolment rates.

In Mexico, our fully accredited online university partnership, UTEL, increased the number of students enrolled by 34% to nearly 12,600.

IMAGE  
REMOVED

IMAGE  
REMOVED

Mpho, MGI graduate, South Africa

Mpho Nethengwe is a 28 year-old MGI graduate who is now a Writing and Communication Skills and English Lecturer at her alma mater in Midrand. She says:

"The skills I acquired at MGI made it easier for me to step into my role in the working world. I am able to take on every challenge as it comes, to reflect on, evaluate and improve on what to do in order to remain productive."

Mpho has ambitions of putting her learning and experience into practice, even exploring a possible future career in communications at Pearson. We think she'd be a real asset.

+14%

Enrolments at our managed schools in India grew 14%

IMAGE REMOVED

In India, Higher Education courseware revenues grew strongly. Cornell University partnered with Pearson to launch the *Cornell-ILR Experienced Managers Programme* in India, with a blended learning approach combining online and in-person instruction.

In the Middle East, our three-year partnership with Taibah University in Saudi Arabia, to enable its transformation to a fully blended and personalised learning model, is progressing with over 4,000 students enrolled in our solution in 2015. Our partnership with the Preparatory Year Deanship at Um Al Qura University (PYP-UQU), to provide online learning and assessment technology has delivered 13,000 MyMathLab, MyITLab and MasteringPhysics licences. We withdrew from an agreement to run three Saudi Arabian Colleges of Excellence, with the colleges transitioning to new providers from 30 June 2015. This resulted in a termination charge.

**+34%**

In Mexico, our fully accredited online university partnership, UTEL, increased the number of students enrolled by 34%.

IMAGE REMOVED

IMAGE  
REMOVED

Alvir, English student, Brazil

Alvir is a 17 year-old who has been studying at Wizard for three years. In the beginning, studying English was only a way to remember his father, who used to love the language. But studying evolved into something bigger and helped him to achieve his goals, he got his first job as an assistant teacher at Wizard, and took the TOEIC exam, achieving the maximum 990 points. Alvir says that English has helped him to meet new people and now his goal is to live abroad some day.

IMAGE REMOVED

## Operating performance continued

### Growth continued

#### Professional

In Pearson English, good growth in direct delivery in China, private expenditure in language schools in Brazil, and English Language Teaching (ELT) was partly offset by the impact of lower public expenditure in language schools in Brazil

In China, Wall Street English (WSE) achieved strong revenue growth, reflecting success in the premium segment and the growth in VIP branded offerings. Overall enrolments grew modestly to over 67,000 with new enrolments growing strongly. We launched the New Student Experience (NSE) in six pilot centres during December 2015. The NSE delivers a major upgrade to the Wall Street English service with adaptive, personalised learning incorporating Pearson's Global Scale of English.

Global Education achieved moderate revenue growth as the market shifted to more intensive premium courses with smaller class sizes and new products, which resulted in enrolments declining 6.5% to 85,110.

We launched around 30 new MyEnglishLab products including *Top Notch 3e* and *Progress MyTOEFL* Lab and the second edition of MyIELTS Lab successfully launched in China in WSE and Global Education. Global student registrations for MyEnglishLab and other ELT digital courseware grew 14% to 739,000. Pearson Test of English grew strongly in India.

Grupo Multi in Brazil saw strong revenue growth at Wizard, our consumer-facing franchised English language learning business, but this was offset by declines in government orders due to public spending cuts. We opened 40 new school-in-school units for Multi English franchises in K-12 sistemas partner schools.

IMAGE  
REMOVED

Angelina, Wall Street English graduate, China

Angelina runs a wedding planning company in Shenzhen, China. Learning English with Wall Street English has enabled her to attract more international clients. She is now qualified with a top wedding planning institution in North America and is realising her dream of giving couples their perfect wedding memories.

IMAGE  
REMOVED



## Penguin Random House

Pearson owns 47% of Penguin Random House, the first truly global consumer book publishing company

Penguin Random House had a strong performance in 2015, boosted by publication of hundreds of Adult and Children's bestsellers across its territories, including the fiction mega-successes of *Grey* and *The Girl on the Train*, which each sold over 7 million copies worldwide

The US business published 584 *New York Times* print and ebook bestsellers in 2015 (2014 760, based on a broader *New York Times* title count than 2015). The division benefited from the multi-million copy successes of *Grey* by E L James and the Adult debut novel *The Girl on the Train* by Paula Hawkins. Children's authors who extended their outstanding sales in 2015 include Dr Seuss, John Green, R J Palacio, James Dashner, Rick Yancey, Drew Daywalt, and Oliver Jeffers. Additional notable Adult titles include *The Life-Changing Magic of Tidying Up* by Marie Kondo, *Rogue Lawyer* by John Grisham, *Lost Ocean* by Johanna Basford, *Between The World and Me* by Ta-Nehisi Coates, and the movie tie-in paperback *The Martian* by Andy Weir.

The UK business published 201 titles on the *Sunday Times* bestseller lists (2014 206). The division enjoyed outstanding sales for *Grey* and *The Girl on the Train*, which each sold more than 2 million UK copies, and for Harper Lee's *Go Set A Watchman* and Jamie Oliver's *Everyday Super Food*. Great demand continued for Jeff Kinney's *Diary of a Wimpy Kid* and John Green's titles, and for DK Publishing's Star Wars publications.

Penguin Random House's promising 2016 publishing lists include new titles from Lisa Brennan-Jobs, Bill Bryson, Lee Child, Harlan Coben, Phil Collins, Janet Evanovich, Ina Garten, John Grisham, Jazz Jennings, Jeff Kinney, Marie Kondo, John le Carre, Jojo Moyes, Jamie Oliver, James Patterson, Nathaniel Philbrick, Pope Francis, Nora Roberts, John Sandford, Danielle Steel and Star Wars.

Penguin Random House completed the sale of Author Solutions, its supported self-publishing services company, to an affiliate of Najafi Companies, an international private-investment firm, on 31 December, and sold its Australian online bookseller Bookworld to online retailer Booktopia in August.

The integration of Penguin and Random House continued to provide net benefits through organisational alignments and systems, and warehouse combinations in 2015, as well as for 2016 and thereafter. The North America warehouse consolidation was completed in February 2015, and in December, the UK business announced it will be gradually closing its Rugby distribution centre and relocating its inventory to two other locations. The integration in Spain and Latin America of Santillana with Grupo Editorial Penguin Random House remains on course.

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## Other financial information

### Net finance costs

All figures in £ millions	2015	2014
Net interest payable	(46)	(64)
Finance income in respect of employee benefit plans	4	1
Other net finance costs	13	(30)
Net finance costs	(29)	(93)

Net interest payable in 2015 was £46m, compared to £64m in 2014. The majority of the movement in net interest payable is due to the release of accrued interest following agreement of historical tax positions. For our debt portfolio, our fixed rate policy reduces the impact of changes in market interest rates, however we were still able to benefit from low average US dollar interest rates during the year as the majority of the Group's debt is US dollar denominated. Year-on-year, average three-month US dollar LIBOR rose by 0.1% to 0.3%. This slight increase in floating market interest rates, along with the impact of changes in our debt portfolio, foreign exchange translation and the effect of slightly lower levels of average net debt in the period led to little change in the year-on-year interest charge on debt. Interest receivable on cash balances held overseas was reduced from the prior year due mainly to the weakening of emerging market currencies against sterling. The Group's average net debt fell by £61m, largely as a result of disposals in the fourth quarter of 2015 offsetting the translation of our predominantly US dollar debt. These combined factors contributed to the overall decrease in the Group's average net interest payable from 3.6% to 2.7%.

Finance income and costs relating to retirement benefits have been excluded from our adjusted earnings as we believe the income statement presentation does not reflect the economic substance of the underlying assets and liabilities. Also included in the statutory definition of net finance costs (but not in our adjusted measure) are finance costs for deferred consideration associated with acquisitions, foreign

exchange and other gains and losses. Finance costs for deferred consideration are excluded from adjusted earnings as they relate to the future potential acquisition of non-controlling interests and do not reflect cash expended. Foreign exchange and other gains and losses are excluded from adjusted earnings as they represent short-term fluctuations in market value and are subject to significant volatility. Other gains and losses may not be realised in due course as it is normally the intention to hold the related instruments to maturity.

In 2015, the total of these items excluded from adjusted earnings was a gain of £17m compared to a loss of £29m in 2014. Both the gain in 2015 and the loss in 2014 mainly relate to foreign exchange differences on unhedged cash and cash equivalents and other financial instruments.

### Funding position and liquid resources

The Group finances its operations by a mixture of cash flows from operations, short-term borrowings from banks and commercial paper markets, and longer-term loans from banks and capital markets. Our objective is to secure continuity of funding at a reasonable cost from diverse sources and with varying maturities. The Group does not use off-balance sheet special purpose entities as a source of liquidity or for any other financing purposes. The net debt position of the Group is set out below.

All figures in £ millions	2015	2014
Cash and cash equivalents	1,703	530
Marketable securities	28	16
Net derivative financial instruments	(55)	40
Bonds	(2,284)	(2,173)
Bank loans and overdrafts	(38)	(42)
Finance leases	(8)	(10)
Net debt	(654)	(1,639)

The largest contributors to the decrease in net debt are the receipt of disposal proceeds, offset by changes in the value of gross debt due to exchange rates and a decrease in the value of our derivative portfolio. Reflecting the geographical and currency split of our business, a large proportion of our debt is denominated in US dollars (see note 19 for our policy). The strengthening of sterling against the US dollar during 2015 (from \$1.56 to \$1.47 £1) increases the sterling equivalent value of our reported net debt.

At the year end, the long-term ratings were Baa1 from Moody's and BBB+ from Standard and Poor's, and the short-term ratings were P2 and A2 respectively. Both long-term ratings were on negative outlook at the year end. In March 2016, Standard & Poor's changed Pearson's long-term rating from BBB+ (Negative) to BBB (Stable). The short-term ratings from Moody's and Standard & Poor's remain unchanged at P2 and A2.

In April 2015, the Group accessed the capital markets, raising €500m through the sale of notes maturing in May 2025 and bearing interest at 1.375%. The notes were swapped to floating rate in US dollars to conform with the policy described in note 19. The Group has a \$1,750m committed revolving credit facility. During the year, the maturity of the facility was extended by one year. The facility now matures in August 2020. At 31 December 2015 this facility was undrawn. The revolving credit facility is used for short-term drawings and providing refinancing capabilities, including acting as a back-up for our US commercial paper programme. This programme is primarily used to finance our US working capital requirements, in particular our US educational businesses which have a peak borrowing requirement in July. At 31 December 2015, no commercial paper was outstanding. The Group also maintains other committed and uncommitted facilities to finance short-term working capital requirements in the ordinary course of business. Further details of the Group's approach to the management of financial risks are set out in note 19 to the financial statements.

### Taxation

The effective tax rate on adjusted earnings in 2015 was 15.5% compared to an effective rate of 17.9% in 2014. Our overseas profits, which arise mainly in the US, are largely subject to tax at higher rates than that in the UK (which had an effective statutory rate of 20.25% in 2015 and 21.5% in 2014). These higher tax rates were largely offset by amortisation-related tax deductions and by adjustments arising from agreement of historical tax positions. Both these items were more significant in 2015 than they had been in 2014.

The reported tax benefit on a statutory basis in 2015 was £81m (18.7%) compared to a charge of £56m (22.0%) in 2014. The statutory tax benefit in 2015 is mainly due to benefits arising on the increase in intangible charges. Operating tax paid in 2015 was £129m compared to £163m in 2014.

### Discontinued operations

Discontinued operations in 2015 relate to the sale of the Financial Times and the Group's 50% interest in The Economist. The Economist sale was substantially completed on 16 October 2015 and realised a gain of £473m before tax. The sale of the Financial Times completed on 30 November 2015 and realised a gain of £711m before tax. We expect both of these transactions to qualify for substantial shareholder exemption in the UK. The gains on these transactions and the results for both 2014 and 2015 to the respective sale dates have been included in discontinued operations.

The sale of Mergermarket to BC Partners, completed on 4 February 2014, resulted in a gain of £244m before tax. The gain on sale and the results for 2014 to the date of sale have been included in discontinued operations. Also included in discontinued operations in 2014 is a gain of £29m relating to adjustments to liabilities arising on the formation of the Penguin Random House group. Although this transaction completed in 2013 there were subsequent adjustments relating to the potential transfer of pension liabilities and tax.

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## Other financial information continued

### Other comprehensive income

Included in other comprehensive income are the net exchange differences on translation of foreign operations. The gain on translation of £175m in 2014 compares to a loss in 2015 of £69m and is principally due to movements in the US dollar. A significant proportion of the Group's operations are based in the US and the US dollar strengthened in 2015 from an opening rate of £1 \$1.56 to a closing rate at the end of 2015 of £1 \$1.47. However at the same time other currencies have weakened compared to sterling and this effect was more than enough to offset gains on the US dollar. At the end of 2014 the US dollar had also strengthened in comparison to the opening rate moving from £1 \$1.66 to £1 \$1.56 and other currencies did not weaken to the same extent as they have done in 2015.

Also included in other comprehensive income in 2015 is an actuarial gain of £118m (including a £8m gain in respect of associates) in relation to pension and other post retirement plans. This gain mainly arises from a higher discount rate used to value the liabilities. The gain compares to an actuarial gain in 2014 of £8m (including a £15m loss in respect of associates).

### Dividends

The dividend accounted for in our 2015 financial statements totalling £423m represents the final dividend in respect of 2014 (34 Op) and the interim dividend for 2015 (18 Op). We are proposing a final dividend for 2015 of 34 Op, bringing the total paid and payable in respect of 2015 to 52 Op, a 2% increase on 2014. This final 2015 dividend which was approved by the board in February 2016, is subject to approval at the forthcoming Annual General Meeting and will be charged against 2016 profits. For 2015, the dividend is covered 1.4 times by adjusted earnings. We plan to hold our future dividend at the 2015 level while we rebuild cover.

### Post-retirement benefits

Pearson operates a variety of pension and post-retirement plans. Our UK Group pension plan has by far the largest defined benefit section. We have some smaller defined benefit sections in the US and Canada but, outside the UK, most of our companies operate defined contribution plans. In addition to pension plans we also operate post-retirement medical benefit plans (PRMBs), the most significant of which is in the US. In 2014 we amended the eligibility criteria for the US PRMB plan. This amendment resulted in a curtailment gain and a reduction in the ongoing service cost of the plan.

The charge to profit in respect of worldwide pensions and retirement benefits for continuing operations amounted to £81m in 2015 (2014: £70m) of which a charge of £85m (2014: £71m) was reported in adjusted operating profit and an income of £4m (2014: £1m) was reported against other net finance costs. The increase charge in 2015 is in part due to the US PRMB curtailment gain taken in 2014 and an increase in costs relating to our defined contribution plans.

The overall surplus on the UK Group pension plan of £190m at the end of 2014 has increased to a surplus of £337m at the end of 2015. The movement has arisen principally due to continuing asset returns, deficit funding and favourable movements in the assumptions used to value the liabilities. In total, our worldwide net surplus in respect of pensions and other post-retirement benefits increased from a net asset of £27m at the end of 2014 to a net asset of £198m at the end of 2015.

### Goodwill and Intangible assets

Following significant economic and market deterioration in the Group's operations in emerging markets and ongoing cyclical and policy related pressures in the Group's mature market operations, management's expectations of future returns were revised down in the course of 2015. It was determined

during the goodwill impairment review that the fair value less costs of disposal of the Growth, North America and Core cash generating units (CGUs) no longer supported the carrying value of the goodwill. An impairment of £507m was booked in respect of the Group's Growth operations, representing impairments of £269m in the Brazil CGU, £181m in the China CGU, £48m in the South Africa CGU and £9m in the Other Growth CGU, thereby bringing the carrying value of goodwill in those CGUs down to £nil. Impairments of £10m and £13m were also booked in respect of other acquired intangibles in the South Africa and Other Growth CGUs respectively, bringing their carrying value down to £nil. Impairments of £282m and £37m were also booked in respect of the North America and Core CGUs respectively, bringing the carrying value of the goodwill in those CGUs down to fair value less costs of disposal.

In 2014 following deterioration in the market conditions for the Group's online tutoring business based in India, it was determined in the course of the impairment review that the value in use of the India CGU no longer supported the carrying value of the goodwill in that CGU. An impairment of £67m was booked, thereby bringing the carrying value of goodwill in the India CGU down to £nil. An impairment of £10m was also booked in respect of other acquired intangibles in that CGU, bringing their carrying value to £nil. Further details on these impairments are included in note 11 of the financial statements.

#### Acquisitions and disposals

There were no significant acquisitions in 2015. The acquisition of Grupo Multi, Brazil's leading adult English language training company, for £437m (plus £49m in net debt assumed) was announced in December 2013 and completed on 11 February 2014.

During 2015 the Group disposed of its interest in the FT Group including its 50% share of The Economist. The Financial Times sale to Nikkei was completed on 30 November 2015 for consideration of £858m and realised a gain on sale of £711m before a tax charge of £49m. The sale of our 50% share of The Economist Group to EXOR was substantially completed on 16 October 2015. The value of the investment in The Economist on Pearson's books was not significant and there was no tax on the transaction with the result that the gain on sale of £473m largely reflects the proceeds received. Also, in July 2015, the Group disposed of its interest in PowerSchool for consideration of £222m realising a pre-tax gain of £30m net of a £70m write down of related software assets.

The sale of the Mergermarket group of companies in 2014, as noted above, realised a profit before tax of £244m. In addition, in 2014, our North America business disposed of its joint venture interests in Safari Books Online and CourseSmart, realising a profit before tax of £40m, and its investment in Nook Media realising a loss before tax of £38m.

#### Return on invested capital (ROIC)

Our ROIC is calculated as total adjusted operating profit less cash tax, expressed as a percentage of average gross invested capital. ROIC increased from 5.6% in 2014 to 5.8% in 2015. Reduced tax payments were the main reason for the movement.

#### Related party transactions

Transactions with related parties are shown in note 35 of the financial statements.

#### Post-balance sheet events

In January 2016, Pearson announced that we are embarking on a restructuring programme to simplify the business, reduce costs and position the company for growth in its major markets. The majority of the programme is expected to be complete by mid-year 2016 and will involve implementation costs in 2016 of approximately £320m.

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## Risk management

The board has carried out a robust assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity. Our principal risks and uncertainties are outlined below, along with a description of how they are being managed.

See pages 82 to 89 in 'Governance' for details on the board and audit committee's risk oversight during 2015, their ongoing monitoring of risks, including deep dives into selected principal risks and the annual effectiveness review.

The goal of our risk management approach is to support Pearson in meeting its strategic and operational objectives of growth and simplification as set out in the chief executive's overview on pages 4 to 7, so that the key business risks are identified, assessed and mitigated. Our aim is to manage risks, understanding that many risks are external in nature and cannot therefore be fully controlled.

### How we manage risk

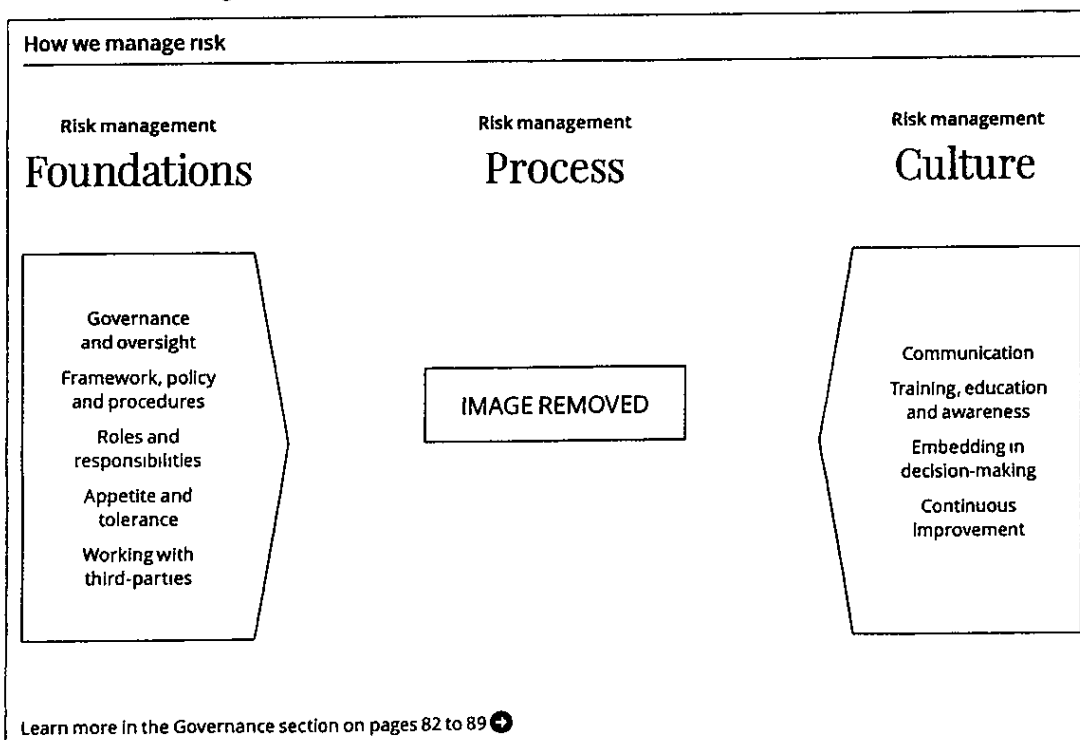
We assessed our risk management maturity in 2014 and made improvements in 2015 towards our 2017 target. The diagram 'how we manage risk' shows our approach to embedding a Pearson-wide risk culture. This framework is being used to drive improvements in

risk management across Pearson, taking a pragmatic approach that assists in eliminating inefficiencies and identifying and closing gaps. Our Enterprise Risk Management (ERM) framework has been developed to be aligned with international standards (COSO and ISO31000) and it aids our compliance with the Financial Reporting Council's (FRC) UK Corporate Governance Code guidance. Risk identification and assessment were also included in the 2015 strategic planning and acquisition processes, to further embed risk management in decision making.

### Identifying and assessing risk

The board is ultimately responsible for the oversight of risk management, assisted by the assurance the audit committee provides with regard to the procedures for the identification, assessment and reporting of risk.

Throughout the year (twice as a minimum), the identification of principal risks is informed using a bottom up and top down approach through discussions with each business area, identifying new risks as well as re-assessing those already being monitored. To aid in the identification of risks and development of associated mitigating actions, risks are categorised into four main areas: strategy and change, operational, financial, and legal and compliance.



The probability of a risk materialising and the potential impact of each risk across multiple parameters is rated based on existing controls, then the adequacy of action plans to address any remaining control gaps is also assessed. Those risks which have a higher probability and significant impact on strategy, reputation or operations, or a financial impact greater than £50m are identified as principal risks.

Pearson executives have oversight of risks relevant to their areas of responsibility, which were included in their 2015 objectives. Management is responsible for executing appropriate actions to mitigate risks where required and whenever possible. It is not possible to identify every risk that could affect our businesses, and the actions taken to mitigate the risks described below cannot provide absolute assurance that a risk will not materialise and/or adversely affect our business or financial performance.

The outputs of the risk assessments described above and below are reported to the audit committee and board in detail. In addition to the company-wide risks, this includes risk maps for our main Pearson business areas and geographies.

### Risk appetite

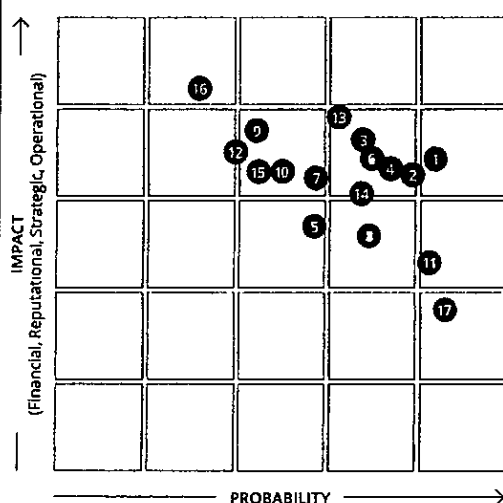
Risk appetite is the target level of risk the board finds appropriate to accept in order to achieve Pearson's strategy and goals. Further work was done in 2015 to define the risk appetite for each of our principal risks, working with the Pearson executive. Recommendations are made annually to the board, as part of the board's oversight of risk management (see page 88 in 'Governance' for more on the board's governance of risk management).

The semi-annual risk assessment reviews take into account the current level of risk compared to appetite. A consideration of target risk appetite is now included in key business decisions, such as acquisitions and strategic planning.

There are certain risk areas where we have a very low appetite, such as complying with all applicable laws, including those on anti-bribery and corruption or the safety and security of learners. This means that we take actions to try to avoid or eliminate this risk as far as possible. In other areas, such as strategy and change, we recognise the importance of managed risk-taking in order to achieve business objectives and goals.

### Our principal risks (as of 31 December 2015)

Outlined here are our most significant risks that may affect our future. We assess the probability of the risk materialising and the impact of the risk. The risks with greatest potential severity are identified as principal risks.



- |                            |  |
|----------------------------|--|
| STRATEGY AND CHANGE RISKS  | 1 Business transformation and change               |
|                            | 2 Digital and services evolution and market forces |
|                            | 3 Talent   |
|                            | 4 Political and regulatory risk                    |
|                            | 5 Acquisitions, divestments and JVs                |
| OPERATIONAL RISKS          | 6 Testing failure                                  |
|                            | 7 Safety and security                              |
|                            | 8 Customer facing systems                          |
|                            | 9 Safeguarding and protection                      |
|                            | 10 Business continuity (new risk)                  |
| FINANCIAL RISKS            | 11 Tax   |
|                            | 12 Treasury (new risk)                             |
| LEGAL AND COMPLIANCE RISKS | 13 Data privacy and information security           |
|                            | 14 Intellectual property                           |
|                            | 15 Competition law (new risk)                      |
|                            | 16 Anti-bribery and corruption                     |
|                            | 17 Data quality and integrity (new risk)           |

## Risk management continued

### Key changes to Pearson risks in 2015

The key themes arising from company-wide risk discussions in 2015 reflect those of our strategic goals – simplification and growth, underpinned by business transformation and change to enable these. As highlighted in the chief executive's strategic overview on page 4, 2015 was a year of change for Pearson. The theme of change is reflected in the relatively high probability of our principal risks, as shown in the map. The level of change increases risk short term, however in the medium to longer term it will enhance our controls for many of our risks, as well as enabling Pearson to achieve its goal of becoming more efficient, simplifying the way we work for our customers and learners.

More robust risk assessments in 2015 have improved our understanding of the nature and scale of risks, such as data privacy and information security (highlighted in the audit committee chair's statement on page 83) where external threats continue to increase and we have programmes of work to close identified gaps.

Good progress has been made in implementing mitigation plans, especially for those risks with lower target risk appetite, such as for ABC and in our direct delivery businesses, where risks such as the safety and security of both our learners and staff have new roles and defined plans underway (both highlighted in the audit committee chair's statement on page 83).

### Risk assessment of prospects and viability

This section should be read together with the full viability statement on page 118 ➔

Pearson's principal risks and our ability to manage them as outlined in this section are linked to our viability as a company. These risks have therefore been taken into account when preparing the viability statement.

The board assessed the prospects of the company over a three-year period, longer than the minimum 12 months of the annual going concern review. The three-year period corresponds with Pearson's strategic planning process and represents the time over which the company can reasonably predict market dynamics and the likely impact of additions to the product portfolio.

The board discusses the company's strategic plan on an annual basis taking account of a range of factors including market conditions, the principal risks to the company, product and capital investment levels as well as available funding. Pearson's strategy and business model are discussed in more detail on pages 2 to 9.

In assessing the company's viability for the three years to December 2018, the board overlaid a 'severe but

### Key assumptions

The key assumptions which underpin our three-year strategic plan to December 2018 are as follows:

- 1 The key cyclical and policy factors that have recently hurt Pearson (US college enrolments and UK qualifications) should stabilise by the end of 2017 and improve modestly thereafter, helped by new product launches.
- 2 Pearson makes modest market share gains in North America higher education subjects where next generation courseware is being launched.
- 3 US state testing revenues continue to decline through 2017, as current contracts unwind, before stabilising in 2018.
- 4 Professional certification and clinical assessment revenues continue to grow.
- 5 Pearson businesses in China and Brazil benefit from the launch of new products, including the Wall Street English New Student Experience.
- 6 Pearson's services businesses (for example, online programme management, virtual schools, blended learning in English) continue to grow as new platforms and products come to market and capitalise on market growth.
- 7 The benefits of the company's restructuring plan are delivered in full, with minimal disruption to sales, market share and operations from this major programme of change.

plausible' downside scenario onto base case strategic plan for the group, focusing on the impact of the following assumptions and key risks:

- › Further revenue shortfalls in US assessments
- › Further revenue shortfalls in higher education courseware assuming enrolments remain flat.
- › Additional revenue shortfalls in growth markets (principally South Africa, Brazil and China) driven by weaker local economic conditions
- › Business transformation and change execution risk associated with timely delivery of the restructuring programme in 2016 causing the benefits to be delayed or not fully realised.

The board also stress tested the impact on our liquidity of all the principal risks listed above occurring together. Although this is not regarded as a plausible scenario the test showed that the company would still have liquid resources subject to a limited number of management actions.

The board's confirmation of Pearson's viability for the three years to 2018 is included alongside the going concern statement on page 118.



# Principal risks and uncertainties

## Strategic and change risks

Risk	2015 activities	2016 plans
<b>1</b> <b>Business transformation and change</b>  The pace and scope of our business transformation initiatives increase the execution risk that benefits may not be fully realised, costs of these changes may increase, or that our business as usual activities do not perform in line with our plans, or our level of customer service may not meet expectations.	<p>2015 was a year of change for Pearson. A number of major transformational change programmes commenced in 2015, including the Enabling Programme – a programme of work to deliver a single Pearson-wide solution to integrate our data systems and processes across HR, Finance, Procurement and Supply Chain), OneCRM and Technology Delivery Centre (TDC) and these continue into 2016. The Enabling Programme runs until 2018 and will deliver sustainable improvements in finance, human resources and operations.</p> <p>In addition to usual good practices in place for project and change management, there is enhanced governance, monitoring and reporting in place for these most significant change initiatives.</p>	<p>At the end of 2015 we undertook a rigorous bottom up review of our markets, operations and financial plans. The chief executive's strategic overview on pages 4 to 7 describes our plans for transforming Pearson. In 2016, we will further simplify our business, reduce our costs and position ourselves for growth in our major markets.</p> <p>The success of the restructuring plan is a key assumption underpinning achieving our goals by 2018, showing how critical it is that this risk is effectively managed.</p>
<b>2</b> <b>Digital and services evolution and market forces</b>  Failure to invest successfully in and deliver the right products and services.	<p>Our global education strategy will drive a faster move to digital and services, recognising that this is a significant opportunity for Pearson, as well as a potential risk. We are transforming our products and services for the digital environment along with managing our print inventories. The 2015 strategic planning process took a more in-depth review and challenge of areas for future investment and re-investment.</p> <p>As indicated in the section above on risk assessment of our prospects and viability, we take into account cyclical market factors in our strategic planning process.</p> <p>The Global Product Lifecycle continued to be embedded across Pearson and won an award for Best Innovation Programme at the Corporate Entrepreneur Awards.</p> <p>You can read more about the Product Lifecycle and its governance on page 61 in the 'Social Impact' section.</p>	<p>Turning this risk into an opportunity – successfully investing in and delivering the right products and services – is key to our strategy for returning to growth by 2018.</p> <p>In the chief executive's strategic overview on pages 4 to 7, we have laid out a strategy for returning to growth. We are combining our lines of business for courseware into a single product organisation, as well as rationalising and integrating our product development capabilities to focus on more adaptive, personalised 'next generation' courseware and we are increasing our assessment focus on more adaptive and personalised online services.</p>

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## Principal risks and uncertainties continued

Strategic and change risks		
Risk	2015 activities	2016 plans
<b>3</b> Talent Failure to attract, retain and develop staff including adapting to new skill sets required to run the business	<p>Throughout 2015, we have been successful in promoting our best internal talent and recruiting individuals who are global leaders in their specific field. Globally consistent performance assessment, and talent and succession management approaches are in place, and the annual engagement survey shows consistent scores overall from the prior year.</p> <p>See pages 59 to 63 in 'Social Impact' for more detail on key findings from the engagement survey, as well as information about our approach to learning and development.</p>	<p>As we are going into a period of change and transformation, we will focus on a number of areas that are key to mitigating talent risk, including: clear employee objectives and development plans, an all-employee engagement survey, with action plans as appropriate, succession planning and talent management, an internal management and leadership development programme supporting 'learning for all'. The employee incentive pool will also be reinstated.</p>
<b>4</b> Political and regulatory risk Changes in policy and/or regulations have the potential to impact business model and/or decisions across all markets	<p>We are expanding our global public affairs capability with a specific focus on coordinated international government relations across our key markets. Building deeper government relations, including working with business and industry associations, policy research organisations and other advocacy groups, we can more proactively identify and mitigate international political and regulatory risk, as well as bring greater coordination, clarity and consistency to our work globally.</p> <p>In the US we actively monitor changes through participation in advisory boards and representation on standard setting committees. Our customer relationship teams have detailed knowledge of each state market. We work with our industry trade associations including the Association of American Publishers and have launched a three-year campaign with America's Promise Alliance to raise high school graduation rates to 90% and to support state led innovations.</p> <p>In the UK we maintain relationships with those government departments and agencies that are responsible for policy and funding. We work proactively with them to ensure our programmes meet existing and new government objectives at the right quality level.</p> <p>Across all of our other markets, there is a government relations programme to support our international markets.</p>	<p>2015 priorities to continue to be actively driven in 2016, with a specific focus on leveraging our resources in the US and UK to build global political and regulatory relationships and partnerships, to elevate our international political profile, and to better understand future international political and regulatory trends, increasingly using trade associations and agencies to inform our decisions and actions.</p> <p>Building a strong brand and reputation in the US remains a priority.</p>
<b>5</b> Acquisitions, divestments and JVs Failure to meet financial and operational targets of acquisitions. Failure to successfully manage JVs and divestments in line with plans	<p>We perform pre-transaction due diligence and closely monitor actual performance against operational and financial targets. Any divergence from these plans will result in management action to improve performance and minimise the risk of any impairments. Executive management and the board receive regular reports on the status of acquisitions and mergers, with a formal review once a year.</p> <p>During 2015, transitional support services to Penguin ended and we completed the sales of the FT, Pearson's stake in The Economist and Powerschool.</p>	<p>Transitional support services to the FT will end in 2016.</p> <p>Our continued priorities for use of cash are:</p> <ul style="list-style-type: none"> <li>- Maintaining a strong balance sheet</li> <li>- Organic investment</li> <li>- Sustaining our dividend and maintaining the commitment to our credit rating</li> <li>- Acquisitions in education with a strong ROIC potential</li> </ul>

## Operational risks

Risk	2015 activities	2016 plans
<b>6</b> Testing failure A control breakdown or service failure in our school assessment and qualifications businesses could result in financial loss and reputational damage	We seek to minimise the risk of a breakdown in our student marking systems with the use of robust quality assurance procedures and controls and oversight of contract performance combined with our investment in technology, project management and skills development of our people, including software security controls, system monitoring, pre-deployment testing, change controls and the use of root cause analysis procedures to learn from incidents and prevent recurrence  In addition to the internal business procedures and controls implemented to ensure we successfully deliver on our contractual commitments, we also seek to develop and maintain good relationships with our customers to minimise risks	Cross Pearson team formed to establish standards for testing risk factors, identify any gaps against standards and implement improvements
<b>7</b> Safety and security Risk to safety and security due to increasing local and global threats	The health and safety policy was updated and released in 2015. Management review processes have been established with key leadership groups and incident data is collected every six months globally  An implementation plan has been developed, with the objective of delivering a pragmatic corporate security function which supports our learners and employees within a safe and secure learning and working environment	The key health and safety focus will be on executing a three-year strategy. We continue to improve risk assessment in the due diligence process with mergers and acquisitions, as well as in our existing and future operations. Ongoing engagement with Pearson leadership ensures that health and safety is integrated into business agendas.  Security activity will be prioritised based upon an assessment of risk, which is constantly evaluated
<b>8</b> Customer facing systems Failure to maintain and support customer facing services, systems, and platforms, including addressing quality issues and execution on time of new products and enhancements	Effective project management disciplines are in place to ensure that enhancements and new products meet the required standards. Real-time monitoring and reporting of operational performance are used to identify any issues and direct appropriate responses.  The Quality Task Force, established in 2014 to improve customers' back-to-school experience, is now part of business as usual. In 2015, this initiative delivered significant improvements with fewer incidents overall, less unplanned downtime, faster resolution of issues, better protection against denial of service attacks	2016 will focus on the next tier of priority products and fully embedding the quality initiative in business as usual. Plans include more thorough testing, easier onboarding and greater access to self-service, plus more proactive monitoring and further upgrades to the network and security. Other longer term initiatives are underway to further improve the customer experience
<b>9</b> Safeguarding and protection Failure to adequately protect children and learners, particularly in our direct delivery businesses	We continue to take safeguarding as a fundamental obligation and high priority.  There is increased understanding and reporting of safeguarding concerns in many of the countries where we deliver services.  See page 61 in the 'Social Impact' section for more on our relationships with learners and customers	Activities will focus on continuing to address risk in the direct delivery businesses, with a focus on those in less regulated countries. The implementation of a safeguarding self-assessment tool and incident reporting system will assist in developing metrics
<b>10</b> Business continuity (new risk) Failure to have plans in place or plans are not properly executed. Crisis management and technology disaster recovery plans may not be comprehensive	Previously reported as a component of other risks, this is now being reported as a separate risk to provide greater clarity.  Pearson's business continuity policy has been refreshed in 2015, identifying our exposure and risk as they relate to key products, sites, services and supply chain. This will be implemented in 2016.  Technology incidents are dealt with reactively and proactive closure of known disaster recovery gaps is prioritised based upon the importance of products and systems. An annual disaster recovery schedule is in place for testing data centres	The new business continuity policy will be implemented in 2016, including additional tools and software to support a standard global approach to business continuity planning.  The new crisis management framework will be embedded through testing and scenarios. The resilience of technology platforms and systems will be further reviewed and improved

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## Principal risks and uncertainties continued

Financial risks		
Risk	2015 activities	2016 plans
<b>11</b> Tax. Risk that changes in tax law or perceptions on tax planning strategies lead to higher effective tax rate or negative reputational impact.	<p>Our tax strategy reflects our business strategy and the locations and financing needs of our operations. In common with many companies, we seek to manage our tax affairs to protect value for our shareholders, in line with our broader fiduciary duties. We are committed to complying with all statutory obligations, to undertake full disclosure to tax authorities and to follow agreed policies and procedures with regard to tax planning and strategy.</p> <p>Oversight of tax strategy is within the remit of the audit committee, which receives a report on this topic at least once a year. All of the audit committee members are independent non-executive directors. The chief financial officer is responsible for tax strategy, the conduct of our tax affairs and the management of tax risk are delegated to a global team of tax professionals.</p> <p>See page 145 for details of tax accounting policy.</p>	<p>There is now known legislative change in the UK on tax reporting requirements in 2016 and almost certain change on tax treatment of financing structures. A change to US legislation is possible.</p> <p>Work has been performed to prepare systems for the increased tax disclosure requirements relating to country by country reporting.</p>
<b>12</b> Treasury (new risk) Inability to mitigate treasury financial risks, including the failure to secure adequate committed funding, the failure to manage exposures to financial counterparties and the failure to manage exposures to market risk such as interest and foreign exchange rates.	<p>The treasury risk is now being reported as a principal risk due to currency and financial market volatility, as well as the recent changes to our credit rating.</p> <p>Our approach to the mitigation of treasury financial risk, including funding risk, financial counterparty risk and exposures to interest and foreign exchange rates is covered in more detail in note 19, starting on page 181.</p>	<p>In 2016, we will continue to operate in line with our treasury policy. More on this can be found in note 19, starting on page 181.</p>
Legal and compliance risks		
Risk	2015 activities	2016 plans
<b>13</b> Data privacy and information security. Risk of a data privacy incident or other failure to comply with data privacy regulations and standards; and/or a weakness in information security, including a failure to prevent or detect a malicious attack on our systems, could result in a major data privacy breach causing reputational damage and financial loss.	<p><b>Data privacy:</b> A data privacy office has been established and a 2015-2016 data privacy strategy developed. The implementation of the strategy is overseen by the data privacy governance board which has operated throughout 2015. We test and re-evaluate our data security procedures and controls across all our businesses with the aim of ensuring personal data is secured, and we seek to comply with relevant legislation and contractual requirements. We regularly monitor regulation changes to assess the impact on existing processes and programmes. The data privacy office is working with those limited parts of the business affected by the Safe Harbor decision to transfer them to model contract clauses.</p> <p>Annual training on data security and privacy was introduced in 2015 for all employees. In addition, all Pearson staff who deal with US student data are required to take educational data protection training.</p> <p><b>Information security:</b> Pearson has an established global security organisational model, and standard-based information security controls and practices. Security policies have all been updated in 2015. We have established a global security operations centre that provides ongoing monitoring of potential malicious attacks on our infrastructure and systems.</p>	<p>The data privacy and information security improvement programmes will continue through 2016 into 2017 and will implement critical processes to drive best practices.</p>

## Legal and compliance risks

Risk	2015 activities	2016 plans
<b>14</b> Intellectual property If we do not adequately protect our intellectual property and proprietary rights our competitive position and profits may be adversely affected and limit our ability to grow	We seek to mitigate these risks by being generally vigilant and deploying policies and internal and external resources to manage and protect our intellectual property. We co-operate and advocate through trade associations, monitor advances in technology and law and, when appropriate, take legal or collective enforcement actions with other publishers to secure our rights. We have in place a patent programme to establish enforceable patent rights to protect our technology innovations and promote appropriate confidentiality and trade secret protocols. Our global IP legal function also helps us clear and protect our key brands and patentable innovations.	We will continue to streamline our portfolios, procure and register expanded rights in our high value IP globally, monitor activities and regulations and proactively enforce our rights, taking necessary legal action.
<b>15</b> Competition law (new risk) Failure to comply with anti-trust and competition legislation	In October 2015, a lawyer specialising in competition law was appointed to ensure we are fully compliant with all laws and regulations. A plan has been put in place to perform a full risk assessment given the evolving complexity of legislation and regulation in this area. This evolving complexity is why this risk has now been included in the principal risks.	Based upon the completed risk assessment, we will develop and implement actions prioritising key risk areas.
<b>16</b> Anti-bribery and corruption (ABC) Failure to effectively manage risks associated with compliance to global and local ABC legislation.	We have a risk based programme of training (online and face to face), with code of conduct certification including a clear statement of ABC policy. The policy was revised in 2015, with no change to Pearson's 'zero tolerance' principle. In 2015, the Business Partner Code of Conduct launched, which will help to mitigate third-party ABC risk.  See page 60 in the 'Social impact' section for more detail on what is covered by the Code of Conduct.	Training and awareness in 2016 will focus on the revised ABC policy for higher risk countries and activities.  Third party due diligence will continue to be enhanced taking into account the benefits from business transformation implementations, such as the Enabling Programme.
<b>17</b> Data quality and integrity (new risk) Unavailability of timely complete and accurate data limits informed decision-making and increased risk of non-compliance with legal, regulatory and reporting requirements.	Data quality and integrity is now being reported as a principal risk due to its importance in supporting business change initiatives such as the Enabling Programme and OneCRM (as highlighted risk 1, business transformation and change). Data is key to their success.  A Pearson Data Services team has been created and a data governance target operating model agreed which defines data ownership accountability at executive level to ensure that data initiatives align to business strategy priorities and initiatives.	The primary focus is on the Enabling Programme which will in time, deliver significant improvements in data quality and facilitate better informed decision-making.  The 2016 roll outs require the migration of a significant number of datasets.

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## Targeting growth through efficacy

### The road to empowering the lives of 200 million learners annually by 2025

#### Introduction

Over the last few years, we have been progressively measuring and increasing our impact on learner outcomes. We are already helping millions of learners progress in their lives, to become more literate and numerate, move from school to college, learn a new language, or secure a new career which offers better prospects for them and their families.

To advance Pearson's reach and impact and to position the company for sustainable growth, we have embarked on an ambitious efficacy programme which has evolved the way we manage our business, our approach to product development and our relationships with customers.

In 2013, our drive to build a company centred around 'what works' in education led to a commitment to publicly report on the learner outcomes delivered by our products in 2018.

In 2014, Pearson started embedding the efficacy framework and approach at the centre of our business model, conducting efficacy reviews and using those insights to improve our products and how we serve our customers. In preparation for 2018 we started the process of publicly reporting on efficacy, profiling the progress of five key products.

In 2015, we expanded the focus of our work, gathering evidence for more products and services. We are seeing increased interest in our efficacy approach from our customers and it has become a bigger factor in sales decisions. We are reporting publicly on the efficacy of many more products alongside this report.

#### Key achievements in 2015

We made great progress in 2015, achieving the following milestones:

##### 2014 first wave products

#### Gathering evidence

For all 'first wave' products (products chosen based on strategic importance, market position and revenue) we have worked with customers to refine their learner outcomes, are now gathering evidence of their impact, and have been completing efficacy-led product improvements.

IMAGE  
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##### 2015 second wave products

#### Defined learner outcomes

We have also defined learner outcomes and metrics for all 'second wave' products (products representing a wider range of geographies in our portfolio). In addition to evaluating existing evidence and implementing plans to gather more evidence of impact. Going forward we will continue to build an evidence base for these products and make improvements.

IMAGE  
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#### Competitive edge

Importantly, we are increasingly seeing our Sales and Marketing teams working with our Efficacy teams to provide a competitive edge to Pearson's proposals. Our commitment to build more effective products has already resulted in increased customer demand for such products and, therefore, increased revenue. We look forward to seeing this trend continue into 2016 and beyond.

In 2016, we continue to make progress evaluating and improving the efficacy of our products. Efficacy has become central to our growth strategy. Our knowledge and capabilities are maturing. Both our current portfolio and the way we identify future acquisitions are grounded in a commitment to demonstrating effective learner outcomes. We are delivering on our commitment to report on these too.

#### Our efficacy journey

**“Hold us accountable for our impact. If we fail, we fail as a business.”**

John Fallon, Chief executive officer

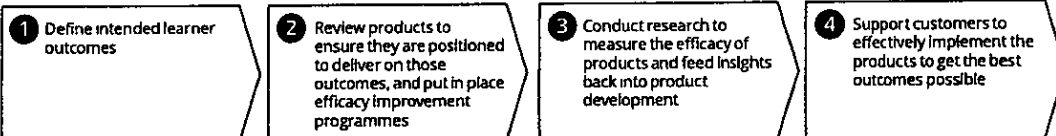
Building on last year's reports, this year our public efficacy reports reflect what we've learnt since 2013. They include more detail on the impact each product is having, improvements made to date, future product research and improvement plans and, importantly, stories from our customers. Highlights of this work follow, but to read the full reports, please visit [efficacy.pearson.com](http://efficacy.pearson.com)

Today we continue to refine our efficacy practice, and, although our knowledge has matured, we remain pioneers. We continue to encourage everyone, from our customers, to learners, to policymakers, to investors, to join in and challenge us, to tell us how we can improve our approach and in turn our products and services.

#### Efficacy leading to product improvement

The efficacy review process has been designed to help teams identify areas of improvement in product, customer relationships and internal capacity to deliver. The product improvement process is specifically designed to ensure that the product will benefit learners and customers, eventually making it more commercially successful. Examples of these improvements are illustrated below.

#### Efficacy approach and activities



Product	Improvement
<b>Wall Street English</b>  New student experience	<ul style="list-style-type: none"> <li>› Launch of algorithm identifying students at risk of dropping out, providing insights for effective interventions. Improves learner outcomes as well as centre profitability.</li> <li>› Class-level analytics to demonstrate that students perform equally, whether they are using print or digital manuals, another change that will improve centre efficiency.</li> <li>› Optimising duration of language videos will increase learner engagement and encourage them not to break their study rhythm.</li> </ul>
<b>Pearson Schools India</b>	<ul style="list-style-type: none"> <li>› Augmentation of teacher numbers and quality as a direct result of the efficacy review.</li> <li>› Improved data systems, which now provide teachers with data at a concept and student level, aiming for 48-hour turnaround time.</li> <li>› Adoption of Big English, an English language learning product, to increase student English proficiency, teachers also being supported to improve their own English skills where required.</li> <li>› More teacher-to-teacher collaboration and interventions driven by efficacy. Our School Management Improvement Framework, as well as a new Professional Development programme to improve school leadership.</li> </ul>

## Targeting growth through efficacy continued

### 2015 efficacy reports: product highlights

Selected examples of our efficacy reports are included below. The remainder of the reports can be found at [efficacy.pearson.com](http://efficacy.pearson.com) ➔

Alongside this annual report, we are publishing several reports to share our efficacy progress and the outcomes achieved by some of our most powerful products and services. We will continue to develop the capability to report transparently on the efficacy of products across our portfolio.

IMAGE REMOVED

**In the last decade, the number of college students majoring in STEM fields – science, technology, engineering, and mathematics – has increased rapidly**

Between 2007 and 2011, STEM majors in the US increased by 48%. Today, approximately 40% of male college graduates and 29% of female college graduates earn a degree in one of the STEM disciplines. These areas of study offer students practical and applicable skills upon entering the professional world and also create significant economic opportunity.

MasteringChemistry is an online tutorial and problem-solving tool for students to practise and reinforce their understanding of college-level chemistry – a vital tool for any successful STEM degree. The product launched in 2004 and today reaches about 350,000 students in the United States, and 50,000 more in 60 countries around the world. MasteringChemistry uses personalised instruction to improve competency in chemistry and prepare students for success in chemistry courses. Learners benefit from self-paced tutorials featuring specific, wrong-answer feedback and hints that emulate the tutor. New content features have been added to increase student achievement and retention. For example, there are additional adaptive opportunities through new Dynamic Study Modules, which are designed to help students study on their own more effectively, using adaptive algorithms that adjust the content based on each student's understanding of the concepts.

For detail on the efficacy of this product go to [efficacy.pearson.com](http://efficacy.pearson.com) ➔

IMAGE REMOVED



IMAGE  
REMOVED

IMAGE  
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Connections Academy schools are accredited, tuition-free, online public schools for K-12 students, providing a personalised approach to learning, supported by certified teachers and a custom curriculum

Since the first Connections Academy opened in 2002, the schools have been established in 26 US states and have served nearly 270,000 students who – for academic, personal or professional reasons – may be better suited to online rather than bricks-and-mortar education

Connections believes that all students perform better when they receive individual attention in a safe, nurturing environment – what Connections calls Personalised Performance Learning®. Students are able to accelerate learning in areas of strength or receive extra attention in areas of weakness. Individualised learning does not mean learning alone – students meet regularly in online LiveLesson sessions and have opportunities to share ideas and experiences, while having fun learning together. In-person events, clubs, activities, and field trips help students stay connected and make friends. Parents, as Learning Coaches, are closely involved in their children's education.

For detail on the efficacy of this product go to [efficacy.pearson.com](http://efficacy.pearson.com) ➔

IMAGE  
REMOVED

CTI Education Group (CTI) is an institute of higher education that serves approximately 11,000 students across 12 campuses in South Africa

The institute focuses on arming students with real-life career skills, training them to succeed as employable graduates in a competitive 21st-century economy

Because career-readiness is such a steadfast priority for the institute, CTI has developed a number of strategies designed to ensure that all of its graduates are well prepared for a highly demanding employment market. For example, a virtual employability centre will open in 2016 to serve as a resource hub for students looking to enter the job market. The virtual hub will be followed by six physical employability centres to provide personalised, face-to-face job coaching. Finally, employability competencies are firmly embedded into the CTI curriculum, which focuses primarily on information technology, commerce and law.

For detail on the efficacy of this product go to [efficacy.pearson.com](http://efficacy.pearson.com) ➔

IMAGE  
REMOVED

## Targeting growth through efficacy continued

IMAGE REMOVED

IMAGE REMOVED

With 85% of young millennials in the US owning smartphones in 2014 according to Nielsen, education innovators have come to understand that hardcover textbooks are no longer in line with students' primary consumption habits

REVEL is a digital resource that offers students online and mobile access to humanities and social sciences course materials. The programme includes embedded assessments, interactive components and videos integrated within the narrative content to reinforce key concepts. REVEL provides instructors an assignment calendar, which allows them to indicate to students when work must be completed with reminders and study tips to help students stay on track throughout the course.

REVEL was launched in 2014 to foster independent self-initiated learning outside the classroom, so that students and educators are better prepared inside the classroom. REVEL allows students to access their learning anytime, anywhere, with an engaging experience that encourages class participation and course completion.

REVEL helps instructors address a particularly thorny challenge they face in the humanities and social sciences – that students don't do their assigned reading and come to class under-prepared. REVEL provides specialised tools to allow instructors to plan for and address this challenge.

For Detail on the efficacy of this product go to [efficacy.pearson.com](http://efficacy.pearson.com) ➔

### The path towards audited efficacy statements

From the start of our efficacy work we planned to have our efficacy statements audited in the same way as our financials each year. In order for our focus on learner outcomes to transform our business, it is essential that our customers trust any efficacy statements that we make. We are pleased to announce that this work is underway. This year we began work with an external auditor, PricewaterhouseCoopers (PwC), to ensure that any efficacy statements we make stand up to audit.

### Auditing efficacy

We have now published 13 product reports. PwC will collaborate with us during 2016 to continue to strengthen our reporting process.

In 2016 PwC will work with us to

- › Standardise and stabilise our efficacy reporting processes
- › Further align our evidence to support product efficacy statements
- › Run a mock audit of a sample of efficacy statements in the 2016 annual report in preparation for 2018

### Our plans for 2016

Expand the evidence of impact With efficacy processes in place for our 'first wave' and 'second wave' products, we will expand the breadth of evidence we are collecting across even more Pearson products, further demonstrating their impact on learner outcomes

Leverage efficacy to develop models of product improvement While all products engaged in the efficacy process undergo an improvement cycle, in 2016 we will deepen our efficacy focus on several products that span our business models (e.g. managed services, courseware) to establish a 'gold standard' model of how our efficacy process leads to product improvement

Further embed efficacy into our organisation and portfolio More product teams around the company will embrace the efficacy approach Efficacy will be better embedded in internal processes such as acquisition and strategic planning

Share our efficacy story with the world Lead a global conversation across the education sector about the impact of Pearson's efficacy work, demonstrating how effective education products and services deliver enhanced learner outcomes and positioning Pearson at the forefront of the industry

### The remaining education challenge

Education matters more than ever It is the most important factor in driving economic and social progress Research shows that better education helps individuals, families and countries prosper, improves health outcomes and builds cohesive societies There are huge challenges to overcome, as noted in the adjacent diagram

There is growing consensus that addressing these pressing educational and global development issues and thereby meeting the needs of learners, employers and governments will require everyone involved in education to work together and focus on solutions which can be shown to make a difference

In 2015 we joined world leaders at the United Nations in committing to the UN World Sustainable Development Goals (SDGs) to make the world a better place by 2030 These goals represent global challenges across both the developed and developing world and all of Pearson's major markets Pearson will use these goals to inform our own sustainability plan We will leverage our investment in efficacy and our growth strategy to fuel the financial success of Pearson, demonstrate progress in achieving our mission, and be a global leader in addressing Goal 4 of the SDGs, "to ensure inclusive and equitable quality education and promote lifelong opportunities for all"

Through efficacy we are capturing our impact on learner outcomes at a product level, thereby providing customers with products and services that are effective learning tools, and, as a result, expanding our reach We now have the opportunity to measure the collective reach and impact of all of our products, and to report on our growth in new ways

In the next ten years, we at Pearson believe that the world should be a place where far more people are making much more progress in their lives through learning – and we are making an ambitious plan to get there

### Access to high quality education

# 58m

primary-aged children are not in school  
250 million children worldwide are in school but are not learning

IMAGE  
REMOVED

### Literacy and numeracy skills

# 750m+

adults, globally, are illiterate In developed countries, 200 million young people still have not mastered basic literacy and numeracy skills

IMAGE  
REMOVED

### Employability and English language skills

# 206m

adults are unemployed 290 million young people are out of work  
Meanwhile 40% of employers are unable to find qualified candidates to fill vacancies

IMAGE  
REMOVED

1 UNESCO Policy Paper, June 2014 (58m children not in school)

2 UNESCO Education For All Monitoring Report, April 2013 (250m in school but not learning)

3 UIS Fact Sheet, Sept. 2015 (750m illiterate)

4 International Labour Organisation, Global Employment Trends 2012 (206m adult unemployed)

5 The Economist, April 2013 (290m young people out of work)

6 The Economist April 2013 (40% unable to find qualified candidates)

## Targeting growth through efficacy continued

### The Plan

By 2025, Pearson commits to empower the lives of 200 million learners annually, more than doubling our current reach and doing it through the delivery of more effective products and services

	Access	Success	Progress
<b>Our goals</b>  To meet our commitment to empower the lives of 200 million learners annually, we have set three goals	<b>Enhance access to high quality education that leads to meaningful outcomes</b>	<b>Help more learners gain the knowledge and skills required for life and career success in the 21st century</b>	<b>Help more people make measurable progress in their life and career through learning</b>
<b>2025 targets</b>  We are building on our efficacy work to set ourselves ambitious growth targets	<ul style="list-style-type: none"> <li>› We will help 10 million primary and secondary learners annually access high quality education</li> <li>› We will help 2 million post-secondary learners annually access high quality education</li> </ul>	<ul style="list-style-type: none"> <li>› We will help increase literacy and numeracy for 50 million learners annually</li> <li>› We will help 50 million learners annually gain the knowledge and skills required for study and employment</li> <li>› We will help advance the English language skills of 75 million learners annually</li> </ul>	<ul style="list-style-type: none"> <li>› We will help 25 million learners annually transition into the workforce after further or higher education</li> <li>› We will help 20 million learners advance their career prospects annually</li> </ul>
<b>Strategic alignment</b>  Our goals and targets align with our core strategic priorities  For more see strategic overview on p04 ➔	Online degree and virtual school programmes can improve learner access to quality primary and secondary education, currently those programmes are helping 1.8 million learners to annually access quality education. By 2025, we aim to help 10 million	Our products that support adult English language learning can provide learners with the skills required for success in a global workforce. Products such as MyEnglishLab and many others allow us to help advance the English language skills of 30 million learners annually. By 2025 we aim to help 75 million learners annually	Our workforce readiness products support learners to make measurable progress in their lives and careers. Products such as MyITLab help approximately 15 million learners to transition into the workforce annually. By 2025 we aim to help 25 million learners annually transition into the workforce after higher or further education

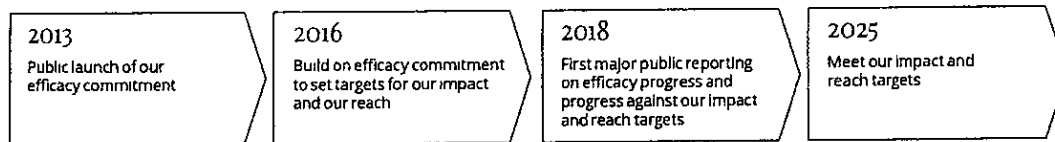
### From 2016 to 2025

While our efficacy work continues, we will sharpen the focus of our portfolio, investments, partnerships, and campaigns to meet the goal of reaching, and positively impacting, 200 million learners with increasingly effective products. This approach will eventually be embedded into every area of our business so that we are positioned for growth.

### In 2016, we will

- › Define company-wide trajectories and set product-level targets and trajectories
- › Tie KPIs to the targets across Pearson, measuring the performance of our business leaders and executives by their contributions to these goals
- › Develop and implement a system capable of tracking our progress towards these goals
- › Agree upon processes for determining new acquisitions and investments in our current and future portfolio based on their contribution to our goals

### Timeline



### Setting the targets

- › Our targets are derived from the key educational challenges facing learners, market realities and opportunities identified by our business leaders where Pearson has opportunity to grow
- › Our product portfolio was evaluated to determine the areas where Pearson can measurably have the greatest impact on global education
- › The targets are set based on current reach and market trends. Choosing these targets will help organise and measure our energy to grow the company

We are at a critical juncture in our history and the education sector is at a critical juncture in its evolution. With far greater data being made available on learners' performance and more willingness to use that data to improve education, we have a singular opportunity to have greater impact with our products as well as reach more people.

Our targets to increase our reach and impact will drive us towards commercial success and our mission to help people make progress in their lives through learning.

### The number of learners reached by Pearson

# 200m

By 2025, Pearson aspires to empower the lives of 200 million learners annually.

IMAGE  
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### Pearson's ambitious research programme

World-leading research continues to be a priority for Pearson. We work with the best minds in education to bring their diverse and independent insights to a wider audience. These include two reports published in 2015 with world-renowned educationalist Professor John Hattie, *What Doesn't Work in Education: the Politics of Distraction*, and *What Works Best in Education: the Politics of Collaborative Expertise*.

These papers have been read 70,000 times via our website and have redefined our ambition for the global reach of Pearson's thought leadership. They have formed the basis of engagements with government officials, stakeholders and academia in key markets across the world.

In 2016, we look forward to building on this momentum with releases on critical topics including adaptive learning, artificial intelligence in education, and building efficacy into learning technologies.

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# Our social impact

Learning is the means by which people progress in their lives.

At Pearson, our commercial success and delivering on our social purpose are mutually reinforcing. Our aim is to help people flourish and make progress in their lives through education and learning.

Our promise is progress for the millions who learn with us and efficacy (p46) is the key mechanism by which we will deliver. This means a clear focus on developing products and services that have a measurable impact on improving students' lives through learning.

This year, we have gone further by setting clear goals on the number of learners we will support through our products and services.

Purpose reinforces success in a number of ways – it attracts and helps us retain talent, something we know to be true from the results of our engagement survey, it inspires our customers, builds confidence, drives performance and helps foster innovation.

Our strategy is focused on extending and deepening our impact, but we also know that 'how' we deliver is central to our purpose. Acting responsibly helps us to deliver better outcomes and to meet the expectations of our stakeholders.

IMAGE REMOVED

## Our social impact strategy

### Sustainability

We invest in our people, our communities and work to reduce our environmental footprint.

### Impact

We contribute to significant social and environmental campaigns.

### Innovation

We actively partner and invest in new models of learning to help find solutions to the biggest unmet educational needs.

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## Overview

Pearson has an active role to play in finding solutions to our global sustainability challenges, which is integral to our business strategy and how we report on our most material issues.

1	Sustainability	p56-58 ➔
2	Our values and behaviours	p59-60 ➔
3	Our relationships	p61-63 ➔
4	Our planet	p63-64 ➔
5	Impact campaigns Project Literacy Employee engagement	p65-66 ➔
6	Social innovation	p67 ➔

From June 2016 we will report in more detail in our 2015 Sustainability Report available on [pearson.com/social-impact](http://pearson.com/social-impact)

## 1. Sustainability

### Towards a new strategy

During 2015 we began a review of our sustainability practice, to ensure that our strategy, activities and reporting efforts

- › Reflect best practice in sustainability
- › Are fit for purpose in a rapidly changing business climate
- › Align with current business and stakeholder priorities
- › Match our ambition and business strategy
- › Reflect how our business model can link to the UN's Sustainable Development Goals

Pearson has a broad definition of responsible business and has established a set of commitments across a range of social, community and human rights principles to

Ensure that our products and services are inclusive, appropriate in content to the age, location and ability of the learner, and are easy and safe to use and access

Respect and protect how we use and share data entrusted to us by learners and our customers

Inform, support and equip colleagues to work collaboratively

Encourage and reward high performance, nurturing talent and creating a culture where all are able to realise their individual potential

Provide a safe and healthy workplace for our employees and the learners we serve

Extend our commitments on labour standards, human rights and environmental responsibility to include our suppliers and business partners. This includes a concern across the value chain for ensuring our activities are free from slavery, servitude, forced or compulsory labour and human trafficking

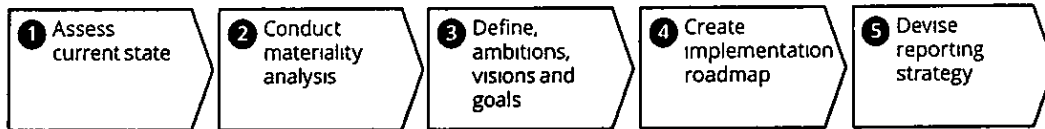
Provide opportunities for Pearson people to be good citizens and to get involved in their local communities

Deliver against our targets on our response to climate change and to make more efficient use of resources

Pearson has in place policies to support recognised human rights principles. These include health and safety, safeguarding, non-discrimination and a right to quality education. As a founder signatory to the UN Global Compact, we have also made a series of commitments to the Universal Declaration of Human Rights, the ILO declarations on fundamental principles and rights at work, the Rio Declaration on Environment and Development and to reflect a zero tolerance approach to bribery and corruption

The approach we've taken for our sustainability review and the resulting sustainability map are opposite on p57 ➔

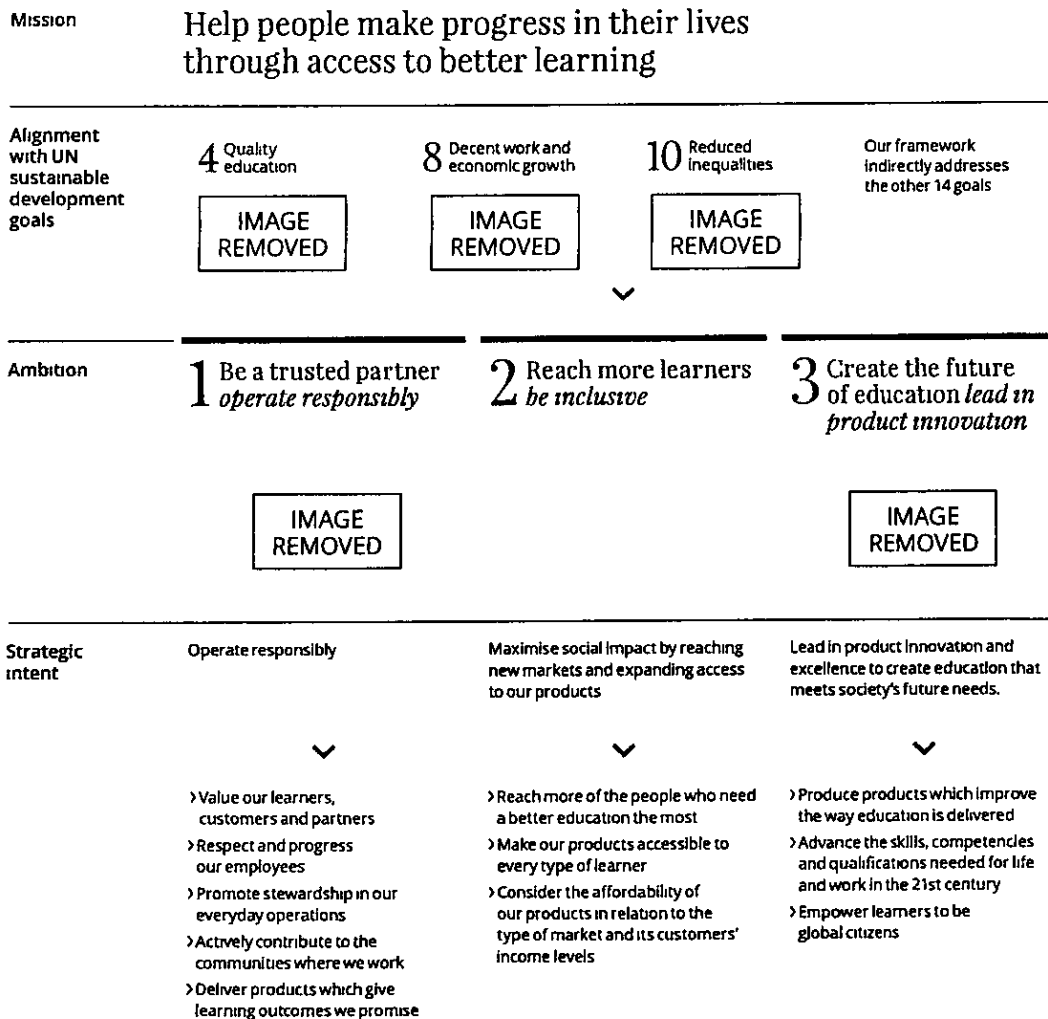
## Pearson sustainability review – five key phases



We have completed a third-party review of policies and reporting, a benchmark against competitors and leaders, as well as internal interviews with Pearson executives. A new sustainability map captures our most material issues.

This has been reviewed by internal experts and, to date, nearly 40 Pearson executives have been consulted. This will be finalised in 2016 and form part of our sustainability reporting. Detailed below is our current thinking.

## Pearson sustainability map



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## 1 Sustainability continued

IMAGE REMOVED

### Pearson and the UN sustainable development goals

In 2015 we joined world leaders at the United Nations in committing to the UN sustainable development goals (SDGs) setting out their ambition for a more peaceful and prosperous world. These goals represent global challenges that impact education across the world. Goal 4 is particularly important for Pearson – “to ensure inclusive and equitable quality education and promote lifelong learning opportunities for all.” We are playing our part in contributing to this goal, through contributing educational expertise, knowledge and resources to help address these pressing challenges.

We are also working in partnership with others to make a difference.

- › We are supporting Project Everyone – an organisation with a simple but mighty ambition – to share the global goals with all 7 billion people on the planet.
- › We have joined the Global Citizen movement – an organisation dedicated to creating change and taking action to address the world’s biggest challenges.

### Governance

Corporate responsibility cannot be separated from our business and reputation. The reputation and responsibility committee, a formal committee of the board, provides ongoing oversight, scrutiny and challenge across the entire responsible business agenda. Learn more on p90.

The Pearson executive drives the implementation of business strategy, including our response to the key issues and opportunities we face. The responsible business leadership council oversees the development and implementation of our responsible business strategy on behalf of the board. It is chaired by our chief corporate affairs officer and comprises senior executives from across the global business.

### Stakeholders

Public and private sector customers regularly seek information on how we go about our business, while many learners and employees want to understand our approach to sustainability. Socially responsible investors and non-governmental organisations look at issues such as supply chain standards and ethics.

Our approach to responsible business is informed by the priorities and views of our many stakeholders. A priority for us will be testing our new sustainability framework with stakeholders as part of a continuing focus on identifying, engaging and inspiring our priority audiences.

## 2. Our values and behaviours

### Employee engagement

Our organisational structure continues to evolve to better deliver on our business strategy and to position the company for growth. We continue to invest in our single operating model, and in particular in standardising systems and a smaller number of global platforms. At the same time, we are accelerating our shift and investment in digital products.

Change can be inspiring but also brings operational risk. The link between employee engagement and business performance is well established, and our 2014 employee engagement survey had some key lessons for us.

- › Our purpose to improve lives through learning is clear and compelling
- › Our focus on efficacy is improving our products and services
- › Values and behaviours are critical to our success, but need to be more clearly articulated
- › In this time of change, our leaders and managers need to communicate more often and more clearly their expectations of working together in a more joined-up way
- › More work is needed to clarify to employees how our new structure works and how it helps deliver outcomes for learners

Based on this, we set the following agenda for the work around our values in 2015 and beyond

Priorities in 2015 and beyond	Activities in 2015
Leaders more consistently model the behaviours required for us to be successful	<ul style="list-style-type: none"> <li>› Many of our leaders have written, spoken or tweeted about our values in 2015, and the values themselves have been integrated into business processes and communication</li> <li>› Following consultation and research, we introduced 'accountable' as a fourth value, alongside our current values of brave, imaginative and decent, to provide positive tension and increase our focus on responsibility and delivery</li> </ul>
Employees see evidence of the values driving the right behaviours across the organisation	<ul style="list-style-type: none"> <li>› We created a clear set of behavioural expectations against each of the values, and defined high, expected and low performance for each behaviour, for all employees as well as for more senior leaders. Clear behavioural expectations provide more clarity in terms of what the values look like day-to-day</li> </ul>
People feel safe to speak out and challenge where our values are not being lived	<ul style="list-style-type: none"> <li>› In 2015, we provided much clearer guidance on how to assess values and behaviours in a performance review</li> <li>› The values and behaviours were used to help shape the revised Pearson Code of Conduct, with a particular focus on speaking up and challenging behaviour that is not consistent with our values</li> </ul>
Candidates are attracted to Pearson by our values, Employee Value Proposition and culture	<ul style="list-style-type: none"> <li>› We created and launched a range of simple but powerful toolkits to help leaders, managers and teams explore and understand what the values and behaviours look like in their own context</li> </ul>
Evidence that our values drive performance, engagement and retention of key talent	<ul style="list-style-type: none"> <li>› Welcome to Pearson, our award-winning global onboarding tool, has been updated to ensure that all new hires are familiar with the values from day one. We continue to have high recall of the values, and strong identification with them, as evidenced in our 2015 engagement survey (see below)</li> </ul>

The 2015 engagement survey found that 89% of employees agree that 'Pearson's values are important to me' – even higher than in 2014 (84%). The survey also indicated that behaviour consistent with our values was significantly more visible to employees, and that all four values are more prevalent within most parts of our company. As part of our work on culture, we found that the way Pearson's colleagues treat one another and the values themselves are factors in the decision to join and stay at Pearson.

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## 2 Our values and behaviours continued

### Our values

#### Brave

Takes bold and decisive action to deliver ambitious outcomes and champions a culture of high performance

#### Decent

Listens, encourages and respects difference, treats all people fairly, with honesty and transparency

IMAGE REMOVED

THE  
LEARNER

#### Imaginative

Looks beyond their immediate job both inside and outside of Pearson and introduces new ways of seeing, thinking and working

#### Accountable

Drives results by owning the solution, getting the right people involved and delivering on promises

### Our behaviours

#### Brave

Shows determination and courage in the face of obstacles and setbacks

Offers ideas or opinions without fear of criticism or professional risk

Sets high standards for own and others' performance

#### Imaginative

Assesses complex issues from multiple angles and addresses problems that don't have clear solutions or outcomes

Offers creative ideas and innovative solutions to solve problems and address opportunities

Takes a broad perspective to identify opportunities and solutions

#### Decent

Is honest, transparent and straightforward when working with others

Builds trusting relationships with a broad range of people inside and outside Pearson

Looks for and includes diverse viewpoints and talents of others

#### Accountable

Takes ownership of own work and drives to successful completion and closure

Identifies and involves others to accomplish individual and group outcomes

Follows through on commitments

### Code of conduct

Our values are reinforced by our code of conduct which covers, among other things, individual conduct, safeguarding of learners, employee rights and responsibilities, community involvement, the environment and our social obligations. We make sure everyone is aware of the Code and this forms part of the onboarding process. This year, we completed a material review and rewrite of the Code including detailed additional guidance and case study support. The Code was circulated early in 2015 to every Pearson employee and they were asked to confirm they had read it, understood it and to affirm that they would comply with it. Over 99% of employees have signed up to the Code.

### Raising concerns

We operate a free, confidential telephone helpline and website for anyone who wants to raise a concern and we have a clear non-retaliation policy in place to encourage people to share the issues they have. In 2015, we had 119 concerns (112 in 2014) raised through the ethics reporting process. These were investigated and, where possible, the outcome shared with the whistleblower. This year, as in most years, the majority of the concerns related to HR practices. Material concerns raised are reported to the Pearson audit committee.

### 3. Our relationships

#### Learners and customers

Our primary responsibility to learners is to ensure that every product or service we sell can be measured by what it helps them to achieve. It is also the primary contribution we can make to society. Our section on efficacy describes the commitments and progress we have made.

Last year, we adopted the Pearson product lifecycle framework for managing our products, services and platforms. This introduced a unified product strategy that brought a single global approach to shape how we invest, develop, market and deliver our products. We have identified a number of priority products for investment, selected for their potential to generate the most business value and deliver the greatest learner outcomes at scale. These are the focus of our commitments. Our products are increasingly digital, offering opportunities to tailor and personalise learning around individual needs. At the same time, many people have concerns over the security and privacy of data. We have established a governance body within Pearson to oversee our global approach to these issues.

Product development is part of a wider approach to better understanding product and customer experience. Last year, we introduced the Net Promoter Score (NPS) system into Pearson. This is one of the most recognised methods of measuring customer loyalty and to date over 150,000 of our customers have shared their comments. Corporately, we have also invested in a brand tracker – seeking the views of learners, parents and educators on Pearson in our largest markets.

One area in which we can do more is to integrate our approach to managing customer relationships. We are now implementing a single global platform – Salesforce – for our marketing, sales and service functions. Starting with our businesses in South Africa and the Higher Education sales teams in the United States, we will be adding new markets, geographies and capabilities in 2016. A single customer view will help improve our responsiveness to customer needs.

As we grow through operating and owning learning institutions, we have new responsibilities to safeguard and protect learners through providing a safe, age-appropriate learning environment, whether in a classroom or online. Our new head of safeguarding has spearheaded our work in this area through assigning local business leads, establishing common reporting frameworks, launching a new safeguarding online learning module and training strategy, as well as piloting a new approach to incident prevention.

#### Our people

##### Highlights during the year include

- › Reinforcing our single global approach to performance assessment. Introduced in 2014 and refined in 2015, this is designed to help our employees agree expectations for the year and to motivate people to act consistently with our values and business strategy.
- › A continuing commitment to internal learning and development. Pearson has a single global platform – Milo – for learning and development. Employees completed approximately 200,000 courses relevant to employee development during 2015. Through Milo, we delivered a global employee induction module called 'Welcome to Pearson' and a suite of management modules on ways of working. Employees and managers use Milo to record their individual goals, monitor their progress, and assess their performance. Pearson also began the implementation of a single global recruitment process, which will allow all employees access to job openings around the world and introduces a consistent approach to internal movement.
- › Ensuring our employees and the learners we serve are safe, resilient and productive. Our goal is to achieve zero harm for our employees, contractors and learners, working to prevent incidents before they occur. In 2013, we launched a revised Global Health & Safety Policy which included 39 minimum performance standards for implementation at all of our locations in the world. In June 2015, Pearson secured the RoSPA Bronze Award for health and safety performance for our global operations. A health and safety strategic plan is in place for 2015-17 with 11 focus areas, each with clear accountability and measures of performance.
- › Helping employees understand how we are doing as a company, including how world and sector trends might affect them and their business. We provide comprehensive and relevant information on our performance including presentations, small group discussions, messages and webinars. Senior leaders also use technology to reach all areas of Pearson, through initiatives such as virtual town halls. The chief executive hosts a regular call to update all employees on strategy and to share new innovations from across the company. In the UK, we have set up an employee engagement group involving members elected by staff as well as trade union representatives.

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### 3 Our relationships continued

#### Diversity and inclusion

At Pearson, we value the power of difference. It drives innovation, productivity and engagement, helping create a culture of opportunity, where every employee and learner is valued. That's why we're committed to ensuring that the core principles of diversity and inclusion are embedded across our entire business, so that we reflect our customers and learners, and where our people can be themselves and contribute fully to our mission to improve lives through learning.

The three pillars of our approach are

Equality	Diversity	Inclusion
Champion fair treatment, respect and equal opportunity for all our people	Celebrate what makes us different, our individual and organisational culture, work styles, values, beliefs, experiences, backgrounds, preferences and behaviours	Create a single global working environment and culture, where all our people can bring their full selves to work, are valued for their differences and can contribute fully to our company purpose

We are committed to attracting, retaining, engaging and developing the best people. We know that creating and sustaining an inclusive work environment is critically important from the boardroom down, regardless of race, gender, gender identity or reassignment, age, disability, religion or sexual orientation.

#### Highlights of our activities include:

- › We have 30% female board members, ahead of the 25% by 2015 target set by Lord Davies for the UK's 350 largest companies
- › We remain an enthusiastic member of the 30% Club which brings together chairs and CEOs to work together on gender balance. We participate in their cross-company mentoring programme which helps the development of talented mid-career women
- › Raising awareness about the impact of unconscious bias on key people management decisions. To date, over 4,000 employees have completed our interactive training on the topic

› In the UK, we are members of the Stonewall Diversity Champions programme and participate in the Stonewall Workplace Equality Index, benchmarking how we perform as an LGBT-friendly employer against over 400 UK organisations. In the United States, Pearson again recorded a perfect score of 100% in the 2015 Corporate Equality Index run by LGBT advocacy organisation, the Human Rights Campaign

› We have involved over 3,000 employees in global employee resources groups. Networks include Women in Learning and Leadership (WILL) which currently has 15 chapters, Pearson Spectrum for LGBT colleagues and allies, Pearson Parents, Pearson Able for colleagues with disabilities and accessibility advocates, Pearson Veterans for military families and veterans, and the Pearson Latino Network, dedicated to addressing the needs of Hispanic and Latino employees and learners

› Disability is an important part of our wider commitment to diversity and inclusion. We work to ensure that appropriate procedures, training and support are in place for people with disabilities to ensure fair access to career and progression opportunities. Our Able network of employees will help us improve practice

#### Women in Pearson (%)

Board of directors	Senior leadership*	All employees
33% 2015	34% 2015	59% 2015
30% 2014	35% 2014	58% 2014
22% 2013	31% 2013	57% 2013

\* Two reporting lines from chief executive

#### All employees (number)

Board of directors	Senior leadership*	All employees**
6 men	68 men	16,781 men
3 women	35 women	24,260 women

\* Two reporting lines from chief executive

\*\* Derived from HR systems and includes the FT

### Supply chain and partners

Pearson purchases goods and services valued at around £1.5bn each year. This total includes our investment in research and development of new digital products and services.

Specific clauses relating to our commitments made under the UN Global Compact are an integral part of our contracts for key suppliers. These standards include the rejection of forced and compulsory labour, a respect for diversity, a minimum age to work on Pearson projects and compliance with employment laws and regulations.

This year, we reviewed our approach to franchise partners and introduced a common contract template governing our responsibilities on health and safety, labour standards, combatting corruption, safeguarding and the environment.

### Communities

In 2015, our community investment was £10.7m, or 1.5% of pre-tax profits. In 2014, Pearson adopted a new strategy which established increasing literacy rates worldwide as our anchor social impact campaign issue, along with a focus on employee engagement in communities. Read more on pages 65-66.

We are committed to playing an active role in helping shape and inform the global debate around education and learning policy. A major milestone this year was the launch of the UN Sustainable Development Goals and, with others, we successfully advocated for the inclusion of education as a core goal. We also contributed to the debate during the UN General Assembly in September as well as to Project Everyone to spread the word on the goals.

We are a board member representing the private sector on the Global Partnership for Education, having been one of the first companies to join the initiative. GPE brings together over 50 developing countries, donor governments, international organisations, the private sector, teachers, and civil society/NGO groups to support developing countries with their education sector plans through financial assistance and technical expertise. [www.globalpartnership.org](http://www.globalpartnership.org)

We also believe that the wider private sector has an important contribution to make in developing education and learning policy. We helped establish, and continue to support, the Global Business Coalition for Education, helping focus the wider business community on the challenges faced by developing countries to promote learning. <http://gbc-education.org/about-us>

## 4. Our planet

We believe that we have a responsibility to play our part in protecting the natural resources on which we all depend.

### Climate change

Pearson maintained our climate neutral status for our directly controlled operations – a commitment we first achieved in 2009. We do this through carbon reduction, purchase of renewable energy, renewable energy generation at our sites and the purchase of carbon offsets.

#### Highlights of our activities include

- › Pearson retains global certification against the Carbon Trust Standard. We were the second ever organisation to secure the standard which recognises leadership in measuring, managing and reducing year-on-year carbon emissions.
- › Pearson completed our work to build a carbon footprint analysis tool for our book publishing in the US and UK. This will help us target the most effective reductions.
- › We maintained our record of purchasing 100% of the electricity we use from green power representing over 141,000 MWh of electricity in 2015. During COP21 in Paris, Pearson announced that we had signed up to RE100, joining over 50 companies helping build the market for renewable electricity.
- › We continue to generate renewable electricity at five sites and have 2.6 MW of wind and solar assets installed.
- › Pearson is certified against ISO14001, the environmental management standard in the UK and Australia. During 2015, Pearson completed the work to become certified against ISO 50001, the energy management standard.
- › Our River Street offices in Hoboken, New Jersey, became the latest to secure LEED certification, an internationally recognised mark of environmental excellence in facilities management. Pearson occupies 840,000 square feet in LEED certified buildings including our offices at 330 Hudson Street in New York.

Our approach to managing other materially important emissions – such as embedded carbon dioxide in purchased raw materials as well as business travel by air – are detailed in our 2015 Environment report. This will be published in June 2016.

### Targets

**25%**

reduction in operational emissions by the end of 2015, based on a 2009 base year. We achieved 30%.

**100%**

To maintain our record of purchasing 100% of the electricity we use from green power. Achieved.

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## 4 Our planet continued

### Global Greenhouse Gas (GHG) emissions data (Metric tonnes of CO<sub>2</sub>e)

Emissions from	Calendar year 2014	Calendar year 2015	Intensity ratios	Calendar year 2014	Calendar year 2015
Combustion of fuel and operation of facilities (GHG Protocol scope 1)	25,027	22,343	Scopes 1 and 2 (tonnes CO <sub>2</sub> e)/ sales revenue £ (millions)	26.6	24.8
Electricity, heat, steam and cooling purchased for own use (GHG Protocol scope 2)	104,715	88,381	Scopes 1 and 2 (tonnes CO <sub>2</sub> e)/FTE	3.17	2.70
Total	129,742	110,724			

Carbon emissions The scope 1 and scope 2 carbon emissions are calculated according to The Greenhouse Gas Protocol Corporate Accounting and Reporting Standard (Revised Edition) together with the latest emission factors from recognised sources including but not limited to DEFRA the International Energy Agency, and the US Environmental Protection Agency. No material scope 1 or scope 2 emissions have been excluded from the reported GHG emissions.

### Material use: Forests

When purchasing paper for our books, security and sustainability of supply are very important to us. Paper use remains a priority environmental issue and we continue to focus on sustainability sourcing and being more efficient in how we use paper. We

- › First adopted and publicly disclosed our environmental sourcing policy for paper in 2003
- › Collect and map data on the forest of origin, certification systems applicable and recycled content for the papers we purchase
- › Talk about our guidelines with our key paper suppliers when we meet and as part of our contract negotiations
- › Discuss our approach to paper purchasing with customers, environmental groups, investor analysts and other interested stakeholders

› Signed up to the WWF Save Forests campaign and added our voice for the inclusion of printed material within the scope of the EU Timber Regulation

› Hold Forest Stewardship Council (FSC) chain of custody certification, allowing books to carry the FSC label for our businesses in North America and in the UK

› Are members of industry bodies dedicated to responsible forest management. We have been members of the WWF forest and trade network for over a decade and are a founder member of PREPS – the publishers database for responsible environmental paper sourcing – which we use across our global business

› Invest in forest-based carbon offsets for any part of our climate footprint we cannot reduce or avoid through other means. Since 2009, this programme has seen over 1,300 hectares of forest protected in Canada, Colombia, Costa Rica, the US and the UK

Visit [pearson.com/environment](http://pearson.com/environment) to learn more 

### Our performance: Our social impact rankings

One way we assess how we are doing as a responsible business is to maintain our position in key indices and benchmarks of social responsibility

Index/year	2011	2012	2013	2014	2015
Dow Jones Sustainability Indices*	Global Sector Leader	Gold Class	Silver Class	Bronze Class	Bronze Class
BITC Corporate Responsibility Index	Platinum	Platinum (retained)	Platinum	Platinum (retained)	95%**
Inclusion in FTSE4Good	Yes	Yes	Yes	Yes	Yes
Corporate Knights index of the Global 100 most sustainable corporations				Yes	Yes

\* For the last decade, we have been included in the DJSI World index which includes only the top 10% of companies in each industry assessed for sustainability performance

\*\* BITC introduced a new rating system in 2015

We welcome feedback on this aspect of the company as we do on any other. Please e-mail [amanda.gardiner@pearson.com](mailto:amanda.gardiner@pearson.com) with any questions or ideas you may have

## 5. Impact campaigns

Pearson has changed its approach to community investment. We believe that we can make more of a difference to people's lives through focusing on a small number of campaigns and issues, where working together with others can accelerate the impact of learning.

As the world's learning company, Pearson has a lot to offer beyond traditional cash donations – we can also bring the expertise and enthusiasm of our people, as well as a wealth of relevant products and services.

This approach also delivers value for the company. By getting involved in social campaigns, our employees can develop new skills, insight and energy and apply this to their work at Pearson. Our social impact campaigns also raise Pearson's profile, differentiate us, and increase awareness of issues that inhibit access to better learning outcomes.

In 2015, our primary focus has been on developing our flagship campaign, Project Literacy. Alongside this, we have also offered employees a range of new ways to get involved in worthy causes and their local communities.

### Project Literacy

Illiteracy remains a huge challenge. One in ten people worldwide, or over 750 million adults, are illiterate, two-thirds of whom are women. This is a staggering number of people.

We also know that being literate is fundamental to building a world in which everyone has the chance to learn.

Literacy is an issue where we believe that Pearson can make a substantial contribution, but is far from sufficient on its own. This is why we launched Project Literacy – a movement with a shared vision to put literacy within everyone's reach, unlocking the potential of people, communities and whole economies. To date, 40 organisations have joined the campaign.

To shape our campaign strategy and focus, we researched the views of the public, the private sector and literacy charities to understand both the current landscape and to benchmark awareness of illiteracy as an urgent issue. We found that:

- Illiteracy is not viewed as a major global or national issue. However, when illiteracy is connected to social and economic challenges such as poverty, interest rises.
- The vast majority of funding is for child literacy leaving adult, and in particular women's, literacy under-funded.
- More investment is needed to support families to help their children develop literacy skills before starting school.

Based on these insights, Project Literacy refined its focus and strategy as a five-year campaign dedicated to building a movement and partnerships that will act together to close the global literacy gap.

**Building partnerships** Partnerships are critical to the success of Project Literacy. Our partnership selection process is based on a theory of change developed in collaboration with the Pearson Efficacy team and Results for Development (R4D), a US non-profit that specialises in monitoring and evaluation for international development programmes.

### Engaging employees in social impact

Our people are our best ambassadors and advocates. One way we support them is to provide opportunities to give time and money to invest in their communities. We use Project Literacy as a lever, but we also support our employees to make an impact on causes they care about through opportunities to volunteer, donate and to share their social impact stories. Over the course of 2015, 30% of employees participated in social impact activities at Pearson.

### Project Literacy – headlines

IMAGE  
REMOVED

969m

people reached through media, social reach and events

11,460

people have sought volunteering opportunities with our Project Literacy partners

IMAGE  
REMOVED

449,477

views of Project Literacy articles published by GOOD Magazine, a social purpose media company

Celebrities and influencers supporting the campaign: Richard Branson, Chelsea Clinton and Piers Morgan.

Events marked by Project Literacy: World Book Day, Mandela Day, International Youth Day, International Literacy Day, UNGA week, International Human Rights Day, and Giving Tuesday.

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## 5 Impact campaigns continued

The three pillars of our theory of change that guide our partnership investment decisions are

### 1 Advancing best practice

We partner with organisations implementing proven literacy interventions to help them grow. Why? Because there are some things that we already know work to improve literacy, and we need more of them.



#### National Literacy Trust (NLT)

Project Literacy and NLT are partnering together to replicate Early Words Together, a targeted literacy peer education programme for families with children aged 2 to 5, in 30 schools across the London metropolitan area. As an integral component of the programme, Pearson and community volunteers are recruited and trained to help parents improve their home learning environment and adopt behaviours that support literacy using evidence-based approaches and materials.

### 2 Innovating new solutions

We partner with organisations to design, build and rigorously test new approaches to tackling illiteracy. Why? Because new solutions will be needed to reach the most marginalised and achieve scale.



#### Worldreader

Project Literacy and Worldreader are partnering together on a mobile technology pilot project in India – Mobile Reading to Children – to empower parents to talk more and read more to their children, specifically through the use of mobile devices. With the Worldreader mobile app, which is available on feature phones and smartphones, we will be providing a rich bank of locally relevant content at low cost for 200,000 low-income parents in Delhi who have children aged 6 and younger. Additional partners include Results for Development, Center for Knowledge Societies, Society for All Round Development, Katha, and Health and Family Planning Organization.

### 3 Raising awareness and mobilising action

We are building a network to advocate collectively for greater investment in and attention to literacy. Why? Because the extent of the problem and its potential impact is huge, we'll need everyone united to close the literacy gap.



#### Unsigned petition

In September 2015, 16 Project Literacy partners joined forces to sign an open letter to world leaders meeting at the United Nations General Assembly (UNGA), calling on them to make literacy a key part of the sustainable development agenda. The letter was published in The New York Times and The Guardian. This letter, combined with the launch of our global 'Unsigned Petition', reached 410 million people through social media. The petition is our major call to action for 2015 and 2016, serving as a striking and visual reminder of the global scale of illiteracy and the 750 million people worldwide who cannot sign for themselves.

#### Volunteering

We now have formal volunteering programmes in place in the US and the UK with Project Literacy partners including Reading Partners, Jumpstart and the National Literacy Trust. In 2015, our employees volunteered over 10,000 hours with 40% of those linked to literacy. For one programme – Read for the Record run by Jumpstart – our employees contributed approximately 1,000 volunteering hours and helped 7,000 children.

#### Sharing

Pearson employees helped inspire others by contributing more than 1,400 stories about literacy volunteering or donating, either on social media or on our internal community engagement hub.

#### Giving

Pearson has teamed up with Kiva, the world's largest micro-lending platform, to provide micro-loans to people around the world who are locked out of traditional banking systems. To date, employees have made more than \$600,000 of loans to Kiva entrepreneurs, making Pearson third globally for total amount loaned by a business on Kiva.

In September, we launched a matching gifts campaign to mark the launch of the Global Goals and Project Literacy presence at UNGA. Throughout the entire month, employees across Pearson who gave to charities received a 4:1 match from Pearson. The campaign raised over \$430,000. Over the course of the year, employees supported more than 1,100 charities.

## 6. Social innovation

Lack of access to quality education for low-income and marginalised families is a global challenge that impacts both developing and developed economies

Central to our approach is a belief that commercial solutions can accelerate access to quality, affordable education, while presenting new business opportunities for Pearson. Uncovering, developing and scaling solutions, especially in places where education standards fall well behind the best in the world, can require us to challenge the way we think about our business. We invest in new technology as well as test innovative partnerships for our products to reach these markets

One example is Every Child Learning – our partnership with Save the Children. Our shared vision is to work together to find sustainable ways for the education system in Jordan to cope with the influx of displaced Syrian refugee children. We have donated £500,000 to fund the establishment of two Save the Children education centres in Amman, which are supporting Syrian refugees and host community children (5 to 13 years old) to get a quality education. We have made a further £1m commitment to work jointly with Save the Children to scope, research, design and develop new education solutions. That means going beyond traditional philanthropy to leverage the full potential of Pearson's global operations, networks and people

IMAGE REMOVED

IMAGE REMOVED

### Social innovation in practice – the Pearson Affordable Learning Fund

The Fund launched in 2012 and has a maximum commitment level of \$65m in capital. Its ambition is to reach millions of students from low income families by 2020, allowing access to high quality affordable education. Integral to its approach is to set improvements in learning outcomes and market-based returns as conditions of continued investment. The Fund has invested in innovative education start-ups in South Africa, Nigeria, Ghana, India and the Philippines. The Fund goes far beyond financial backing in that it contributes to good governance, and operational support to education entrepreneurs. The Fund enables innovation from which both Pearson and governments can learn, the cost per student in the schools in the fund portfolio is on par or lower than the per pupil cost in the public sector

### Every Child Learning

Providing education for children in conflict and emergency settings presents many unique challenges. As the conflict in Syria enters its sixth year, over two million Syrian children are no longer in school and even more are vulnerable to the risks of child labour, early marriage and recruitment into militia groups. To address this critical issue we have joined forces with the international organisation Save the Children to launch Every Child Learning. The three-year partnership worth £1.5m will increase educational opportunities for Syrian refugees and host communities, and innovate new solutions to help improve the delivery of education in emergency and conflict-affected settings

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# Governance report

IMAGE REMOVED

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Note: This section constitutes our directors' report as required by UK legislation.

# Governance overview

From Vivienne Cox, Senior independent director

Vivienne Cox  
Senior independent director

IMAGE REMOVED

During times of change, good governance is paramount. As a board we organise our work around four major themes where we believe we can add value: governance, strategy, performance and people.

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## Dear shareholders

The past year has seen some notable changes at Pearson, in terms of both personnel and portfolio, and as senior independent director, the board felt it was appropriate for me to set out these changes for you in greater detail

After ten years at Pearson, during which our business and the wider economy in which we operate have transformed markedly, Glen Moreno stepped down as chairman at the end of 2015. Whilst the last few months of 2015 were challenging for Pearson, Glen's legacy to the company can be seen in the well balanced and forward-thinking board of directors he has assembled which is working hard to steer Pearson back to growth. Having worked alongside Glen for the past four years on the board, and on behalf of Pearson as a whole, I would like to thank him for his deep commitment to Pearson and its mission and wish him the very best for the future.

Glen's successor as Pearson chairman, Sidney Taurel, officially took up his post in January 2016 and we are confident that his experience and dedication will help guide Pearson towards successful delivery of its key priorities. Read more about Chairman succession on p79 ➔

## Governance principles

During times of change, good governance is paramount. The board was closely involved with the strategic decisions to sell Pearson's interests in the Financial Times, The Economist and PowerSchool, providing input and challenge as matters progressed. We will continue to do so throughout the current phase of change.

**Our role and activities** As a board we organise our work around four major themes where we believe we can add value: governance, strategy, performance and people. Our board calendar and agenda provide ample time to focus on these themes and we have set out some examples of the business considered by the board, as well as the governance practices to which we adhere, on the pages that follow. Learn more about Board meetings and activities on p75 ➔

**UK Corporate Governance Code** This year, for the first time, we are reporting against the 2014 edition of the UK Corporate Governance Code (the Code). The board believes that during 2015 the company was in full compliance with all relevant provisions of the Code. A detailed account of the provisions of the Code can be found on the FRC's website at [www.frc.org.uk](http://www.frc.org.uk) and we encourage readers to view our compliance schedule on the company website at [www.pearson.com/governance](http://www.pearson.com/governance).

## Board and management

The Pearson board consists of senior executive management alongside a strong team of non-executive directors drawn from successful international businesses and education institutions with experience of corporate strategy, education, emerging markets, technology and consumer marketing

**Board changes** As is best practice, we continually assess and refresh the board to ensure we maintain an appropriate balance and diversity of skills and experience. In April 2015 we also bid farewell to David Arculus and Ken Hydon, who each served on the board for nine years, as remuneration and audit committee chairmen respectively. In addition to our new chairman, we have also welcomed two other directors to our board since our last report to shareholders. Coram Williams – a long-time Pearson and Penguin Random House colleague – joined the board on 1 August 2015, assuming the role of chief financial officer following Robin Freestone's departure, and in January 2016, Lincoln Wallen joined the board as a non-executive director bringing with him a wealth of digital and technology experience. We welcome Coram and Lincoln to the board, where they are already making valuable contributions to our governance and deliberations. Learn more about our Board of directors on p72-73 ➔

**Board and executive structure and balance** Our board consists primarily of non-executive directors, who bring a strong independent viewpoint, complementing the executive perspectives of John Fallon and Coram Williams. In addition, we invite members of the Pearson executive to attend a number of the board's sessions to bring insights and thoughts from across the business, such as at the board's overseas strategy sessions in Palo Alto, California and New Delhi, India. Learn more about the Overseas strategy sessions on p93 ➔

## Accountability See full section on p82-89 ➔

A key element of the board and audit committee's work each year is consideration of Pearson's risk appetite and the review of our principal risks. The 2014 edition of the Code introduced a requirement for the board to assess the company's prospects taking into account the current position and principal risks, and to make a viability statement on this basis. The audit committee supported the board in this process by examining the analysis and assumptions underlying the viability statement, considering the required inputs and evaluating the proposed disclosures resulting from the process. Learn more about Risk management on p38-40 and read the Viability statement on p118 ➔

## Engagement

See full section on p90-93 ➔

Engagement with shareholders and society as a whole is key to Pearson's mission to help people make progress in their lives through access to better learning. We have announced important partnerships during the past year, such as Project Literacy and our partnership with Save the Children, and the launch of the UN's Sustainable Development Goals has presented an opportunity for Pearson to become engaged with a wide section of stakeholders. As a result, our reputation & responsibility committee continues to expand its areas of focus, with increased sight of Pearson's social impact initiatives, social and traditional media engagement activity, and employee engagement matters. We also welcomed a number of shareholders to our Annual General Meeting (AGM) which, as always, was a valuable opportunity for our board and senior management to respond to shareholders' views and questions.

## Remuneration

See full section on p94-117 ➔

This year's directors' remuneration report refers to further incremental changes we have made in line with policy in 2015 to better align executive director compensation with the interests of our shareholders and how this policy was operated in 2015. To put our report into context, we have included a summary of the approved directors' remuneration policy report from 2013 which is not subject to a vote. Our remuneration policy was reviewed in 2013 to align with the company's strategy and organisation and was approved by shareholders at the 2014 AGM. We continue to operate executive remuneration in line with the approved policy and at present do not anticipate seeking shareholder approval for our policy again until required to do so at the 2017 AGM.

## Conclusion

I hope this report clearly sets out how your company is run, and how we align governance and our board agenda with the strategic direction of Pearson. We always welcome questions or comments from shareholders, either via our website ([www.pearson.com](http://www.pearson.com)) or in person at our Annual General Meeting.

IMAGE REMOVED

Vivienne Cox  
Senior independent director

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# Board of directors

## Chairman

IMAGE REMOVED

**Sidney Taurel** Chairman  
aged 67, appointed 1 January 2016

Sidney has over 40 years of experience in business and finance and is currently a board director and chairman of the Compensation Committee at IBM Corporation. He is also a director at McGraw Hill Financial Inc., a role from which he will step down during 2016. Sidney is senior advisor at global investment bank Moelis & Co and an advisory board member at pharmaceutical firms Takeda Pharmaceutical and Almirall. He was chief executive officer of global pharmaceutical firm Eli Lilly and Company from 1998 until 2008, chairman of the business from 1999 until 2008, and has been chairman emeritus since 2009. Sidney has received three US presidential appointments to the Homeland Security Advisory Council, the President's Export Council and the Advisory Committee for Trade Policy and Negotiations, and is an officer of the French Legion of Honour.

## Executive directors

IMAGE REMOVED

**John Fallon** Chief executive  
aged 53, appointed 3 October 2012

John became Pearson's chief executive on 1 January 2013. Since 2008 he had been responsible for the company's education businesses outside North America, and a member of the Pearson management committee. He joined Pearson in 1997 as director of communications and was appointed president of Pearson Inc. in 2000. In 2003, he was appointed CEO of Pearson's educational publishing businesses for Europe, Middle East and Africa. Prior to joining Pearson, John was director of corporate affairs at Powergen plc, and was also a member of the company's executive committee. Earlier in his career, John held senior public policy and communications roles in UK local government. He is an advisory board member of the Global Business Coalition for Education and a member of the Council of the University of Hull.

IMAGE REMOVED

**Coram Williams** Chief financial officer  
aged 42, appointed 1 August 2015

Coram joined Pearson in 2003 and has held a number of senior positions including finance and operations director for Pearson's English Language Teaching business in Europe, Middle East & Africa, interim president of Pearson Education Italia and head of financial planning and analysis for Pearson. In 2008 Coram became CFO of The Penguin Group and was latterly appointed CFO of Penguin Random House in 2013. Coram was trained at Arthur Andersen, and subsequently worked in both the auditing and consulting practices of the firm.

## Non-executive directors

### Key to committees

④	○
Audit Committee	Committee Chair
⑤	④
Nomination Committee	Remuneration Committee
⑥	
Reputation & Responsibility	

IMAGE REMOVED

**Linda Lorimer** Non-executive director  
aged 63, appointed 1 July 2013

Linda has a deep background in education strategy, administration and public affairs. She is senior counsellor to the president and provost of Yale University and until recently served as vice president for Global & Strategic Initiatives at Yale, where her duties included oversight of Yale's Office of International Affairs and Office of Digital Dissemination. Over a 30 year career in higher education, she has been responsible for many of Yale's administrative services including the university's public communications, alumni relations and Office of Sustainability. Previously Linda served as president of Randolph-Macon Woman's College in Virginia and was chair of the board of the Association of American Colleges and Universities. She also served on the boards of several public companies including as presiding director of the McGraw-Hill Companies.

IMAGE REMOVED

**Harish Manwani** Non-executive director  
aged 62, appointed 1 October 2013

Harish has an extensive background in emerging markets and senior experience in a successful global organisation. He was previously chief operating officer of consumer products company Unilever, having joined the company in 1976 as a marketing management trainee in India, and held senior management roles around the world, including North America, Latin America, Europe, Africa and Asia. He is non-executive chairman of Hindustan Unilever Limited in India, and serves on the boards of Whirlpool Corporation, Qualcomm Inc. and Nielsen Holdings. He is also on the board of the Indian School of Business and the Economic Development Board (EDB) of Singapore, and is global executive advisor at Blackstone Private Equity.

## Non-executive directors

IMAGE REMOVED

**Elizabeth Corley, CBE**  
Non-executive director  
aged 59, appointed 1 May 2014

Elizabeth is non-executive vice chair of Allianz Global Investors, where she was chief executive officer from 2005 to 2016. She was previously at Merrill Lynch Investment Managers (formerly Mercury Asset Management) and Coopers & Lybrand. Elizabeth is acting chair of the FICC Markets Standards Board, a member of the ESMA stakeholder group and an advisory council member of TheCityUK. She is a non-executive director of BAE Systems plc and the Financial Reporting Council. In addition, she is a member of FEAM's management committee, the CFA Future of Finance Council, the Supervisory Board of Euler SA, a council member of the City of London IRSG and a member of the Committee of 200. She is a fellow of the CFA and the Royal Society of Arts and is also a crime fiction author.

IMAGE REMOVED

**Vivienne Cox, CBE**  
Senior independent director  
aged 56, appointed 1 January 2012

Vivienne has wide experience in energy, natural resources and business innovation. She worked for BP plc for 28 years, in Britain and Continental Europe, in posts including executive vice president and chief executive of BP's gas, power and renewables business and its alternative energy unit. She is non-executive director of Stena International and chairman of the supervisory board of Vallourec, which supplies tubular systems for the energy industry. She is also lead independent director at the UK Department for International Development. Vivienne was appointed Commander of the Order of the British Empire (CBE) in the 2016 New Year Honours for services to the UK Economy and Sustainability.

IMAGE REMOVED

**Josh Lewis** Non-executive director  
aged 53, appointed 1 March 2011

Josh's experience spans finance, education and the development of digital enterprises. He is the founder of Salmon River Capital LLC, a New York based private equity/venture capital firm focused on technology-enabled businesses in education, financial services and other sectors. Over a 25-year career in active, principal investing, he has been involved in a broad range of successful companies including several pioneering enterprises in the education sector. In addition, he has long been active in the non-profit education sector, with associations including New Leaders, New Classrooms and the Bill & Melinda Gates Foundation. He is also a non-executive director of several enterprises in the fin-tech/data, education and other sectors.

## Non-executive directors

IMAGE REMOVED

**Tim Score** Non-executive director  
aged 55, appointed 1 January 2015

Tim has extensive experience of the technology sector in both developed and emerging markets, having served as chief financial officer of ARM Holdings plc, the world's leading semiconductor IP company, a position he held for 13 years. He is an experienced non-executive director and currently sits on the boards of The British Land Company plc and HM Treasury. He served on the board of National Express Group plc from 2005 to 2014, including time as interim chairman and six years as the senior independent director. Earlier in his career, Tim held senior finance roles with Rebus Group, William Baird, BTR plc and others.

IMAGE REMOVED

**Lincoln Wallen** Non-executive director  
aged 55, appointed 1 January 2016

Lincoln is chief technology officer for DreamWorks Animation, the global family entertainment company, a position he has held since 2012, having joined the company as head of research and development in 2008. Prior to this, Lincoln served as chief technology officer for the mobile business of Electronic Arts, Inc., a leading interactive entertainment software company. He has held senior positions at Criterion Software, MathEngine plc and is a non-executive director of the Smith Institute for Industrial Mathematics & System Engineering. Lincoln is also an advisory board member of Hewlett Packard Enterprise and a member of the STEM Advisory Committee of the National Academy foundation. Lincoln was formerly a lecturer and reader in computation at the University of Oxford.

**Pearson board members bring a wide range of experience, skills and backgrounds which complement our strategy.**

## Experience of chairman and non-executive directors

Digital/technology experience

63%

IMAGE REMOVED

Emerging market experience

38%

IMAGE REMOVED

Education/learning sector experience

63%

IMAGE REMOVED

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## Board governance and activities

### Board of directors

**Composition of the board** The board currently consists of the chairman, Sidney Taurel, two executive directors including the chief executive, John Fallon, and seven independent non-executive directors

**Chairman and chief executive** There is a defined split of responsibilities between the chairman and the chief executive. The roles and responsibilities of the chairman and chief executive are clearly defined, set out in writing and reviewed and agreed by the board annually

**Chairman's significant commitments** There were no changes to the chairman's significant commitments between his appointment to the Pearson board on 1 January 2016 and the date of this report. Mr Taurel has announced that he will step down from the board of McGraw Hill Financial, Inc. at its 2016 annual shareholders' meeting

**Independence of chairman** Sidney Taurel was considered to be independent upon his appointment as chairman on 1 January 2016

**Independence of directors** All of the non-executive directors who served during 2015 were considered by the board to be independent for the purposes of the Code. Lincoln Wallen was considered to be independent upon his appointment to the board on 1 January 2016. The board reviews the independence of each of the non-executive directors annually. This includes reviewing their external appointments and any potential conflicts of interest as well as assessing their individual circumstances in order to ensure that there are no relationships or matters likely to affect their character or judgement. In addition to this review, each of the non-executive directors is asked annually to complete an independence questionnaire to satisfy requirements arising from Pearson's US listing

### Key roles

Role	Name	Responsibility
Chairman	Sidney Taurel	The chairman is primarily responsible for the leadership of the board and ensuring its effectiveness. The chairman sets the board's agenda and promotes open, constructive debate of all agenda items and effective decision-making. He also ensures that the views of shareholders are communicated to the board.
Chief executive	John Fallon	The chief executive is responsible for the operational management of the business and for the development and implementation of the company's strategy as agreed by the board and management. He is responsible for developing operational proposals and policies for approval by the board, and promotes Pearson's culture and standards.
Senior independent director	Vivienne Cox	The senior independent director's role includes meeting regularly with the chairman and chief executive to discuss specific issues, as well as being available to shareholders generally should they have concerns that have not been addressed through the normal channels.
Committee chairmen	Tim Score, Elizabeth Corley, Vivienne Cox and Sidney Taurel	The committee chairmen are responsible for leading the board committees and ensuring their effectiveness. They set the committees' agendas, in consultation with the company's management, and report to the board on committee proceedings.
Company secretary	Stephen Jones	The company secretary acts as secretary to the board and its committees, ensuring compliance with board procedures and advising on governance matters. He is responsible, under the direction of the chairman, for ensuring the board receives accurate, timely and clear information. The company secretary organises new director inductions and ongoing director training.

### Gender split of board

● Men	7
● Women	3

Figures as at 4 March 2016

IMAGE  
REMOVED

### Length of tenure of non-executive directors

● Under 3 years	5
● 3 to 6 years	2

Figures as at 4 March 2016

IMAGE  
REMOVED



**Conflicts of interest** Under the Companies Act 2006 (the Act), directors have a statutory duty to avoid conflicts of interest with the company. The company's articles of association (Articles) allow the directors to authorise conflicts of interest. The company has established a procedure to identify actual and potential conflicts of interest, including all directorships or other appointments to, or relationships with, companies which are not part of the Pearson group and which could give rise to actual or potential conflicts of interest. Once notified to the chairman or company secretary, such potential conflicts are considered for authorisation by the board at its next scheduled meeting. The relevant director cannot vote on an authorisation resolution, or be counted in the quorum, in relation to the resolution relating to his/her conflict or potential conflict. The board reviews any authorisations granted on an annual basis.

#### Board meetings

The board held six scheduled meetings in 2015, with discussions and debates focused on the key strategic issues facing the company. Major items covered by the board in 2015 are shown in the table below. In addition to the six formal meetings, the board met by telephone in January 2015 to consider the January trading update to be issued to the market, and by telephone in October 2015 to consider the market's reaction to Pearson's October trading update and to begin to plan the proposed strategic course of action.

#### The role and business of the board

The board is deeply engaged in developing and measuring the company's long-term strategy, performance and value. We believe that it adds a valuable and diverse set of external perspectives and that robust, open debate about significant business issues brings an additional discipline to major decisions.

#### Board meeting focus during the year 2015

Topic	Activity	
Governance	Annual review of authorised conflicts of interest	Focus on forthcoming AGM and review of shareholder issues
	Review of division of responsibilities between chairman and chief executive	Shareholder activism and defence plan
	Appointment of company secretary	Treasury policy approval
	Update on Pearson System of Courses (PSoC) including hands-on demonstration of courseware	Risk appetite
	South African Black Economic Empowerment (BEE) overview	Approval of committee terms of reference
	Supply chain outsourcing arrangements	Enterprise risk management review Read more on p38
Strategy	Operating and strategic plan updates	Approval of schedule of authority limits
	Brand strategy Read more on p7	Offsite strategy meeting in California focusing on digital disruption in education
	Regular product demonstrations	Offsite strategy meeting in New Delhi focusing on Brazil, China, India and South Africa Read more on p93
	Consideration of proposed corporate transactions including sales of PowerSchool, the Financial Times and The Economist	
Performance	2014 preliminary results and annual report and accounts	Triennial pension valuation
	Review of investor relations strategy and share price performance	Final and interim dividend proposals
	Interim results and trading updates	Monthly management reports
	Balance sheet strategy	Draft 2016 operating plan and three-year financials
People	Overview of 'The Summit' – Pearson's senior leadership conference	India key talent and leadership team dinner at New Delhi strategy meeting
	Rising Stars breakfast at overseas strategy meetings	

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## Board governance and activities continued

A schedule of formal matters reserved for the board's decision and approval is available on our website, at [www.pearson.com/governance](http://www.pearson.com/governance)

The board receives timely, regular and necessary financial, management and other information to fulfil its duties. Comprehensive board papers are circulated to the board and committee members at least one week in advance of each meeting and the board receives regular reports from the chief executive. In addition to meeting papers, a library of current and historic corporate information is made available to directors electronically to support the board's decision-making process. Directors can obtain independent professional advice, at the company's expense, in the performance of their duties as directors. All directors have access to the advice and services of the company secretary.

Non-executive directors meet with local senior management every time board meetings are held at the locations of operating companies, such as during the board's 2015 visits to Palo Alto, California and New Delhi, India. This allows the non-executive directors to share their experience and expertise with senior managers as well as allowing them to better understand the abilities and motivations of senior management, which in turn will help them assess the company's prospects and plans for succession.

### Standing committee

A standing committee of the board was established to approve certain ordinary course of business items such as banking matters, guarantees, intra-group transactions and to make routine approvals relating to employee share plans.

The committee has written terms of reference, reviewed and approved each year, which clearly set out its authority and duties. These can be found on the company website at [www.pearson.com/governance](http://www.pearson.com/governance).

### Culture and values of the board

As evidenced during its externally facilitated evaluation in 2014, as a whole and at an individual level, the board feels wholly committed to Pearson's values and mission. The reputation & responsibility committee's remit includes oversight of Pearson's values and culture, and it has continued to monitor work in these areas throughout the year.

### Board attendance

The following table sets out the attendance of the company's directors at scheduled board meetings during 2015.

	Board meetings attended
<b>Chairman</b>	
Glen Moreno	6/6
<b>Executive directors</b>	
John Fallon	6/6
Robin Freestone (note 1)	4/4
Coram Williams (note 2)	2/2
<b>Non-executive directors</b>	
David Arculus (note 3)	2/2
Elizabeth Corley	6/6
Vivienne Cox	6/6
Ken Hydon (note 4)	1/2
Josh Lewis	6/6
Linda Lorimer	6/6
Harish Manwani	6/6
Tim Score	6/6

Note 1. Stood down on 1 August 2015.

Note 2. Appointed on 1 August 2015.

Note 3. Stood down on 24 April 2015.

Note 4. Stood down on 24 April 2015. Unable to attend one meeting due to personal reasons.

### Succession planning

The board considers oversight of succession planning – not only at board and executive management level but for all key positions throughout the business – as one of its prime responsibilities. At board level, the primary focus during the year was to identify suitable candidates for the role of chairman.

The company has formal contingency plans in place for temporary absence of the chief executive for health or other reasons. The matter of chief executive succession is a standing item for discussion and review by the chairman and chief executive annually. Succession planning for the board and chair is considered annually, and as part of the recent restructuring programme, there has been a review of key positions at executive management level.

### Board evaluation

As reported last year, towards the end of 2014, an externally facilitated board effectiveness review was conducted by external evaluator, JCA Group. In addition to facilitating this review, JCA Group used the information and insight they had gleaned from the individual members of the board to help them form a brief and an overview of the characteristics that Pearson would be looking for in a new chairman. JCA then used this insight to inform the chairman search which took place during 2015, and resulted in the eventual appointment of Sidney Taurel as Pearson chairman. See p79 for a full review of chairman succession at Pearson.

The board evaluation for 2015 was conducted on an internal basis. With the forthcoming departure of Glen Moreno, the arrival of a new chairman, together with the appointment of a new CFO and the imminent appointment of a new company secretary, it was agreed that the 2015 review should focus mainly on the support and information that the board and committees receive in order to ensure that the existing processes are sufficient and fit for purpose. To that end, Stephen Jones, Pearson's company secretary, interviewed each of the non-executive directors to understand their thinking on a number of board and committee-related support activities.

### Process and recommendations

The review focused on the scheduling, arrangements and logistics for all board and committee meetings, the quality and usefulness of the regular information flow to the board and committees, including the use of electronic board papers, regular CEO and CFO updates and other information, board induction and training, the payment of non-executives' fees and expenses and any other items or suggestions for improvements. The exercise proved very useful as an opportunity to take stock of current practice, to test whether the board views that as appropriate, and to think about those areas where improvements could be made. As a result of these discussions, we are re-thinking the schedule of board and committee meetings during the course of the year, including the topics to be considered at those meetings and their venues. In addition, we are refining some of the information that the board receives in order that the non-executives be able to be more effective. We heard that more could be done by management to 'curate' some of the information that is sent to non-executives and to make clear to them what is key information and what is useful to know. We are also refining the regular CEO and CFO updates to the board, in order to ensure they provide exactly the information that the

board requires to help it track progress against a number of key milestones. This is an ongoing process, and we will continue to monitor the effectiveness of our internal processes and to compare what we do against others.

### Personal objectives

In addition to the evaluation of the board as a whole, executives are also evaluated each year on their performance against personal objectives under the company's annual incentive plan.

The non-executive directors, led by the senior independent director, also conduct a review of the chairman's performance.

### Committee evaluation

In addition to the review of the board, committees and individual directors described above, the audit and remuneration committees each undertook a further evaluation process to review their performance and effectiveness, as they do each year.

The process involves distribution of questionnaires to audit and remuneration committee members, as well as key stakeholders in each committee, seeking views on matters including committee roles and responsibilities, quality and timeliness of meeting materials, opportunity for discussion and debate, dialogue with management and access to independent advice. Responses are then evaluated and presented to the respective committee at a scheduled meeting, with key themes being drawn out for discussion.

### Directors' training and induction

Directors receive a significant bespoke induction programme and a range of information about Pearson when they join the board. This includes background information on Pearson and details of board procedures, directors' responsibilities and various governance-related issues, including procedures for dealing in Pearson shares and their legal obligations as directors. The induction also typically includes a series of meetings with members of the board, the Pearson executive and senior management, presentations regarding the business from senior executives and a briefing on Pearson's investor relations programme. The induction programme for Lincoln Wallen is ongoing, tailored to his specific areas of focus, such as time with Pearson's technology leaders, and relevant to the board committees he has joined. Read about the induction programme for Pearson's new chairman, Sidney Taurel on p79.

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## Board governance and activities continued

All directors receive training in the form of presentations about the company's operations, through board meetings held at operational locations and by encouraging the directors to visit local facilities and management as and when their schedule allows, including if they are travelling to a country or region on non-Pearson business. The company secretary and general counsel, in conjunction with Pearson's advisers, monitor legal and governance developments and update the board on such matters as agreed with the chairman. Directors can also make use of external courses.

### Directors' indemnities

A qualifying third party indemnity (QTPI), as permitted by the Articles and sections 232 and 234 of the Act, has been granted by the company to each of its directors. Under the provisions of the QTPI the company undertakes to indemnify each director against liability to third parties (excluding criminal and regulatory penalties) and to pay directors' costs as incurred, provided that they are reimbursed to the company if the director is found guilty, the court refuses to grant the relief sought or, in an action brought by the company, judgment is given against the director. The indemnity has been in force for the financial year ended 31 December 2015 and is currently in force.

The company has purchased and maintains directors' and officers' insurance cover against certain legal liabilities and costs for claims in connection with any act or omission by such directors and officers in the execution of their duties.

### Board committees

The board has established four formal committees: audit, nomination, remuneration, and reputation & responsibility. The chairmen and members of these committees are appointed by the board on the recommendation (where appropriate) of the nomination committee and in consultation with each relevant committee chairman. In addition to these formal board committees, the standing committee also operates with board level input.

### More committee information

Audit committee	p82 ➔
Nomination committee	p80 ➔
Remuneration committee	p94 ➔
Reputation & responsibility committee	p90 ➔
Standing committee	p76 ➔

The committees focus on their own areas of expertise, enabling the board meetings to focus on governance, strategy, performance and people, thereby making the best use of the board's time together as a whole. The committee chairmen report to the full board at each meeting immediately following their sessions, ensuring a good communication flow whilst retaining the ability to escalate items to the full board's agenda if appropriate.

### Board committee attendance

The following table shows attendance by directors at committee meetings throughout 2015.

	Audit	Remuneration	Nomination	Reputation & responsibility
Glen Moreno	-	4/4	6/6	-
David Arculus (note 1)	2/2	2/2	2/2	-
Elizabeth Corley	-	4/4	6/6	-
Vivienne Cox	4/4	4/4	6/6	3/3
Ken Hydon (note 2)	2/2	1/2	1/2	-
Josh Lewis	-	4/4	6/6	-
Linda Lorimer	4/4	-	6/6	3/3
Harish Manwani	-	-	6/6	3/3
Tim Score (note 3)	4/4	1/1	6/6	-

Note 1 Stood down on 24 April 2015

Note 2 Stood down on 24 April 2015. Unable to attend one remuneration committee and one nomination committee meeting due to personal reasons

Note 3 Joined remuneration committee on 2 October 2015

# Chairman's succession

## Commencing the search

Following Glen Moreno's announcement at the 2015 AGM that he was planning to step down as chairman by the end of the year, Pearson commenced its search for a suitable successor. The selection process was led by Vivienne Cox, our senior independent director, and an external search firm, JCA Group, was engaged to assist and advise Pearson on the search and appointment process.

Taking the findings from the 2014 board effectiveness review as a starting point, and in consultation with the nomination committee and the chief executive, JCA designed a specification for the desired candidate which included the following key attributes:

- › Highly experienced leader of large global businesses, ideally with a proven track record as a chairman
- › Truly global player in outlook, approach and understanding with deep knowledge of and experience in Pearson's key geographic markets
- › Genuine interest in embracing digital technology to benefit the customer and the company

In agreeing the specification, the board emphasised the importance of finding someone who was excited by and demonstrated empathy with Pearson's mission, values, goals and people.

## Choosing a successor

Candidate profiles were prepared by JCA for consideration by Ms Cox, who then consulted the nomination committee and chief executive to agree a shortlist of strong candidates. She held initial meetings with the shortlisted candidates, and recommended a number of them to progress through to the next stage, where they met with the chief executive, following which a search sub-committee was formed, comprising Linda Lorimer and Tim Score, who each met with the strongest candidates.

Ms Cox reported regularly to the nomination committee throughout the search and interview stages, and following consideration of interview feedback it became clear to the board and the nomination committee that Sidney Taurel was the most suitable candidate to succeed Glen Moreno as chairman. Agreement having been reached, the nomination committee recommended that the final decision be delegated to a standing committee of the board to formalise Mr Taurel's appointment once the necessary checks had been satisfactorily completed.

## Chairman's selection process

JCA Group was engaged with a clear set of criteria to find a highly experienced global business leader, with proven ability to lead an industry through a period of change, of which technology is a key part, and in dealing with a complex regulatory environment.

- 1 Identify** Using the agreed brief, JCA and the senior independent director considered and refined a list of potential candidates, seeking input from the nomination committee on which candidates should be approached.
- 2 Interview** The senior independent director led a series of interviews with the shortlisted candidates. Preferred candidates then met with the chief executive and with the two members of the search committee, following which the nomination committee met to discuss feedback.
- 3 Select** After further meetings, including with Glen Moreno, Sidney Taurel was recommended for appointment. He was selected having successfully led a global multinational company, operating in some of the most challenging political and regulatory environments, and having lived and worked all over the world, including the US, UK and Brazil – three of Pearson's most important markets.
- 4 Appoint** Sidney's appointment as chairman was approved and announced in October 2015 to take effect on 1 January 2016, the date of his formal appointment to the Pearson board.

## Appointment and induction

Pearson approved and announced the appointment of Sidney Taurel on 26 October 2015, and he joined the board on 1 January 2016, assuming the role of chairman immediately upon appointment.

Mr Taurel met the independence requirements set out in the Code on appointment and has confirmed he is able to dedicate the requisite time to the role.

A comprehensive induction programme was put in place for Sidney during the three months following the announcement of his appointment. A series of one to one meetings was held with members of the Pearson executive to enable Sidney to understand all aspects of Pearson's global business, the challenges facing the enabling functions such as technology, HR and corporate affairs, and the wider trends in education. Sidney also met with Pearson's brokers, corporate advisers and lawyers to understand broader regulatory matters and obligations. During his US-based induction, Sidney attended Pearson's national sales conference focusing on issues and hot topics in the US business, and spent time in Washington, DC with the corporate affairs and government relations team.

# Nomination committee report

Chairman of nomination committee  
Sidney Taurel

Members Elizabeth Corley,  
Vivienne Cox, Josh Lewis,  
Linda Lorimer, Harish Manwani,  
Tim Score, Sidney Taurel  
and Lincoln Wallen

IMAGE  
REMOVED

“As chairman of the nomination committee, one of Glen Moreno’s outstanding legacies to Pearson was his ability to attract first-rate non-executives to the Pearson board. I look forward to chairing this committee as we work to continually refresh the board, its committees and to think about succession planning at senior levels”

## Committee responsibilities include

- 1 Appointments** Identifying and nominating candidates for board vacancies
- 2 Balance** Ensuring that the board and its committees have the appropriate balance of skills, experience, independence, diversity and knowledge to operate effectively
- 3 Succession planning** Reviewing the company’s leadership needs with a view to ensuring the continued ability of the organisation to compete effectively in the marketplace

## Key activities in 2015

Objectives	Actions
Succession process and appointment of new chairman of the board	Appointment of Sidney Taurel as chairman
Identify and appoint additional non-executive director with digital technology experience	Appointment of Lincoln Wallen as non-executive director with experience in digital technology
Complete search process for new chief financial officer	Appointment of Coram Williams as chief financial officer

For nomination committee attendance see overview table on p78

## Nomination committee role and composition

The committee primarily monitors the composition and balance of the board and its committees, and identifies and recommends to the board the appointment of new directors and/or committee members. The chairman of the board also chairs the nomination committee, and all non-executive directors serve as members of the committee. The chief executive attends committee meetings by invitation.

## Chairman role

Although the chairman of the board chairs the nomination committee, he is not permitted to chair meetings when the appointment of his successor is being considered or during a discussion regarding his performance. At such times, the senior independent director will chair the meetings, such as during the search process for Glen Moreno’s replacement during 2015 when Vivienne Cox chaired the committee’s meetings. [Learn more about Chairman succession on p79](#)

## Committee meetings and appointments

The nomination committee meets at least once a year and at other times as and when required. During 2015, the committee met six times with its primary focus being to discuss the search criteria, prepare role descriptions and consider suitable candidates for the role of chairman of the board and for an additional non-executive director with particular experience in digital technology to complement our strategy. The non-executive search culminated in the successful appointment of Lincoln Wallen to the board with effect from 1 January 2016.

## Terms of reference

The committee has written terms of reference which clearly set out its authority and duties. These are reviewed annually and can be found on the company website at [www.pearson.com/governance](http://www.pearson.com/governance)

Pearson uses a number of leading firms in its board and executive search activities. JCA Group was engaged to assist with the recruitment of Sidney Taurel. In addition to board search activity, JCA Group facilitated Pearson's board evaluation in 2014. JCA Group has no other connection to Pearson apart from in relation to search activity and the external facilitation of the 2014 board evaluation. An external search consultancy, Spencer Stuart, was used during the recruitment process for Lincoln Wallen. Spencer Stuart does not have any other connection to Pearson apart from as a search consultancy.

Learn more about the Board of directors on p72-73 ➔

#### Diversity

The board embraces the Code's underlying principles with regard to board balance and diversity, including gender diversity. The nomination committee ensures that the directors of Pearson demonstrate a broad balance of skills, experience and nationalities, to support Pearson's strategic development and reflect the global nature of our business.

The nomination committee and the board always take account of diversity in its broadest sense when considering board appointments whilst ensuring that appointments are made based on merit and relevant experience. We believe the global backgrounds of our board members contribute to diversity of experience and thought.

In 2011, Lord Davies set FTSE 100 companies a target of having 25% female representation on their boards by 2015. Pearson is proud of the gender diversity of its board, having exceeded Lord Davies' target with 30% female representation on the board, and notes Lord Davies' recommended next steps for continued improvement in diversity on boards, including the extension of good diversity practices to the layers of executive management below the board.

Immediately below board level, the Pearson executive, not including the chief executive and chief financial officer who are main board directors, has two female members out of a total of nine (representing 22%). Our senior leadership team, up to and including two reporting levels from the chief executive, shows a strong pipeline of female talent with women representing 34% of our senior leaders.

Pearson considers diversity as an important issue across the company, not just at board level. One of the key aims of Pearson's diversity policy is to increase the number of leaders coming from a diverse background, such as through our range of networks and advancement programmes for employees. Learn more about Diversity and inclusion throughout Pearson on p62 ➔

IMAGE REMOVED

Sidney Taurel  
Chairman of nomination committee

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## Audit committee report

**Chairman of audit committee**  
Tim Score

**Members** Vivienne Cox,  
Linda Lorimer, Tim Score  
and Lincoln Wallen

IMAGE  
REMOVED

“During 2015, the committee conducted a number of deep dives into selected principal risks, and as chairman of the committee, I work closely with Coram Williams to ensure Pearson’s finance function is well-placed to support the global business effectively.”

### Committee responsibilities include oversight of

- 1 **Reporting** The quality and integrity of financial reporting and statements and related disclosure
- 2 **Policy** Group policies, including accounting policies and practices
- 3 **External audit** External audit, including the appointment, qualification, independence and the performance of the external auditor
- 4 **Risk and internal control** Risk management systems and internal control environment including the performance of the internal audit function
- 5 **Compliance** Compliance with legal and regulatory requirements in relation to financial reporting and accounting matters

For audit committee meeting attendance see overview table on p78 ➔

### Terms of reference

The committee has written terms of reference which clearly set out its authority and duties. These are reviewed annually and can be found on the company website at [www.pearson.com/governance](http://www.pearson.com/governance) ➔

### Audit committee role

The committee has been established by the board primarily for the purpose of overseeing the accounting, financial reporting, internal control and risk management processes of the company and the audit of the financial statements of the company. As a committee, we are responsible for assisting the board’s oversight of the quality and integrity of the company’s external financial reporting and statements and the company’s accounting policies and practices.

Pearson’s internal auditor has a dual reporting line to the chief financial officer and to me, and external auditors have direct access to the committee to raise any matters of concern and to report on the results of work directed by the committee. As audit committee chairman, I report to the full board at every board meeting immediately following a committee meeting. As a committee, we also review the independence of the external auditors, including the provision of non-audit services (further details of which can be found on page 119 and note 4 to the financial statements), ensure that there is an appropriate audit relationship and that auditor objectivity and independence are upheld.

### Audit committee changes

2015 saw the retirement from Pearson of Ken Hydon, who had been chairman of the committee for nine years, and David Arculus, also a long-serving member of the committee. I took over from Ken as committee chairman in April, and have since worked with Coram Williams looking closely at Pearson’s finance function to ensure it is well-placed to support the global business effectively. In March 2016 Lincoln Wallen joined the committee, bringing extensive technology experience, and together we have a good balance of skills and knowledge on the committee with experience covering all aspects of the sector in which Pearson operates.

### Fair, balanced and understandable reporting

We are mindful of the Code’s provision C 1.1 relating to fair, balanced and understandable reporting and we build sufficient time into our annual report timetable to ensure that the full board receives sufficient opportunity to review, consider and comment on the report as it progresses. Learn more about Fair, balanced and understandable reporting on p119 ➔

### Risk assessment, assurance and integrity

A key role of the committee is to provide oversight and reassurance to the board with regard to the integrity of the company’s financial reporting, internal control policies, and procedures for the identification, assessment and reporting of risk. During 2015 we



conducted a number of deep dives into selected principal risks. Learn more about Principal risks and uncertainties on p41-45 ➔

#### Data security and data privacy

Recognising particular sensitivities around the schools and assessment data held on our systems, the committee undertook deep dives in each of these risk areas, and updates from the chief information security officer and newly-appointed chief privacy officer feature as regular items on the committee's agenda. To ensure adequate visibility of data security and privacy protocols throughout the company, new policies and procedures were developed during the year, including the introduction of mandatory data security and privacy training for employees.

Focusing on data security, the committee considered progress made to date and reviewed the roadmap for the next two years, including the aim of continuing to increase Pearson's data security risk maturity. Key to developing this maturity has been the shift of data security from a purely technical risk to a business critical one.

The risk management framework around data privacy needs to take Pearson's global footprint into account. Challenges exist in North America due to the large number of federal and state laws on data privacy, which are coupled with a changing picture globally as jurisdictions update their laws in a fast moving environment. Data privacy has been identified as a global strategic risk for Pearson, leading to the appointment of a chief privacy officer at the start of 2015. Meaningful progress has been made since that appointment, including the development of a new governance framework to address data privacy risks.

#### Business transformation

Ongoing business transformation, the next wave of which was announced in January 2016, is another of Pearson's key risks and opportunities. The committee receives regular updates on the transformation as a whole and during the year carried out a deep dive into The Enabling Program. As an important operational simplification project, The Enabling Program will feature as a standing item on the committee's agenda in 2016 as work progresses. Learn more about The Enabling Program on p6 and 41 ➔

#### Update on previous areas of focus

Last year, we highlighted health and safety (H&S) and anti-bribery and corruption (ABC) as areas to which the committee had paid particular attention. During 2015, the committee continued to monitor those areas, reviewing progress made and audit results.

The committee reviewed the overall H&S landscape at Pearson, in particular evaluating the progress made since the launch of the global H&S policy in December 2013. It noted that continued improvements are being implemented in standards, facilitated by the support of H&S coordinators, and was satisfied with the developments in relation to safeguarding and the progress that the safeguarding officer has made since appointment in August 2014.

The committee reviewed the ongoing implementation of ABC policies, where progress to date has been good, and noted that a more comprehensive and risk-based ABC training programme would continue to be rolled out in 2016. We also considered how the compliance and legal functions were working together to ensure appropriate stances in each jurisdiction, while maintaining Pearson's zero tolerance approach to ABC.

#### Audit committee meetings and activities

The committee met four times during the year with the following in attendance: the chief financial officer, general counsel, SVP internal audit and compliance, members of the senior management team, and the external auditors. Additionally, the chief executive and chairman periodically attended committee meetings. One of the internal audit directors and the VP compliance and risk assurance also attend meetings, giving the committee direct contact with key leadership in those areas. The committee also met regularly in private with the external auditors and the SVP internal audit and compliance.

At every meeting, the committee considered reports on the activities of the internal audit and compliance functions, including the results of internal audits, risk reviews, project assurance reviews and fraud and whistleblowing reports. The committee also monitored the company's financial reporting, internal controls and risk management procedures, reviewed the non-audit services provided by PwC and considered any significant legal claims and regulatory issues in the context of their impact on financial reporting.

Learn more about the Key activities of the audit committee on p84 ➔

IMAGE REMOVED

Tim Score  
Chairman of audit committee

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## Audit committee report continued

### Audit committee meeting focus during 2015

Reporting	Accounting and technical updates	The 2014 annual report and accounts preliminary announcement, financial statements and income statement	Form 20 F and related disclosures including the annual Sarbanes Oxley Act section 404 attestation of financial reporting internal controls
	Impact of legal claims and regulatory issues on financial reporting		Review of interim results and trading updates
Policy	Accounting matters and Group accounting policies	Analysis supporting viability statement Read more on p40	Annual review of treasury policy and strategy
		Annual review and approval of external auditor policy	
External audit	Provision of non-audit services by PwC	Receipt of the external auditors' report on the Form 20 F and on the year end audit	Remuneration and engagement letter of the external auditors
		Reappointment of the external auditors	Review opinion on interim results
		Confirmation of auditor independence	Review of the effectiveness of the external auditors
		2015 external audit plan	
Risk and internal control	Internal audit activity reports and review of key findings	Assessment of the effectiveness of the internal control environment and risk management systems	Risk deep dives: data security, data privacy, health & safety, legal risks and legal function
	Enterprise risk management Read more on p38	Review of internal audit terms of reference	anti bribery and corruption, tax
	2016 internal audit plan		Data security incidents reporting
			Treasury risk review
Compliance and governance	Fraud, whistleblowing reports and Code of Conduct matters	Compliance with the UK Corporate Governance Code	Review of the committee's terms of reference
	Review of The Enabling Program as it proceeded	Compliance with SEC and NYSE requirements including Sarbanes-Oxley Act	Review of the effectiveness of the committee and the group internal audit function

### Members

All of the audit committee members are independent non-executive directors and have financial and/or related business experience due to the senior positions they hold or have held in other listed or publicly traded companies and/or similar public organisations. Tim Score, who assumed the chairmanship of the committee in April 2015, is the company's designated financial expert, having recent and relevant financial experience, and is an Associate Chartered Accountant. He also serves as audit committee chairman for The British Land Company plc and until 2014 was audit committee chairman at National Express Group plc.

The qualifications and relevant experience of the other committee members are detailed on p72-73.

### Audit committee meetings during 2015

During the year, the matters considered by the committee included those shown in the table above.

In February 2016, the committee also considered the 2015 annual report and accounts, including the preliminary announcement, financial statements, strategic report, directors' report and corporate governance compliance statement.

### External audit

The committee reviews and approves the appointment of the external auditors, taking account of the views of management. The committee reviewed the effectiveness and independence of the external auditors during 2015, as it does every year, and remains satisfied that the auditors provide effective independent challenge to management.

In 2015, the external auditor review was conducted by distributing a questionnaire to key audit stakeholders including members of the audit committee, the chief executive, chief financial officer, company secretary, SVP internal audit and compliance, SVP finance for each Geography and Line of Business and other heads of corporate functions. Overall, responses to the questionnaire were very positive, indicating an effective external audit process. As part of the follow-up to the review, the lead audit partner explained to the committee how PwC were monitoring and evaluating each area highlighted in the review and confirmed that they would consider how to adapt their approach in light of specific comments received.

In addition, in accordance with Pearson's external auditor policy, internal audit performs an annual assessment of audit fees, services and independence which forms the basis of a recommendation by the committee to the board in respect of the appointment and compensation of the external auditors.

The committee will continue to review the performance of the external auditors on an annual basis and will consider their independence and objectivity, taking account of all appropriate guidelines. There are no contractual obligations restricting the committee's choice of external auditors. In any event, the external auditors are required to rotate the audit partner responsible for the Pearson audit every five years. The current lead audit partner rotated onto Pearson's audit in 2013.

Pearson's last audit tender was in respect of the 1996 year end, and resulted in the appointment of Price Waterhouse as auditors. Developments at an EU level regarding mandatory audit rotation for listed companies have changed the UK landscape on audit tendering and rotation. The committee has reviewed the timetable for tendering and has taken into account all relevant regulation and guidance. New EU regulations and the ruling by the Competition and Markets Authority (CMA) has imposed mandatory tendering and rotation requirements from 2016.

In considering the appropriate audit tender timetable for Pearson in light of these requirements, the committee has also taken account of the significant business change being experienced by the Group and is monitoring the extent to which the Group is drawing upon the services of other accounting firms. The Group has commenced a series of programmes to implement major efficiency improvements across all our enabling functions – technology, finance, HR – to bring the general and administrative costs of running Pearson more in line with global best practice, these include a major finance transformation programme, including the implementation of new financial systems and changes to our transaction processing and control activities, that we expect to continue through 2016, 2017 and into 2018. The Group is supported in these changes, and more broadly, by external advisers including accounting firms.

It is the committee's intention to appropriately manage auditor independence and rotation, firstly, to ensure that a tender has the right level of suitably qualified and independent firms competing, including allowing for a planned transition and, secondly, to undertake this in a way that does not unnecessarily disrupt the business changes underway and provides consistency of independent oversight from external auditors through those changes.

Notwithstanding that the above EU mandatory rotation rules require a new auditor to be appointed no later than for the 2024 year end, it is the current expectation of the committee that an audit tender process will be conducted in 2018 in order for the auditor selected as a result of the tender to be appointed for the financial year ending 31 December 2018. For the reasons outlined above, the committee considers this timing to be in the best interests of the Group's members and will continue to monitor this annually in light of the effectiveness and independence of the current auditors.

Once the next audit tender occurs, the Group will adopt a policy of putting the audit contract out to tender at least every ten years.

### Compliance with the CMA Order

Pearson confirms that it was in compliance with the provisions of The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 during the financial year ended 31 December 2015. Learn more about Auditors' independence and non-audit services on p119 ➔

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## Audit committee report continued

## Significant issues

Area of focus	Issue	Action taken by audit committee	Outcome
<b>Impairment reviews</b> Read more in note 11 on p164 ➔	Pearson carries significant goodwill intangible asset balances. There is judgement exercised in the identification of CGUs and the process of allocating goodwill to CGUs and aggregate CGUs and in the assumptions underlying the impairment review. In 2015 Pearson made significant impairments to goodwill and intangible assets in certain CGUs.	The committee considered the results of the Group's annual goodwill impairment review and the key assumptions which are considered to be the cash flows derived from strategic and operating plans, long term growth rates and the weighted average cost of capital. The committee considered the sensitivities to changes in assumptions and the related disclosures required by IAS 36 'Impairment of Assets'. The committee noted that significant impairments had arisen primarily as a result of deterioration in expected cash flow over the strategic plan period and considered sensitivity to assumptions in relation to other businesses.	Annual impairment review finalised with confirmation of an impairment in China, Brazil, North America and other Growth and Core territories, and sufficient headroom in other CGUs.
<b>Revenue recognition</b>	Pearson has a number of revenue streams where revenue recognition practices are complex and management assumptions and estimates are necessary.	The committee regularly reviews revenue recognition practice and the underlying assumptions and estimates. In addition, the committee has visibility of internal audit findings relating to revenue recognition controls and processes and routinely monitors the views of external auditors on revenue recognition issues. During the year the committee reviewed revenue recognition in respect of services provided to charter schools through Pearson's Connections business, and onerous contracts. The committee also continued to monitor the impact of the new revenue recognition standard IFRS 15 'Revenue from Contracts with Customers' and noted that although the standard would not be adopted by Pearson until 2018 the committee would need to understand the implications of the change well before that date.	Assumptions underlying revenue recognition were reviewed and challenged and considered to be appropriate.
<b>Tax</b>	There are a number of issues in different countries where management judgements and assumptions are made as to the correct tax treatment.	The committee considered Pearson's approach to tax provisioning. Pearson operates in a large number of countries and, accordingly, its earnings are subject to tax in many jurisdictions. The judgement in relation to tax provisioning is a combination of the committee's assessment of the specific open tax issues and also a review of the time periods in which Pearson's tax affairs are open to enquiry by local tax inspectors in jurisdictions where it has a larger taxable presence. The committee addressed this matter through the presentation of a management report on Pearson's tax affairs by the head of group tax and through a presentation of the external auditors' assessment of the company's tax provisioning.	The committee was satisfied with Pearson's approach to tax provisioning taking account of the views of management and the assessment of the external auditors.
<b>Disposal accounting</b>	Pearson disposed of its interest in The Financial Times, The Economist and PowerSchool.	The committee reviewed the disposal accounting and disclosure and considered the main judgements relating to tax treatments, and impairment of related assets on the PowerSchool disposal.	Accounting treatments and valuations confirmed as appropriate.

### Significant issues continued

During the year, the committee discussed the planning, conduct and conclusions of the external audit as it proceeded

At the July 2015 audit committee meeting, the committee discussed and approved the external audit plan and reviewed the key risks of misstatement of Pearson's financial statements, which were updated at the December 2015 committee meeting

The table opposite sets out the significant issues considered by the audit committee together with details of how these items have been addressed. The committee discussed these issues with the auditors at the time of their review of the half-year interim financial statements in July 2015 and again at the conclusion of their audit of the financial statements for the full year in February 2016

All the significant issues were areas of focus for the auditors. Learn more in the Independent auditors' report on p126 ➔

In December 2015, the committee discussed with the auditors the status of their work, focusing in particular on internal controls and Sarbanes-Oxley testing, and covering the significant issues outlined above

As the auditors concluded their audit, they explained to the committee

- › The work they had conducted over revenue, working alongside management to assess several complex revenue contracts
- › The work they had done to understand Pearson's tax strategy and identify business and legislative risks, to evaluate key underlying assumptions and assess the recoverability of deferred tax assets
- › Their evaluation of the recoverability of digital platforms and pre-publication assets
- › Their focus on segments, CGUs and goodwill impairment and the impact of Pearson's transformation on those
- › The results of their controls testing for Sarbanes-Oxley Act section 404 reporting purposes and in support of their financial statements audit
- › The results of the company's 'going concern' and viability statement reports

The auditors also reported to the committee the misstatements that they had found in the course of their work, which were insignificant, and the committee confirmed that there were no material items remaining unadjusted in these financial statements

### Audit committee training

The committee receives regular technical updates as well as specific or personal training as appropriate

Committee members also meet with local management on an ongoing basis, such as when travelling for overseas board meetings, in order to gain a better understanding of how Pearson's policies are embedded in operations

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## Risk governance and control

### Control environment

The board of directors has overall responsibility for Pearson's systems of internal control and risk management, which are designed to manage, and where possible mitigate, the risks facing Pearson, safeguard assets and provide reasonable, but not absolute, assurance against material financial misstatement or loss. The directors confirm they have conducted a review of the effectiveness of Pearson's systems of risk management and internal control in accordance with provision C 2.3 of the Code and the FRC's Code Guidance. These systems have been operating throughout the year and to the date of this report.

Responsibility for monitoring the effectiveness of the company's risk management and internal control systems has been delegated to the audit committee by the board. At each meeting, the audit committee considers reports from management, internal audit and the external auditors, with the aim of reviewing the effectiveness of the internal financial and operating control environment.

Each business area, including the corporate centre, maintains internal controls and procedures appropriate to its structure, business environment and risk assessment, while complying with company-wide policies, standards and guidelines.


### Internal control and risk management

Our internal controls and risk oversight have been reviewed as a result of the FRC Guidance and changes made to ensure compliance. These changes include more robust executive ownership and assessment of controls and PLC risks as well as the preparation of a viability statement.

The board, assisted by the assurance the audit committee provides, oversees the enterprise risk management (ERM) framework, risk appetite validation and viability statement verification processes outlined in the Principal Risks and Uncertainties section on p41. Day-to-day enterprise risk management is undertaken by a dedicated team, accountable to the board and audit committee. The board validates the risk appetite for each principal risk (as recommended by executive management) early in the year. The identification and mitigation of significant business risks is the responsibility of senior management and leadership teams for each business area.

The results of risk assessments and reviews are reported to the Pearson executive, the board and the audit committee. For example, in 2015, all identified Pearson-wide top risks were reviewed by executive management, then by the board and audit committee on a semi-annual basis. In addition, throughout the year, the audit committee considered the oversight of specific selected principal risks, through a series of risk deep dives. The internal audit plan is also aligned to our greatest areas of risk and the audit committee considers issues and risks arising from internal audits.

The risk assessment and reporting criteria are designed to provide the board with a consistent, Pearson-wide perspective of the key risks. The reports to the board, which are submitted twice per year, include an assessment of the probability and impact of risks materialising, as well as risk mitigation initiatives and their effectiveness.

Learn more about our risk management process, the principal risks and mitigating factors on p38-45 

### Financial management and reporting

There is a comprehensive strategic planning, budgeting and forecasting system with an annual operating plan approved by the board of directors. Monthly financial information, including trading results, balance sheets, cash flow statements, capital expenditures and indebtedness, is reported against the corresponding figures for the plan and prior years, with corrective action outlined by the appropriate senior executive. Pearson's senior management meet periodically with business area management to review their business and financial performance against plan and forecast. Major risks relevant to each business area as well as performance against the stated financial and strategic objectives are reviewed in these meetings.

We have an ongoing process to monitor the risks and effectiveness of controls in relation to the financial reporting and consolidation process including the related information systems. This includes up-to-date Pearson financial policies, formal requirements for finance functions, consolidation reviews and analysis of material variances, finance technical reviews, and review and sign-off by senior finance managers. The PLC finance function also monitors and assesses these processes, through a finance compliance function.

These controls include those over external financial reporting which are documented and tested in accordance with the requirements of section 404 of the Sarbanes-Oxley Act, which is relevant to our US listing. One key control in this area is the disclosure committee, which submits reports to the audit committee. This committee is chaired by the SVP internal audit and compliance, and members include the chief financial officer, general counsel, SVP investor relations, company secretary as well as senior members of financial management. The primary responsibility of this committee is to review Pearson's public reporting and disclosures to ensure that information provided to shareholders is complete, accurate and compliant with all applicable legislation and listing regulations.

The effectiveness of key financial controls is subject to management review and self-certification and independent evaluation by the external auditors.

#### Internal audit

The internal audit function is responsible for providing independent assurance to management and the audit committee on the design and effectiveness of internal controls to mitigate strategic, financial, operational and compliance risks. The risk-based annual internal audit plan is approved by the audit committee. Management action plans to improve internal controls and to mitigate risks, or both, are agreed with each business area after each audit. Formal management self-assessments allow internal audit to monitor business areas' progress in implementing management action plans agreed as part of internal audits to resolve any control deficiencies. Progress of management action plans is reported to the audit committee at each meeting. Internal audit has a formal collaboration process in place with the external auditors to ensure efficient coverage of internal controls. Regular reports on the work of internal audit are provided to executive management and, via the audit committee, to the board.

The SVP internal audit and compliance oversees compliance with our Code of Conduct and works with senior legal and human resources personnel to investigate any reported incidents including ethical, corruption and fraud allegations. The audit committee is provided with an update of all significant matters received through our whistleblowing reporting system, together with an annual review of the effectiveness of this system. The Pearson anti-bribery and corruption programme provides the framework to support our compliance with various anti-bribery and corruption regulations such as the UK Bribery Act 2010 and the US Foreign Corrupt Practices Act.

#### Treasury management

The treasury department operates within policies approved by the board and its transactions and procedures are subject to regular internal audit. Major transactions are authorised outside the department at the requisite level, and there is an appropriate segregation of duties. Frequent reports are made to the chief financial officer and regular reports are prepared for the audit committee and the board. The treasury policy is described in more detail in note 19 to the financial statements.

#### Insurance

Pearson reviews its risk financing options regularly to determine how the company's insurable risk exposures are managed and protected. Pearson purchases comprehensive insurance cover and annually reviews coverage, insurers and premium spend, ensuring the programme is fit for purpose and cost-effective.

Pearson's insurance subsidiary, Spear Insurance Company Limited, is used to leverage Pearson's risk retention capability and to achieve a balance between retaining insurance risk and transferring it to external insurers.

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## Reputation & responsibility committee report

**Chairman**  
Vivienne Cox

**Members** Vivienne Cox,  
Josh Lewis, Linda Lorimer,  
Harish Manwani

IMAGE  
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“Throughout the year, the committee provided oversight and input as Pearson continued to develop its sustainability practices, including the launch of Project Literacy and progress towards efficacy reporting. Our priority is to ensure Pearson’s activities and policies align with our business strategy and stakeholder priorities.”

### Reputation & responsibility committee role

Having been formalised in 2014, the remit of the reputation & responsibility committee expanded during 2015, reflecting Pearson’s continuing commitment and ambition around its corporate reputation, our belief in the importance of fulfilling our obligations to the communities in which we work, and maximising Pearson’s positive impact on society

The committee’s work is closely aligned with the company’s sustainable business initiatives and our meetings are now preceded by meetings of Pearson’s responsible business leadership council – an internal governance group – ensuring that we are able to provide the necessary scrutiny and challenge to the council as our sustainability strategy is developed and integrated into the business. Read more about Social impact on p55-67

### Terms of reference

The committee has written terms of reference which clearly set out its authority and duties. These are reviewed annually and can be found on the company website at [www.pearson.com/governance](http://www.pearson.com/governance)

### Progress against 2015 targets

At the start of 2015, we set out to achieve a number of ambitious goals during our first full year as a formal board committee. You can read more about our progress below

Areas of focus	Progress
Oversee delivery of our strategy for managing our reputation and maximising our contribution to society within the organisation	<p>This was a regular feature of our meetings throughout the year as Pearson builds its reputation management capabilities through an increasingly proactive approach. In particular we have explored in depth the work being done in our US market to proactively manage Pearson’s reputation.</p> <p>We also developed and adopted a new process for managing global reputation risk, which takes into account our expanded activity and exposure in growth markets, as well as our presence in certain high-risk countries.</p>
Monitor integration of social impact into Pearson’s business following the closure of the Pearson Charitable Foundation	<p>The committee provided input into a number of social impact projects established and accelerated in 2015, particularly high-profile initiatives such as Project Literacy and our Every Child Learning partnership with Save the Children.</p>
Review progress towards 2018 efficacy commitments	<p>Through focused sessions at two committee meetings, we reviewed progress toward meeting our efficacy commitment, and made recommendations for improving the efficacy measurement, reporting and auditing processes. Learn more about Efficacy on p46-53 ➔</p>



### Key activities in 2015

Key areas of focus for the committee were the launch of Project Literacy, our progress towards external efficacy reporting, plans to link the UN's sustainable development goals to our business model, and the ongoing work around Pearson's brand and culture. In all of these areas, our priority is to ensure Pearson's activities and policies align with our business strategy and stakeholder priorities, while reflecting best practice.

In addition, Pearson has formalised a process for its reputational risk management, involving business leaders and corporate affairs representatives, and the committee now receives a reputational risk report at every meeting. The committee also conducts deep dives into areas of particular reputational impact, such as through a focused session in 2015 on Pearson's US reputational strategy.

More detail about the committee's responsibilities, and the activities it undertook in each area of its remit, is given below. For reputation & responsibility committee meeting attendance see overview table on p78 ➔

### Committee aims for 2016

In 2016 the committee will continue to maintain a clear focus on reputational management in the US – our largest, and most reputationally high-profile market. We will oversee Pearson's continuous progress in embedding social impact into our strategy and business model, continue to monitor our corporate culture, ensuring employee engagement and values remain strong to help ensure Pearson is in good shape for the future, and we will undertake a review of the ethical business priorities identified in 2015.

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Vivienne Cox  
Chairman of reputation  
& responsibility committee

### Committee responsibilities

Topic	Responsibility	Activity	Strategy
Reputation	Pearson's reputation among major stakeholders including governments, investors, employees, customers, learners and the education community	<ul style="list-style-type: none"> <li>Updates on reputational 'hot topics' at each meeting</li> <li>Review of US reputational strategy</li> <li>Working with the audit committee to ensure that health &amp; safety issues are properly considered from a reputation and responsibility perspective</li> </ul>	Communications strategies, policies and plans related to reputational issues and the people, processes and policies that are in place to manage them
Risk	Oversight of Pearson's approach to reputational risk, including ensuring that clear roles have been assigned for management	<ul style="list-style-type: none"> <li>Overview of reputational risk approach in growth and US markets through in-country personnel and central corporate affairs team</li> <li>Regular consideration of reputational risk dashboards</li> </ul>	
Social	Social impact initiatives, including Pearson's non-financial public commitments and progress towards them	<ul style="list-style-type: none"> <li>Progress on efficacy, including launch of 'On the Road' publication and draft reporting framework</li> <li>Introduction to new reach and impact strategy</li> <li>Commitment to UN sustainable development goals and integration into business model</li> <li>Launch of Save the Children partnership</li> </ul>	
Brand and culture	Management of the Pearson brand to ensure that its value and reputation are maintained and enhanced. Pearson's approach to monitoring and supporting the values and desired behaviours that form our corporate culture	<ul style="list-style-type: none"> <li>Brand tracker update</li> <li>Review of progress on employee values and engagement</li> <li>Employee participation in social impact activities</li> </ul>	
Ethics	Ethical business standards, including Pearson's approach to issues relevant to its reputation as a responsible corporate citizen	Consideration of ethical issues in the wider context of reputational risk identification	

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## Shareholder engagement

### Engaging with shareholders

Pearson has an extensive programme of communication with all of its shareholders – large and small, institutional and private

**Shareholder outreach** In 2015, we continued with our shareholder outreach programme, seeing approximately 790 institutional and private investors at more than 450 different institutions in Australia, Canada, Dubai, Greater China, Continental Europe, India, Japan, Singapore, South Korea, Taiwan, the UK and the US

**Trading updates** There are five trading updates each year and the chief executive and chief financial officer present our preliminary and interim results updates. They also attend regular meetings throughout the year with investors in the UK and around the world, tailored to investor requirements, to discuss the performance of the company, the company's strategy, our change programme, structural changes in our markets, and risks and opportunities for the future

**Chairman meetings** The chairman meets regularly with significant shareholders to understand any issues and concerns they may have. This is in accordance with both the Code and the UK Stewardship Code. The non-executive directors meet informally with shareholders both before and after the AGM and respond to shareholder queries and requests as necessary. The chairman ensures that the board is kept informed of principal investors' and advisers' views on strategy, and corporate governance

**Consultations** During the year we also consulted with our major shareholders and with shareholder representative bodies on our directors' remuneration report, and the significant minority vote against the 2013 annual remuneration report at the 2014 AGM. Read about Remuneration on p94 ➔

**Private investors** Private investors represent over 80% of the shareholders on our register and we make a concerted effort to engage with them regularly. Shareholders who cannot attend the AGM are invited to e-mail questions to the chairman in advance at [chairman-agm@pearson.com](mailto:chairman-agm@pearson.com) ➔

We encourage our private shareholders to become more informed investors and have provided a wealth of information on our website about managing Pearson shareholdings, see [www.pearson.com/investors/shareholder-information.html](http://www.pearson.com/investors/shareholder-information.html) for further information, or turn to p227 of this report. We also encourage all shareholders, who have not already done so, to register their e-mail addresses through our website and with our registrar. This enables them to receive e-mail alerts when trading updates and other important announcements are added to our website. See additional Shareholder information on p227 ➔

### Visit [pearson.com](http://pearson.com)

- › Investor relations information
- › Company announcements and shareholder presentations, webcasts and conference calls
- › Past announcements and presentations
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- › Share price data
- › Calendar of events
- › Information about our businesses and their websites
- › Corporate responsibility policies and activities

IMAGE REMOVED

## Wider engagement

### Share dealing

Due to its continued popularity we again provided shareholders with smaller holdings the opportunity to use our registrar's low-cost share dealing service, giving them the chance to add to or reduce their stake in Pearson at significantly reduced dealing rates, or to donate shares to charity with ease. This service proved very popular with shareholders, and consequently we intend to offer it again at a future date.

We believe it is important that our employees have a shared interest in the direction and achievements of Pearson and are pleased to say that a large number of our employees are shareholders in the company.

### Annual General Meeting

Our AGM, on 29 April 2016, is an opportunity for all shareholders to meet the board and to hear presentations about Pearson's businesses and results.

### Engaging with all stakeholders

We post all company announcements on our website, [www.pearson.com](http://www.pearson.com), as soon as they are released, and key shareholder presentations are made accessible via webcast or conference call. Our website contains a dedicated investor relations section with an extensive archive of past announcements and presentations, historical financial performance, share price data and a calendar of events. It also includes information about all of our businesses, links to their websites and details of our corporate responsibility policies and activities. Learn more about our approach to corporate responsibility in the Social Impact section on p55 ➔

### Board visit to India

IMAGE REMOVED

In October 2015, the board visited New Delhi, India, for a three-day meeting focused on our four most important Growth markets – Brazil, China, India and South Africa.

In each of these countries, Pearson's presence has grown markedly in the last few years and in each of them, to varying degrees, Pearson is operating in a challenging economic climate, whilst continuing to chart a path to the next phase of sustainable growth. These are important markets to Pearson's long-term future, where the fundamental demand for good quality education and training, leading to a job and a better life, remain strong.

**Overview of growth markets** Providing context for the meeting, Pearson's President, Growth and SVP finance, Growth led an overview of performance and strategy across the four main Growth markets, following which the business leaders of each of Brazil, China and South Africa gave a more in depth review of the opportunities and challenges in those countries, considering the macro economic conditions and demographics particular to each territory.

**Focus on India** Non executive director Harish Manwani set the scene for the focus on India, and the board then took a closer look at Pearson's operations through a session with the head of our India business, learning about the huge potential in India and the demand for better, more job relevant education. The board also spent time with Pearson's India leadership team and key talent and heard from a range of partners, policymakers and key influencers.

**Learning in action** The board visited Jaypee public school, which provided an opportunity to see first-hand the impact of Pearson's school management improvement framework, to view the MyPedia integrated learning tool in action and learn about our health & safety and safeguarding initiatives. The board also spent time at a Pearson learning centre, learning about Pearson's work to translate education and training into employment, and engaged with representatives of Avanti Learning Centres and Zaya, two initiatives funded by the Pearson Affordable Learning Fund.

Learn more about our Growth markets on p29 32 ➔

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# Report on directors' remuneration

## Part 1 Letter from the chairman of the remuneration committee

Chairman of the  
remuneration committee  
Elizabeth Corley

Current Members  
Tim Score, Vivienne Cox,  
Elizabeth Corley, Josh Lewis  
and Sidney Taurel

IMAGE  
REMOVED

"It has been a tough year for Pearson and our remuneration outcomes have reflected this. 2015 brought challenging market conditions and significant changes. As we continue into 2016 we will be considering our remuneration policy proposals for 2017 in this new environment and context for the business."

### In this remuneration section

Part 1 Letter from the chairman	p94 ➔
Part 2 Summary of remuneration policy	p97 ➔
Part 3 Annual remuneration report	p101 ➔

### Terms of reference

The committee's full charter and terms of reference are available on the Governance page of the company's website at [www.pearson.com/governance](http://www.pearson.com/governance)

IMAGE REMOVED

### Dear shareholder

On behalf of the board, I am pleased to present the report on directors' remuneration for 2015. This is my first report as chairman of Pearson's remuneration committee, having succeeded Sir David Arculus at the Annual General Meeting (AGM) in April 2015. The opportunity to learn about and study the history, policies and procedures of remuneration at Pearson, with the support of fellow committee members, has been invaluable, as has the feedback and engagement with key shareholders. My board colleagues and I are aware of the importance and sensitivity among investors and the public more generally, of remuneration topics and we feel our responsibilities keenly.

As outlined in our strategic report, 2015 was a year of change and challenge for Pearson with continued market headwinds and the in-year disposals of PowerSchool, the Financial Times Group and our stake in The Economist. While we have been performing well competitively and gained market share across many areas of our business, year end results were lower than projected at the start of the year. This was largely driven by the persisting cyclical and policy-related turbulence in our major education markets. While this is expected to abate over the next two years, we saw a reduction in our annual operating profit for 2015 of approximately £230m from its peak.

Despite the challenges encountered, we remain focused on executing the business strategy, transforming Pearson to be the standout company in education globally and developing our long-term growth opportunities. The 2015 divestments were an important part of these aims. We are confident that education remains an attractive investment opportunity with

IMAGE REMOVED

the growth potential to enable us both to serve more students around the world, and to deliver good, sustainable returns to our shareholders

We do not intend to make any remuneration policy revisions ahead of the 2017 AGM. However, we keep the effectiveness of our current remuneration programmes under review and, partly in light of recent trading conditions and the specific strategic goals for 2016, we have concluded that some changes are warranted. These are detailed in this report and, for those yet to be finalised, we are engaging with our key investors.

#### What happened in 2015

Remuneration for executive directors is closely tied to business performance with a high proportion of total remuneration delivered through variable pay designed to reward achievement of short and long term strategic objectives. As a result of the performance challenges noted in this report, the outcomes under these schemes were as follows:

- › Annual incentives paid to executives for 2015 were zero, reflecting below-threshold performance in a tough trading environment.
  - › Long-term incentives vesting in 2015 did not pay out. This is the third consecutive year of nil pay-out, reflecting below-threshold performance against the company's three-year targets for earnings per share growth, return on invested capital and relative total shareholder return.
- Given the environment within which the leadership team is expected to guide Pearson through a very significant period of change, without receiving any bonus or long-term incentive payments, the committee agreed for 2016 incentive and retention arrangements for selected key employees, which will vest, or not, in 2017. No executive directors participate in these incentives.

#### Future measures of performance against pay

We expect our business to stabilise in 2017 and return to growth in 2018. Our business plan until then focuses on operational execution, tight cost management and a sharper, more focused strategy. The focus of restructuring is not only to reduce costs but also to make the company faster, leaner and more agile.

We are creating a single global product organisation, integrating our school, clinical and professional assessment operations in North America and are scaling back our exposure to large, direct delivery operations. We are also making productivity improvements across all our enabling functions such as Technology, HR and Finance and we plan to rationalise our property portfolio and consolidate major agreements to drive greater cost efficiency.

#### Committee responsibilities

- 1 Determine and review policy** Determine and regularly review the remuneration policy for the executive directors, the presidents and other members of the Pearson executive who report directly to the CEO (executive management). This policy includes base salary, annual and long-term incentives, pension arrangements, any other benefits and termination of employment.
- 2 Review and approve implementation** Regularly review the implementation and operation of the remuneration policy for executive management and approve the individual remuneration and benefits packages of the executive directors.
- 3 Approve performance related plans** Approve the design of, and determine targets for, any performance-related pay plans operated by the company and approve the total payments to be made under such plans.
- 4 Review long-term plans** Review the design of the company's long-term incentive and other share plans for approval by the board and shareholders.
- 5 Set termination arrangements** Advise and decide on general and specific arrangements in connection with the termination of employment of executive directors.
- 6 Review targets** Review and approve corporate goals and objectives relevant to CEO remuneration and evaluate the CEO's performance in light of those goals and objectives.
- 7 Determine chairman's remuneration** Delegated responsibility for determining the remuneration and benefits package of the chairman of the board.
- 8 Shareholder engagement** Ensure the company maintains an appropriate level of engagement with its shareholders and shareholder representative bodies in relation to the remuneration policy and its implementation.
- 9 Appoint remuneration consultants** Appoint and set the terms of engagement for any remuneration consultants who advise the committee and monitor the cost of such advice.

In these circumstances, we intend to design our incentive plans for 2016 to ensure that our executive and other employees are motivated and incentivised to achieve our important aims over the short term, while sustaining a strategic focus on longer-term goals. The plan targets are still to be finalised but the current thinking suggests:

#### For the Annual Incentive Plan (AIP)

- › The 2016 sales and cash metrics and weightings remain unchanged from 2015. However, to align the AIP with the specific restructuring achievements required in 2016, as noted in the income statement measure in our guidance to investors, Operating Profit after the cost of restructuring will be added to the metrics with a 30% weighting. To accommodate this change, the weighting for earnings per share (EPS) would also be 30% (down from 60% weight for 2015).

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## Part 1 Letter from the chairman of the remuneration committee continued

- For 2016, the range of normal rewarded performance would be wider than in previous years – and, in consequence, both the threshold performance and the on-target funding are set to be lower than in 2015

For the Long-Term Incentive Plan (LTIP)

- Targets for the 2016 LTIP awards are planned to be set following the April remuneration committee meeting, having allowed key shareholders the opportunity to consider our plans on how to account for the revised growth expectations explained in our January 2016 trading update, and in line with policy
- The targets will be fully disclosed in the 2016 report on directors' remuneration
- The targets and weightings will continue to be based on EPS (one-half), ROIC (one-third) and TSR (one-sixth) with on-target levels planned to be in line with the delivery of the market guidance operating profit of £800 million in 2018

#### Looking forward to 2016

The committee has reviewed the base salary levels for executive directors in light of 2015 business performance and concluded that it would not be appropriate to award a salary increase for 2016

In preparation for the policy vote in 2017, we expect to conduct a thorough review of our remuneration policy

in 2016 to test and ensure its effectiveness and appropriateness for the company, which finds itself in a new operating environment and context to that prevailing in 2014. We are committed to engagement with our shareholders during this review and will welcome comments and feedback

The operation of the current LTIP will be considered as part of the policy review, in parallel with a periodic review of the remuneration committee's terms of reference. Our new policy – changed or not – and any new or renewed plans will be put to shareholders for approval at the 2017 AGM. For information on our anticipated changes to remuneration for 2016 see page 116

My meetings with shareholders in 2015 have been helpful in understanding perspectives and I look forward to continuing the dialogue in 2016 and beyond

We are confident that our response to the changes and challenges described here will make Pearson a simpler, focused and stronger company and that we will position the company to achieve a sustained period of growth

IMAGE REMOVED

Elizabeth Corley  
Chairman of remuneration committee  
4 March 2016

#### Principles of remuneration policy

The purpose of the remuneration policy is to support the company's strategy to deliver sustained performance and create long-term value in the interests of all stakeholders. Our remuneration policy principles are highlighted in the panel below and a summary of our directors' remuneration policy report, approved by shareholders at the 2014 AGM, is provided on pages 97 and 98

We continue to operate executive remuneration in line with the approved policy and do not anticipate seeking shareholder approval for our policy again until required to do so at the 2017 AGM. See table on page 98

#### Sustainability and affordability

Base salary	<ul style="list-style-type: none"> <li>Robust and transparent</li> <li>Link to pay conditions across the Group</li> <li>Strong rationale for increases</li> </ul>
Annual incentives	<ul style="list-style-type: none"> <li>Funded through results</li> <li>Strong link to performance</li> <li>Malus and clawback</li> </ul>
Long-term incentives	<ul style="list-style-type: none"> <li>Strong link to performance</li> <li>Malus and clawback</li> </ul>

#### Pay for performance

Annual incentives	<ul style="list-style-type: none"> <li>Pay mix focuses on variable pay</li> <li>Funded through results</li> <li>Aligned fully with KPIs: EPS, operating profit, sales and operating cash flow</li> <li>Malus and clawback</li> </ul>
Long-term incentives	<ul style="list-style-type: none"> <li>Pay mix focuses on variable pay</li> <li>Funded through results</li> <li>Aligned with strategy through KPIs: EPS, ROIC and TSR</li> <li>Malus and clawback</li> </ul>

#### Alignment

Annual incentives	<ul style="list-style-type: none"> <li>Designed to reflect shareholder value creation</li> </ul>
Long-term incentives	<ul style="list-style-type: none"> <li>Designed to reflect shareholder value creation</li> <li>2-year holding post vesting</li> </ul>
Shareholding guidelines	<ul style="list-style-type: none"> <li>CEO 300%</li> <li>CFO 200%</li> <li>Pearson executive 100%</li> </ul>

# Report on directors' remuneration continued

## Part 2 Summary of remuneration policy

### Introduction to summary of remuneration policy

The company's policy on directors' remuneration was approved by shareholders at the Annual General Meeting on 25 April 2014. We issued an RNS statement of further information on the remuneration policy on 9 April 2014, to clarify the use of the committee's discretion over certain elements of remuneration in exceptional circumstances.

To help shareholders understand the context of remuneration practice reported in the annual remuneration report that follows, and specifically the limits applied to directors' remuneration, we have included below some key points and a summary of pertinent sections of the remuneration policy for information only. For further detail, please refer to the full remuneration policy and the clarification statement on the Governance page of the company's website at [www.pearson.com/governance](http://www.pearson.com/governance).

#### Scope of policy

The policy applies to executive directors, the chairman and non-executive directors.

Reference is also made to the remuneration policy for other members of the Pearson executive (currently nine in number) who are not directors but who fall within the committee's remit.

#### Duration of policy

The policy took effect on 25 April 2014 and is expected to remain in force until the next binding vote on our remuneration policy, which is planned for the 2017 AGM.

#### Use of discretion

The committee has avoided, where possible, including general discretions in the policy table. However, exceptional or genuinely unforeseen circumstances may arise in the future and in those circumstances it may be in shareholders' interests for Pearson to put in place remuneration arrangements that are outside the terms of the policy. If this happens, the committee will be permitted to implement remuneration arrangements that it considers appropriate in the circumstances. In these circumstances, Pearson would consult in advance with major shareholders before it does so and would explain the exercise of this discretion in the following year's directors' remuneration report.

As clarified in the RNS statement of further information on the remuneration policy on 9 April 2014, this discretion would only be used in the very narrow circumstances articulated in the policy – that is, in exceptional or genuinely unforeseen circumstances. The committee considers that these circumstances would arise highly infrequently, if at all, in the lifetime of the policy. The committee would regard reliance on this discretion as a matter of utmost seriousness and, in relation to our stated obligation to consult in advance with major shareholders, would not proceed unless there was clear consensus in favour among those consulted. Further, the committee would ensure that the value of the remuneration arrangement put in place in reliance on this discretion would fall within the normal limit (as stated in the policy) for the element of remuneration to which the arrangement relates.

As part of the approved policy, the committee also has discretion to award base salary increases, allowances and benefits, and long-term incentive plan awards in excess of the normal maximum limits to current or new directors. As clarified in the RNS statement, this discretion will only be exercised in exceptional circumstances other than in the case of increases in the cost of benefits that are outside Pearson's control and changes in benefit providers. Again, Pearson would consult with major shareholders before exercising any such discretion and such exercise would be limited by reference to the safeguards described above, including only proceeding where there was clear consensus in favour among those consulted. In these circumstances, the committee would ensure that the maximum value of the remuneration arrangement put in place in reliance on this discretion did not exceed a margin of 25% over the normal maximum limit for the element in question (as stated in the policy).

#### Legacy arrangements

Given the long-term nature of some of Pearson's remuneration structures – including obligations under service contracts, incentive plans and pension arrangements – a number of pre-existing obligations remained in place at the time that the new policy became effective, including obligations that are 'grandfathered' by virtue of being in force at 27 June 2012. Pearson's policy is to honour pre-existing obligations, commitments or other entitlements that were entered into before the effective date of this policy.

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## Part 2 Summary of remuneration policy continued

## Summary of remuneration policy

For more information please refer to the full remuneration policy on the Governance page of the company's website at [www.pearson.com/governance](http://www.pearson.com/governance)

Element of remuneration	Purpose and link to strategy	Performance conditions	Normal limit	Exceptional limit as clarified in RNS statement of 9 April 2014
<b>Base salary</b>	Helps to recruit, reward and retain. Reflects competitive market level role, skills, experience and individual contribution	Performance of both the company and the individual are taken into account when determining an appropriate level of base salary. Increase each year, if any	Base salary increases are not ordinarily more than 10% per annum	Up to 25% over normal limit in specific individual situations including internal promotions and material changes to the business or the role
<b>Allowances and benefits</b>	Help to recruit and retain. Reflect the local competitive market	None	Total value not ordinarily in excess of 15% of base salary in any year	Up to 25% over normal limit in specific individual situations including changes in individual circumstances such as health status and changes in the role such as relocation. In excess of 25% over normal limit in the case of increases in the cost of benefits that are outside of Pearson's control and changes in benefit providers
<b>Retirement benefits</b>	Help to recruit and retain. Recognise long term commitment	None	As set out in approved remuneration policy	None
<b>Annual incentives</b>	Motivate achievement of annual strategic goals. Focus on key financial metrics. Reward individual contribution	The committee has the discretion to select the performance measures, targets and relative weightings from year to year. Funded by Pearson global annual financial results, normally related to the performance against targets for Pearson's adjusted earnings per share (or operating profit), sales, and operating cash flow. Individual annual incentive pay-outs also take into account individual performance against personal objectives	Overall limit 200% of base salary. 2015 maximum opportunity is 180% for the chief executive and no more than 170% for other executive directors and members of the Pearson executive	None
<b>Long term incentives</b>	Help to recruit, reward and retain. Drive long-term earnings, share price growth and value creation and align interests of executives and shareholders. Encourage long term shareholding and commitment to company. Link management's long term reward and wealth to corporate performance in a flexible way	The committee will determine the performance measures, weightings and targets governing an award of restricted shares prior to grant to ensure continuing alignment with strategy and that the targets are sufficiently stretching. Awards vest subject to the following performance conditions: one-half on earnings per share growth, one-third on return on invested capital (ROIC), one-sixth on relative total shareholder return (TSR). Performance tested over three years	Maximum face value of 400% of base salary. Other than in exceptional circumstances on recruitment, it is the company's normal policy not to award restricted shares to executive directors and other members of the Pearson executive without performance conditions	Up to 25% over normal limit in exceptional circumstances, for example, for retention purposes or to reflect particular business situations. The discretion to award restricted shares without performance conditions to executive directors will not be used other than where it is appropriate to compensate a new director on a 'like for like' basis for incentives foregone at a previous employer

See Total single figure remuneration chart on page 105



### Non-executive directors and chairman

Non-executive director remuneration has been designed to attract and retain high calibre individuals, with appropriate experience or industry relevant skills, by offering market competitive fee levels

The structure of non-executive directors' fees with effect from 1 May 2014 is as follows

Director	Fee
Non-executive director	£70,000
Chairmanship of audit committee	£27,500
Chairmanship of remuneration committee	£22,000
Chairmanship of reputation & responsibility committee	£10,000
Membership of audit committee	£15,000
Membership of remuneration committee	£10,000
Membership of reputation & responsibility committee	£5,000
Senior independent director	£22,000

The total fees payable to the non-executive directors (excluding the Chairman) are subject to the limit set out in the articles of association of the company (currently £750,000) and are increased by ordinary resolution from time to time

The chairman's fees remain unchanged at £500,000 per year

For more information on non-executive directors' remuneration, please refer to the full remuneration policy on the Governance page of the company's website at [www.pearson.com/governance](http://www.pearson.com/governance)

### Pay and performance scenario analysis

The remuneration policy approved by shareholders in 2014 required a scenario chart in the format set out below for 2014 remuneration. Although not required, the company has updated the scenario charts below so as to apply to 2016 remuneration

Consistent with its policy, the committee places considerable emphasis on the performance-linked elements, i.e. annual and long-term incentives

The chart overleaf shows what each director could expect to receive in 2016 under different performance scenarios, based on the following definitions of performance

Performance scenario	Elements of remuneration and assumptions
Maximum	2016 base salary, allowances, benefits, and retirement benefits at the same percentage of base salary as in 2015, maximum individual annual incentive as per policy; maximum value of 2015 long term incentive award
Target	2016 base salary, allowances, benefits, and retirement benefits at the same percentage of base salary as in 2015, target individual annual incentive as per policy; target value of 2015 long term incentive award (Willis Towers Watson's independent assessment of the expected value of the award, i.e. the net present value taking into account all the conditions)
Minimum	2016 base salary, allowances, benefits, and retirement benefits at the same percentage of base salary as in 2015, no annual or long term incentives

**Note** The value of long-term incentives does not take into account dividend awards that are payable on the release of restricted shares nor any changes in share price.

On this basis, the relative weighting of fixed and performance-related remuneration and the absolute size of the remuneration packages for the chief executive and the chief financial officer (as represented by the current incumbent) are set out on the next page

We will continue to review the mix of fixed and performance-linked remuneration on an annual basis, consistent with our overall policy

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## Part 2: Summary of Remuneration policy continued

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IMAGE REMOVED

### Further information on remuneration policy

For further information on the following aspects of the remuneration policy, please refer to the full remuneration policy and the RNS statement of further information on the remuneration policy of 9 April 2014 on the Governance page of the company's website at [www.pearson.com/governance](http://www.pearson.com/governance) 

- › Selection of performance measures and target setting
- › Legacy arrangements under the annual bonus share matching plan
- › Remuneration policy for other employees
- › Service contracts and termination provisions
- › Recruitment policy
- › Employment conditions elsewhere in the company
- › Executive directors' non-executive directorships
- › Shareholder views

In 2016, we intend to conduct a review of our remuneration policy to put to shareholders for our next policy vote in 2017

# Report on directors' remuneration continued

## Part 3 Annual remuneration report

### This report comprises a number of sections

The remuneration committee and its activities	p102 103 ➔	Movements in directors' interests in share options*	p111 ➔
Voting outcome at 2015 Annual General Meeting	p104 ➔	Payments to former directors*	p111 ➔
Single figure of total remuneration and prior year comparison*	p105 ➔	Interests of directors and value of shareholdings*	p112 ➔
Annual incentive*	p106 ➔	Executive directors' non-executive directorships	p113 ➔
Long-term incentives*	p107 ➔	Historical performance and remuneration	p114 ➔
Retirement benefits*	p108 ➔	Comparative information	p115 ➔
Remuneration paid to the chairman and non-executive directors*	p108 ➔	Information on changes to remuneration for 2016	p116-117 ➔
Movements in directors' interests in share awards*	p110 ➔		

Where required under current regulations the tables marked \* have been subject to audit

### Annual remuneration report

The remuneration committee presents the annual remuneration report, which will be put to shareholders, along with the annual statement, as an advisory (non-binding) vote at the Annual General Meeting to be held on 29 April 2016

### Remuneration compliance

This report was compiled in accordance with Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 and was approved by the board of directors on 4 March 2016

The committee believes that the company has complied with the provisions regarding remuneration matters contained within the UK Corporate Governance Code

### Strategic alignment of pay

Financial objectives	KPI	Incentive scheme
Drive revenue growth	Sales	AIP
Deliver sustainable returns	Total adjusted earnings	AIP / LTIP
	Return on Invested capital	LTIP
	Total shareholder return	LTIP
Manage our cash position effectively	Operating cash flow	AIP

Non-financial objectives	KPI	Incentive scheme
Reduce our carbon footprint	GHG emissions	AIP (as part of a scorecard used to determine the individual discretionary element of the payout)
Strategic objectives	KPI	Incentive scheme
Transform to digital and services	Revenue share	AIP
Grow presence in emerging markets	Revenue share	AIP

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## Part 3 Annual remuneration report continued

## The remuneration committee in 2015

Role	Name	Title
Chairman	Elizabeth Corley (from 24 April 2015)	Independent non executive directors
	David Arculus (to 24 April 2015)	
Members	Vivienne Cox	
	Josh Lewis	
	Tim Score (from 2 October 2015)	
	Ken Hydon (to 24 April 2015)	
	Elizabeth Corley (to 24 April 2015)	
	Glen Moreno	Chairman of the board
	John Fallon	Chief executive
Internal advisers	Coram Williams (from 1 August 2015)	Chief financial officer
	Robin Freestone (to 1 August 2015)	Chief financial officer
	Melinda Wolfe	Chief human resources officer
	Stuart Nolan	SVP, reward
	Stephen Jones	Company secretary
External advisers	Willis Towers Watson	

See remuneration committee activities in 2015  
on p103 ➔

Sidney Taurel joined the committee as a member  
on his appointment as Chairman of the Board on  
1 January 2016

Internal advisers provided material assistance to the  
committee during the year. They attended meetings of  
the committee, although none of them were involved in  
any decisions relating to his or her own remuneration

To ensure that the committee receives independent  
advice, Willis Towers Watson supplies survey data and  
advises on market trends, long-term incentives and  
other general remuneration matters. Willis Towers  
Watson was selected and appointed by the committee  
through a formal tendering process. Willis Towers  
Watson also advised the company on health and  
welfare benefits in the US and provided consulting  
advice directly to certain Pearson operating companies.  
Willis Towers Watson is a member of the Remuneration  
Consultants' Group, the body that oversees the Code of  
Conduct in relation to executive remuneration consulting  
in the UK.

During the year, Willis Towers Watson was paid fees for  
advice to the committee, which were charged on a time  
spent basis, of £151,254. As part of its annual review of its  
performance and effectiveness, the committee remains  
satisfied that Willis Towers Watson's advice was objective  
and independent and that Willis Towers Watson's  
provision of other services in no way compromises  
its independence.

## Committee performance

Annually, the committee reviews its own performance,  
constitution, and charter and terms of reference to  
ensure it is operating at maximum effectiveness and  
recommends any changes it considers necessary to the  
board for approval.

The committee participated in a survey to review its  
performance and effectiveness in July 2015, looking at  
areas such as the clarity of roles and responsibilities,  
the composition of the committee, the use of time,  
the quality and timeliness of meeting materials, the  
opportunity for discussion and debate, dialogue  
with management and shareholders and access to  
independent advice.

The committee concluded that it is operating effectively.

## Meetings, activities and decisions in 2015

The remuneration committee met four times during 2015. The key topics were as follows

Market	Noted Willis Towers Watson's overview of the current remuneration environment and 2014/15 market data	Noted update to remuneration aspects of the UK Corporate Governance Code and principles of remuneration of the Investment Association		
Performance	Noted management's overview of prior year and year to date performance and business plans	Noted and reviewed the status of the outstanding long-term incentive awards based on the current view of likely Pearson financial performance		
Implementation	<p>Reviewed and approved the 2014 annual incentive pay out and 2015 remuneration package for John Fallon</p> <p>Reviewed and approved 2014 annual incentive plan pay-outs</p> <p>Approved nil pay-out of 2012 annual bonus share matching awards and release of shares</p>	<p>Approved nil pay-out under 2012 long-term incentive plan</p> <p>Reviewed and approved 2015 long-term incentive awards for the Pearson executive</p>	<p>Considered timeline and principles for determining the basis of Robin Freestone's exit arrangements</p> <p>Noted 2015 long-term incentive awards for senior leaders and managers below Pearson executive</p>	<p>Noted remuneration package for a new appointment to the Pearson executive</p> <p>Considered matter of former CEO's double taxation in the US and UK and related issues</p>
Governance	Noted the activity of the standing committee of the board in relation to the operation of the company's equity-based reward programmes	Noted company's use of equity for employee share plans	Reviewed the committee's performance	Reviewed the committee's charter and terms of reference
Policy	<p>Reviewed and approved 2014 directors' remuneration report</p> <p>Reviewed and approved increases in base salaries for 2015 for the Pearson executive</p> <p>Reviewed and approved 2015 Pearson annual incentive plan targets</p>	<p>Reviewed and approved 2015 individual annual incentive opportunities for the Pearson executive</p> <p>Reviewed 2015 long-term incentive performance conditions for the Pearson executive</p>	<p>Noted guidance notes on treatment of leavers and exercise of discretion</p> <p>Considered approach to 2015 long-term incentive awards for senior leaders and managers below the Pearson executive</p>	
Disclosure and engagement	Noted shareholder feedback on 2014 directors' remuneration report	Reviewed 2015 Annual General Meeting season, shareholder voting and engagement strategy	Noted template and outline of 2015 report on directors' remuneration and considered shareholder engagement strategy	Noted feedback from Committee Chairman's meetings with key shareholders

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### Part 3 Annual remuneration report continued

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#### Voting at 2015 Annual General Meeting

The following table summarises the details of votes cast in respect of the resolutions on the report on directors' remuneration at the 2015 Annual General Meeting

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#### Voting on remuneration policy at 2014 AGM

IMAGE REMOVED

IMAGE REMOVED

As in previous years and as required by law, details of the voting on all resolutions at the 2016 Annual General Meeting will be announced via the RNS and posted on the Pearson website following the Annual General Meeting

### Single total figure of remuneration and prior year comparison

Total aggregate emoluments for executive and non-executive directors were £3 299m in 2015. These emoluments are included within the total employee benefit expense in note 5 to the financial statements (page 155).

#### Executive directors

The remuneration received by executive directors in respect of the financial years ended 31 December 2015 and 31 December 2014 is set out below. Figures for Coram Williams and Robin Freestone are based on their period of employment – see note on page 106.

#### Executive director remuneration

	John Fallon		Coram Williams		Robin Freestone		Total	
£000s	2015	2014	2015	2014	2015	2014	2015	2014
<b>Base salary</b>	776	761	258	-	417	553	1,451	1,314
<b>Allowances and benefits</b>	62	83	0	-	13	15	75	98
Travel	28	50	0	-	11	12	39	62
Healthcare	2	2	0	-	2	2	4	4
Risk	32	31	0	-	0	1	32	32
<b>Annual incentives</b>	0	692	0	-	0	365	0	1,057
Percentage of maximum	0%	51%	0%	-	0%	39%	-	-
Percentage of target	0%	91%	0%	-	0%	78%	-	-
Percentage of salary	0%	91%	0%	-	0%	66%	-	-
<b>Long-term incentives</b>	54	74	-	-	41	63	95	137
Long-term incentive plan	0	0	-	-	0	0	0	0
Annual bonus share-matching plan	0	0	-	-	0	0	0	0
Dividend equivalents	46	74	-	-	38	63	84	137
Worldwide Save For Shares	8	0	-	-	3	0	11	0
<b>Retirement benefits</b>	371	285	18	-	126	166	515	451
Defined contribution plan	0	0	0	-	18	23	18	23
Defined benefit accrual	169	87	18	-	-	0	187	87
Allowances in lieu of benefits	202	198	0	-	108	143	310	341
<b>Total remuneration</b>	1,263	1,895	276	-	597	1,162	2,136	3,057

See summary of remuneration policy on page 98 ➔

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## Part 3. Annual remuneration report continued

## Notes to single figure table

Single total figure of remuneration In accordance with the regulations, we show a single total figure of remuneration, which includes retirement benefits and long-term incentives in addition to the other elements of remuneration that have been shown in previous reports

Coram Williams and Robin Freestone Figures relate to full period of employment, for Coram commencing 1 July 2015, and for Robin ending 30 September 2015 Note that Coram became an executive director and Robin stepped down as an executive director on 1 August 2015

Base salary In accordance with policy, the committee considered a report from the chief executive and chief human resources officer on general pay trends in the market and the level of pay increases across the company as a whole For 2015, the company had reiterated its starting principles that base compensation provides the appropriate rate of remuneration for the job, taking into account relevant recruitment markets,

business sectors and geographic regions and that total remuneration should reward both short and long-term results, delivering competitive rewards for target performance, but higher rewards for exceptional company performance For the US and UK, the budget guideline issued for adjustments to base pay for 2015 was 2% Local inflation rates and market conditions were taken into account in particular markets

Allowances and benefits Travel benefits comprise company car, car allowance and private use of a driver Health benefits comprise healthcare, health assessment and gym subsidy Risk benefits comprise additional life cover and long-term disability insurance In addition to the above benefits and allowances, executive directors may also participate in company benefit or policy arrangements that have no taxable value

Annual incentive For more detail, see table below Annual incentives for the directors are funded by Pearson global annual financial results and pay-outs take into account individual performance against personal objectives

## Executive directors' annual incentive payments in 2015

For 2015, annual incentives were funded by Pearson global annual financial results based on the performance measures set out below Individual pay-outs take into account performance against personal objectives Actual performance against the financial targets for 2015, and the respective AIP pool funding level, were as follows

Measures	Weighting	Threshold for 2015	Target for 2015	Maximum for 2015	Actual performance in 2015	Funding in 2015 (% of target)	Weighting ratio
Group EPS (p)	60%	70.4	79.0	87.7	69.8	0%	
Group sales (£m)	20%	5,046	5,312	5,578	5,083	0%	
Operating cash flow (£m)	20%	680	765	850	435	0%	
<b>Total</b>	<b>100%</b>					<b>0%</b>	

Measures	Group funding	Pro rating factor	Target AIP as % of salary	Actual % of target in 2015	Final pay-out in 2015 (£000s)
John Fallon	0%	1.0	100%	0%	£0
Coram Williams	0%	0.5	85%	0%	£0
Robin Freestone	0%	0.75	85%	0%	£0
<b>Total</b>					<b>£0</b>

IMAGE  
REMOVED

- Group EPS (p)
- Group sales (£m)
- Operating cashflow (£m)

Note 1 Although the threshold for the Group sales element was reached in 2015, the committee has exercised its discretion to reduce the bonus to nil due to poor overall underlying performance

Note 2 Actual performance provided like for like with targets, based on plan exchange rates for 2015 and constant portfolio consistent with prior years

Note 3 Pro-rated due to part year employed (relates to full period employed rather than period as a director)



**Long-term incentives** The single figure of remuneration for 2015 includes all long-term incentive awards that were subject to a performance condition where the performance period ended, or was substantially (but not fully) completed, at 31 December 2015, and awards where the performance condition has been satisfied but where the release of shares is subject to a further holding period. The same methodology has been applied for the single figure of remuneration for 2014.

In 2015, the performance conditions for the 2013 Long-Term Incentive Plan (LTIP) and 2013 Annual Bonus Share-Matching Plan (ABSMP) were not met. The executive directors both held vested shares under the 2010 LTIP that were released on 5 March 2015 at the end of the two-year holding period and these shares were part of the single figure of remuneration for 2013 as reported in the 2012 report on directors' remuneration. However, the dividend equivalent shares that were awarded in respect of these shares and released on 5 March 2015 have been included in the single figure of remuneration for 2015, as below.

**Worldwide Save For Shares** All share options that become exercisable during a year are included in the single figure of total remuneration for that year. The value included in the single figure of total remuneration is the number of options multiplied by the difference between the discounted option price and the market value on the earliest exercise date. Share options which became exercisable in 2015 are included in the single figure of total remuneration for 2015 based on the share price on August 1, 2015 of 1,203.0p. See page 111 for details of share options vesting in the year.

#### Long-term incentive plan vesting

Director	Date of award	Date of release	Number of shares	Value £000	Share price on release	Notes
John Fallon	-	5 Mar 15	3,191	46	1,444.0p	Dividend shares relating to final portion of 2010 award vesting
	3 Mar 10	5 Mar 15	13,752	199	1,444.0p	25% of 2010 award pay-out subject to continued employment released
			16,943	245		
Robin Freestone	-	5 Mar 15	2,659	38	1,444.0p	Dividend shares relating to final portion of 2010 award vesting
	3 Mar 10	5 Mar 15	11,460	165	1,444.0p	25% of 2010 award pay-out subject to continued employment released
			14,119	203		
<b>Total</b>			<b>31,062</b>	<b>448</b>		

#### Notes

Dividend equivalent shares only included in single figure table. The underlying 25% of the 2010 Award having been disclosed in the 2012 single figure table. Shares vested on 3 March 2015 but were released on 5 March together with related dividend shares per RNS announcement.

## Part 3 Annual remuneration report continued

## Executive directors' retirement benefits and entitlements

Details of the directors' pension entitlements and pension related benefits during the year are as follows

Director	Value of defined benefit over the period £000	Other pension costs to the company over the period £000	Other allowances in lieu of pension £000	Total annual value in 2015 £000	Normal retirement age	Accrued pension at 31 Dec 15 £000
John Fallon	169	–	202	371	62	90.5
Coram Williams	18	–	–	18	62	25.7
Robin Freestone	–	18	108	126	62	–

## Plans

John Fallon – Pearson Group Pension Plan Accrual rate of 1/30th of pensionable salary per annum. In addition, he received a taxable and non-pensionable cash supplement.

Coram Williams – Pearson Group Pension Plan Accrual rate of 1/60th of pensionable salary per annum with continuous service with a service gap in accordance with earlier commitments given to him about the arrangements that would apply should he rejoin Pearson in the UK having moved from Pearson to Penguin US and subsequently Penguin Random House.

Robin Freestone – Money Purchase 2003 section of the Pearson Group Pension Plan. In addition, he received a taxable and non-pensionable cash supplement.

John, Coram and Robin's pension benefits are subject to the notional earnings cap.

Note 1 The accrued pension at 31 December 2015 is the deferred pension to which the member would be entitled on ceasing pensionable service on 31 December 2015. For John Fallon and Coram Williams it relates to the pension payable from the UK Plan. Robin Freestone did not accrue defined benefits.

Note 2 Value of defined benefit over the period comprises the DB Input value, less inflation, less individual contribution.

Note 3 Other pension costs to the company over the period comprises contributions to defined contribution arrangements for UK benefits.

Note 4 Other allowances in lieu of pension represents the cash allowances paid in lieu of the previous FURBS arrangements.

Note 5 Total annual value is the sum of the previous three columns.

## Chairman and non-executive director remuneration

The remuneration paid to the chairman and non-executive directors in respect of the financial years ended 31 December 2015 and 31 December 2014 is as follows

Director £000s	2015						2014					
	Salary/ basic fee	Committee chairmanship	Committee membership	SID	Taxable benefits	Total	Salary/ basic fee	Committee chairmanship	Committee membership	SID	Taxable benefits	Total
Glen Moreno	500	–	–	–	–	500	500	–	–	–	–	500
David Arculus	22	7	5	–	1	35	68	21	14	–	2	105
Elizabeth Corley	70	15	3	–	1	89	47	–	4	–	1	52
Vivienne Cox	70	10	25	22	5	132	68	7	22	21	6	124
Ken Hydon	22	9	3	–	7	41	68	27	8	–	8	111
Josh Lewis	70	–	10	–	12	92	68	–	8	–	9	85
Linda Lorimer	70	–	20	–	7	97	68	–	17	–	8	93
Harish Manwani	70	–	5	–	5	80	68	–	4	–	7	79
Tim Score	70	19	7	–	1	97	–	–	–	–	–	–
<b>Total</b>	<b>964</b>	<b>60</b>	<b>78</b>	<b>22</b>	<b>39</b>	<b>1,163</b>	<b>955</b>	<b>55</b>	<b>77</b>	<b>21</b>	<b>41</b>	<b>1,149</b>

Note Taxable benefits refer to travel, accommodation and subsistence expenses incurred while attending board meetings during 2015 that were paid or reimbursed by the company which are deemed by HMRC to be taxable in the UK. The amounts in the table above include the grossed-up cost of UK tax to be paid by the company on behalf of the directors.

### Long-term incentives

The status of outstanding awards under the long-term incentive plan (LTIP) and the legacy annual bonus share matching plan (ABSMP) and performance against the performance conditions as at 31 December 2015 are described in the table below

For each executive director, details of awards under the LTIP and ABSMP that were awarded, vested, released, lapsed or held during 2015 are summarised in the adjacent table. Notes to this table and the following table are provided overleaf

### Status of outstanding awards under the long-term incentive plan and annual bonus share matching plan in 2015

#### Long-term Incentive plan (LTIP)

Date of award	Share price on date of award	Vesting date	Performance measures	Weighting	Performance period	Pay out at threshold	Pay out at maximum	Actual performance	% of award vested	Status
1 May 2015	1,337.0p	1 May 2018	Relative TSR	1/6	1 Jan 2015 to 31 Dec 2017	25% at median	100% at upper quartile	-	-	Outstanding subject to performance
			ROIC	1/3	2017	25% for ROIC of 6.5%	100% for ROIC of 7.5%			
			EPS growth	1/2	2017 compared to 2014	25% for EPS growth of 6.0%	100% for EPS growth of 12.0%			
1 May 2014	1,102.0p	1 May 2017	Relative TSR	1/6	2014 to 2017	30% at median	100% at upper quartile	-	-	Outstanding subject to performance
			ROIC	1/3	2016	30% for ROIC of 6.5%	100% for ROIC of 7.5%			
			EPS growth	1/2	2016 compared to 2013	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%			
1 May 2013	1,183.0p	1 May 2016	Relative TSR	1/3	2013 to 2016	30% at median	100% at upper quartile	17th percentile	Nil	Estimated to lapse in 2016
			ROIC	1/3	2015	0% for ROIC of 8.5%	100% for ROIC of 10.5%	5.8%	Nil	Will lapse in 2016
			EPS growth	1/3	2015 compared to 2012	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%	-5.2%	Nil	Will lapse in 2016

#### Annual Bonus Share Matching Plan (ABSMP)

Date of award	Share price on date of award	Vesting date	Performance measures	Weighting	Performance period	Pay out at threshold	Pay-out at maximum	Actual performance	% of award vested	Status
15 May 2013	1,206.0p	15 May 2016	Real compound annual EPS growth		2012 to 2015	50% of matching award for EPS growth of 3.0%	100% of matching award for EPS growth of 5.0%	-6.9%	Nil	Performance condition not met. Will lapse in 2016

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## Movements in directors' interests in share awards during 2015

Plan	Date of award	Vesting date	Number of shares as at 1 Jan 2015	Awarded	Released	Dividends awarded and released	Lapsed	Number of shares as at 31 Dec 2015	Status
<b>John Fallon</b>									
LTIP	1 May 2015	1 May 2018	0	230,000	-	-	-	230,000	Outstanding subject to performance
	1 May 2014	1 May 2017	274,000	-	-	-	-	274,000	Outstanding subject to performance
	1 May 2013	1 May 2016	250,000	-	-	-	250,000	0	Expected to lapse in 2016
	3 Mar 2010	3 Mar 2013	13,752	-	13,752	3,191	-	0	Released 5 Mar 2015 (balancing 75% of vested shares released in 2013)
ABSMP	15 May 2013	15 May 2016	6,083	-	-	-	6,083	0	Will lapse in 2016
<b>Total</b>			<b>543,835</b>	<b>230,000</b>	<b>13,752</b>	<b>3,191</b>	<b>256,083</b>	<b>504,000</b>	
<b>Coram Williams</b>									
LTIP	1 Aug 2015	1 Aug 2018	0	129,000	-	-	-	129,000	Outstanding subject to performance
<b>Total</b>			<b>0</b>	<b>129,000</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>129,000</b>	
<b>Robin Freestone</b>									
LTIP	1 May 2014	1 May 2017	162,000	-	-	-	-	162,000	Outstanding subject to performance (also see page 112)
	1 May 2013	1 May 2016	150,000	-	-	-	150,000	0	Expected to lapse in 2016 (also see page 112)
	3 Mar 2010	3 Mar 2013	11,460	-	11,460	2,659	-	0	Released 5 Mar 2015 (balancing 75% of vested shares released in 2013)
<b>Total</b>			<b>323,460</b>	<b>0</b>	<b>11,460</b>	<b>2,659</b>	<b>150,000</b>	<b>162,000</b>	

Note 1 For all awards, Pearson's reported financial results for the relevant period were used to measure performance and no discretion has been exercised

Note 2 Vested means where awards are no longer subject to performance conditions. Released means where shares have been transferred to participants. Held means where awards have vested but shares are held pending release on the relevant anniversary of the award date. Outstanding means awards that have been granted but are still subject to the achievement of performance conditions. Dividends refers to dividend equivalent shares that have been added without performance conditions to vested shares under the LTIP and released immediately on award.

Note 3 No variations to terms and conditions of plan interests were made during the year

Note 4 TSR is measured relative to the constituents of the FTSE World Media Index over a three-year period.

Note 5 In relation to the LTIP award made on 1 May 2014 potential vesting is 50% of maximum for attainment of ROIC of 7%.

Note 6 For the LTIP award made on 1 May 2013 and due to vest on 1 May 2016 we have estimated the out turn of the relative TSR performance condition based on performance as at 26 February 2016 at nil. If actual relative TSR performance is different on the date of vesting, we will set this out in the annual remuneration report for 2016

Note 7 The single figure of remuneration for 2015 includes all awards that were subject to a performance condition where the performance period ended or was substantially (but not fully) completed at 31 December 2015 and awards where the performance condition has been satisfied but where the release of shares is subject to a further holding period. The same methodology has been applied for earlier periods and the single figure for earlier reporting periods has been restated where necessary

Note 8 The value of shares included in the single figure of remuneration is the number of shares multiplied by the share price on release.

Note 9 Coram's 2015 award was made on his appointment to the board on 1 August 2015 and will vest three years from this date on 1 August 2018 subject to the same performance conditions and holding periods as for other executives.

Note 10 The value of the LTIP awards in 2015 for the executive directors is shown below based on the relevant share price on the date of award also shown:

Director	Date of award	Vesting date	Number of shares	Face value	Face value (% of base salary)	Value for threshold performance (% of 2014 salary)	Share price at date of award
John Fallon	1 May 2015	1 May 2018	230,000	£3,075,100	394%	99%	1,337.0p
Coram Williams	1 Aug 2015	1 Aug 2018	129,000	£1,551,870	301%	75%	1,203.0p

**Movements in directors' interests in share options during 2015**

John Fallon and Robin Freestone also hold options under the Worldwide Save For Shares plan as follows

Director	Date of grant	Number of shares under option held as at 31 Dec 2015	Option price	Normal earliest exercise date	Expiry date	Value in 2015 single figure £
John Fallon	7 May 2010	–	805 6p	1 Aug 15	1 Feb 16	7,670
	30 Apr 2014	1,109	811 2p	1 Aug 17	1 Feb 18	0
Robin Freestone	4 May 2012	–	909 0p	1 Aug 15	1 Feb 16	2,911
	30 Apr 2014	1,109	811 2p	1 Aug 17	1 Feb 18	0

Note 1 The share option awards made in 2010 to John Fallon in respect of 1 930 shares and 2012 to Robin Freestone in respect of 990 shares vested and became exercisable in the year and were exercised on 3 August 2015.

Note 2 No variations to terms and conditions of share options were made during the year

Note 3 Acquisition of shares under the Worldwide Save For Shares plan is not subject to a performance condition

Note 4 All share options that become exercisable during a year are included in the single figure of total remuneration for that year. The value included in the single figure of total remuneration is the number of options multiplied by the difference between the discounted option price and the market value on the earliest exercise date. Share options which became exercisable in 2015 are included in the single figure of total remuneration for 2015 based on the share price on 1 August 2015 of 1 203 0p

Note 5 The market price on 31 December 2015 was 736 0p per share and the range during the year was 695 0p to 1 508 0p

**Payments to former directors**

It is the committee's intention to disclose any payments to past directors, including any release of share-based awards post-departure

The number of shares retained from the number of shares originally awarded takes into account lapses due to performance, releases prior to ceasing to be a director and pro-rating for service in the performance period (where applied)

Former directors Will Ethridge and John Makinson, who retained the balancing 25% of their 2010 LTIP awards (which vested in 2013) when they stepped down from the board in 2013, received a release of shares under these awards, together with associated dividend shares, during 2015. Details of the vested awards released in 2015 were reported in the 2012 and 2013 reports on directors' remuneration, details of the dividend shares released in 2015 are Will Ethridge (3,191 shares) and John Makinson (2,659 shares)

**2013 long-term incentive awards**

Will Ethridge retained a long-term incentive plan award made on 1 May 2013, subject to performance. As disclosed elsewhere in this report, this award is expected to lapse in 2016

**Robin Freestone**

Robin Freestone received no payment for loss of office when he stepped down from the board with effect from 1 August 2015 and left employment on 30 September 2015

Robin held LTIP awards granted in 2013 and 2014 and, in February 2016, the remuneration committee set out a clear process and engaged with key shareholders to consider whether those awards should be preserved. The remuneration committee considered the circumstances of Robin's service and the facts surrounding his departure, taking account of the following factors that we normally consider whenever a decision to treat any person within the LTIP as a good leaver

- › the different types of leaver,
- › the circumstances at the time the award was originally made,
- › the individual's performance, and
- › the circumstances in which the individual left employment.

After careful consideration of these factors and consultation with key shareholders, the remuneration committee noted that:

- › Robin is leaving to take up several non-executive director appointments and so is ceasing full-time employment,
- › normal conditions applied at date of grant for any award under the LTIP and no award was made in 2015 (similarly, he did not receive a base salary increase in 2015),
- › Robin carried out all duties expected of him during his period of notice and in the preceding years prior to his leaving. He gave good service to the Pearson Board for nine years, and
- › Robin did not leave to take up employment in an executive capacity but rather as a non-executive board member

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The remuneration committee also took into account the effective and smooth handover of his role to Coram Williams

The remuneration committee determined that Robin would be treated as a good leaver, so that outstanding LTIP awards would be preserved on a time pro-rated basis, would receive no special treatment and remain subject to all of the applicable performance tests

Robin will therefore remain eligible to receive up to 116,667 (78%) of the shares awarded on 1 May 2013 and 72,000 (44%) of the shares awarded on 1 May 2014, both of which will vest, subject to performance, in 2016 and 2017 respectively. The 2013 award is expected to lapse in 2016 due to not meeting the performance targets

Robin will be treated as a retiree in respect of his outstanding WWSFS options granted in 2014

#### Marjorie Scardino

In the 2014 report, we made shareholders aware of a payroll processing error during the years 2007 to 2010, as a result of which taxes deducted from Marjorie Scardino's compensation were incorrectly allocated by Pearson among tax authorities in the UK and the US. This resulted in her being subject to temporary double taxation. The committee has concluded that Pearson would reimburse (on an after-tax basis) certain costs incurred by Marjorie Scardino in relation to this double taxation error. As a result, a payment of £27,842 has been made to her to conclude this matter.

#### Payments for loss of office

There were no payments for loss of office made to or agreed for executive directors in 2015

### Directors' interests in shares and value of shareholdings

#### Directors' interests

The share interests of the directors and their connected persons are as follows

Director	Ordinary shares at 31 Dec 15	Conditional shares at 31 Dec 15	Total number of ordinary and conditional shares at 31 Dec 15	Current shareholding	Current value (% salary)	Guideline (% salary)	Guideline met
<b>Chairman</b>							
Glen Moreno	210,000	-	-	see Note 8	-	-	-
Sidney Taurel	see Note 8	-	-	50,000	-	-	-
<b>Executive directors</b>							
John Fallon	293,056	0	293,056	293,056	327%	300%	Yes
Coram Williams	10	0	10	5,010	8%	200%	n/a
<b>Non-executive directors</b>							
Elizabeth Corley	1,267	-	-	1,267	-	-	-
Vivienne Cox	2,938	-	-	2,938	-	-	-
Josh Lewis	7,740	-	-	7,740	-	-	-
Linda Lorimer	2,675	-	-	2,675	-	-	-
Harish Manwani	2,571	-	-	2,571	-	-	-
Tim Score	849	-	-	849	-	-	-
Lincoln Wallen	see Note 8	-	-	-	-	-	-

Note 1 Conditional shares means shares which have vested but remain held subject to continuing employment for a pre-defined holding period

Note 2 The current value of the executive directors' current shareholdings is based on the closing market value of Pearson shares of 870.50p on 1 March 2016 against base salaries at 31 December 2015. The shareholding guidelines do not apply to the chairman and non-executive directors.

Note 3 Ordinary shares include both ordinary shares listed on the London Stock Exchange and American Depositary Receipts (ADRs) listed on the New York Stock Exchange. The figures include both shares and ADRs acquired by individuals investing part of their own after-tax annual bonus in Pearson shares under the annual bonus share matching plan.

Note 4 The market price on 31 December 2015 was 736.0p per share and the range during the year was 695.0p to 1,508.0p.

Note 5 On 29 February 2016, Coram Williams purchased 5,000 shares which are included under current shareholding in the table above and shown in the chart overleaf. On 2 March 2016, Sidney Taurel purchased 50,000 shares which are also shown in the table above.

Note 6 Ordinary shares do not include any shares vested but held pending release under a restricted share plan.

Note 7 As a new appointee, the guidelines are not yet applicable in full for Coram Williams.

Note 8 Sidney Taurel and Lincoln Wallen were appointed as directors on 1 January 2016. Glen Moreno left Pearson on 31 December 2015 and as such we have not shown a current shareholding figure in the table above.

IMAGE REMOVED

#### Shareholding guidelines

Executive directors are expected to build up a substantial shareholding in the company in line with the policy of encouraging widespread employee ownership and to align further the interests of executives and shareholders. With effect from 2014, target holding is 300% of salary for the chief executive and 200% of salary for the other executive directors.

Shares that count towards these guidelines include any shares held unencumbered by the executive, their spouse and/or dependent children plus any shares vested but held pending release under a restricted share plan. Executive directors have five years from the date of appointment to reach the guideline.

With effect from 2014, these guidelines were extended to include all members of the Pearson executive at 100% of salary.

The shareholding guidelines do not apply to the chairman and non-executive directors. However, a minimum of 25% of the basic non-executive directors' fee is paid in Pearson shares that the non-executive directors have committed to retain for the period of their directorships.

#### Dilution and use of equity

We can use existing shares bought in the market, treasury shares or newly-issued shares to satisfy awards under the company's various share plans.

For restricted stock awards under the long-term incentive plan and matching share awards under the annual bonus share matching plan, we would normally expect to use existing shares.

There are limits on the amount of new-issue equity we can use. In any rolling ten-year period, no more than 10% of Pearson equity will be issued, or be capable of being issued, under all Pearson's share plans, and no more than 5% of Pearson equity will be issued, or be capable of being issued, under executive or discretionary plans.

At 31 December 2015, stock awards to be satisfied by new-issue equity granted in the last ten years under all Pearson share plans amounted to 1.6% of the company's issued share capital. No stock awards granted in the last ten years under executive or discretionary share plans will be satisfied by new-issue equity.

In addition, for existing shares, no more than 5% of Pearson equity may be held in trust at any time. Against this limit, shares held in trust at 31 December 2015 amounted to 0.8% of the company's issued share capital.

The headroom available for all Pearson plans, executive or discretionary plans and shares held in trust is as follows:

Headroom	2015	2014	2013
All Pearson plans	8.4%	8.3%	8.4%
Executive or discretionary plans	5.0%	5.0%	5.0%
Shares held in trust	4.2%	4.1%	3.9%

#### Executive directors' non-executive directorships

Although the policy permits executive directors to serve as non-executive directors elsewhere with the board's agreement, none of the executive directors held an external directorship during 2015.

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## Part 3 Annual remuneration report continued

## Historical performance and remuneration

## Total shareholder return performance

We set out below Pearson's total shareholder return (TSR) performance relative to the FTSE All-Share index on an annual basis over the seven-year period 2008 to 2015. This comparison has been chosen because the FTSE All-Share represents the broad market index within which Pearson Shares are traded. TSR is the measure of the returns that a company has provided for its shareholders, reflecting share price movements and assuming reinvestment of dividends. (source: DataStream)

In accordance with the reporting regulations, this section also presents Pearson's TSR performance alongside the single figure of total remuneration for the CEO over the last seven years and a summary of the variable pay outcomes relative to the prevailing maximum at the time. The table below summarises the total remuneration for the CEO over the last seven years, and the outcomes of annual and long-term incentive plans as a proportion of maximum.

IMAGE REMOVED

CEO remuneration	Marjorie Scardino				John Fallon		
Total remuneration (single figure, £000s)	6,370	8,466	8,340	5,330	1,727	1,895	1,263
Annual incentive – incumbent (% of maximum)	91.3%	92.1%	75.7%	24.2%	34.3%	50.5%	Nil
Long-term incentive – incumbent (% of maximum)	80.0%	97.5%	68.3%	36.7%	Nil	Nil	Nil

Annual incentive is the actual annual incentive received by the incumbent as a percentage of maximum opportunity.

Long-term incentive is the pay-out of performance related restricted shares under the long-term incentive plan where the year shown is the final year of the performance period for the purposes of calculating the single total figure of remuneration.

Total remuneration: John Fallon. John Fallon's total remuneration opportunity is lower than that of the previous incumbent. Variable pay-outs under the annual and long-term incentive plans reflect performance for the relevant periods.



**Comparative information**

The following information is intended to provide additional context regarding the total remuneration for executive directors

**Relative percentage change in remuneration for CEO**  
The following table sets out the change between 2014 and 2015 in three elements of remuneration for the CEO, in comparison to the average for all employees

While the committee considers the increase in base pay for the CEO relative to the broader employee population, benefits are driven by local practices and eligibility is determined by level and individual circumstances which do not lend themselves to comparison

**Change in CEO remuneration 2014/15**

Base salary	Allowances and benefits
↑ +2%	↓ -25%
Annual incentives	Total
↓ -100%	↓ -33%

**Change in employee remuneration 2014/15**

Base salary	Allowances and benefits
↑ +3%	↑ +12%
Annual incentives	Total
↓ -38%	= No change

**Note 1** The figures for all employees reflect average salaries and average employee numbers each year. Annual incentives include all plans, including sales incentives.

**Note 2** The increase in allowances and annual incentives for John Fallon is attributable respectively to (a) the first full-year of reporting of his private use of a driver based on the benefit in-kind charge for the 2014/2015 tax year and (b) the year-on-year increase in his pay-out under the Pearson annual incentive plan.

**Relative importance of pay spend**

The committee considers directors' remuneration in the context of the company's allocation and disbursement of resources to different stakeholders

In particular, we chose operating profit because this is a measure of our ability to reinvest in the company. We include dividends because these constitute an important element of our return to shareholders

All figures in £ millions	2015	2014	Change	
			£m	%
Operating profit	723	722	1	0%
Dividends	423	397	26	7%
Total wages and salaries	1,507	1,607	-100	-6%

**Note 1** Operating profit is as set out in the financial statements

**Note 2** Wages and salaries include continuing operations only and include directors 2014 is restated on the same basis. Average employee numbers for continuing operations for 2015 were 37,265 (2014: 38,654). Further details are set out in note 5 to the financial statements on page 155

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## Part 3 Annual remuneration report continued

## Information on changes to remuneration for 2016

## Executive directors' base salaries

We have undertaken a regular periodic review of base salaries for 2016, taking into account general economic and market conditions, the level of increases made across the company as a whole, the remuneration of executives in similar positions in comparable companies and individual performance

As a result of this review, the 2016 base salaries for the CEO and CFO are unchanged as follows

£000s	John Fallon	Coram Williams
Base salary at 31 December 2015	£780.3	£515.0
Change	0%	0%
Base salary at 1 April 2016	£780.3	£515.0

## Annual incentive

The key design principles underlying the company's approach to annual incentives for 2016 are the same as for 2015, namely

- › Full alignment of annual incentives with the global business and education strategy to reinforce a 'one Pearson' focus - the size of the overall annual incentive pay-out will continue to be linked to overall Pearson performance
- › A clear, transparent, coherent, consistent, organisation-wide approach to incentives and performance management with a common incentive framework for all business units and enabling functions

It is anticipated that the 2016 sales and cash metrics and weightings remain unchanged from 2015. However, to align the AIP with the specific restructuring achievements required in 2016, as noted in the income statement measure in our guidance to investors, operating profit after the cost of restructuring would be added to the metrics with a 30% weighting. To accommodate this change, the weighting for EPS would also be 30% (down from 60% weight for 2015).

The Pearson financial targets are set each year as part of the normal operating plan process. The CEO and CFO have recommended the overall Pearson incentive funding metrics (including performance measures, targets and weightings) to the committee for approval in the normal way. For 2016, the range of normal rewarded performance is expected to be wider than in previous years – and, in consequence, both the threshold performance and the on-target funding are set to be lower than in 2015.

The board considers the performance targets for 2016 to be commercially sensitive. Details of all performance measures, weightings and targets will be disclosed in the annual remuneration report for 2016 unless the committee determines that they remain commercially sensitive.

There has been no change in individual annual incentive opportunities for the executive directors and the Pearson executive.

Annual incentive pay-outs are determined according to a combination of Pearson-wide performance and individual goals. The sum of the CEO's and the Pearson executives' 'on-target' annual incentive constitutes the incentive pool for this group which flexes up or down based on overall Pearson performance. Individual performance is assessed against goals set at the start of the year. Individual pay-outs up to individual maximum opportunities and within the total pool are recommended by the CEO (or by the chairman in the case of the CEO himself) for review and, in the case of the executive directors, for approval by the committee.

## Special incentive and retention arrangements

The committee agreed for 2016 incentive and retention arrangements for selected key employees, which will vest, or not, in 2017. No executive directors participate in these incentives.

**Long-term incentives**

The committee will continue to operate the long-term incentive plan for the executive directors and other members of the Pearson executive in line with the arrangements outlined in the 2013 report on directors' remuneration

- › The weighting of the performance metrics will remain half on earnings per share, one-third on return on invested capital and one-sixth on relative total shareholder return. However, the EPS target is planned to be absolute rather than a growth target, and aligned with our external guidance to the market in January 2016
  - › Performance will be tested over three years and 75% of the vested shares will be released at that point. However, there is a mandatory restriction on participants' ability to dispose of the 75% of the vested shares (other than to meet personal tax liabilities) for a further two years. Furthermore, participants' rights to the release of the remaining 25% of the vested shares are subject to continued employment over the same period
  - › At the time of writing, the committee has yet to approve the 2016 long-term incentive awards and the associated performance targets for the executive directors and other members of the Pearson executive. These are expected to be determined at the April meeting prior to the anticipated May grant. We expect to set targets for the 2016 awards that are consistent with the company's market guidance over the period to 2018
- We will set the level of individual awards consistent with those seen in recent years and within the policy maximum taking into account.
- › The face value of individual awards at the time of grant,
  - › assuming that performance targets are met in full
  - › Individual roles and responsibilities
  - › Company and individual performance
  - › Market practice for comparable companies and market assessments of total remuneration from our independent advisers

Full details of individual awards for the executive directors and the performance targets for 2016 will be set out in the annual remuneration report for 2016

**Appointment of chairman**

Our new chairman, Mr Sidney Taurel, has agreed to lead our board for the same package that the outgoing chairman received, that is a flat fee of £500,000 per year. He will not participate in any form of Pearson incentive arrangement. He became the chairman effective 1 January 2016.

**Chairman and non-executive directors**

The fee for the chairman and fees for the non-executive directors remain unchanged for 2016. Full details will be set out in the annual remuneration report and included in the single figure of total remuneration for 2016.

However, we intend to review these fees in line with our remuneration policy in late 2016 in time for our 2017 policy vote.

The directors' remuneration report has been approved by the board on 4 March 2016 and signed on its behalf by

IMAGE REMOVED

Elizabeth Corley  
Chairman of the remuneration committee

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## Additional disclosures

### Report of the directors

Pages 70 to 123 of this document comprise the directors' report for the year ended 31 December 2015

Other information that is required by the Companies Act 2006 (the Act) to be included in the directors' report, and which is incorporated by reference, can be located as follows

Summary disclosures index	See more
Dividend recommendation	p11
Financial instruments and financial risk management	note 19
Important events since year end	p37
Future development of the business	p06-07
Research and development activities	p53
Employment of disabled persons	p62
Employee involvement	p59
Greenhouse gas emissions	p64

With the exception of the dividend waiver described on page 122, there is no information to be disclosed in accordance with Listing Rule 9.8.4

#### Going concern

The directors have made an assessment of the company's ability to continue as a going concern and consider it appropriate to adopt the going concern basis of accounting

#### Viability statement

As set out on page 40 the board has also reviewed the prospects of Pearson over the three year period to December 2018 taking account of the company's strategic plans, a 'severe but plausible' downside case and further stress testing based on the principal risks set out on pages 41-45

Based on the results of these procedures, and considering the company's strong balance sheet following the sale of the FT group, the directors have a reasonable expectation that Pearson will be able to continue in operation and meet its liabilities as they fall due over the three year period ending December 2018. This assumes a reasonable level of ongoing access to capital either via issuing commercial paper or drawing on our revolving credit facility (see note 18 on p178)

#### Share capital

Details of share issues are given in note 27 to the accounts on page 200. The company has a single class of shares which is divided into ordinary shares of 25p each. The ordinary shares are in registered form. As at 31 December 2015, 821,068,560 ordinary shares were in issue. At the AGM held on 24 April 2015, the company was authorised, subject to certain conditions, to acquire up to 82,027,776 ordinary shares by market purchase. Shareholders will be asked to renew this authority at the AGM on 29 April 2016.

Information provided to the company pursuant to the Financial Conduct Authority's Disclosure and Transparency Rules (DTR) is published on a Regulatory Information Service and on the company's website.

As at 31 December 2015, the company had been notified under DTR 5 of the following holders of significant voting rights in its shares

	Number of voting rights	Percentage as at date of notification
BlackRock, Inc	42,201,515	5.13%
Schroders plc	42,151,560	5.13%

Between 31 December 2015 and 2 March 2016, being the latest practicable date before the publication of this report, the company did not receive any further notifications under DTR 5.

#### Annual General Meeting

The notice convening the AGM, to be held at 12 noon on Friday, 29 April 2016 at IET London, 2 Savoy Place, London WC2R 0BL, is contained in a circular to shareholders to be dated 23 March 2016.

#### Registered auditors

In accordance with section 489 of the Act, a resolution proposing the reappointment of PricewaterhouseCoopers LLP (PwC) as auditors to the company will be proposed at the AGM, at a level of remuneration to be agreed by the directors.

### Auditors' independence

In line with best practice, our relationship with PwC is governed by our external auditors policy, which is reviewed and approved annually by the audit committee. The policy establishes procedures to ensure the auditors' independence is not compromised, as well as defining those non-audit services that PwC may or may not provide to Pearson.

These allowable services are in accordance with relevant UK and US legislation. The audit committee approves all audit and non-audit services provided by PwC. Certain categories of allowable non-audit services have been pre-approved by the audit committee subject to the authorities below.

- › Pre-approved non-audit services can be authorised by the chief financial officer up to £100,000 per project, subject to a cumulative limit of £500,000 per annum.
- › Acquisition or disposal transactions and due diligence up to £100,000 per project may be performed by our external auditors, in light of the need for confidentiality. Any project/transaction generating fees in excess of £100,000 must be specifically approved by the audit committee.
- › Tax compliance and related activities up to the greater of £1,000,000 per annum or 50% of the external audit fee.
- › For forward-looking tax advisory services we use the most appropriate adviser, usually after a tender process. Where we decide to use our independent auditors, authority, up to £100,000 per project subject to a cumulative limit of £500,000 per annum, has been delegated by the audit committee to management.

Services provided by PwC above these limits and all other allowable non-audit services, irrespective of value, must be approved by the audit committee. Where appropriate, services will be tendered prior to a decision being made as to whether to award work to the auditors.

The audit committee receives regular reports summarising the amount of fees paid to the auditors. During 2015, Pearson spent considerably more on non-audit fees with PwC compared to 2014, due to costs relating to carve-out audits for businesses disposed. For 2015, non-audit fees represented 56% of external audit fees (37% in 2014).

For all non-audit work in 2015, PwC were selected only after consideration that they were best able to provide the services we required at a reasonable fee and within the terms of our external auditors policy.

To assist in ensuring that independence and objectivity is maintained, for forward-looking tax advisory and due diligence work PwC assign a different partner from the one leading the external audit.

Significant non-audit work performed by PwC during 2015 included:

- › Audit-related work in relation to potential and actual corporate finance transactions.
- › Tax compliance services related to a routine audit by the US Internal Revenue Service.
- › Tax advisory work on a number of UK, US and international tax matters.
- › Assurance services on a corporate bond issued in May 2015.
- › Consulting services related to the establishment of an auditable efficacy framework.
- › Audit of IT general controls mandated by contractual commitments.

A full statement of the fees for audit and non-audit services is provided in note 4 to the accounts on page 154.

### Fair, balanced and understandable reporting

As required by the Code, we have established arrangements to ensure that all information we report to investors and regulators is fair, balanced and understandable. A process and timetable for the production and approval of this year's report was agreed by the board at its meeting in December 2015. The full board then had opportunity to review and comment on the report as it progressed.

Representatives from financial reporting, corporate affairs, company secretarial, legal and internal audit and compliance are involved in the preparation and review of the annual report to ensure a cohesive and balanced approach and, as with all of our financial reporting, our disclosure committee conducts a thorough verification of narrative and financial statements.

The audit committee is also available to advise the board on certain aspects of the report, to enable the directors to fulfil their responsibility in this regard.

The directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy.

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## Report of the Directors continued

The directors also confirm that, for each director in office at the date of this report

- › So far as the director is aware, there is no relevant audit information of which the company's auditors are unaware
- › They have taken all the steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information

### Directors in office

The following directors were in office during the year and up until signing of the financial statements

G R Moreno (stepped down 31 December 2015)	S J Lewis L K Lorimer
J J Fallon	H Manwani
R A D Freestone (stepped down 1 August 2015)	T Score
T D G Arculus (stepped down 24 April 2015)	S Taurel (appointed 1 January 2016)
E P L Corley	L Wallen (appointed 1 January 2016)
V Cox	C Williams (appointed 1 August 2015)
K J Hydon (stepped down 24 April 2015)	

The directors' report has been approved by the board on 4 March 2016 and signed on its behalf by

IMAGE REMOVED

Stephen Jones  
Company secretary

### Statement of directors' responsibilities

The directors are responsible for preparing the annual report in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the Group and parent company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and the Group and of the profit or loss of the Group for that period.

In preparing these financial statements, the directors are required to

- › Select suitable accounting policies and then apply them consistently
- › Make judgements and accounting estimates that are reasonable and prudent
- › State whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements
- › Prepare the financial statements on a going concern basis, unless it is inappropriate to presume that the company will continue in business

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and the Group and enable them to ensure that the financial statements and the report on directors' remuneration comply with the Act and, as regards the Group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the directors, whose names and functions are listed on p72-73 confirms that, to the best of their knowledge

- › The Group financial statements, which have been prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group
- › The strategic report contained in the annual report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces

This responsibility statement has been approved by the board on 4 March 2016 and signed on its behalf by

IMAGE REMOVED

Coram Williams  
Chief financial officer

## Additional shareholder information

### Additional information for shareholders

Set out below is other statutory and regulatory information that Pearson is required to disclose in its directors' report in compliance with DTR 7.2.6

### Amendment to articles of association

Any amendments to the articles of association of the company (the Articles) may be made in accordance with the provisions of the Act by way of a special resolution

### Rights attaching to shares

The rights attaching to the ordinary shares are defined in the Articles. A shareholder whose name appears on the company's register of members can choose whether his/her shares are evidenced by share certificates (i.e. in certificated form) or held electronically (i.e. uncertificated form) in CREST (the electronic settlement system in the UK)

Subject to any restrictions below, shareholders may attend any general meeting of the company and, on a show of hands, every shareholder (or his/her representative) who is present at a general meeting has one vote on each resolution, and on a poll, every shareholder (whether an individual or a corporation) present in person or by proxy shall have one vote for every 25 pence of nominal share capital held. A resolution put to the vote at a general meeting is decided on a show of hands unless before, or on the declaration of the result of, a vote on a show of hands, a poll is demanded. A poll can be demanded by the chairman of the meeting, or by at least three shareholders (or their representatives) present in person and having the right to vote, or by any shareholders (or their representatives) present in person having at least 10% of the total voting rights of all shareholders, or by any shareholders (or their representatives) present in person holding ordinary shares on which an aggregate sum has been paid up of at least 10% of the total sum paid up on all ordinary shares. At this year's AGM voting will again be conducted on a poll, consistent with best practice.

Shareholders can declare a final dividend by passing an ordinary resolution but the amount of the dividend cannot exceed the amount recommended by the board. The board can pay interim dividends on any class of shares of the amounts and on the dates and for the periods they decide. In all cases the distributable profits of the company must be sufficient to justify the payment of the relevant dividend.

The board may, if authorised by an ordinary resolution of the shareholders, offer any shareholder the right to elect to receive new ordinary shares, which will be credited as fully paid, instead of their cash dividend.

Any dividend which has not been claimed for 12 years after it became due for payment will be forfeited and will then belong to the company, unless the directors decide otherwise.

If the company is wound up, the liquidator can, with the sanction of a special resolution passed by the shareholders, divide among the shareholders all or any part of the assets of the company and he/she can value assets and determine how the division shall be carried out as between the shareholders or different classes of shareholders. The liquidator can also, with the same sanction, transfer the whole or any part of the assets to trustees upon such trusts for the benefit of the shareholders.

### Voting at general meetings

Any form of proxy sent by the shareholders to the company in relation to any general meeting must be delivered to the company (via its registrars), whether in written or electronic form, not less than 48 hours before the time appointed for holding the meeting or adjourned meeting at which the person named in the appointment proposes to vote.

The board may decide that a shareholder is not entitled to attend or vote either personally or by proxy at a general meeting or to exercise any other right conferred by being a shareholder if he/she or any person with an interest in shares has been sent a notice under section 793 of the Act (which confers upon public companies the power to require information with respect to interests in their voting shares) and he/she or any interested person failed to supply the company with the information requested within 14 days after delivery of that notice. The board may also decide, where the relevant shareholding comprises at least 0.25% of the nominal value of the issued shares of that class, that no dividend is payable in respect of those default shares and that no transfer of any default shares shall be registered.

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## Additional shareholder information continued

Pearson operates an employee benefit trust to hold shares, pending employees becoming entitled to them under the company's employee share plans. There were 6,704,505 shares held as at 31 December 2015. The trust has an independent trustee which has full discretion in relation to the voting of such shares. A dividend waiver operates on the shares held in the trust.

Pearson also operates two nominee shareholding arrangements which hold shares on behalf of employees. There were 2,871,174 shares held in the Sharestore account and 309,841 shares held in the Global Nominee account as at 31 December 2015. The beneficial owners of shares held in Sharestore are invited to submit voting instructions online at [www.shareview.co.uk](http://www.shareview.co.uk) and Global Nominee participants are invited to submit voting instructions by e-mail to [nominee@equiniti.com](mailto:nominee@equiniti.com). If no instructions are given by the beneficial owner by the date specified, the trustees holding these shares will not exercise the voting rights.

### Transfer of shares

The board may refuse to register a transfer of a certificated share which is not fully paid, provided that the refusal does not prevent dealings in shares in the company from taking place on an open and proper basis. The board may also refuse to register a transfer of a certificated share unless (i) the instrument of transfer is lodged, duly stamped (if stampable), at the registered office of the company or any other place decided by the board, and is accompanied by the certificate for the share to which it relates and such other evidence as the board may reasonably require to show the right of the transferor to make the transfer, (ii) it is in respect of only one class of shares, and (iii) it is in favour of not more than four transferees.

Transfers of uncertificated shares must be carried out using CREST and the board can refuse to register a transfer of an uncertificated share in accordance with the regulations governing the operation of CREST.

### Variation of rights

If at any time the capital of the company is divided into different classes of shares, the special rights attaching to any class may be varied or revoked either

(i) with the written consent of the holders of at least 75% in nominal value of the issued shares of the relevant class or

(ii) with the sanction of a special resolution passed at a separate general meeting of the holders of the shares of the relevant class.

Without prejudice to any special rights previously conferred on the holders of any existing shares or class of shares, any share may be issued with such preferred, deferred, or other special rights, or such restrictions, whether in regard to dividend, voting, return of capital or otherwise as the company may from time to time by ordinary resolution determine.

### Appointment and replacement of directors

The Articles contain the following provisions in relation to directors:

Directors shall be no less than two in number.

Directors may be appointed by the company by ordinary resolution or by the board. A director appointed by the board shall hold office only until the next AGM and shall then be eligible for reappointment, but shall not be taken into account in determining the directors or the number of directors who are to retire by rotation at that meeting.

The board may from time to time appoint one or more directors to hold executive office with the company for such period (subject to the provisions of the Act) and upon such terms as the board may decide and may revoke or terminate any appointment so made.



The Articles provide that, at every AGM of the company, at least one-third of the directors shall retire by rotation (or, if their number is not a multiple of three, the number nearest to one-third). The first directors to retire by rotation shall be those who wish to retire and not offer themselves for re-election. Any further directors so to retire shall be those of the other directors subject to retirement by rotation who have been longest in office since they were last re-elected but, as between persons who became or were last re-elected on the same day, those to retire shall (unless they otherwise agree among themselves) be determined by lot. In addition, any director who would not otherwise be required to retire shall retire by rotation at the third AGM after they were last re-elected.

Notwithstanding the provisions of the Articles, the board has resolved that all directors should offer themselves for re-election annually, in accordance with the Code.

The company may by ordinary resolution remove any director before the expiration of his/her term of office. In addition, the board may terminate an agreement or arrangement with any director for the provision of his/her services to the company.

#### **Powers of the directors**

Subject to the company's Articles, the Act and any directions given by special resolution, the business of the company will be managed by the board who may exercise all the powers of the company, including powers relating to the issue and/or buying back of shares by the company (subject to any statutory restrictions or restrictions imposed by shareholders in general meeting).

#### **Significant agreements**

The following significant agreements contain provisions entitling the counterparties to exercise termination or other rights in the event of a change of control of the company.

Under the \$1,750,000,000 revolving credit facility agreement dated August 2014 which matures in August 2020 between, amongst others, the company, Barclays Bank plc (Agent) and the banks and financial institutions named therein as lenders (the Facility), any such bank may, upon a change of control of the company, require its outstanding advances, together with accrued interest and any other amounts payable in respect of such Facility, and its commitments, to be cancelled, each within 60 days of notification to the banks by the Agent. For these purposes, a 'change of control' occurs if the company becomes a subsidiary of any other company or one or more persons acting either individually or in concert, obtains control (as defined in section 1124 of the Corporation Tax Act 2010) of the company.

Shares acquired through the company's employee share plans rank *pari passu* with shares in issue and have no special rights. For legal and practical reasons, the rules of these plans set out the consequences of a change of control of the company.

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### Report of the directors

Pages 70 to 123 of this document comprise the directors' report for the year ended 31 December 2015

Other information that is required by the Companies Act 2006 (the Act) to be included in the directors' report, and which is incorporated by reference, can be located as follows

Summary disclosures index	See more
Dividend recommendation	p11
Financial instruments and financial risk management	note 19
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With the exception of the dividend waiver described on page 122, there is no information to be disclosed in accordance with Listing Rule 9.8.4

#### Going concern

The directors have made an assessment of the company's ability to continue as a going concern and consider it appropriate to adopt the going concern basis of accounting

#### Viability statement

As set out on page 40 the board has also reviewed the prospects of Pearson over the three year period to December 2018 taking account of the company's strategic plans, a 'severe but plausible' downside case and further stress testing based on the principal risks set out on pages 41-45

Based on the results of these procedures, and considering the company's strong balance sheet following the sale of the FT group, the directors have a reasonable expectation that Pearson will be able to continue in operation and meet its liabilities as they fall due over the three year period ending December 2018. This assumes a reasonable level of ongoing access to capital either via issuing commercial paper or drawing on our revolving credit facility (see note 18 on p178)

#### Share capital

Details of share issues are given in note 27 to the accounts on page 200. The company has a single class of shares which is divided into ordinary shares of 25p each. The ordinary shares are in registered form. As at 31 December 2015, 821,068,560 ordinary shares were in issue. At the AGM held on 24 April 2015, the company was authorised, subject to certain conditions, to acquire up to 82,027,776 ordinary shares by market purchase. Shareholders will be asked to renew this authority at the AGM on 29 April 2016.

Information provided to the company pursuant to the Financial Conduct Authority's Disclosure and Transparency Rules (DTR) is published on a Regulatory Information Service and on the company's website.

As at 31 December 2015, the company had been notified under DTR 5 of the following holders of significant voting rights in its shares

	Number of voting rights	Percentage as at date of notification
BlackRock, Inc	42,201,515	5.13%
Schroders plc	42,151,560	5.13%

Between 31 December 2015 and 2 March 2016, being the latest practicable date before the publication of this report, the company did not receive any further notifications under DTR 5.

#### Annual General Meeting

The notice convening the AGM, to be held at 12 noon on Friday, 29 April 2016 at IET London, 2 Savoy Place, London WC2R 0BL, is contained in a circular to shareholders to be dated 23 March 2016.

#### Registered auditors

In accordance with section 489 of the Act, a resolution proposing the reappointment of PricewaterhouseCoopers LLP (PwC) as auditors to the company will be proposed at the AGM, at a level of remuneration to be agreed by the directors.

### Auditors' independence

In line with best practice, our relationship with PwC is governed by our external auditors policy, which is reviewed and approved annually by the audit committee. The policy establishes procedures to ensure the auditors' independence is not compromised, as well as defining those non-audit services that PwC may or may not provide to Pearson.

These allowable services are in accordance with relevant UK and US legislation. The audit committee approves all audit and non-audit services provided by PwC. Certain categories of allowable non-audit services have been pre-approved by the audit committee subject to the authorities below.

- › Pre-approved non-audit services can be authorised by the chief financial officer up to £100,000 per project, subject to a cumulative limit of £500,000 per annum.
- › Acquisition or disposal transactions and due diligence up to £100,000 per project may be performed by our external auditors, in light of the need for confidentiality. Any project/transaction generating fees in excess of £100,000 must be specifically approved by the audit committee.
- › Tax compliance and related activities up to the greater of £1,000,000 per annum or 50% of the external audit fee.
- › For forward-looking tax advisory services we use the most appropriate adviser, usually after a tender process. Where we decide to use our independent auditors, authority, up to £100,000 per project subject to a cumulative limit of £500,000 per annum, has been delegated by the audit committee to management.

Services provided by PwC above these limits and all other allowable non-audit services, irrespective of value, must be approved by the audit committee. Where appropriate, services will be tendered prior to a decision being made as to whether to award work to the auditors.

The audit committee receives regular reports summarising the amount of fees paid to the auditors. During 2015, Pearson spent considerably more on non-audit fees with PwC compared to 2014, due to costs relating to carve-out audits for businesses disposed. For 2015, non-audit fees represented 56% of external audit fees (37% in 2014).

For all non-audit work in 2015, PwC were selected only after consideration that they were best able to provide the services we required at a reasonable fee and within the terms of our external auditors policy.

To assist in ensuring that independence and objectivity is maintained, for forward-looking tax advisory and due diligence work PwC assign a different partner from the one leading the external audit.

Significant non-audit work performed by PwC during 2015 included

- › Audit-related work in relation to potential and actual corporate finance transactions
- › Tax compliance services related to a routine audit by the US Internal Revenue Service
- › Tax advisory work on a number of UK, US and international tax matters
- › Assurance services on a corporate bond issued in May 2015
- › Consulting services related to the establishment of an auditable efficacy framework
- › Audit of IT general controls mandated by contractual commitments

A full statement of the fees for audit and non-audit services is provided in note 4 to the accounts on page 154.

### Fair, balanced and understandable reporting

As required by the Code, we have established arrangements to ensure that all information we report to investors and regulators is fair, balanced and understandable. A process and timetable for the production and approval of this year's report was agreed by the board at its meeting in December 2015. The full board then had opportunity to review and comment on the report as it progressed.

Representatives from financial reporting, corporate affairs, company secretarial, legal and internal audit and compliance are involved in the preparation and review of the annual report to ensure a cohesive and balanced approach and, as with all of our financial reporting, our disclosure committee conducts a thorough verification of narrative and financial statements.

The audit committee is also available to advise the board on certain aspects of the report, to enable the directors to fulfil their responsibility in this regard.

The directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy.

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## Report of the Directors continued

The directors also confirm that, for each director in office at the date of this report

- › So far as the director is aware, there is no relevant audit information of which the company's auditors are unaware
- › They have taken all the steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information

**Directors in office**

The following directors were in office during the year and up until signing of the financial statements

G R Moreno (stepped down 31 December 2015)	S J Lewis
J J Fallon	L K Lorimer
R A D Freestone (stepped down 1 August 2015)	H Manwani
T D G Arculus (stepped down 24 April 2015)	T Score
E P L Corley	S Taurel (appointed 1 January 2016)
V Cox	L Wallen (appointed 1 January 2016)
K J Hydon (stepped down 24 April 2015)	C Williams (appointed 1 August 2015)

The directors' report has been approved by the board on 4 March 2016 and signed on its behalf by

IMAGE REMOVED

Stephen Jones  
Company secretary

**Statement of directors' responsibilities**

The directors are responsible for preparing the annual report in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the Group and parent company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and the Group and of the profit or loss of the Group for that period.

In preparing these financial statements, the directors are required to

- › Select suitable accounting policies and then apply them consistently
- › Make judgements and accounting estimates that are reasonable and prudent
- › State whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements
- › Prepare the financial statements on a going concern basis, unless it is inappropriate to presume that the company will continue in business

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and the Group and enable them to ensure that the financial statements and the report on directors' remuneration comply with the Act and, as regards the Group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the directors, whose names and functions are listed on p72-73 confirms that, to the best of their knowledge

- › The Group financial statements, which have been prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group
- › The strategic report contained in the annual report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces

This responsibility statement has been approved by the board on 4 March 2016 and signed on its behalf by

IMAGE REMOVED

Coram Williams  
Chief financial officer



## Additional shareholder information

### Additional information for shareholders

Set out below is other statutory and regulatory information that Pearson is required to disclose in its directors' report in compliance with DTR 7.2.6

### Amendment to articles of association

Any amendments to the articles of association of the company (the Articles) may be made in accordance with the provisions of the Act by way of a special resolution

### Rights attaching to shares

The rights attaching to the ordinary shares are defined in the Articles. A shareholder whose name appears on the company's register of members can choose whether his/her shares are evidenced by share certificates (i.e. in certificated form) or held electronically (i.e. uncertificated form) in CREST (the electronic settlement system in the UK).

Subject to any restrictions below, shareholders may attend any general meeting of the company and, on a show of hands, every shareholder (or his/her representative) who is present at a general meeting has one vote on each resolution, and on a poll, every shareholder (whether an individual or a corporation) present in person or by proxy shall have one vote for every 25 pence of nominal share capital held. A resolution put to the vote at a general meeting is decided on a show of hands unless before, or on the declaration of the result of, a vote on a show of hands, a poll is demanded. A poll can be demanded by the chairman of the meeting, or by at least three shareholders (or their representatives) present in person and having the right to vote, or by any shareholders (or their representatives) present in person having at least 10% of the total voting rights of all shareholders, or by any shareholders (or their representatives) present in person holding ordinary shares on which an aggregate sum has been paid up of at least 10% of the total sum paid up on all ordinary shares. At this year's AGM voting will again be conducted on a poll, consistent with best practice.

Shareholders can declare a final dividend by passing an ordinary resolution but the amount of the dividend cannot exceed the amount recommended by the board. The board can pay interim dividends on any class of shares of the amounts and on the dates and for the periods they decide. In all cases the distributable profits of the company must be sufficient to justify the payment of the relevant dividend.

The board may, if authorised by an ordinary resolution of the shareholders, offer any shareholder the right to elect to receive new ordinary shares, which will be credited as fully paid, instead of their cash dividend.

Any dividend which has not been claimed for 12 years after it became due for payment will be forfeited and will then belong to the company, unless the directors decide otherwise.

If the company is wound up, the liquidator can, with the sanction of a special resolution passed by the shareholders, divide among the shareholders all or any part of the assets of the company and he/she can value assets and determine how the division shall be carried out as between the shareholders or different classes of shareholders. The liquidator can also, with the same sanction, transfer the whole or any part of the assets to trustees upon such trusts for the benefit of the shareholders.

### Voting at general meetings

Any form of proxy sent by the shareholders to the company in relation to any general meeting must be delivered to the company (via its registrars), whether in written or electronic form, not less than 48 hours before the time appointed for holding the meeting or adjourned meeting at which the person named in the appointment proposes to vote.

The board may decide that a shareholder is not entitled to attend or vote either personally or by proxy at a general meeting or to exercise any other right conferred by being a shareholder if he/she or any person with an interest in shares has been sent a notice under section 793 of the Act (which confers upon public companies the power to require information with respect to interests in their voting shares) and he/she or any interested person failed to supply the company with the information requested within 14 days after delivery of that notice. The board may also decide, where the relevant shareholding comprises at least 0.25% of the nominal value of the issued shares of that class, that no dividend is payable in respect of those default shares and that no transfer of any default shares shall be registered.

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## Additional shareholder information continued

Pearson operates an employee benefit trust to hold shares, pending employees becoming entitled to them under the company's employee share plans. There were 6,704,505 shares held as at 31 December 2015. The trust has an independent trustee which has full discretion in relation to the voting of such shares. A dividend waiver operates on the shares held in the trust.

Pearson also operates two nominee shareholding arrangements which hold shares on behalf of employees. There were 2,871,174 shares held in the Sharestore account and 309,841 shares held in the Global Nominee account as at 31 December 2015. The beneficial owners of shares held in Sharestore are invited to submit voting instructions online at [www.shareview.co.uk](http://www.shareview.co.uk) and Global Nominee participants are invited to submit voting instructions by e-mail to [nominee@equiniti.com](mailto:nominee@equiniti.com). If no instructions are given by the beneficial owner by the date specified, the trustees holding these shares will not exercise the voting rights.

**Transfer of shares**

The board may refuse to register a transfer of a certificated share which is not fully paid, provided that the refusal does not prevent dealings in shares in the company from taking place on an open and proper basis. The board may also refuse to register a transfer of a certificated share unless (i) the instrument of transfer is lodged, duly stamped (if stampable), at the registered office of the company or any other place decided by the board, and is accompanied by the certificate for the share to which it relates and such other evidence as the board may reasonably require to show the right of the transferor to make the transfer; (ii) it is in respect of only one class of shares, and (iii) it is in favour of not more than four transferees.

Transfers of uncertificated shares must be carried out using CREST and the board can refuse to register a transfer of an uncertificated share in accordance with the regulations governing the operation of CREST.

**Variation of rights**

If at any time the capital of the company is divided into different classes of shares, the special rights attaching to any class may be varied or revoked either

- (i) with the written consent of the holders of at least 75% in nominal value of the issued shares of the relevant class or
- (ii) with the sanction of a special resolution passed at a separate general meeting of the holders of the shares of the relevant class.

Without prejudice to any special rights previously conferred on the holders of any existing shares or class of shares, any share may be issued with such preferred, deferred, or other special rights, or such restrictions, whether in regard to dividend, voting, return of capital or otherwise as the company may from time to time by ordinary resolution determine.

**Appointment and replacement of directors**

The Articles contain the following provisions in relation to directors:

Directors shall be no less than two in number. Directors may be appointed by the company by ordinary resolution or by the board. A director appointed by the board shall hold office only until the next AGM and shall then be eligible for reappointment, but shall not be taken into account in determining the directors or the number of directors who are to retire by rotation at that meeting. The board may from time to time appoint one or more directors to hold executive office with the company for such period (subject to the provisions of the Act) and upon such terms as the board may decide and may revoke or terminate any appointment so made.

The Articles provide that, at every AGM of the company, at least one-third of the directors shall retire by rotation (or, if their number is not a multiple of three, the number nearest to one-third). The first directors to retire by rotation shall be those who wish to retire and not offer themselves for re-election. Any further directors so to retire shall be those of the other directors subject to retirement by rotation who have been longest in office since they were last re-elected but, as between persons who became or were last re-elected on the same day, those to retire shall (unless they otherwise agree among themselves) be determined by lot. In addition, any director who would not otherwise be required to retire shall retire by rotation at the third AGM after they were last re-elected.

Notwithstanding the provisions of the Articles, the board has resolved that all directors should offer themselves for re-election annually, in accordance with the Code.

The company may by ordinary resolution remove any director before the expiration of his/her term of office. In addition, the board may terminate an agreement or arrangement with any director for the provision of his/her services to the company.

#### **Powers of the directors**

Subject to the company's Articles, the Act and any directions given by special resolution, the business of the company will be managed by the board who may exercise all the powers of the company, including powers relating to the issue and/or buying back of shares by the company (subject to any statutory restrictions or restrictions imposed by shareholders in general meeting).

#### **Significant agreements**

The following significant agreements contain provisions entitling the counterparties to exercise termination or other rights in the event of a change of control of the company.

Under the \$1,750,000,000 revolving credit facility agreement dated August 2014 which matures in August 2020 between, amongst others, the company, Barclays Bank plc (Agent) and the banks and financial institutions named therein as lenders (the Facility), any such bank may, upon a change of control of the company, require its outstanding advances, together with accrued interest and any other amounts payable in respect of such Facility, and its commitments, to be cancelled, each within 60 days of notification to the banks by the Agent. For these purposes, a 'change of control' occurs if the company becomes a subsidiary of any other company or one or more persons acting either individually or in concert, obtains control (as defined in section 1124 of the Corporation Tax Act 2010) of the company.

Shares acquired through the company's employee share plans rank *pari passu* with shares in issue and have no special rights. For legal and practical reasons, the rules of these plans set out the consequences of a change of control of the company.

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# Independent auditors' report to the members of Pearson plc

## Report on the financial statements

### Our opinion

#### In our opinion

- › Pearson plc's consolidated financial statements and company financial statements (the 'financial statements') give a true and fair view of the state of the Group's and of the company's affairs as at 31 December 2015 and of the Group's profit and the Group's and the company's cash flows for the year then ended,
- › The consolidated financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union,
- › The company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006, and
- › The financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the consolidated financial statements, Article 4 of the IAS Regulation

### Separate opinion in relation to IFRSs as issued by the IASB

As explained in note 1 to the financial statements, the Group, in addition to applying IFRSs as adopted by the European Union, has also applied IFRSs as issued by the International Accounting Standards Board (IASB)

### Our audit approach Overview

IMAGE REMOVED

*In our opinion, the consolidated financial statements comply with IFRSs as issued by the IASB*

### What we have audited

The financial statements, included within the annual report and accounts (the 'annual report'), comprise

- › The consolidated and company balance sheets as at 31 December 2015,
- › The consolidated income statement and consolidated statement of comprehensive income for the year then ended,
- › The consolidated and company cash flow statements and statements of changes in equity for the year then ended, and
- › The notes to the financial statements, which include a summary of significant accounting policies and other explanatory information

Certain required disclosures have been presented elsewhere in the annual report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and IFRSs as adopted by the European Union and, as regards the company financial statements, as applied in accordance with the provisions of the Companies Act 2006

› Overall Group materiality £27m, which represents 4% of adjusted profit before tax as disclosed in note 8 to the financial statements. Refer to page 130 for further details

› We conducted work in five key territories: US, UK, Brazil, China and South Africa. In addition we obtained an audit opinion on the financial information reported by the associate Penguin Random House (PRH)

› The territories where we conducted audit procedures, together with work performed at corporate functions, shared service centres and consolidated Group level, accounted for approximately 68% of the Group's revenue, 104% of the Group's loss profit before tax, and 76% of the Group's adjusted profit before tax

› We focused on

- Revenue recognition including risk of fraud
- Carrying value of goodwill and intangible assets
- Major transactions
- Provision for uncertain tax liabilities
- Returns provisions
- Recoverability of pre-publication assets

**The scope of our audit and our areas of focus**

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK & Ireland))

We designed our audit by determining materiality and assessing the risks of material misstatement in the consolidated and company financial statements. In particular, we looked at where management made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by management that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as areas of focus in the table below. We have also set out how we tailored our audit to address these specific areas. In order to provide an opinion on the consolidated and company financial statements as a whole, any comments we make on the results of our procedures should be read in this context. For each area of focus below, to the extent relevant, we evaluated the design and tested the operating effectiveness of key internal controls over financial reporting set in place by management, including testing the operation of IT systems from which financial information is generated. Each of the areas of focus below are also referred to in the audit committee report on pages 86 and 87 and in the accounting policies on pages 140 and 147. This is not a complete list of all risks identified by our audit.

**Area of focus****Revenue recognition including risk of fraud**

Refer to note 1 to the consolidated financial statements

There are two types of complex contracts that require significant judgements and estimates, which could be subject to either accidental errors or deliberate fraud:

- › Multiple element arrangements, such as the sale of physical textbooks accompanied by digital content or supplementary workbooks, where revenue is recognised for each element as if it were an individual contractual arrangement requiring the estimation of its relative fair value, and
- › Certain long-term contracts that span year end, where revenue is recognised using estimated percentage of completion based on costs. These include contracts to design, develop and deliver testing and accreditation and contracts to secure students and support the online delivery of their teaching.

These complex contracts generate material deferred revenue and accrued income balances and are areas where misstatements in the underlying assumptions or estimation calculations could have a material effect on the financial statements.

In addition there are material shipments towards the period end from major distribution locations giving rise to the potential risk of a cut-off error.

**How our audit addressed the area of focus**

Where books are sold together with workbooks delivered later or companion digital materials available online we assessed the basis for allocation of the purchase price between each element and then tested the detailed calculations supporting these revenue deferrals. We found the revenue deferrals to be based on reasonable estimates of the relative fair value of each element and the methods used to calculate the deferrals properly calculated and consistently applied. For a selection of the larger, more judgemental and more recent long-term contracts, covering both testing activities and online delivery of teaching, we read the contracts and assessed the accounting methodologies being applied to calculate the proportion of revenue being recognised. We also tested costs incurred to date and management's estimates of forecast costs and revenues by reference to historical experience and current contract status, including examining correspondence where contracts are experiencing disputes.

Our testing showed that revenue recognition practices are in accordance with Group policies and related accounting standards with appropriate methods for calculating the revenue recognised. See our work performed over the returns provisions which includes our work over the risk of cut-off.

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## Independent auditors' report to the members of Pearson plc continued

Area of focus	How our audit addressed the area of focus
<p><b>Carrying values of goodwill and intangible assets</b></p> <p>Refer to note 11 to the consolidated financial statements</p> <p>The Group has £4,134m of goodwill and £1,030m of other intangible assets including software, acquired customer lists, contracts and relationships, acquired trademarks and brands and acquired publishing rights at 31 December 2015</p> <p>During the year, the Group recognised an £826m goodwill impairment charge across six aggregated cash generating units (CGUs): North America (£282m), Brazil (£269m), China (£181m), South Africa (£48m), Other Growth (£9m), and Core (£37m). In addition performance in specific businesses also resulted in a £23m Intangibles impairment charge. The total impairment charge from these items is £849m</p> <p>The carrying values of goodwill and intangible assets are dependent on future cash flows of the underlying CGUs and there is risk that if these cash flows do not meet management's expectations the assets will be impaired. This risk increases in periods when the Group's trading performance and projections do not meet prior expectations, such as in 2015</p> <p>The impairment reviews performed by management contain a number of significant judgements and estimates including CGU identification, operating profit forecasts, cash conversion, perpetuity growth rates and discount rates. Changes in these assumptions can result in materially different impairment charges or available headroom</p>	<p>We obtained management's goodwill impairment model and tested and agreed the reasonableness of key assumptions including CGU identification, operating profit forecasts, perpetuity growth rates and discount rates. We tested the mathematical integrity of the forecasts and carrying values in management's impairment model and confirmed that management's estimate of each CGU's recoverable amount is appropriately based on the higher of fair value less cost of disposal and value in use</p> <p>We agreed the forecast cash flows to board-approved budgets and market communications, assessed how these budgets are compiled and understood key judgements and estimates within them, including short-term growth rates, cost allocations and the inclusion of restructuring costs and benefits in a fair value less cost of disposal model</p> <p>We compared short and long-term growth rates including cash conversion, to historical trends and expectations. We also considered the accuracy of prior period forecasts</p> <p>We used valuations specialists to assess the perpetuity growth rate and discount rate for each CGU by comparison to third party information, past performance, the Group's cost of capital and relevant risk factors</p> <p>We performed our own sensitivity analyses to understand the impact of reasonable changes in the key assumptions. We agree with management's decision to provide additional disclosures in note 11 of the financial statements given that reasonably possible changes in the assumptions could materially impact the impairment charges or available headroom</p> <p>We checked for additional impairment triggers by reading board minutes, holding regular discussions with Group and local management, and examining the performance of recently acquired businesses to identify underperforming operations. We did not identify any further impairments</p> <p>As a result of our work we determined that the impairment charge recognised in 2015 was reasonably calculated and recorded at materially appropriate exchange rates. For those CGUs where management determined that no impairment charge was required and that no additional sensitivity disclosures should be given, we consider these judgements to be well supported by reasonable assumptions that would require significant downside changes before an impairment charge was necessary</p>
<p><b>Major transactions</b></p> <p>Refer to note 31 to the consolidated financial statements</p> <p>In July 2015 Pearson completed the sale of PowerSchool to Vista Equity Partners for cash consideration of £222m, resulting in a net pre-tax impact of £30m within continuing operations (after related write downs of £70m)</p> <p>In October 2015 Pearson completed the first tranche of the sale of its 50% stake in The Economist Group to Exor S.p.A. and to The Economist Group itself for cash consideration of £377m and remeasurement of the retained 11% investment of £92m, resulting in a pre-tax gain on disposal of £473m presented in discontinued operations. The Group's remaining 11% investment does not constitute significant influence so is being held as an available for sale investment at fair value until the second tranche completes</p> <p>In November 2015 Pearson completed the sale of the Financial Times Group (FT) to Nikkel Inc. for cash consideration of £858m, resulting in a pre-tax gain on disposal of £711m presented in discontinued operations</p> <p>These amounts are highly material and include judgements in areas such as the write downs related to PowerSchool and the retained investment in The Economist Group</p>	<p>We obtained the sales documents and related contracts and agreed the elements of the gain calculations to them</p> <p>We agreed the cash consideration to bank statements, any retained investment or assets to the contracts and verified the underlying carrying value before disposal to financial records. We agreed the remeasurement of the retained investment of the Economist to fair value implied by the contract. We reperformed the calculations for mathematical accuracy, considered the appropriateness of the disposal costs and related write downs and vouched them to supporting evidence. We assessed the presentation of each disposed business (as continuing or discontinued) by reference to its size and nature. We also considered the related tax judgements and recoverability of linked pre-publication assets</p> <p>No material misstatements were identified by our testing. We were satisfied that the presentation of each gain, and the related write downs, was supportable and we found that appropriate disclosures were included in the annual report</p>

## Area of focus

## How our audit addressed the area of focus

## Provision for uncertain tax liabilities

Refer to notes 7 and 13 to the consolidated financial statements  
The Group is subject to several tax regimes due to the geographical diversity of its businesses

Management is required to exercise significant judgement in determining the appropriate amount to provide in respect of potential tax exposures and uncertain tax provisions. The most significant of these relate to US tax

Changes in assumptions about the views that might be taken by tax authorities can materially impact the level of provisions recorded in the financial statements and there are significant judgements in estimating the amount of any provision required

We engaged with our tax experts and obtained an understanding of the Group's tax strategy to identify tax risks relating to business and legislative developments. To assess the adequacy of the Group's tax provisions we first recalculated the valuation of tax provisions and determined whether the treatments adopted were in line with the Group's tax policies and had been applied consistently

We then evaluated the key underlying assumptions, particularly in the US and in territories with new cross-border tax structures. In doing this we considered the status of recent and current tax authority audits and enquiries, the outcome of previous claims judgemental positions taken in tax returns and current year estimates including those arising from significant disposals, and developments in the tax environment. We also evaluated the consistency of management's approach to establishing or changing provision estimates

We were satisfied that management's provision estimates for uncertain tax positions were consistent with our own assessment of the related risks and correspondence with the relevant tax authorities

## Returns provisions

Refer to note 22 to the consolidated financial statements

There are material judgemental provisions for anticipated book returns on the balance sheet as at 31 December 2015, particularly in US Higher Education

As the Group transitions from print to digital the returns profile will change with a corresponding impact on returns provisions

We performed testing over returns provisions in a number of locations, including US Higher Education

We tested the calculation of the provisions, assessing judgements for reasonableness against historical experience and the impact on returns of the ongoing business transition from print to digital

We also performed detailed testing of shipment and returns provisioning. This included checking cut off at year end and evaluating whether any changes in shipping volumes around year end might increase the risk of returns. No misstatements were identified

We evaluated changes in estimates to check they were not indicators of management bias. We found the estimates used by management in the determination of the returns provisions to appropriately reflect both past experience and changes in the business

## Recoverability of pre-publication assets

Refer to note 20 to the consolidated financial statements

The Group has £841m of pre-publication assets at 31 December 2015. Pre-publication assets represent direct costs incurred in the development of education platforms, programmes and titles prior to their public release

The PowerSchool disposal caused management to assess the carrying value of a series of pre-publication and platform investments and consequently record a write down of £70m.

Judgement is required to assess the recoverability of the carrying value of these assets, this is further complicated by the transition to digital as the Group invests in new, less proven, inter-linked digital content and platforms

We first assessed the appropriateness of capitalisation policies and then selected a sample of costs deferred to the balance sheet as pre-publication assets to test their magnitude and appropriateness for capitalisation

We then assessed the amortisation profiles of pre-publication assets against cash flows to test that the existing amortisation profiles remained appropriate in light of the transition towards digital products

We challenged the carrying value of certain pre-publication assets where products are yet to be launched, are less proven, or where sales are lower than originally anticipated. We assessed forecast cash flows against historical experience and obtained supporting evidence for management's explanations. We compared short and long term growth rates to historical trends and expectations

We challenged the life of the assets compared to similar Pearson products and found the Group's policies to be appropriate and consistently applied. While the carrying value of some assets depends on considerable future sales growth, overall we considered the year end carrying values to be reasonable

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## Independent auditors' report to the members of Pearson plc continued

**How we tailored our audit scope**

We tailored our audit scope to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the geographic structure of the Group, the accounting processes and controls, and the industry in which the Group operates

The Group is organised into three reportable segments, being North America, Core and Growth, plus the associate investment in associate Penguin Random House. Each segment comprises a number of reporting units. The consolidated financial statements comprise these reporting units plus the Group's centralised functions.

In establishing the overall approach to the Group audit, we determined the type of work that needed to be performed at the reporting units by us, as the Group engagement team, or component auditors within PwC UK and from other PwC network firms operating under our instruction. Where the work was performed by component auditors, we determined the level of involvement we needed to have in the audit work at those reporting units to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the consolidated financial statements as a whole.

During the year members of the Group engagement team visited each of the US, Brazilian, Chinese and South African component audit teams, held a planning meeting attended by partners from the Group engagement team and our UK and US component teams, and had regular dialogue with component teams throughout the year.

We identified two reporting units in the US and UK that required an audit of their complete financial information due to their financial significance, plus a further 13 reporting units in the US, UK, Brazil, China and South Africa that required either an audit or specified procedures on certain transactions and balances. We also obtained an audit opinion from PwC Germany on the financial information of the associate Penguin Random House. The Group consolidation, financial statement disclosures and corporate functions were audited by the Group engagement team. This included our work over derivative financial instruments, hedge accounting, goodwill and intangible assets impairment reviews, litigation, pensions and share-based payments.

The reporting units where we performed audit work, together with work performed at corporate functions, shared service centres and consolidated Group level, accounted for approximately 68% of the Group's revenue, 104% of the Group's loss before tax and 76% of the Group's adjusted profit before tax. This provided the evidence we needed for our opinion on the consolidated financial statements taken as a whole.

**Materiality** The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

<b>Overall Group materiality</b>	£27m (2014: 26m)
<b>How we determined it</b>	4% of adjusted profit before tax of £677m
<b>Rationale for benchmark applied</b>	Note 8 of the financial statements explains that the Group's principal measure of performance is adjusted operating profit (£723m), which excludes one-off gains and losses and acquired intangible asset amortisation. In order to present results from operating activities on a consistent basis, from adjusted operating profit we deducted net finance costs of £46m (see note 8) because these mainly reflect recurring finance charges. To the resulting adjusted profit before tax we then applied 4% (rather than the usual 5%) as our materiality calculation was based on an adjusted measure.
<b>Component materiality</b>	For each component in our audit scope, we allocated a materiality that is less than our overall Group materiality. The range of materiality allocated across components was between £3m and £24m.

We agreed with the audit committee that we would report to them misstatements identified during our audit above £2m (2014: £2m) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons

**Going concern** Under the Listing Rules we are required to review the directors' statement, set out on page 118, in relation to going concern. We have nothing to report having performed our review

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to the directors' statement about whether they considered it appropriate to adopt the going concern basis in preparing the financial statements. We have nothing material to add or to draw attention to

#### Other required reporting

#### Consistency of other information Companies Act 2006 opinions

In our opinion

- › The information given in the strategic report and the report of the directors for the financial year for which the financial statements are prepared is consistent with the financial statements, and
- › The information given in the Governance Report set out on pages 69 to 93 with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements

#### ISAs (UK & Ireland) reporting

Under ISAs (UK & Ireland) we are required to report to you if, in our opinion

- |  |  |
|--|--|
| <ul style="list-style-type: none"> <li>› Information in the annual report is               <ul style="list-style-type: none"> <li>– materially inconsistent with the information in the audited financial statements,</li> <li>– apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group and company acquired in the course of performing our audit, or</li> <li>– otherwise misleading</li> </ul> </li> </ul>   | <p>We have no exceptions to report</p> |
| <ul style="list-style-type: none"> <li>› The explanation given by the directors on page 119, in accordance with provision C 1.1 of the UK Corporate Governance Code (the 'Code'), as to why the annual report does not include a statement that they consider the annual report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the Group's and company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Group and company acquired in the course of performing our audit</li> </ul> | <p>We have no exceptions to report</p> |
| <ul style="list-style-type: none"> <li>› The section of the annual report on pages 82 to 87, as required by provision C 3.8 of the Code, describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee</li> </ul>  | <p>We have no exceptions to report</p> |

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## Independent auditors' report to the members of Pearson plc continued

**The directors' assessment of the prospects of the Group and of the principal risks that would threaten the solvency or liquidity of the Group**

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to

› The directors' confirmation on pages 40 and 118 of the annual report, in accordance with provision C 2.1 of the Code, that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity	We have nothing material to add or to draw attention to
› The disclosures in the annual report that describe those risks and explain how they are being managed or mitigated	We have nothing material to add or to draw attention to
› The directors' explanation on pages 40 and 118 of the annual report, in accordance with provision C 2.2 of the Code, as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions	We have nothing material to add or to draw attention to

Under the Listing Rules we are required to review the directors' statement that they have carried out a robust assessment of the principal risks facing the Group and the directors' statement in relation to the longer-term viability of the Group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the directors' process supporting their statements, checking that the statements are in alignment with the relevant provisions of the Code, and considering whether the statements are consistent with the knowledge acquired by us in the course of performing our audit. We have nothing to report having performed our review.

**Adequacy of accounting records and information and explanations received**

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

- › We have not received all the information and explanations we require for our audit, or
- › Adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us, or
- › The company financial statements and the part of the directors' remuneration report to be audited are not in agreement with the accounting records and returns

We have no exceptions to report arising from this responsibility

**Directors' remuneration**

**Directors' remuneration report - Companies Act 2006 opinion** In our opinion, the part of the directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006

**Other Companies Act 2006 reporting** Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

**Corporate governance statement**

Under the Companies Act 2006 we are required to report to you if, in our opinion, a corporate governance statement has not been prepared by the company. We have no exceptions to report arising from this responsibility.

Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to ten further provisions of the Code. We have nothing to report having performed our review.

### Responsibilities for the financial statements and the audit

#### Our responsibilities and those of the directors

As explained more fully in the statement of directors' responsibilities set out on page 120, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

#### What an audit of financial statements involves

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- › Whether the accounting policies are appropriate to the Group's and the company's circumstances and have been consistently applied and adequately disclosed,
- › The reasonableness of significant accounting estimates made by the directors, and
- › The overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies, we consider the implications for our report.

*Stuart Newman*  
Stuart Newman  
(Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London

4 March 2016

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# Consolidated income statement

Year ended 31 December 2015

All figures in £ millions	Notes	2015	2014 restated
Sales	2	4,468	4,540
Cost of goods sold	4	(1,981)	(2,021)
<b>Gross profit</b>		<b>2,487</b>	<b>2,519</b>
Operating expenses	4	(2,094)	(2,125)
Impairment of intangible assets	11	(849)	(77)
Share of results of joint ventures and associates	12	52	31
<b>Operating (loss)/profit</b>	<b>2</b>	<b>(404)</b>	<b>348</b>
Finance costs	6	(100)	(140)
Finance income	6	71	47
<b>(Loss)/profit before tax</b>		<b>(433)</b>	<b>255</b>
Income tax	7	81	(56)
<b>(Loss)/profit for the year from continuing operations</b>		<b>(352)</b>	<b>199</b>
Profit for the year from discontinued operations	3	1,175	271
<b>Profit for the year</b>		<b>823</b>	<b>470</b>
<b>Attributable to</b>			
Equity holders of the company		823	471
Non-controlling interest		-	(1)
<b>Earnings per share for profit from continuing and discontinued operations attributable to equity holders of the company during the year (expressed in pence per share)</b>			
- basic	8	101 2p	58 1p
- diluted	8	101 2p	58 0p
<b>(Loss)/earnings per share for (loss)/profit from continuing operations attributable to equity holders of the company during the year (expressed in pence per share)</b>			
- basic	8	(43 3)p	24 7p
- diluted	8	(43 3)p	24 6p

# Consolidated statement of comprehensive income

Year ended 31 December 2015

All figures in £ millions	Notes	2015	2014
Profit for the year		823	470
<b>Items that may be reclassified to the income statement</b>			
Net exchange differences on translation of foreign operations – Group		(85)	150
Net exchange differences on translation of foreign operations – associates		16	25
Currency translation adjustment disposed – Group		(10)	(2)
Attributable tax	7	5	(6)
<b>Items that are not reclassified to the income statement</b>			
Remeasurement of retirement benefit obligations – Group	25	110	23
Remeasurement of retirement benefit obligations – associates		8	(15)
Attributable tax	7	(24)	(1)
Other comprehensive income for the year		20	174
Total comprehensive income for the year		843	644
<b>Attributable to</b>			
Equity holders of the company		845	645
Non-controlling interest		(2)	(1)

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# Consolidated balance sheet

As at 31 December 2015

All figures in £ millions	Notes	2015	2014
<b>Assets</b>			
<b>Non-current assets</b>			
Property, plant and equipment	10	320	334
Intangible assets	11	5,164	6,310
Investments in joint ventures and associates	12	1,103	1,118
Deferred income tax assets	13	276	295
Financial assets – derivative financial instruments	16	78	90
Retirement benefit assets	25	337	190
Other financial assets	15	143	54
Trade and other receivables	22	115	82
		7,536	8,473
<b>Current assets</b>			
Intangible assets – pre publication	20	841	820
Inventories	21	211	224
Trade and other receivables	22	1,284	1,310
Financial assets – derivative financial instruments	16	32	24
Financial assets – marketable securities	14	28	16
Cash and cash equivalents (excluding overdrafts)	17	1,703	530
		4,099	2,924
<b>Total assets</b>		<b>11,635</b>	<b>11,397</b>
<b>Liabilities</b>			
<b>Non-current liabilities</b>			
Financial liabilities – borrowings	18	(2,048)	(1,883)
Financial liabilities – derivative financial instruments	16	(136)	(73)
Deferred income tax liabilities	13	(560)	(714)
Retirement benefit obligations	25	(139)	(163)
Provisions for other liabilities and charges	23	(71)	(82)
Other liabilities	24	(356)	(310)
		(3,310)	(3,225)

# Consolidated balance sheet continued

As at 31 December 2015

All figures in £ millions	Notes	2015	2014
<b>Current liabilities</b>			
Trade and other liabilities	24	(1,390)	(1,601)
Financial liabilities – borrowings	18	(282)	(342)
Financial liabilities – derivative financial instruments	16	(29)	(1)
Current income tax liabilities		(164)	(190)
Provisions for other liabilities and charges	23	(42)	(53)
		(1,907)	(2,187)
<b>Total liabilities</b>		<b>(5,217)</b>	<b>(5,412)</b>
<b>Net assets</b>		<b>6,418</b>	<b>5,985</b>
<b>Equity</b>			
Share capital	27	205	205
Share premium	27	2,590	2,579
Treasury shares	28	(72)	(75)
Translation reserve		(7)	70
Retained earnings		3,698	3,200
<b>Total equity attributable to equity holders of the company</b>		<b>6,414</b>	<b>5,979</b>
Non-controlling interest		4	6
<b>Total equity</b>		<b>6,418</b>	<b>5,985</b>

These financial statements have been approved for issue by the board of directors on 4 March 2016 and signed on its behalf by

Coram Williams  
Chief financial officer



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# Consolidated statement of changes in equity

Year ended 31 December 2015

All figures in £ millions	Equity attributable to equity holders of the company						Non-controlling interest	Total equity
	Share capital	Share premium	Treasury shares	Translation reserve	Retained earnings	Total		
At 1 January 2015	205	2,579	(75)	70	3,200	5,979	6	5,985
Profit for the year	-	-	-	-	823	823	-	823
Other comprehensive income	-	-	-	(77)	99	22	(2)	20
<b>Total comprehensive income</b>	-	-	-	(77)	922	845	(2)	843
Equity-settled transactions	-	-	-	-	26	26	-	26
Tax on equity-settled transactions	-	-	-	-	(1)	(1)	-	(1)
Issue of ordinary shares under share option schemes	-	11	-	-	-	11	-	11
Purchase of treasury shares	-	-	(23)	-	-	(23)	-	(23)
Release of treasury shares	-	-	26	-	(26)	-	-	-
Changes in non-controlling interest	-	-	-	-	-	-	-	-
Dividends	-	-	-	-	(423)	(423)	-	(423)
<b>At 31 December 2015</b>	<b>205</b>	<b>2,590</b>	<b>(72)</b>	<b>(7)</b>	<b>3,698</b>	<b>6,414</b>	<b>4</b>	<b>6,418</b>

All figures in £ millions	Equity attributable to equity holders of the company						Non-controlling interest	Total equity
	Share capital	Share premium	Treasury shares	Translation reserve	Retained earnings	Total		
At 1 January 2014	205	2,568	(98)	(103)	3,128	5,700	6	5,706
Profit for the year	-	-	-	-	471	471	(1)	470
Other comprehensive income	-	-	-	173	1	174	-	174
<b>Total comprehensive income</b>	-	-	-	173	472	645	(1)	644
Equity-settled transactions	-	-	-	-	32	32	-	32
Tax on equity-settled transactions	-	-	-	-	(3)	(3)	-	(3)
Issue of ordinary shares under share option schemes	-	11	-	-	-	11	-	11
Purchase of treasury shares	-	-	(9)	-	-	(9)	-	(9)
Release of treasury shares	-	-	32	-	(32)	-	-	-
Changes in non-controlling interest	-	-	-	-	-	-	2	2
Dividends	-	-	-	-	(397)	(397)	(1)	(398)
<b>At 31 December 2014</b>	<b>205</b>	<b>2,579</b>	<b>(75)</b>	<b>70</b>	<b>3,200</b>	<b>5,979</b>	<b>6</b>	<b>5,985</b>

The translation reserve includes exchange differences arising from the translation of the net investment in foreign operations and of borrowings and other currency instruments designated as hedges of such investments. Changes in non-controlling interest in 2014 relate to the disposal of a non-controlling interest in a Chinese business.

# Consolidated cash flow statement

Year ended 31 December 2015

All figures in £ millions	Notes	2015	2014
<b>Cash flows from operating activities</b>			
Net cash generated from operations	32	518	704
Interest paid		(75)	(86)
Tax paid		(232)	(163)
<b>Net cash generated from operating activities</b>		<b>211</b>	<b>455</b>
<b>Cash flows from investing activities</b>			
Acquisition of subsidiaries, net of cash acquired	30	(9)	(448)
Acquisition of joint ventures and associates		(11)	(12)
Purchase of investments		(7)	(3)
Purchase of property, plant and equipment		(86)	(75)
Purchase of intangible assets		(161)	(107)
Disposal of subsidiaries, net of cash disposed	31	1,030	327
Proceeds from sale of associates		379	39
Proceeds from sale of investments		13	9
Proceeds from sale of property, plant and equipment	32	2	9
Proceeds from sale of intangible assets		1	2
Proceeds from sale of liquid resources		17	12
Loans repaid by/(advanced to) related parties		7	(10)
Loans advanced		-	(2)
Investment in liquid resources		(29)	(22)
Interest received		24	13
Dividends received from joint ventures and associates		162	120
<b>Net cash received from/(used in) investing activities</b>		<b>1,332</b>	<b>(148)</b>
<b>Cash flows from financing activities</b>			
Proceeds from issue of ordinary shares	27	11	11
Purchase of treasury shares	28	(23)	(9)
Proceeds from borrowings		372	404
Repayment of borrowings		(300)	(538)
Finance lease principal payments		(1)	(4)
Dividends paid to company's shareholders	9	(423)	(397)
Dividends paid to non-controlling interest		-	(1)
<b>Net cash used in financing activities</b>		<b>(364)</b>	<b>(534)</b>
Effects of exchange rate changes on cash and cash equivalents		(19)	(2)
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>1,160</b>	<b>(229)</b>
Cash and cash equivalents at beginning of year		511	740
<b>Cash and cash equivalents at end of year</b>	<b>17</b>	<b>1,671</b>	<b>511</b>

The consolidated cash flow statement includes discontinued operations (see note 3)

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# Notes to the consolidated financial statements

## General information

Pearson plc (the company), its subsidiaries and associates (together the Group) are international businesses covering educational courseware, assessments and services, and consumer publishing through its associate interest in Penguin Random House

The company is a public limited company incorporated and domiciled in England. The address of its registered office is 80 Strand, London WC2R 0RL

The company has its primary listing on the London Stock Exchange and is also listed on the New York Stock Exchange

These consolidated financial statements were approved for issue by the board of directors on 4 March 2016

## 1. Accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below

### a Basis of preparation

These consolidated financial statements have been prepared on the going concern basis and in accordance with International Financial Reporting Standards (IFRS) and IFRS Interpretations Committee interpretations as adopted by the European Union (EU) and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. In respect of the accounting standards applicable to the Group there is no difference between EU-adopted and IASB-adopted IFRS

These consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation of financial assets and liabilities (including derivative financial instruments) to fair value through profit or loss

The prior year financial statements have been restated to reflect the classification of FT Group as a discontinued operation

1 Interpretations and amendments to published standards effective 2015. The following amendments and interpretations were adopted in 2015

- › Amendments to IAS 19 'Employee Benefits - Defined Benefit Plans - Employee Contributions'
- › Amendments to IFRS 2 'Share based Payment Definition of vesting conditions'

› Amendments to IFRS 3 'Business Combinations Accounting for contingent consideration in a business combination and scope exemptions for joint ventures'

› Amendments to IFRS 8 'Operating Segments Aggregation of operating segments and reconciliation of segment assets to entity's assets'

› Amendments to IAS 24 'Related Party Disclosures Key management personnel'

› Amendments to IFRS 13 'Fair Value Measurement Short term receivables and payables'

The adoption of these new pronouncements from 1 January 2015 does not have a material impact on the consolidated financial statements

2 Standards, interpretations and amendments to published standards that are not yet effective. The Group has not early adopted the following new pronouncements that are not yet effective

IFRS 9 'Financial Instruments', effective for annual reporting periods beginning on or after 1 January 2018. The new standard details the requirements for the classification, measurement and recognition of financial assets and liabilities. The Group is yet to assess the full impact of IFRS 9

IFRS 15 'Revenue from Contracts with Customers', effective for annual reporting periods beginning on or after 1 January 2018. The new standard specifies how and when an entity will recognise revenue, and requires more detailed disclosure. Adoption of the new standard is likely to have an impact on the Group and management is currently assessing the impact.

IFRS 16 'Leases', effective for annual reporting periods beginning on or after 1 January 2019. The new standard details the requirements for the classification, measurement and recognition of lease arrangements. Adoption of the new standard is likely to have an impact on the Group and management is currently assessing the impact.

In June 2015 the IASB issued an exposure draft ED/2015/5 'Remeasurement on a Plan Amendment, Curtailment or Settlement/Availability of a Refund from a Defined Benefit Plan (Proposed Amendments to IAS 19 and IFRIC 14)'. Management are currently evaluating these proposals and although the proposals have not yet been finalised, it should be noted that the current draft, if adopted, may restrict the Group's ability to recognise a pension asset in respect of pension surpluses in its UK defined benefit pension plan.

## 1 Accounting policies continued

### a Basis of preparation continued

In addition, the current draft may require certain elements of committed minimum funding contributions to be recognised as a liability on the balance sheet

### 3 Critical accounting assumptions and judgements

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting assumptions. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas requiring a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are discussed in the relevant accounting policies under the following headings and in the notes to the accounts where appropriate

Consolidation Business combinations – classification of investments

Consolidation Business combinations – determination of fair values

Intangible assets Goodwill

Intangible assets Pre-publication assets

Taxation

Revenue recognition

Employee benefits Pensions

### b Consolidation

**1 Business combinations** The acquisition method of accounting is used to account for business combinations

The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred and the equity interest issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition related costs are expensed as incurred in the operating expenses line of the income statement

Identifiable assets and contingent assets acquired and identifiable liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The determination of fair values often requires significant judgements and the use of estimates, and, for material acquisitions, the fair value of the acquired intangible assets is determined by an independent valuer. The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition

date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill

See note 1e(1) for the accounting policy on goodwill. If this is less than the fair value of the net assets of the subsidiary acquired, in the case of a bargain purchase, the difference is recognised directly in the income statement

On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets

Management exercises judgement in determining the classification of its investments in its businesses, in line with the following

**2 Subsidiaries** Subsidiaries are entities over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases

**3 Transactions with non-controlling interests** Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions, that is, as transactions with the owners in their capacity as owners. Any surplus or deficit arising from disposals to a non-controlling interest is recorded in equity. For purchases from a non-controlling interest, the difference between consideration paid and the relevant share acquired of the carrying value of the subsidiary is recorded in equity

**4 Joint ventures and associates** Joint ventures are entities in which the Group holds an interest on a long-term basis and has rights to the net assets through contractually agreed sharing of control. Associates are entities over which the Group has significant influence but not the power to control the financial and operating policies, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in joint ventures and associates are accounted for by the equity method and are initially recognised at the fair value of consideration transferred

The Group's share of its joint ventures' and associates' post-acquisition profits or losses is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in reserves

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## Notes to the consolidated financial statements continued

**1 Accounting policies continued****b Consolidation continued**

The Group's share of its joint ventures' and associates' results is recognised as a component of operating profit as these operations form part of the core publishing business of the Group and are an integral part of existing wholly-owned businesses. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in a joint venture or associate equals or exceeds its interest in the joint venture or associate, the Group does not recognise further losses unless the Group has incurred obligations or made payments on behalf of the joint venture or associate.

5 Contribution of a subsidiary to an associate or joint venture. The gain or loss resulting from the contribution or sale of a subsidiary to an associate or a joint venture is recognised in full. Where such transactions do not involve cash consideration, significant judgements and estimates are used in determining the fair values of the consideration received.

**c Foreign currency translation**

1 Functional and presentation currency. Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The consolidated financial statements are presented in sterling, which is the company's functional and presentation currency.

2 Transactions and balances. Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying net investment hedges.

3 Group companies. The results and financial position of all Group companies that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- i) Assets and liabilities are translated at the closing rate at the date of the balance sheet.
- ii) Income and expenses are translated at average exchange rates.
- iii) All resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. The Group treats specific inter-company loan balances, which are not intended to be repaid in the foreseeable future, as part of its net investment. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

The principal overseas currency for the Group is the US dollar. The average rate for the year against sterling was \$1.53 (2014: \$1.65) and the year end rate was \$1.47 (2014: \$1.56).

**d Property, plant and equipment**

Property, plant and equipment are stated at historical cost less depreciation. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for intended use. Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost less their residual values over their estimated useful lives as follows:

Buildings (freehold)	20–50 years
Buildings (leasehold)	over the period of the lease
Plant and equipment	3–10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

The carrying value of an asset is written down to its recoverable amount if the carrying value of the asset is greater than its estimated recoverable amount.

**e Intangible assets**

1 Goodwill. For the acquisition of subsidiaries made on or after 1 January 2010, goodwill represents the excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired. For the acquisition of subsidiaries made from the date of transition to IFRS to 31 December 2009, goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets acquired. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisition of associates and joint ventures represents the excess of the cost of an acquisition over the fair value of the Group's share

## 1 Accounting policies continued

### e Intangible assets continued

of the net identifiable assets acquired. Goodwill on acquisitions of associates and joint ventures is included in investments in associates and joint ventures.

Goodwill is tested at least annually for impairment and carried at cost less accumulated impairment losses. An impairment loss is recognised to the extent that the carrying value of goodwill exceeds the recoverable amount. The recoverable amount is the higher of fair value less costs of disposal and value in use. These calculations require the use of estimates and significant management judgement. A description of the key assumptions and sensitivities is included in note 11. Goodwill is allocated to aggregated cash-generating units for the purpose of impairment testing. The allocation is made to those aggregated cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

IFRS 3 'Business Combinations' has not been applied retrospectively to business combinations before the date of transition to IFRS.

**2 Acquired software** Software separately acquired for internal use is capitalised at cost. Software acquired in material business combinations is capitalised at its fair value as determined by an independent valuer. Acquired software is amortised on a straight-line basis over its estimated useful life of between three and eight years.

**3 Internally developed software** Internal and external costs incurred during the preliminary stage of developing computer software for internal use are expensed as incurred. Internal and external costs incurred to develop computer software for internal use during the application development stage are capitalised if the Group expects economic benefits from the development. Capitalisation in the application development stage begins once the Group can reliably measure the expenditure attributable to the software development and has demonstrated its intention to complete and use the software. Internally developed software is amortised on a straight-line basis over its estimated useful life of between three and eight years.

**4 Acquired intangible assets** Acquired intangible assets include customer lists, contracts and relationships, trademarks and brands, publishing rights, content, technology and software rights. These assets are

capitalised on acquisition at cost and included in intangible assets. Intangible assets acquired in material business combinations are capitalised at their fair value as determined by an independent valuer. Intangible assets are amortised over their estimated useful lives of between two and 20 years, using an amortisation method that reflects the pattern of their consumption.

**5 Pre-publication assets** Pre-publication assets represent direct costs incurred in the development of educational programmes and titles prior to their publication. These costs are recognised as current intangible assets where the title will generate probable future economic benefits and costs can be measured reliably. Pre-publication assets are amortised upon publication of the title over estimated economic lives of five years or less, being an estimate of the expected operating life cycle of the title, with a higher proportion of the amortisation taken in the earlier years.

The investment in pre-publication assets has been disclosed as part of cash generated from operations in the cash flow statement (see note 32).

The assessment of the recoverability of pre-publication assets and the determination of the amortisation profile involve a significant degree of judgement based on historical trends and management estimation of future potential sales. An incorrect amortisation profile could result in excess amounts being carried forward as intangible assets that would otherwise have been written off to the income statement in an earlier period.

Reviews are performed regularly to estimate recoverability of pre-publication assets. The carrying amount of pre-publication assets is set out in note 20.

### f Other financial assets

Other financial assets, designated as available for sale investments, are non-derivative financial assets measured at estimated fair value. Changes in the fair value are recorded in equity in the fair value reserve. On the subsequent disposal of the asset, the net fair value gains or losses are taken to the income statement.

### g Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the first in first out (FIFO) method. The cost of finished goods and work in progress comprises raw materials, direct labour, other direct costs and related production overheads. Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs necessary to make the sale. Provisions are made for slow moving and obsolete stock.

## Notes to the consolidated financial statements continued

**1 Accounting policies continued****h Royalty advances**

Advances of royalties to authors are included within trade and other receivables when the advance is paid less any provision required to adjust the advance to its net realisable value. The realisable value of royalty advances relies on a degree of management judgement in determining the profitability of individual author contracts. If the estimated realisable value of author contracts is overstated, this will have an adverse effect on operating profits as these excess amounts will be written off.

The recoverability of royalty advances is based upon an annual detailed management review of the age of the advance, the future sales projections for new authors and prior sales history of repeat authors.

The royalty advance is expensed at the contracted or effective royalty rate as the related revenues are earned. Royalty advances which will be consumed within one year are held in current assets. Royalty advances which will be consumed after one year are held in non-current assets.

**i. Cash and cash equivalents**

Cash and cash equivalents in the cash flow statement include cash in hand, deposits held on call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are included in borrowings in current liabilities in the balance sheet.

Short-term deposits and marketable securities with maturities of greater than three months do not qualify as cash and cash equivalents. Movements on these financial instruments are classified as cash flows from financing activities in the cash flow statement where these amounts are used to offset the borrowings of the Group or as cash flows from investing activities where these amounts are held to generate an investment return.

**j Share capital**

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Where any Group company purchases the company's equity share capital (treasury shares) the consideration paid, including any directly attributable incremental costs, net of income taxes, is deducted from equity attributable to the company's equity holders until the

shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable transaction costs and the related income tax effects, is included in equity attributable to the company's equity holders.

**k Borrowings**

Borrowings are recognised initially at fair value, which is proceeds received net of transaction costs incurred. Borrowings are subsequently stated at amortised cost with any difference between the proceeds (net of transaction costs) and the redemption value being recognised in the income statement over the period of the borrowings using the effective interest method. Accrued interest is included as part of borrowings. Where a debt instrument is in a fair value hedging relationship, an adjustment is made to its carrying value in the income statement to reflect the hedged risk. Interest on borrowings is expensed in the income statement as incurred.

**l Derivative financial instruments**

Derivatives are recognised at fair value and remeasured at each balance sheet date. The fair value of derivatives is determined by using market data and the use of established estimation techniques such as discounted cash flow and option valuation models. The Group designates certain of the derivative instruments within its portfolio to be hedges of the fair value of its bonds (fair value hedges) or hedges of net investments in foreign operations (net investment hedges).

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

The effective portion of changes in the fair value of derivatives that are designated and qualify as net investment hedges are recognised in other comprehensive income. Gains and losses accumulated in equity are included in the income statement when the corresponding foreign operation is disposed of. Gains or losses relating to the ineffective portion are recognised immediately in finance income or finance costs in the income statement.

Certain derivatives do not qualify or are not designated as hedging instruments. Such derivatives are classified at fair value and any movement in their fair value is recognised immediately in finance income or finance costs in the income statement.

## 1 Accounting policies continued

### m Taxation

Current tax is recognised on the amounts expected to be paid or recovered under the tax rates and laws that have been enacted or substantively enacted at the balance sheet date

Deferred income tax is provided, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts. Deferred income tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred income tax liability is settled

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised

Deferred income tax is provided in respect of the undistributed earnings of subsidiaries other than where it is intended that those undistributed earnings will not be remitted in the foreseeable future

Current and deferred tax are recognised in the income statement, except when the tax relates to items charged or credited directly to equity or other comprehensive income, in which case the tax is also recognised in equity or other comprehensive income

The Group is subject to income taxes in numerous jurisdictions. Significant judgement is required in determining the estimates in relation to the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made

Deferred tax assets and liabilities require management judgement in determining the amounts to be recognised. In particular, significant judgement is used when assessing the extent to which deferred tax assets should be recognised with consideration given to the timing and level of future taxable income together with any future tax planning strategies

### n Employee benefits

**1 Pensions** The retirement benefit asset and obligation recognised in the balance sheet represents the net of the present value of the defined benefit obligation and the fair value of plan assets at the balance sheet date. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting estimated future cash flows using yields on high quality corporate bonds which have terms to maturity approximating the terms of the related liability

When the calculation results in a potential asset, the recognition of that asset is limited to the asset ceiling – that is the present value of any economic benefits available in the form of refunds from the plan or a reduction in future contributions. Management uses judgement to determine the level of refunds available from the plan in recognising an asset

The determination of the pension cost and defined benefit obligation of the Group's defined benefit pension schemes depends on the selection of certain assumptions, which include the discount rate, inflation rate, salary growth and longevity

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise

The service cost, representing benefits accruing over the year, is included in the income statement as an operating cost. Net interest is calculated by applying the discount rate to the net defined benefit obligation and is presented as finance costs or finance income

Obligations for contributions to defined contribution pension plans are recognised as an operating expense in the income statement as incurred

**2 Other post-retirement obligations** The expected costs of post-retirement medical and life assurance benefits are accrued over the period of employment, using a similar accounting methodology as for defined benefit pension obligations. The liabilities and costs relating to significant other post-retirement obligations are assessed annually by independent qualified actuaries

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## Notes to the consolidated financial statements continued

**1 Accounting policies continued****n Employee benefits continued**

**3 Share-based payments** The fair value of options or shares granted under the Group's share and option plans is recognised as an employee expense after taking into account the Group's best estimate of the number of awards expected to vest. Fair value is measured at the date of grant and is spread over the vesting period of the option or share. The fair value of the options granted is measured using an option model that is most appropriate to the award. The fair value of shares awarded is measured using the share price at the date of grant unless another method is more appropriate. Any proceeds received are credited to share capital and share premium when the options are exercised.

**o Provisions**

Provisions are recognised if the Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are discounted to present value where the effect is material.

The Group recognises a provision for deferred consideration at fair value. Where this is contingent on future performance or a future event, judgement is exercised in establishing the fair value.

The Group recognises a provision for onerous lease contracts when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract.

The provision is based on the present value of future payments for surplus leased properties under non-cancellable operating leases, net of estimated sub-leasing income.

**p Revenue recognition**

The Group's revenue streams are courseware, assessments and services. Courseware includes curriculum materials provided in book form and/or via access to digital content. Assessments includes test development, processing and scoring services provided to governments, educational institutions, corporations and professional bodies. Services includes the operation of schools, colleges and universities, including sistemas in Brazil and English language teaching centres around the world as well as the provision of online learning services in partnership with universities and other academic institutions.

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services net of sales taxes, rebates and discounts, and after eliminating sales within the Group.

Revenue from the sale of books is recognised when title passes. A provision for anticipated returns is made based primarily on historical return rates. If these estimates do not reflect actual returns in future periods then revenues could be understated or overstated for a particular period.

Revenue from the sale of off-the-shelf software is recognised on delivery or on installation of the software where that is a condition of the contract. In certain circumstances, where installation is complex, revenue is recognised when the customer has completed their acceptance procedures. Where software is provided under a term licence, revenue is recognised on a straight-line basis over the period of the licence.

Revenue from the provision of services to academic institutions, such as programme development, student acquisition, education technology and student support services, is recognised as performance occurs.

Revenue from multi-year contractual arrangements, such as contracts to process qualifying tests for individual professions and government departments, is recognised as performance occurs. The assumptions, risks, and uncertainties inherent to long-term contract accounting can affect the amounts and timing of revenue and related expenses reported. Certain of these arrangements, either as a result of a single service spanning more than one reporting period or where the contract requires the provision of a number of services that together constitute a single project, are treated as long-term contracts with revenue recognised on a percentage of completion basis. Percentage of completion is calculated on a cost basis using the proportion of the total estimated costs incurred to date. Losses on contracts are recognised in the period in which the loss first becomes foreseeable. Contract losses are determined to be the amount by which estimated total costs of the contract exceed the estimated total revenues that will be generated.

Where a contractual arrangement consists of two or more separate elements that can be provided to customers either on a stand-alone basis or as an optional extra, such as the provision of supplementary materials or online access with textbooks and multiple deliverables within testing or service contracts, revenue is recognised for each element as if it were an individual contractual arrangement.

## 1 Accounting policies continued

### p Revenue recognition continued

On certain contracts, where the Group acts as agent, only commissions and fees receivable for services rendered are recognised as revenue. Any third-party costs incurred on behalf of the principal that are rechargeable under the contractual arrangement are not included in revenue.

Income from recharges of freight and other activities which are incidental to the normal revenue generating activities is included in other income.

Circulation and advertising revenue is recognised when the newspaper or other publication is published. Subscription revenue is recognised on a straight-line basis over the life of the subscription.

### q Leases

Leases of property, plant and equipment where the Group has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the commencement of the lease at the lower of the fair value of the leased property and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in financial liabilities – borrowings. The interest element of the finance cost is charged to the income statement over the lease period to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life of the asset or the lease term.

Leases where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases by the lessee. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

### r Dividends

Dividends are recorded in the Group's financial statements in the period in which they are approved by the company's shareholders.

### s Discontinued operations

A discontinued operation is a component of the Group's business that represents a separate major line of business or geographical area of operations that has been disposed of or meets the criteria to be classified as held for sale.

Discontinued operations are presented in the income statement as a separate line and are shown net of tax.

### t Assets and liabilities held for sale

Assets and liabilities are classified as held for sale and stated at the lower of carrying amount and fair value less costs to sell if it is highly probable that the carrying amount will be recovered principally through a sale transaction rather than through continuing use. No depreciation is charged in respect of non-current assets classified as held for sale. Amounts relating to non-current assets and liabilities held for sale are classified as discontinued operations in the income statement where appropriate.

### u Trade receivables

Trade receivables are stated at fair value after provision for bad and doubtful debts and anticipated future sales returns (see also note 1p).

## 2 Segment information

The primary segments for management and reporting are geographies as outlined below. In addition, the Group separately discloses the results from the Penguin Random House (PRH) associate.

The chief operating decision-maker is the Pearson Executive.

### Continuing operations

North America School, Higher Education and Professional businesses in US and Canada.

Growth School, Higher Education and Professional businesses in emerging markets which are investment priorities, including Brazil, China, India and South Africa.

Core School, Higher Education and Professional businesses in more mature markets including UK, Australia and Italy.

The results of the FT Group segment (to 30 November 2015) and Mergermarket (to 4 February 2014) are shown as discontinued in the relevant periods.

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## Notes to the consolidated financial statements continued

## 2 Segment information continued

For more detail on the services and products included in each business segment refer to the strategic report

								2015
All figures in £ millions	Notes	North America	Core	Growth	PRH	Corporate	Discontinued operations	Group
<b>Continuing operations</b>								
Sales		2,940	836	692	-	-	-	4,468
Adjusted operating profit/(loss)		480	114	(12)	90	-	-	672
Intangible charges		(386)	(79)	(583)	(41)	-	-	(1,089)
Other net gains and losses		19	(5)	-	(1)	-	-	13
<b>Operating (loss)/profit</b>		<b>113</b>	<b>30</b>	<b>(595)</b>	<b>48</b>	<b>-</b>	<b>-</b>	<b>(404)</b>
Finance costs	6							(100)
Finance income	6							71
<b>Loss before tax</b>								<b>(433)</b>
Income tax	7							81
<b>Loss for the year from continuing operations</b>								<b>(352)</b>
Segment assets		6,399	1,573	719	-	1,841	-	10,532
Joint ventures	12	1	-	3	-	-	-	4
Associates	12	-	6	-	1,093	-	-	1,099
<b>Total assets</b>		<b>6,400</b>	<b>1,579</b>	<b>722</b>	<b>1,093</b>	<b>1,841</b>	<b>-</b>	<b>11,635</b>
<b>Other segment items</b>								
Share of results of joint ventures and associates	12	(9)	-	(3)	64	-	16	68
Capital expenditure	10, 11	85	33	110	-	-	15	243
Pre-publication investment	20	218	63	66	-	-	-	347
Depreciation	10	42	9	18	-	-	6	75
Amortisation	11, 20	338	95	109	-	-	15	557
Impairment	11	282	37	530	-	-	-	849

## 2 Segment information continued

								2014 restated
All figures in £ millions	Notes	North America	Core	Growth	PRH	Corporate	Discontinued operations	Group
<b>Continuing operations</b>								
Sales		2,906	910	724	-	-	-	4,540
Adjusted operating profit		444	122	32	69	-	-	667
Intangible charges		(108)	(21)	(132)	(54)	-	-	(315)
Acquisition costs		(2)	(1)	(3)	-	-	-	(6)
Other net gains and losses		2	-	-	-	-	-	2
Operating profit/(loss)		336	100	(103)	15	-	-	348
Finance costs	6							(140)
Finance income	6							47
Profit before tax								255
Income tax	7							(56)
Profit for the year from continuing operations								199
Segment assets		6,580	1,426	1,394	-	660	219	10,279
Joint ventures	12	1	-	3	-	-	9	13
Associates	12	1	8	-	1,095	-	1	1,105
Total assets		6,582	1,434	1,397	1,095	660	229	11,397
<b>Other segment items</b>								
Share of results of joint ventures and associates	12	-	(1)	(3)	35	-	20	51
Capital expenditure	10, 11	97	32	49	-	-	16	194
Pre-publication investment	20	209	77	72	-	-	-	358
Depreciation	10	41	10	16	-	-	7	74
Amortisation	11, 20	306	99	121	-	-	16	542
Impairment	11	-	-	77	-	-	-	77

For further information on adjusted measures above, see note 8

There were no material inter-segment sales in either 2014 or 2015

Included in other net gains and losses within continuing operations in 2015 in the North America segment is the profit on disposal of PowerSchool of £30m, net of small losses on other investments. In the Core segment the loss on disposal relates to adjustments to prior year disposals

Included in other net gains and losses in continuing operations in 2014 are gains on the sale of joint venture interests in Safari Books Online and CourseSmart (£40m) and a loss on disposal of an investment in Nook Media (£38m)

Both operating profit and adjusted operating profit in 2015 are stated after the following restructuring charges: North America £24m (2014: £37m), Core £nil (2014: £21m), Growth £11m, (2014: £6m), Penguin Random House £12m (2014: £19m)

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## Notes to the consolidated financial statements continued

## 2 Segment information continued

Corporate costs are allocated to business segments including discontinued operations on an appropriate basis depending on the nature of the cost, therefore the segment result is equal to the Group operating profit. Segment assets consist of property, plant and equipment, intangible assets, inventories, receivables, deferred taxation and other financial assets and exclude cash and cash equivalents and derivative assets. Corporate assets comprise cash and cash equivalents, marketable securities and derivative financial instruments. Capital expenditure comprises additions to property, plant and equipment and software (see notes 10 and 11).

Property, plant and equipment and intangible assets acquired through business combination were £1m (2014 £263m) (see note 30).

The following tables analyse the Group's revenue streams. Courseware includes curriculum materials provided in book form and/or via access to digital content. Assessments includes test development, processing and scoring services provided to governments, educational institutions, corporations and professional bodies. Services includes the operation of schools, colleges and universities, including sistemas in Brazil and English language teaching centres around the world as well as the provision of online learning services in partnership with universities and other academic institutions. School Systems includes PowerSchool and Family Education Network, both of which were disposed during 2015.

All figures in £ millions	2015			
	North America	Core	Growth	Group
<b>Courseware</b>				
School Courseware	406	186	104	696
Higher Education Courseware	1,207	96	55	1,358
English Courseware	22	84	79	185
	1,635	366	238	2,239
<b>Assessments</b>				
School and Higher Education Assessments	420	301	15	736
Clinical Assessments	126	32	-	158
Professional Certification	269	82	36	387
	815	415	51	1,281
<b>Services</b>				
School Services	209	1	47	257
Higher Education Services	223	26	70	319
English Services	18	28	286	332
School Systems	40	-	-	40
	490	55	403	948
<b>Total</b>	<b>2,940</b>	<b>836</b>	<b>692</b>	<b>4,468</b>

## 2 Segment information continued

	2014 restated			
All figures in £ millions	North America	Core	Growth	Group
<b>Courseware</b>				
School Courseware	389	214	120	723
Higher Education Courseware	1,179	114	66	1,359
English Courseware	22	92	75	189
	1,590	420	261	2,271
<b>Assessments</b>				
School and Higher Education Assessments	416	312	14	742
Clinical Assessments	115	34	-	149
Professional Certification	228	93	19	340
	759	439	33	1,231
<b>Services</b>				
School Services	253	-	56	309
Higher Education Services	215	22	90	327
English Services	20	29	284	333
School Systems	69	-	-	69
	557	51	430	1,038
<b>Total</b>	<b>2,906</b>	<b>910</b>	<b>724</b>	<b>4,540</b>

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## Notes to the consolidated financial statements continued

**2 Segment information continued**

The Group operates in the following main geographic areas

All figures in £ millions	Sales		Non current assets	
	2015	2014 restated	2015	2014
<b>Continuing operations</b>				
UK	421	444	991	1,056
Other European countries	246	281	121	180
US	2,800	2,762	5,000	5,243
Canada	107	109	235	288
Asia Pacific	590	565	211	416
Other countries	304	379	144	661
<b>Total continuing</b>	<b>4,468</b>	<b>4,540</b>	<b>6,702</b>	<b>7,844</b>
<b>Discontinued operations</b>				
UK	134	170	-	-
Other European countries	64	66	-	-
US	72	68	-	-
Canada	2	1	-	-
Asia Pacific	35	34	-	-
Other countries	5	4	-	-
<b>Total discontinued</b>	<b>312</b>	<b>343</b>	<b>-</b>	<b>-</b>
<b>Total</b>	<b>4,780</b>	<b>4,883</b>	<b>6,702</b>	<b>7,844</b>

Sales are allocated based on the country in which the customer is located. This does not differ materially from the location where the order is received. The geographical split of non-current assets is based on the subsidiary's country of domicile. This is not materially different to the location of the assets. Non-current assets comprise property, plant and equipment, intangible assets, investments in joint ventures and associates and trade and other receivables.

### 3 Discontinued operations

Discontinued operations relate to FT Group, Penguin and Mergermarket. An analysis of the results and cash flows of discontinued operations is as follows

All figures in £ millions	2015				2014 restated	
	FT Group	Total	Penguin	Mergermarket	FT Group	Total
Sales	312	312	-	9	334	343
Operating profit	48	48	-	2	50	52
Finance income	-	-	-	-	-	-
Profit before tax	48	48	-	2	50	52
Income tax	(8)	(8)	-	(1)	(7)	(8)
Profit after tax	40	40	-	1	43	44
Profit on disposal of Penguin	-	-	29	-	-	29
Profit on disposal of The Economist	473	473	-	-	-	-
Profit on disposal of Financial Times	711	711	-	-	-	-
Attributable tax expense	(49)	(49)	-	-	-	-
Profit on disposal of Mergermarket	-	-	-	244	-	244
Attributable tax expense	-	-	-	(46)	-	(46)
Profit for the year from discontinued operations	1,175	1,175	29	199	43	271
Operating cash flows	31	31	-	2	24	26
Investing cash flows	3	3	-	-	(5)	(5)
Financing cash flows	-	-	-	-	-	-
Total cash flows	34	34	-	2	19	21

### 4 Operating expenses

All figures in £ millions	2015	2014 restated
<b>By function.</b>		
Cost of goods sold	1,981	2,021
<b>Operating expenses</b>		
Distribution costs	80	84
Selling, marketing and product development costs	895	931
Administrative and other expenses	1,195	1,168
Restructuring costs	35	64
Other net gains and losses	(13)	(2)
Other income	(98)	(120)
Total net operating expenses	2,094	2,125
Impairment of intangible assets	849	77
<b>Total</b>	<b>4,924</b>	<b>4,223</b>

Included in other income is service fee income from Penguin Random House of £16m (2014 £41m). Included in administrative and other expenses are research and efficacy costs of £33m (2014 £22m). In addition to the restructuring costs shown above there were restructuring costs in Penguin Random House of £12m (2014 £19m) and in discontinued operations of £nil (2014 £1m).

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## Notes to the consolidated financial statements continued

**4 Operating expenses continued**

All figures in £ millions	Notes	2015	2014 restated
<b>By nature</b>			
Royalties expensed		249	242
Other product costs		566	620
Employee benefit expense	5	1,742	1,832
Contract labour		182	183
Employee related expense		127	136
Promotional costs		163	149
Depreciation of property, plant and equipment	10	69	67
Amortisation of intangible assets – pre-publication	20	281	292
Amortisation of intangible assets – software	11	61	51
Amortisation of intangible assets – other	11	199	184
Impairment of intangible assets	11	849	77
Property and facilities		219	204
Technology and communications		153	123
Professional and outsourced services		262	253
Other general and administrative costs		132	121
Capitalised costs		(219)	(195)
Acquisition costs		-	6
Other net gains and losses		(13)	(2)
Other income		(98)	(120)
<b>Total</b>		<b>4,924</b>	<b>4,223</b>

During the year the Group obtained the following services from the Group's auditors

All figures in £ millions	2015	2014
The audit of parent company and consolidated financial statements	4	5
The audit of the company's subsidiaries	2	2
<b>Total audit fees</b>	<b>6</b>	<b>7</b>
Other assurance services	2	1
Other non-audit services	1	-
<b>Total other services</b>	<b>3</b>	<b>1</b>
Tax compliance services	1	1
Tax advisory services	-	-
<b>Total tax services</b>	<b>1</b>	<b>1</b>
<b>Total non-audit services</b>	<b>4</b>	<b>2</b>
<b>Total</b>	<b>10</b>	<b>9</b>

#### 4 Operating expenses continued

Reconciliation between audit and non-audit service fees is shown below

All figures in £ millions	2015	2014
Group audit fees including fees for attestation under section 404 of the Sarbanes-Oxley Act	6	7
Non-audit fees	4	2
<b>Total</b>	<b>10</b>	<b>9</b>

Fees for attestation under section 404 of the Sarbanes-Oxley Act are allocated between fees payable for the audits of consolidated and subsidiary accounts

Included in non-audit fees are amounts related to carve out audits for disposals of £1m

#### 5 Employee information

All figures in £ millions	Notes	2015	2014 restated
<b>Employee benefit expense</b>			
Wages and salaries (including termination benefits and restructuring costs)		1,507	1,607
Social security costs		124	122
Share-based payment costs	26	26	32
Retirement benefits – defined contribution plans	25	66	61
Retirement benefits – defined benefit plans	25	19	21
Other post-retirement benefits	25	–	(11)
<b>Total</b>		<b>1,742</b>	<b>1,832</b>

The details of the emoluments of the directors of Pearson plc are shown in the report on directors' remuneration

Average number employed	2015	2014 restated
<b>Employee numbers</b>		
North America	19,951	20,927
Core	5,936	6,139
Growth	11,114	11,406
Other	264	182
<b>Continuing operations</b>	<b>37,265</b>	<b>38,654</b>

The employee benefit expense relating to discontinued operations was £132m (2014 £151m) and the average number employed was 2,282 (2014 2,295)

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## Notes to the consolidated financial statements continued

**6 Net finance costs**

All figures in £ millions	Notes	2015	2014 restated
Interest payable		(61)	(81)
Net foreign exchange losses		(36)	(53)
Derivatives not in hedging relationships		(3)	(6)
Finance costs		(100)	(140)
Interest receivable		15	17
Net finance income in respect of retirement benefits	25	4	1
Net foreign exchange gains		43	17
Derivatives not in hedging relationships		9	12
Finance income		71	47
Net finance costs		(29)	(93)
Analysed as:			
Net interest payable reflected in adjusted earnings		(46)	(64)
Other net finance income/(costs)		17	(29)
Total net finance costs		(29)	(93)

Included in interest receivable is £1m (2014 £1m) of interest receivable from related parties. There was a net movement of £nil on fair value hedges in 2015 (2014 £nil), comprising a gain of £22m (2014 loss of £27m) on the underlying bonds, offset by a loss of £22m (2014 gain of £27m) on the related derivative financial instruments.

For further information on adjusted measures above, see note 8.

**7 Income tax**

All figures in £ millions	Notes	2015	2014 restated
<b>Current tax</b>			
Charge in respect of current year		(155)	(96)
Adjustments in respect of prior years		42	30
<b>Total current tax charge</b>		<b>(113)</b>	<b>(66)</b>
<b>Deferred tax</b>			
In respect of temporary differences		185	8
Other adjustments in respect of prior years		9	2
<b>Total deferred tax credit</b>	13	<b>194</b>	<b>10</b>
<b>Total tax credit/(charge)</b>		<b>81</b>	<b>(56)</b>

The adjustments in respect of prior years in both 2015 and 2014 mainly relate to changes in estimates arising from uncertain tax positions following agreement of historical tax positions

The tax on the Group's (loss)/profit before tax differs from the theoretical amount that would arise using the UK tax rate as follows

All figures in £ millions	2015	2014 restated
(Loss)/profit before tax	(433)	255
Tax calculated at UK rate (2015 20.25%, 2014 21.5%)	88	(55)
Effect of overseas tax rates	52	(10)
Joint venture and associate income reported net of tax	10	7
Net expense not subject to tax	(66)	(11)
Gains and losses on sale of businesses not subject to tax	(32)	-
Unutilised tax losses	(22)	(19)
Adjustments in respect of prior years	51	32
<b>Total tax credit/(charge)</b>	<b>81</b>	<b>(56)</b>
UK	(25)	-
Overseas	106	(56)
<b>Total tax credit/(charge)</b>	<b>81</b>	<b>(56)</b>
<b>Tax rate reflected in earnings</b>	<b>18.7%</b>	<b>22.0%</b>

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## Notes to the consolidated financial statements continued

**7 Income tax continued**

The tax rate reflected in adjusted earnings is calculated as follows

All figures in £ millions	2015	2014 restated
(Loss)/profit before tax	(433)	255
<b>Adjustments</b>		
Other net gains and losses	(13)	(2)
Acquisition costs	-	6
Intangible charges	1,089	315
Other net finance (income)/costs	(17)	29
<b>Adjusted profit before tax – continuing operations</b>	<b>626</b>	<b>603</b>
Adjusted profit before tax – discontinued operations	51	55
<b>Total adjusted profit before tax</b>	<b>677</b>	<b>658</b>
<b>Total tax credit/(charge)</b>	<b>81</b>	<b>(56)</b>
<b>Adjustments</b>		
Tax charge on other net gains and losses	40	1
Tax benefit on acquisition costs	-	(1)
Tax benefit on intangible charges	(257)	(72)
Tax charge/(benefit) on other net finance costs	7	(5)
Tax amortisation benefit on goodwill and intangibles	33	24
<b>Adjusted income tax charge – continuing operations</b>	<b>(96)</b>	<b>(109)</b>
Adjusted income tax charge – discontinued operations	(9)	(9)
<b>Total adjusted income tax charge</b>	<b>(105)</b>	<b>(118)</b>
<b>Tax rate reflected in adjusted earnings</b>	<b>15.5%</b>	<b>17.9%</b>

For further information on adjusted measures above, see note 8

The tax (charge)/benefit recognised in other comprehensive income is as follows

All figures in £ millions	2015	2014
Net exchange differences on translation of foreign operations	5	(6)
Remeasurement of retirement benefit obligations	(24)	(1)
	(19)	(7)

A tax charge of £1m (2014 tax charge £3m) relating to share-based payments has been recognised directly in equity

## 8 Earnings per share

### Basic

Basic earnings per share is calculated by dividing the profit attributable to equity shareholders of the company by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the company and held as treasury shares

### Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares to take account of all dilutive potential ordinary shares and adjusting the profit attributable, if applicable, to account for any tax consequences that might arise from conversion of those shares

All figures in £ millions	Notes	2015	2014 restated
(Loss)/profit for the year from continuing operations		(352)	199
Non-controlling interest		-	1
Earnings from continuing operations		(352)	200
Profit for the year from discontinued operations	3	1,175	271
Earnings		823	471
Weighted average number of shares (millions)		813.3	810.9
Effect of dilutive share options (millions)		-	1.0
Weighted average number of shares (millions) for diluted earnings		813.3	811.9
<b>Earnings per share from continuing and discontinued operations</b>			
Basic		101.2p	58.1p
Diluted		101.2p	58.0p
<b>(Loss)/earnings per share from continuing operations</b>			
Basic		(43.3)p	24.7p
Diluted		(43.3)p	24.6p
<b>Earnings per share from discontinued operations</b>			
Basic		144.5p	33.4p
Diluted		144.5p	33.4p

### Adjusted

In order to show results from operating activities on a consistent basis, an adjusted earnings per share is presented. The company's definition of adjusted earnings per share may not be comparable to other similarly titled measures reported by other companies.

Adjusted earnings includes the results from continuing and discontinued operations. The following items are excluded from adjusted earnings:

Other net gains and losses represent profits and losses on the acquisition and disposal of subsidiaries, joint ventures, associates and other financial assets that are included within continuing or discontinued operations but which distort the performance of the Group.

Amortisation and impairment of acquired intangibles, acquisition costs and movements in contingent acquisition consideration are also excluded from adjusted earnings as these items are not considered to be fully reflective of the underlying performance of the Group.

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## Notes to the consolidated financial statements continued

**8 Earnings per share continued**

Other net finance income/costs include finance costs in respect of retirement benefits, finance costs of deferred consideration and foreign exchange and other gains and losses. Finance costs relating to retirement benefits are excluded as the consolidated income statement presentation under IAS 19 does not reflect the economic substance of the underlying assets and liabilities. Finance costs of put options and deferred consideration are excluded as they relate to future earn outs and similar payments on acquisitions and do not reflect cash expended. Foreign exchange and other gains and losses are excluded as they represent short-term fluctuations in market value and are subject to significant volatility. Other gains and losses may not be realised in due course as it is normally the intention to hold the related instruments to maturity. Other net finance costs of Group companies are included in finance costs or finance income as appropriate. Other net finance costs of joint ventures and associates are included within the share of results of joint ventures and associates within operating profit.

Tax on the above items is excluded from adjusted earnings. Where relevant the Group also excludes the benefit from recognising previously unrecognised pre-acquisition and capital losses. The tax benefit from tax deductible goodwill and intangibles is added to the adjusted income tax charge as this benefit more accurately aligns the adjusted tax charge with the expected rate of cash tax payments.

Non-controlling interest for the above items is excluded from adjusted earnings. The following tables reconcile statutory earnings to adjusted earnings.

	2015							
All figures in £ millions	Statutory income statement	Discontinued operations	Other net gains and losses	Acquisition costs	Intangible charges	Other net finance income/costs	Tax amortisation benefit	Adjusted income statement
Operating (loss)/profit	(404)	51	(13)	-	1,089	-	-	723
Net finance costs	(29)	-	-	-	-	(17)	-	(46)
(Loss)/profit before tax	(433)	51	(13)	-	1,089	(17)	-	677
Income tax	81	(9)	40	-	(257)	7	33	(105)
(Loss)/profit for the year from continuing operations	(352)	42	27	-	832	(10)	33	572
Profit for the year from discontinued operations	1,175	(42)	(1,135)	-	2	-	-	-
Profit for the year	823	-	(1,108)	-	834	(10)	33	572
Non-controlling interest	-	-	-	-	-	-	-	-
Earnings	823	-	(1,108)	-	834	(10)	33	572
Weighted average number of shares (millions)	813.3							813.3
Weighted average number of shares (millions) for diluted earnings	813.3							813.3
Earnings per share (basic)	101.2p							70.3p
Earnings per share (diluted)	101.2p							70.3p

## 8 Earnings per share continued

All figures in £ millions								2014 restated
	Statutory income statement	Discontinued operations	Other net gains and losses	Acquisition costs	Intangible charges	Other net finance income/ costs	Tax amortisation benefit	Adjusted income statement
Operating profit	348	55	(2)	6	315	–	–	722
Net finance costs	(93)	–	–	–	–	29	–	(64)
Profit before tax	255	55	(2)	6	315	29	–	658
Income tax	(56)	(9)	1	(1)	(72)	(5)	24	(118)
Profit for the year from continuing operations	199	46	(1)	5	243	24	24	540
Profit for the year from discontinued operations	271	(46)	(227)	–	2	–	–	–
Profit for the year	470	–	(228)	5	245	24	24	540
Non-controlling interest	1	–	–	–	–	–	–	1
Earnings	471	–	(228)	5	245	24	24	541
Weighted average number of shares (millions)	810.9							810.9
Weighted average number of shares (millions) for diluted earnings	811.9							811.9
Earnings per share (basic)	58.1p							66.7p
Earnings per share (diluted)	58.0p							66.6p

## 9 Dividends

All figures in £ millions	2015	2014
Final paid in respect of prior year 34.0p (2014 32.0p)	277	259
Interim paid in respect of current year 18.0p (2014 17.0p)	146	138
	423	397

The directors are proposing a final dividend in respect of the financial year ended 31 December 2015 of 34.0p per share which will absorb an estimated £277m of shareholders' funds. It will be paid on 6 May 2016 to shareholders who are on the register of members on 8 April 2016. These financial statements do not reflect this dividend.

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## Notes to the consolidated financial statements continued

## 10 Property, plant and equipment

All figures in £ millions	Land and buildings	Plant and equipment	Assets in course of construction	Total
<b>Cost</b>				
At 1 January 2014	375	568	32	975
Exchange differences	11	17	-	28
Additions	10	58	19	87
Disposals	(9)	(46)	(2)	(57)
Acquisition through business combination	-	2	-	2
Disposal through business disposal	-	(1)	-	(1)
Reclassifications	1	3	(4)	-
Transfer to software	-	-	(16)	(16)
At 31 December 2014	388	601	29	1,018
Exchange differences	8	10	1	19
Additions	15	42	25	82
Disposals	(20)	(86)	-	(106)
Acquisition through business combination	-	-	-	-
Disposal through business disposal	(48)	(76)	-	(124)
Reclassifications	16	17	(33)	-
At 31 December 2015	359	508	22	889

## 10 Property, plant and equipment continued

All figures in £ millions	Land and buildings	Plant and equipment	Assets in course of construction	Total
<b>Depreciation</b>				
At 1 January 2014	(210)	(423)	-	(633)
Exchange differences	(7)	(15)	-	(22)
Charge for the year	(23)	(51)	-	(74)
Disposals	9	36	-	45
At 31 December 2014	(231)	(453)	-	(684)
Exchange differences	(5)	(12)	-	(17)
Charge for the year	(22)	(53)	-	(75)
Disposals	18	82	-	100
Disposal through business disposal	48	59	-	107
At 31 December 2015	(192)	(377)	-	(569)
<b>Carrying amounts</b>				
At 1 January 2014	165	145	32	342
At 31 December 2014	157	148	29	334
At 31 December 2015	167	131	22	320

Depreciation expense of £19m (2014 £16m) has been included in the income statement in cost of goods sold and £50m (2014 £51m) in operating expenses. In 2015 £6m (2014 £7m) relates to discontinued operations.

The Group leases certain equipment under a number of finance lease agreements. The net carrying amount of leased plant and equipment included within property, plant and equipment was £8m (2014 £13m).

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## Notes to the consolidated financial statements continued

## 11 Intangible assets

All figures in £ millions	Goodwill	Software	Acquired customer lists, contracts and relationships	Acquired trademarks and brands	Acquired publishing rights	Other intangibles acquired	Total
<b>Cost</b>							
At 1 January 2014	4,666	469	855	237	198	398	6,823
Exchange differences	198	17	34	5	-	14	268
Impairment	(67)	-	-	-	-	-	(67)
Additions - internal development	-	54	-	-	-	-	54
Additions - purchased	-	53	-	-	-	-	53
Disposals	-	(7)	-	-	-	-	(7)
Acquisition through business combination	238	-	5	69	-	186	498
Disposal through business disposal	(5)	(5)	-	(3)	(1)	-	(14)
Transfer from PPE	-	16	-	-	-	-	16
<b>At 31 December 2014</b>	<b>5,030</b>	<b>597</b>	<b>894</b>	<b>308</b>	<b>197</b>	<b>598</b>	<b>7,624</b>
Exchange differences	105	17	25	(17)	(7)	(40)	83
Impairment	(826)	-	-	-	-	-	(826)
Additions - internal development	-	125	-	-	-	-	125
Additions - purchased	-	36	-	-	-	-	36
Disposals	-	(18)	-	(4)	(10)	(29)	(61)
Acquisition through business combination	-	-	-	-	-	1	1
Disposal through business disposal	(175)	(138)	(59)	(6)	-	(21)	(399)
<b>At 31 December 2015</b>	<b>4,134</b>	<b>619</b>	<b>860</b>	<b>281</b>	<b>180</b>	<b>509</b>	<b>6,583</b>

## 11 Intangible assets continued

All figures in £ millions	Goodwill	Software	Acquired customer lists, contracts and relationships	Acquired trademarks and brands	Acquired publishing rights	Other intangibles acquired	Total
<b>Amortisation</b>							
At 1 January 2014	-	(316)	(249)	(93)	(148)	(216)	(1,022)
Exchange differences	-	(13)	(11)	(3)	-	(12)	(39)
Impairment	-	-	(6)	(2)	-	(2)	(10)
Charge for the year	-	(63)	(83)	(25)	(12)	(67)	(250)
Disposals	-	5	-	-	-	-	5
Disposal through business disposal	-	1	-	1	-	-	2
At 31 December 2014	-	(386)	(349)	(122)	(160)	(297)	(1,314)
Exchange differences	-	(14)	(8)	1	6	(6)	(21)
Impairment	-	-	(13)	(1)	(9)	-	(23)
Charge for the year	-	(74)	(99)	(40)	(10)	(53)	(276)
Disposals	-	18	-	4	10	29	61
Disposal through business disposal	-	99	39	3	-	13	154
At 31 December 2015	-	(357)	(430)	(155)	(163)	(314)	(1,419)
<b>Carrying amounts</b>							
At 1 January 2014	4,666	153	606	144	50	182	5,801
At 31 December 2014	5,030	211	545	186	37	301	6,310
At 31 December 2015	4,134	262	430	126	17	195	5,164

**Goodwill**

The goodwill carrying value of £4,134m relates to acquisitions completed after 1 January 1998. Prior to 1 January 1998 all goodwill was written off to reserves on the date of acquisition. For acquisitions completed between 1 January 1998 and 31 December 2002 no value was ascribed to intangibles other than goodwill and the goodwill on each acquisition was amortised over a period of up to 20 years. On adoption of IFRS on 1 January 2003, the Group chose not to restate the goodwill balance and at that date the balance was frozen (i.e. amortisation ceased). If goodwill had been restated then a significant value would have been ascribed to other intangible assets, which would be subject to amortisation, and the carrying value of goodwill would be significantly lower. For acquisitions completed after 1 January 2003 value has been ascribed to other intangible assets which are amortised.

**Other intangible assets**

Other intangibles acquired include content, technology and software rights.

Intangible assets are valued separately for each acquisition and the primary method of valuation used is the discounted cash flow method. The majority of acquired intangibles are amortised using an amortisation profile based on the projected cash flows underlying the acquisition date valuation of the intangible asset, which generally results in a larger proportion of amortisation being recognised in the early years of the asset's life. The Group keeps the expected pattern of consumption under review.

Amortisation of £13m (2014: £12m) is included in the income statement in cost of goods sold and £247m (2014: £223m) in operating expenses. In 2015, £16m (2014: £15m) of amortisation relates to discontinued operations.

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## Notes to the consolidated financial statements continued

## 11 Intangible assets continued

The range of useful economic lives for each major class of intangible asset (excluding goodwill and software) is shown below

	2015
Class of intangible asset	Useful economic life
Acquired customer lists, contracts and relationships	3–20 years
Acquired trademarks and brands	2–20 years
Acquired publishing rights	5–20 years
Other intangibles acquired	2–20 years

The expected amortisation profile of acquired intangible assets is shown below

	2015			
All figures in £ millions	One to five years	Six to ten years	More than ten years	Total
Class of intangible asset				
Acquired customer lists, contracts and relationships	268	122	40	430
Acquired trademarks and brands	56	47	23	126
Acquired publishing rights	15	2	–	17
Other intangibles acquired	146	43	6	195

## Impairment tests for cash-generating units (CGUs) containing goodwill

Impairment tests have been carried out where appropriate as described below

Following a reorganisation of the business effective 1 January 2014 goodwill was allocated to CGUs, or an aggregation of CGUs, where goodwill could not be reasonably allocated to individual business units. Impairment reviews were conducted on these CGUs. The carrying value of the goodwill in each of the CGUs, after the impact of impairments, is summarised below

All figures in £ millions	2015	2014
North America	3,155	3,422
Core	635	618
Growth (includes Brazil, China, India and South Africa)	–	612
Pearson VUE	344	327
Financial Times Group	–	51
Total	4,134	5,030

The recoverable amount of each aggregated cash generating unit (CGU) is based on fair value less costs of disposal or value in use calculations as appropriate. Goodwill is tested at least annually for impairment. Other than goodwill there are no intangible assets with indefinite lives. The goodwill is generally denominated in the currency of the relevant cash flows and therefore the impairment review is not materially sensitive to exchange rate fluctuations.

## 11 Intangible assets continued

### Impairment tests for cash-generating units containing goodwill continued

Following significant economic and market deterioration in the Group's operations in emerging markets and ongoing cyclical and policy-related pressures in the Group's mature market operations, management's expectations of future returns were revised down in the course of 2015. It was determined during the impairment review that the fair value less costs of disposal of the Growth, North America and Core CGUs no longer supported the carrying value of the goodwill. An impairment of £507m was booked in respect of the Group's Growth operations, representing impairments of £269m in the Brazil CGU, £181m in the China CGU, £48m in the South Africa CGU and £9m in the Other Growth CGU, thereby bringing the carrying value of goodwill in those CGUs down to £nil. Impairments of £10m and £13m were also booked in respect of other acquired intangibles in the South Africa and Other Growth CGUs respectively, bringing their carrying value down to £nil. Impairments of £282m and £37m were also booked in respect of the North America and Core CGUs respectively, bringing the carrying value of the goodwill in those CGUs down to fair value less costs of disposal. Fair value less costs of disposal was determined using post-tax discount rates of 17.4% for Brazil, 11.0% for China, 13.6% for South Africa, 12.8% for Other Growth, 8.6% for North America and 8.7% for Core. Following the above impairments, the recoverable amounts of the Growth, North America and Core CGUs are £350m, £4,750m and £926m respectively.

### Key assumptions

For the purpose of estimating the fair value less costs of disposal of the CGUs, management has used an income approach based on present value techniques. The calculations use cash flow projections based on financial budgets approved by management covering a five-year period, management's best estimate about future developments and market assumptions. The fair value less costs of disposal measurement is categorised as Level 3 on the fair value hierarchy. The key assumptions used by management in the fair value less costs of disposal calculations were:

**Discount rates** The discount rate is based on the risk-free rate for government bonds, adjusted for a risk premium to reflect the increased risk in investing in equities. The risk premium adjustment is assessed for each specific CGU. The average post-tax discount rates range from 7.2% to 17.4%. Discount rates are lower for those businesses which operate in more mature markets with low inflation and higher for those operating in emerging markets with higher inflation.

**Perpetuity growth rates** A perpetuity growth rate of 2.0% (2014: 2.0%) was used for cash flows subsequent to the approved budget period for CGUs operating in mature markets. This perpetuity growth rate is a conservative rate and is considered to be lower than the long-term historical growth rates of the underlying territories in which the CGU operates and the long-term growth rate prospects of the sectors in which the CGU operates. CGU growth rates between 5.0% and 8.5% were used for cash flows subsequent to the approved budget period for CGUs operating in emerging markets with high inflation. These growth rates are also below the long-term historical growth rates in these markets.

The key assumptions used by management in setting the financial budgets for the initial five-year period were as follows:

**Forecast sales growth rates** Forecast sales growth rates are based on past experience adjusted for the strategic direction and near-term investment priorities within each CGU. Key factors include USA and UK college enrolment rates, assessment growth rates, the success of new product launches, growth rates and economic conditions in emerging markets and the rate of growth in new services businesses. The five-year sales forecasts use average nominal growth rates between 1.1% and 1.6% for mature markets and between 0.1% and 5.6% for emerging markets with high inflation.

**Operating profits** Operating profits are forecast based on historical experience of operating margins, adjusted for the impact of changes to product costs and cost saving initiatives, including the impact of the global restructuring programme planned in 2016.

**Cash conversion** Cash conversion is the ratio of operating cash flow to operating profit. Management forecasts cash conversion rates based on historical experience, adjusted for the impact of product investment priorities and the shift to digital and service based business.

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**11 Intangible assets continued****Sensitivities**

The Group's impairment review is sensitive to a change in assumptions used, most notably the discount rates and the perpetuity growth rates. As the carrying value of goodwill in the Growth market CGUs has been written down to £nil, the value of other intangible assets in Brazil and China is sensitive to any increase in discount rates or reduction in perpetuity growth rates. In the North America and Core CGUs goodwill has been written down to fair value less costs of disposal and any further increase in discount rates or reduction in perpetuity growth rates would give rise to further impairment. A 0.1% increase in discount rates would cause the fair value less costs of disposal of the Brazil, China, North America and Core CGUs to reduce by £3m, £5m, £120m and £25m respectively. A 0.1% reduction in perpetuity growth rates would cause the fair value less costs of disposal of the Brazil, China, North America and Core CGUs to reduce by £2m, £5m, £100m and £21m respectively. All CGUs which have been written down to fair value less costs of disposal are highly sensitive to any reductions in short-term cash flows, whether driven by lower sales growth, lower operating profits or lower cash conversion. A 5% reduction in total annual operating profits, spread evenly across all CGUs, would give rise to an impairment of £29m in the Growth CGUs, £241m in the North America CGU and £62m in the Core CGU.

**2014 impairment tests**

In 2014 following deterioration in the market conditions for the Group's online tutoring business based in India, it was determined in the course of the impairment review that the value in use of the India CGU no longer supported the carrying value of the goodwill in that CGU. An impairment of £67m was booked, thereby bringing the carrying value of goodwill in the India CGU down to £nil. An impairment of £10m was also booked in respect of other acquired intangibles in that CGU, bringing their carrying value to £nil. The India CGU incorporates all the Group's trading operations in India. A pre-tax discount rate of 13.6% was used to determine the value in use of the India CGU. No previous assessment had been made of the value in use of that CGU as the Group's India operations, prior to the 1 January 2014 reorganisation, were previously part of a larger Emerging Markets aggregated CGU.

**12 Investments in joint ventures and associates**

The amounts recognised in the balance sheet are as follows

All figures in £ millions	2015	2014
Associates	1,099	1,105
Joint ventures	4	13
<b>Total</b>	<b>1,103</b>	<b>1,118</b>

The amounts recognised in the income statement are as follows

All figures in £ millions	2015	2014
Associates	72	54
Joint ventures	(4)	(3)
<b>Total</b>	<b>68</b>	<b>51</b>

Included within the 2015 results are discontinued operations consisting of £17m profit from associates (2014: £21m profit) and £1m loss from joint ventures (2014: £1m loss). For further information on discontinued operations and the profit on sale of associates and joint ventures, see notes 3 and 31.

## 12 Investments in joint ventures and associates continued

### Investment in associates

On 16 October 2015, the Group sold 39% of its 50% stake in The Economist (see note 31 for further information). As at 31 December 2015, the Group holds an 11% stake in The Economist which has been classified as an 'Other financial asset' (see note 15).

The Group has the following material associates

	Principal place of business	Ownership interest	Nature of relationship	Measurement method
Penguin Random House Ltd	UK/Global	47%	See below	Equity
Penguin Random House LLC	US	47%	See below	Equity

On 1 July 2013 Penguin Random House was formed, upon the completion of an agreement between Pearson and Bertelsmann to merge their respective trade publishing companies, Penguin and Random House, with the parent companies owning 47% and 53% of the combined business respectively. The shareholder agreement includes protection rights for Pearson as the minority shareholder, including rights to dividends. Management considers ownership percentage, board composition and the additional protective rights, and exercises judgement to determine that Pearson has significant influence over Penguin Random House and Bertelsmann has the power to direct the relevant activities and therefore control. Penguin Random House does not have a quoted market price.

The summarised financial information of the material associates is detailed below

	2015		2014	
	Penguin Random House	The Economist	Penguin Random House	The Economist
All figures in £ millions				
<b>Assets</b>				
Current assets	1,354	-	1,355	110
Non-current assets	1,244	-	1,429	166
<b>Liabilities</b>				
Current liabilities	(1,034)	-	(1,113)	(190)
Non-current liabilities	(358)	-	(424)	(86)
<b>Net assets</b>	<b>1,206</b>	<b>-</b>	<b>1,247</b>	<b>-</b>
<b>Sales</b>	<b>2,453</b>	<b>276</b>	<b>2,416</b>	<b>320</b>
Profit from continuing operations	136	-	74	-
Profit from discontinued operations	-	34	-	42
Other comprehensive income/(expense)	51	-	42	(20)
<b>Total comprehensive income</b>	<b>187</b>	<b>34</b>	<b>116</b>	<b>22</b>
Dividends received from associate	142	20	95	21

The information above reflects the amounts presented in the financial statements of the associates, adjusted for fair value and similar adjustments. Amounts presented for The Economist cover the period up until the date of the partial disposal. The tax on Penguin Random House LLC is settled by the partners. For the purposes of clear and consistent presentation, the tax has been shown in the associate line items in the consolidated income statement and consolidated balance sheet, recording the Group's share of profit after tax consistently for the Penguin Random House associates.

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## Notes to the consolidated financial statements continued

**12 Investments in joint ventures and associates continued****Investment in associates continued**

A reconciliation of the summarised financial information to the carrying value of the material associates is shown below

All figures in £ millions	2015		2014	
	Penguin Random House	The Economist	Penguin Random House	The Economist
Opening net assets	1,247	-	1,232	16
Exchange differences	(1)	-	(1)	-
Profit for the period	136	34	74	42
Other comprehensive income/(expense)	51	-	42	(20)
Dividends, net of tax paid	(229)	(40)	(100)	(42)
Additions	2	-	-	-
Distribution from associate in excess of carrying value	-	-	-	4
Reversal of distribution from associate in excess of carrying value	-	(3)	-	-
Disposal	-	9	-	-
Closing net assets	1,206	-	1,247	-
Share of net assets	567	-	586	-
Goodwill	526	-	509	-
Carrying value of associate	1,093	-	1,095	-

Information on other individually immaterial associates is detailed below

All figures in £ millions	2015	2014
Loss from continuing operations	(9)	(2)
Other comprehensive income	-	-
Total comprehensive expense	(9)	(2)

**Transactions with material associates**

The Group has loans to Penguin Random House which are unsecured and interest is calculated based on market rates. The amount outstanding at 31 December 2015 was £47m (2014: £54m). The loans are provided under a working capital facility and fluctuate during the year. The loan outstanding at 31 December 2015 was repaid in its entirety in January 2016.

The Group also has a current asset receivable of £27m (2014: £41m) from Penguin Random House arising from the provision of services. Included in other income (note 4) is £16m (2014: £41m) of service fees.

**12 Investments in joint ventures and associates continued****Investment in joint ventures**

Information on joint ventures, all of which are individually immaterial, is detailed below

All figures in £ millions	2015	2014
Loss from continuing operations	(3)	(3)
Loss from discontinued operations	(1)	-
Other comprehensive income	-	-
<b>Total comprehensive expense</b>	<b>(4)</b>	<b>(3)</b>

**13 Deferred income tax**

All figures in £ millions	2015	2014
Deferred income tax assets	276	295
Deferred income tax liabilities	(560)	(714)
<b>Net deferred income tax</b>	<b>(284)</b>	<b>(419)</b>

Substantially all of the deferred income tax assets are expected to be recovered after more than one year

Deferred income tax assets and liabilities may be offset when there is a legally enforceable right to offset current income tax assets against current income tax liabilities and when the deferred income taxes relate to the same fiscal authority. At 31 December 2015 the Group has unrecognised deferred income tax assets of £nil (2014 £4m) in respect of UK losses, £11m (2014 £14m) in respect of US losses and approximately £70m (2014 £44m) in respect of losses in other territories. The US losses relate to state taxes and therefore have expiry periods of between five and 20 years.

The recognition of the deferred income tax assets is supported by management's forecasts of the future profitability of the relevant business units.

The movement on the net deferred income tax account is as follows

All figures in £ millions	Notes	2015	2014
At beginning of year		(419)	(362)
Exchange differences		(26)	(22)
Income statement benefit	7	196	10
Disposal through business disposal		1	(1)
Tax charge to other comprehensive income or equity		(36)	(18)
Transfer to current tax		-	(26)
<b>At end of year</b>		<b>(284)</b>	<b>(419)</b>

Included in the income statement above for 2015 is a £2m benefit (2014 £nil) relating to discontinued operations

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## Notes to the consolidated financial statements continued

## 13 Deferred income tax continued

The movement in deferred income tax assets and liabilities during the year is as follows

All figures in £ millions	Trading losses	Returns provisions	Retirement benefit obligations	Other	Total
<b>Deferred income tax assets</b>					
At 1 January 2014	15	39	42	154	250
Exchange differences	1	2	4	5	12
Acquisition through business combination	2	-	-	-	2
Income statement benefit	10	3	7	35	55
Tax benefit/(charge) to other comprehensive income or equity	-	-	10	(7)	3
Transfer to current tax	-	-	-	(26)	(26)
Disposal through business disposal	-	-	(1)	-	(1)
At 31 December 2014	28	44	62	161	295
Exchange differences	5	3	4	9	21
Income statement charge	(14)	(4)	(3)	(15)	(36)
Tax charge to other comprehensive income or equity	-	-	(4)	-	(4)
At 31 December 2015	19	43	59	155	276

Other deferred income tax assets include temporary differences on goodwill, deferred income, share-based payments, inventory and other provisions

All figures in £ millions	Goodwill and intangibles	Other	Total
<b>Deferred income tax liabilities</b>			
At 1 January 2014	(584)	(28)	(612)
Exchange differences	(30)	(4)	(34)
Acquisition through business combination	(2)	-	(2)
Income statement benefit/(charge)	18	(63)	(45)
Tax charge to other comprehensive income or equity	-	(21)	(21)
At 31 December 2014	(598)	(116)	(714)
Exchange differences	(41)	(6)	(47)
Income statement benefit	180	52	232
Disposal through business disposal	1	-	1
Tax charge to other comprehensive income or equity	-	(32)	(32)
At 31 December 2015	(458)	(102)	(560)

Other deferred income tax liabilities include temporary differences in respect of depreciation and royalty advances

#### 14 Classification of financial instruments

The accounting classification of each class of the Group's financial assets and financial liabilities, together with their carrying values and market values, is as follows

		2015							
		Fair value				Amortised cost		Total carrying value	Total market value
		Available for sale	Derivatives deemed held for trading	Derivatives in hedging relationships	Other liabilities	Loans and receivables	Other liabilities		
All figures in £ millions	Notes								
Investments in listed securities	15	-	-	-	-	-	-	-	-
Investments in unlisted securities	15	143	-	-	-	-	-	143	143
Cash and cash equivalents	17	-	-	-	-	1,703	-	1,703	1,703
Marketable securities		28	-	-	-	-	-	28	28
Derivative financial instruments	16	-	29	81	-	-	-	110	110
Trade receivables	22	-	-	-	-	963	-	963	963
<b>Total financial assets</b>		<b>171</b>	<b>29</b>	<b>81</b>	<b>-</b>	<b>2,666</b>	<b>-</b>	<b>2,947</b>	<b>2,947</b>
Derivative financial instruments	16	-	(36)	(129)	-	-	-	(165)	(165)
Trade payables	24	-	-	-	-	-	(319)	(319)	(319)
Bank loans and overdrafts	18	-	-	-	-	-	(38)	(38)	(38)
Borrowings due within one year	18	-	-	-	-	-	(244)	(244)	(244)
Borrowings due after more than one year	18	-	-	-	-	-	(2,048)	(2,048)	(2,009)
<b>Total financial liabilities</b>		<b>-</b>	<b>(36)</b>	<b>(129)</b>	<b>-</b>	<b>-</b>	<b>(2,649)</b>	<b>(2,814)</b>	<b>(2,775)</b>

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## Notes to the consolidated financial statements continued

## 14 Classification of financial instruments continued

									2014	
			Fair value			Amortised cost				
			Derivatives deemed held for trading	Derivatives in hedging relationships	Other liabilities	Loans and receivables	Other liabilities	Total carrying value	Total market value	
All figures in £ millions	Notes	Available for sale								
Investments in listed securities	15	9	-	-	-	-	-	9	9	
Investments in unlisted securities	15	45	-	-	-	-	-	45	45	
Cash and cash equivalents	17	-	-	-	-	530	-	530	530	
Marketable securities		16	-	-	-	-	-	16	16	
Derivative financial instruments	16	-	6	108	-	-	-	114	114	
Trade receivables	22	-	-	-	-	989	-	989	989	
Total financial assets		70	6	108	-	1,519	-	1,703	1,703	
Derivative financial instruments	16	-	(33)	(41)	-	-	-	(74)	(74)	
Trade payables	24	-	-	-	-	-	(329)	(329)	(329)	
Bank loans and overdrafts	18	-	-	-	-	-	(42)	(42)	(42)	
Borrowings due within one year	18	-	-	-	-	-	(305)	(305)	(319)	
Borrowings due after more than one year	18	-	-	-	-	-	(1,878)	(1,878)	(1,888)	
Total financial liabilities		-	(33)	(41)	-	-	(2,554)	(2,628)	(2,652)	

**15 Other financial assets**

All figures in £ millions	2015	2014
At beginning of year	54	94
Exchange differences	3	6
Acquisition of investments	101	12
Disposal of investments	(15)	(58)
At end of year	143	54

Other financial assets comprise listed securities of £nil (2014 £9m) and unlisted securities of £143m (2014 £45m). Acquisition of investments includes the remaining 11% stake in The Economist, see note 31 for further information.

**16 Derivative financial instruments**

The Group's approach to the management of financial risks is set out in note 19. The Group's outstanding derivative financial instruments are as follows:

All figures in £ millions	2015			2014		
	Gross notional amounts	Assets	Liabilities	Gross notional amounts	Assets	Liabilities
Interest rate derivatives – in a fair value hedge relationship	1,952	70	(10)	1,607	84	(5)
Interest rate derivatives – not in a hedge relationship	848	-	(6)	673	-	(7)
Cross-currency rate derivatives – in a hedge relationship	1,879	10	(119)	889	24	(36)
Cross-currency rate derivatives – not in a hedge relationship	120	30	(30)	451	6	(26)
<b>Total</b>	<b>4,799</b>	<b>110</b>	<b>(165)</b>	<b>3,620</b>	<b>114</b>	<b>(74)</b>
<b>Analysed as expiring</b>						
In less than one year	324	32	(29)	200	24	(1)
Later than one year and not later than five years	1,255	44	(4)	1,386	67	(8)
Later than five years	3,220	34	(132)	2,034	23	(65)
<b>Total</b>	<b>4,799</b>	<b>110</b>	<b>(165)</b>	<b>3,620</b>	<b>114</b>	<b>(74)</b>

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## Notes to the consolidated financial statements continued

## 16 Derivative financial instruments continued

The carrying value of the above derivative financial instruments equals their fair value. Fair values are determined by using market data and the use of established estimation techniques such as discounted cash flow and option valuation models.

At the end of 2015, the currency split of the mark-to-market values of rate derivatives, including the exchange of principal on cross-currency rate derivatives, was US dollar £(917)m, sterling £102m, euro £759m and Brazilian real £nil (2014 US dollar £(607)m, sterling £214m, euro £430m and Brazilian real £4m).

The fixed interest rates on outstanding rate derivative contracts at the end of 2015 range from 1.10% to 14.48% (2014 1.10% to 14.48%) and the floating rates are based on LIBOR in US dollar, euro and sterling.

The Group's portfolio of rate derivatives is diversified by maturity, counterparty and type. Natural offsets between transactions within the portfolio and the designation of certain derivatives as hedges significantly reduce the risk of income statement volatility. The sensitivity of the portfolio to changes in market rates is set out in note 19.

Derivative financial assets and liabilities subject to offsetting arrangements are as follows:

	2015			2014		
	Gross derivative assets	Gross derivative liabilities	Net derivative assets/liabilities	Gross derivative assets	Gross derivative liabilities	Net derivative assets/liabilities
All figures in £ millions						
Counterparties in an asset position	50	(22)	28	94	(28)	66
Counterparties in a liability position	60	(143)	(83)	20	(46)	(26)
Total as presented in the balance sheet	110	(165)	(55)	114	(74)	40

All of the Group's derivative financial instruments are subject to enforceable netting arrangements with individual counterparties, allowing net settlement in the event of default of either party. Offset arrangements in respect of cash balances are shown in note 17.

Counterparty exposure from all derivatives is managed, together with that from deposits and bank account balances, within credit limits that reflect published credit ratings and by reference to other market measures (e.g. market prices for credit default swaps) to ensure that there is no significant risk to any one counterparty. No single derivative transaction had a market value (positive or negative) at the balance sheet date that exceeded 3% of the Group's consolidated total equity.

In accordance with IAS 39 'Financial Instruments: Recognition and Measurement' the Group has reviewed all of its material contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements, and has concluded that there are no material embedded derivatives.

**17 Cash and cash equivalents (excluding overdrafts)**

All figures in £ millions	2015	2014
Cash at bank and in hand	627	483
Short-term bank deposits	1,076	47
	<b>1,703</b>	<b>530</b>

Short-term bank deposits are invested with banks and earn interest at the prevailing short-term deposit rates

At the end of 2015 the currency split of cash and cash equivalents was US dollar 23% (2014 18%), sterling 57% (2014 13%), euro 2% (2014 3%), renminbi 8% (2014 28%) and other 10% (2014 38%)

Cash and cash equivalents have fair values that approximate to their carrying value due to their short-term nature  
Cash and cash equivalents include the following for the purpose of the cash flow statement

All figures in £ millions	2015	2014
Cash and cash equivalents – continuing operations	1,703	530
Bank overdrafts – continuing operations	(32)	(19)
	<b>1,671</b>	<b>511</b>

The Group has the following cash pooling arrangements in US dollars, sterling, euro and canadian dollars where both the company and the bank have a legal right of offset

All figures in £ millions	2015			2014		
	Offset asset	Offset liability	Net offset asset	Offset asset	Offset liability	Net offset asset
US dollars	446	(442)	4	267	(266)	1
Sterling	290	(289)	1	430	(427)	3
Euro	5	(3)	2	9	(8)	1
Canadian dollars	36	(10)	26	10	–	10
<b>Total for continuing operations as presented in the balance sheet</b>			<b>33</b>			<b>15</b>

Offset arrangements in respect of derivatives are shown in note 16

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**18 Financial liabilities – borrowings**

The Group's current and non-current borrowings are as follows

All figures in £ millions	2015	2014
<b>Non-current</b>		
4 0% US dollar notes 2016 (nominal amount \$350m)	-	231
6 25% Global dollar bonds 2018 (nominal amount \$550m)	403	390
4 625% US dollar notes 2018 (nominal amount \$300m)	218	210
1 875% Euro notes 2021 (nominal amount €500m)	386	408
3 75% US dollar notes 2022 (nominal amount \$500m)	342	319
3 25% US dollar notes 2023 (nominal amount \$500m)	336	315
1 375% Euro notes 2025 (nominal amount €500m)	359	-
Bank loans and overdrafts	-	5
Finance lease liabilities	4	5
	<b>2,048</b>	<b>1,883</b>
<b>Current</b>		
Due within one year or on-demand		
6 0% Sterling bonds 2015 (nominal amount £300m)	-	300
4 0% US dollar notes 2016 (nominal amount \$350m)	240	-
Bank loans and overdrafts	38	37
Finance lease liabilities	4	5
	<b>282</b>	<b>342</b>
<b>Total borrowings</b>	<b>2,330</b>	<b>2,225</b>

Included in the non-current borrowings above is £15m of accrued interest (2014 £13m) Included in the current borrowings above is £1m of accrued interest (2014 £1m)

The maturity of the Group's non-current borrowing is as follows

All figures in £ millions	2015	2014
Between one and two years	3	239
Between two and five years	622	602
Over five years	1,423	1,042
	<b>2,048</b>	<b>1,883</b>

## 18 Financial liabilities – borrowings continued

The carrying amounts and market values of borrowings are as follows

All figures in £ millions	2015			2014		
	Effective interest rate	Carrying value	Market value	Effective interest rate	Carrying value	Market value
Bank loans and overdrafts	n/a	38	38	n/a	42	42
6.0% Sterling bonds 2015	–	–	–	6.27%	300	314
4.0% US dollar notes 2016	4.26%	240	240	4.26%	231	233
6.25% Global dollar bonds 2018	6.46%	403	405	6.46%	390	397
4.625% US dollar notes 2018	4.69%	218	213	4.69%	210	205
1.875% Euro notes 2021	2.04%	386	380	2.04%	408	407
3.75% US dollar notes 2022	3.94%	342	335	3.94%	319	327
3.25% US dollar notes 2023	3.36%	336	322	3.36%	315	314
1.375% Euro notes 2025	1.44%	359	350	n/a	–	–
Finance lease liabilities	n/a	8	8	n/a	10	10
		2,330	2,291		2,225	2,249

The market values stated above are based on clean market prices at the year end or, where these are not available, on the quoted market prices of comparable debt issued by other companies. The effective interest rates above relate to the underlying debt instruments.

The carrying amounts of the Group's borrowings are denominated in the following currencies

All figures in £ millions	2015	2014
US dollar	1,563	1,491
Sterling	1	303
Euro	759	408
Other	7	23
	2,330	2,225

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## Notes to the consolidated financial statements continued

**18 Financial liabilities – borrowings continued**

The Group has the following undrawn capacity on its committed borrowing facilities as at 31 December

All figures in £ millions	2015	2014
<b>Floating rate</b>		
– expiring within one year	–	–
– expiring beyond one year	1,187	1,122
	<b>1,187</b>	<b>1,122</b>

In addition to the above facilities, there are a number of short-term facilities that are utilised in the normal course of business

All of the Group's borrowings are unsecured. In respect of finance lease obligations, the rights to the leased asset revert to the lessor in the event of default

The maturity of the Group's finance lease obligations is as follows

All figures in £ millions	2015	2014
<b>Finance lease liabilities – minimum lease payments</b>		
Not later than one year	4	5
Later than one year and not later than two years	3	3
Later than two years and not later than three years	1	1
Later than three years and not later than four years	–	1
Later than four years and not later than five years	–	–
Later than five years	–	–
Future finance charges on finance leases	–	–
<b>Present value of finance lease liabilities</b>	<b>8</b>	<b>10</b>

The present value of finance lease liabilities is as follows

All figures in £ millions	2015	2014
Not later than one year	4	5
Later than one year and not later than five years	4	5
Later than five years	–	–
	<b>8</b>	<b>10</b>

The carrying amounts of the Group's lease obligations approximate their fair value

## 19 Financial risk management

The Group's approach to the management of financial risks together with sensitivity analyses of its financial instruments is set out below

### Treasury policy

The Group holds financial instruments for two principal purposes: to finance its operations and to manage the interest rate and currency risks arising from its operations and its sources of finance. The Group finances its operations by a mixture of cash flows from operations, short-term borrowings from banks and commercial paper markets, and longer-term loans from banks and capital markets. The Group borrows principally in US dollars, euros and sterling, at both floating and fixed rates of interest, using derivative financial instruments ('derivatives'), where appropriate, to generate the desired currency profile and interest rate basis. The derivatives used for this purpose are principally rate swaps, rate caps and collars, currency rate swaps and forward foreign exchange contracts. The main risks arising from the Group's financial instruments are interest rate risk, liquidity and refinancing risk, counterparty risk and foreign currency risk. These risks are managed by the chief financial officer under policies approved by the board, which are summarised in this note. All the key treasury policies remained unchanged throughout the year, except for revisions to the Group's bank counterparty risk limits and clarifications in respect of the Group's approach to compliance with laws and regulations.

The audit committee receives regular reports on the Group's treasury activities, policies and procedures.

The treasury department is not a profit centre and its activities are subject to regular internal audit.

### Liquidity and refinancing risk management

The Group's objective is to secure continuity of funding at a reasonable cost. To do this it seeks to arrange committed funding for a variety of maturities from a diversity of sources. The Group's policy objective is to maintain the weighted average maturity of its core gross borrowings (treating short-term advances as having the final maturity of the facilities available to refinance them) to be between three and ten years. At the end of 2015 the average maturity of gross borrowings was 5.1 years (2014: 4.7 years) of which bonds represented 98% (2014: 97%) of these borrowings.

The Group believes that ready access to different funding markets also helps to reduce its liquidity risk, and that published credit ratings and published financial policies improve such access. At the year end, the long-term ratings were Baa1 from Moody's and BBB+ from Standard & Poor's, and the short-term ratings were P2 and A2 respectively. All of the Group's credit ratings remained unchanged during the year, although in October 2015, Standard & Poor's changed the outlook on their long-term rating from 'Stable' to 'Negative'. In February 2016, Moody's changed Pearson's long-term rating from Baa1 (negative) to Baa2 (stable). In March 2016, Standard & Poor's changed Pearson's long-term rating from BBB+ (Negative) to BBB (Stable). The short-term ratings from Moody's and Standard & Poor's remain unchanged at P2 and A2. The Group's policy is to strive to maintain a rating of Baa1/BBB+ over the long term. The Group also uses a range of ratios to monitor and manage its finances internally. These include interest cover, net debt to operating profit and cash flow to debt measures. The Group also maintains undrawn committed borrowing facilities. At the end of 2015 the committed facilities amounted to \$1,750m (£1,187m) and their weighted average maturity was 4.6 years.

### Interest rate risk management

The Group's exposure to interest rate fluctuations on its borrowings is managed by borrowing on a fixed rate basis and by entering into rate swaps, rate caps and forward rate agreements. The Group also aims to avoid undue exposure to a single interest rate setting. Reflecting this objective, the Group has predominantly swapped its fixed rate bond issues to floating rate at their launch. This creates a group of derivatives, under which the Group is a receiver of fixed rates and a payer of floating rates.

The Group's policy objective has continued to be to set a target proportion of its forecast borrowings (taken at the year end, with cash netted against floating rate debt and before certain adjustments for IAS 39) to be hedged (i.e. fixed or capped at the year end) over the next four years, subject to a maximum of 65% and a minimum that starts at 40% and falls by 10% at each year end. At the end of 2015 the fixed to floating hedging ratio, on the above basis, was approximately 90%. The higher than policy ratio is a result of higher cash balances due to divestments in 2015. Our policy is to not close out contracts where we anticipate reverting to compliance with the policy over the longer term. A simultaneous 1% change on 1 January 2016 in the Group's variable interest rates in US dollar and sterling, taking into account forecast seasonal debt, would have a £6m effect on profit before tax.



## Notes to the consolidated financial statements continued

### 19 Financial risk management continued

#### Interest rate risk management continued

The policy described above creates a further group of derivatives, under which the Group is a payer of fixed rates and a receiver of floating rates. The Group's accounting objective in relation to its use of interest rate derivatives is to minimise the impact on the income statement of changes in the mark-to-market value of its derivative portfolio as a whole. It uses duration calculations to estimate the sensitivity of the derivatives to movements in market rates. The Group also identifies which derivatives are eligible for fair value hedge accounting (which reduces the income statement impact of changes in the market value of a derivative). The Group then balances the total portfolio between hedge-accounted and pooled segments, so that the expected movement on the pooled segment is minimal.

#### Financial counterparty risk management

Counterparty credit limits, which take published credit rating and other factors into account, are set to cover the Group's total aggregate exposure to a single financial institution. The limits applicable to published credit ratings bands are approved by the chief financial officer within guidelines approved by the board. Exposures and limits applicable to each financial institution are reviewed on a regular basis.

#### Foreign currency risk management

Although the Group is based in the UK, it has its most significant investment in overseas operations. The most significant currency for the Group is the US dollar. The Group's policy on routine transactional conversions between currencies (for example, the collection of receivables, and the settlement of payables or interest) remains that these should be transacted at the relevant spot exchange rate. The majority of the Group's operations are domestic within their country of operation. No unremitted profits are hedged with foreign exchange contracts, as the company judges it inappropriate to hedge non cash flow translational exposure with cash flow instruments. However, the Group does seek to create a natural hedge of this exposure through its policy of aligning approximately the currency composition of its core net borrowings (after the impact of cross-currency rate derivatives) with its forecast operating profit before depreciation and amortisation. This policy aims to soften the impact of changes in foreign exchange rates on consolidated interest cover and earnings. The policy above applies only to currencies that account for more than 15% of Group operating profit before depreciation and amortisation, which currently is only the US dollar. The Group still borrows small amounts in other currencies, typically for seasonal working capital needs. The Group policy does not require existing currency debt to be terminated to match declines in that currency's share of Group operating profit before depreciation and amortisation. In addition, currencies that account for less than 15% of Group operating profit before depreciation and amortisation can be included in the above hedging process at the request of the chief financial officer.

Included within year end net debt, the net borrowings/(cash) in the hedging currencies above (taking into account the effect of cross-currency swaps) were US dollar £1,345m and sterling £(385)m.

#### Use of currency debt and currency derivatives

The Group uses both currency denominated debt and derivative instruments to implement the above policy.

Its intention is that gains/losses on the derivatives and debt offset the losses/gains on the foreign currency assets and income. Each quarter the value of hedging instruments is monitored against the assets in the relevant currency and, where practical, a decision is made whether to treat the debt or derivative as a net investment hedge (permitting foreign exchange movements on it to be taken to reserves) for the purposes of IAS 39.

## 19 Financial risk management continued

### Analysis of Group debt, including the impact of derivatives

The following tables analyse the Group's sources of funding and the impact of derivatives on the Group's debt instruments

The Group's net debt position is set out below

All figures in £ millions	2015	2014
Cash and cash equivalents	1,703	530
Marketable securities	28	16
Derivative financial instruments	(55)	40
Bank loans, overdrafts and loan notes	(38)	(42)
Bonds	(2,284)	(2,173)
Finance lease liabilities	(8)	(10)
<b>Net debt</b>	<b>(654)</b>	<b>(1,639)</b>

The split of net debt between fixed and floating rate, stated after the impact of rate derivatives, is as follows

All figures in £ millions	2015	2014
Fixed rate	577	597
Floating rate	77	1,042
<b>Total</b>	<b>654</b>	<b>1,639</b>

Gross borrowings, after the impact of cross-currency rate derivatives, analysed by currency are as follows

All figures in £ millions	2015	2014
US dollar	2,308	2,099
Sterling	1	104
Other	21	22
<b>Total</b>	<b>2,330</b>	<b>2,225</b>

As at 31 December 2015 the exposure of the borrowings of the Group to interest rate changes when the borrowings re-price is as follows

All figures in £ millions	Less than one year	One to five years	More than five years	Total
Re-pricing profile of borrowings	282	625	1,423	2,330
Effect of rate derivatives	1,449	(33)	(1,416)	-
<b>Total</b>	<b>1,731</b>	<b>592</b>	<b>7</b>	<b>2,330</b>

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## Notes to the consolidated financial statements continued

## 19 Financial risk management continued

The maturity of contracted cash flows associated with the Group's financial liabilities is as follows

All figures in £ millions				2015
	USD	GBP	Other	Total
Not later than one year	470	58	73	601
Later than one year and not later than five years	705	-	-	705
Later than five years	1,578	-	-	1,578
<b>Total</b>	<b>2,753</b>	<b>58</b>	<b>73</b>	<b>2,884</b>
<b>Analysed as</b>				
Bonds	1,745	-	829	2,574
Rate derivatives – inflows	(335)	(858)	(919)	(2,112)
Rate derivatives – outflows	1,155	858	90	2,103
Trade payables	188	58	73	319
<b>Total</b>	<b>2,753</b>	<b>58</b>	<b>73</b>	<b>2,884</b>

All figures in £ millions				2014
	USD	GBP	Other	Total
Not later than one year	398	160	99	657
Later than one year and not later than five years	877	-	-	877
Later than five years	1,126	-	-	1,126
<b>Total</b>	<b>2,401</b>	<b>160</b>	<b>99</b>	<b>2,660</b>
<b>Analysed as</b>				
Bonds	1,711	318	439	2,468
Rate derivatives – inflows	(379)	(656)	(537)	(1,572)
Rate derivatives – outflows	893	444	98	1,435
Trade payables	176	54	99	329
<b>Total</b>	<b>2,401</b>	<b>160</b>	<b>99</b>	<b>2,660</b>

All cash flow projections shown above are on an undiscounted basis. Any cash flows based on a floating rate are calculated using interest rates as set at the date of the last rate reset. Where this is not possible, floating rates are based on interest rates prevailing at 31 December in the relevant year. All derivative amounts are shown gross, although the Group net settles these amounts wherever possible.

Any amounts drawn under revolving credit facilities and commercial paper are assumed to mature at the maturity date of the relevant facility, with interest calculated as payable in each calendar year up to and including the date of maturity of the facility.

## 19 Financial risk management continued

### Financial instruments – fair value measurement

The following table provides an analysis of those financial instruments that are measured subsequently to initial recognition at fair value, grouped into levels 1 to 3, based on the degree to which the fair value is observable

Level 1 fair value measurements are those derived from unadjusted quoted prices in active markets for identical assets or liabilities,

Level 2 fair value measurements are those derived from inputs, other than quoted prices included within level 1, that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices), and

Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs)

All figures in £ millions	2015				2014			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
<b>Financial assets at fair value</b>								
Derivative financial assets	-	110	-	110	-	114	-	114
Marketable securities	-	28	-	28	-	16	-	16
<b>Available for sale financial assets</b>								
Investments in listed securities	-	-	-	-	-	9	-	9
Investments in unlisted securities	-	-	143	143	-	-	45	45
<b>Financial liabilities at fair value</b>								
Derivative financial liabilities	-	(165)	-	(165)	-	(74)	-	(74)
<b>Total</b>	-	(27)	143	116	-	65	45	110

The following table analyses the movements in level 3 fair value measurements

All figures in £ millions	2015	2014
	Investments in unlisted securities	Investments in unlisted securities
At beginning of year	45	94
Exchange differences	3	6
Additions	101	3
Fair value movements	-	-
Disposals	(6)	(58)
<b>At end of year</b>	<b>143</b>	<b>45</b>

The fair value of the 11% stake in The Economist is valued by reference to the disposal transaction terms. The fair value of the remaining investments in unlisted securities is determined by reference to the financial performance of the underlying asset and amounts realised on the sale of similar assets.

## Notes to the consolidated financial statements continued

## 19 Financial risk management continued

## Financial instruments – sensitivity analysis

As at 31 December 2015 the sensitivity of the carrying value of the Group's financial instruments to fluctuations in interest rates and exchange rates is as follows

All figures in £ millions	Carrying value	Impact of 1% increase in interest rates	Impact of 1% decrease in interest rates	Impact of 10% strengthening in sterling	Impact of 10% weakening in sterling
Investments in listed securities	-	-	-	-	-
Investments in unlisted securities	143	-	-	(4)	5
Cash and cash equivalents	1,703	-	-	(67)	82
Marketable securities	28	-	-	-	-
Derivative financial instruments	(55)	(93)	99	14	(18)
Bonds	(2,284)	97	(103)	208	(254)
Other borrowings	(46)	-	-	5	(6)
Other net financial assets	644	-	-	(57)	68
<b>Total financial instruments</b>	<b>133</b>	<b>4</b>	<b>(4)</b>	<b>99</b>	<b>(123)</b>

The table shows the sensitivities of the fair values of each class of financial instruments to an isolated change in either interest rates or foreign exchange rates. The class 'Other net financial assets' comprises trade receivables less trade payables.

The sensitivities of derivative instruments are calculated using established estimation techniques such as discounted cash flow and option valuation models. Where modelling an interest rate decrease of 1% led to negative interest rates, these points on the yield curve were adjusted to 0%. A large proportion of the movements shown above would impact equity rather than the income statement, due to the location and functional currency of the entities in which they arise and the availability of net investment hedge treatment. The changes in valuations are estimates of the impact of changes in market variables and are not a prediction of future events or anticipated gains or losses.

**20 Intangible assets – Pre-publication**

All figures in £ millions	2015	2014
<b>Cost</b>		
At beginning of year	2,138	1,933
Exchange differences	66	80
Additions	347	358
Disposal through business disposal	(90)	-
Disposals	(260)	(234)
Acquisition through business combination	-	1
At end of year	2,201	2,138
<b>Amortisation</b>		
At beginning of year	(1,318)	(1,216)
Exchange differences	(47)	(60)
Charge for the year	(281)	(292)
Disposal through business disposal	26	-
Disposals	260	234
Transfer to receivables	-	16
At end of year	(1,360)	(1,318)
<b>Carrying amounts</b>		
At end of year	841	820

Included in the above are pre-publication assets amounting to £580m (2014 £546m) which will be realised in more than one year

Amortisation is included in the income statement in cost of goods sold. There was no amortisation within discontinued operations in either year.

Disposal through business disposal amounts relate to the disposal of PowerSchool, see note 31 for further information.

**21 Inventories**

All figures in £ millions	2015	2014
Raw materials	8	9
Work in progress	8	10
Finished goods	195	205
	211	224

The cost of inventories relating to continuing operations recognised as an expense and included in the income statement in cost of goods sold amounted to £331m (2014 £379m). In 2015, £33m (2014 £38m) of inventory provisions was charged in the income statement. None of the inventory is pledged as security.

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**22 Trade and other receivables**

All figures in £ millions	2015	2014
<b>Current</b>		
Trade receivables	938	963
Royalty advances	20	18
Prepayments and accrued income	118	107
Other receivables	208	222
	1,284	1,310
<b>Non-current</b>		
Trade receivables	25	26
Royalty advances	13	8
Prepayments and accrued income	43	30
Other receivables	34	18
	115	82

Trade receivables are stated at fair value, net of provisions for bad and doubtful debts and anticipated future sales returns. The movements on the provision for bad and doubtful debts are as follows

All figures in £ millions	2015	2014
At beginning of year	(73)	(58)
Exchange differences	3	-
Income statement movements	(31)	(21)
Utilised	32	17
Acquisition through business combination	-	(11)
Disposal through business disposal	5	-
At end of year	(64)	(73)

Concentrations of credit risk with respect to trade receivables are limited due to the Group's large number of customers, who are internationally dispersed

The ageing of the Group's trade receivables is as follows

All figures in £ millions	2015	2014
Within due date	754	869
Up to three months past due date	253	203
Three to six months past due date	58	40
Six to nine months past due date	19	15
Nine to 12 months past due date	13	15
More than 12 months past due date	16	11
<b>Total trade receivables</b>	<b>1,113</b>	<b>1,153</b>
Less provision for sales returns	(150)	(164)
<b>Net trade receivables</b>	<b>963</b>	<b>989</b>

The Group reviews its bad debt provision at least twice a year following a detailed review of receivable balances and historical payment profiles. Management believes all the remaining receivable balances are fully recoverable

## 23 Provisions for other liabilities and charges

All figures in £ millions	Deferred consideration	Property	Disposals and closures	Legal and other	Total
At 1 January 2015	57	7	20	51	135
Exchange differences	3	-	-	(4)	(1)
Charged to income statement	-	-	-	12	12
Released to income statement	(1)	-	-	(4)	(5)
Disposal through business disposal	-	(1)	-	(1)	(2)
Utilised	(6)	-	-	(20)	(26)
At 31 December 2015	53	6	20	34	113

## Analysis of provisions

	2015				
All figures in £ millions	Deferred consideration	Property	Disposals and closures	Legal and other	Total
Current	5	3	15	19	42
Non-current	48	3	5	15	71
	53	6	20	34	113
	2014				
Current	7	4	20	22	53
Non-current	50	3	-	29	82
	57	7	20	51	135

Deferred consideration primarily relates to the formation of a venture in a North America business in 2011  
 Disposals and closures include liabilities related to the disposal of Penguin. Legal and other includes legal claims, contract disputes and potential contract losses

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## Notes to the consolidated financial statements continued

**24 Trade and other liabilities**

All figures in £ millions	2015	2014
Trade payables	319	329
Social security and other taxes	22	21
Accruals	371	501
Deferred income	766	801
Interest payable	19	28
Other liabilities	249	231
	<b>1,746</b>	<b>1,911</b>
<b>Less, non-current portion</b>		
Accruals	20	22
Deferred income	262	201
Interest payable	-	19
Other liabilities	74	68
	<b>356</b>	<b>310</b>
<b>Current portion</b>	<b>1,390</b>	<b>1,601</b>

The carrying value of the Group's trade and other liabilities approximates its fair value

The deferred income balance comprises principally multi-year obligations to deliver workbooks to adoption customers in school businesses, advance payments in assessment, testing and training businesses, subscription income in school and college businesses, and obligations to deliver digital content in future periods

**25 Retirement benefit and other post-retirement obligations****Background**

The Group operates a number of defined benefit and defined contribution retirement plans throughout the world

The largest plan is the Pearson Group Pension Plan (UK Group plan) in the UK, which is sectionalised to provide both defined benefit and defined contribution pension benefits. The defined benefit section was closed to new members from 1 November 2006. The defined contribution section, opened in 2003, is open to new and existing employees. Finally, there is a separate section within the UK Group plan set up for auto-enrolment. The defined benefit section of the UK Group plan is a final salary pension plan which provides benefits to members in the form of a guaranteed level of pension payable for life. The level of benefits depends on the length of service and final pensionable pay. The UK Group plan is funded with benefit payments from trustee administered funds. The UK Group plan is administered in accordance with the Trust Deed and Rules in the interests of its beneficiaries by Pearson Group Pension Trustee Limited.

At 31 December 2015 the UK Group plan has approximately 25,000 members, analysed in the following table

All figures in %	Active	Deferred	Pensioners	Total
Defined benefit	1	27	34	62
Defined contribution	14	24	-	38
<b>Total</b>	<b>15</b>	<b>51</b>	<b>34</b>	<b>100</b>

## 25 Retirement benefit and other post-retirement obligations continued

### Background continued

The other major defined benefit plans are based in the US. These are also final salary pension plans which provide benefits to members in the form of a guaranteed pension payable for life, with the level of benefits dependent on length of service and final pensionable pay. The majority of the US plans are funded.

The Group also has several post-retirement medical benefit plans (PRMBs), principally in the US. PRMBs are unfunded but are accounted for and valued similarly to defined benefit pension plans.

The defined benefit schemes expose the Group to actuarial risks, such as life expectancy, inflation risks, and investment risk including asset volatility and changes in bond yields. The Group is not exposed to any unusual, entity specific or plan specific risks.

### Assumptions

The principal assumptions used for the UK Group plan and the US PRMB are shown below. Weighted average assumptions have been shown for the other plans, which primarily relate to US pension plans.

All figures in %	2015			2014		
	UK Group plan	Other plans	PRMB	UK Group plan	Other plans	PRMB
Inflation	3.1	2.5	2.5	3.0	2.5	2.5
Rate used to discount plan liabilities	3.7	4.0	4.0	3.6	3.7	3.7
Expected rate of increase in salaries	3.6	3.0	3.0	3.5	3.9	4.0
Expected rate of increase for pensions in payment and deferred pensions	1.9 to 5.10	-	-	1.9 to 5.05	-	-
Initial rate of increase in healthcare rate	-	-	7.0	-	-	7.0
Ultimate rate of increase in healthcare rate	-	-	5.0	-	-	5.0

The UK discount rate is based on corporate bond yields adjusted to reflect the duration of liabilities. The US discount rate is set by reference to a US bond portfolio matching model.

The inflation rate for the UK Group plan of 3.1% reflects the RPI rate. In line with changes to legislation in 2010, certain benefits have been calculated with reference to CPI as the inflationary measure and in these instances a rate of 2.1% has been used.

The expected rate of increase in salaries has been set at 3.6% for 2015 with a short-term assumption of 2.0% for three years.

For the UK plan, the mortality base table assumptions have been derived from the SAPS 'all pensioners' tables for males and the SAPS 'normal health pensioners' tables for females, adjusted to reflect the observed experience of the plan, with CMI model improvement factors. A 1.5% long-term rate improvement on the CMI model is applied for both males and females.

For the US plans, the mortality table (RP - 2014) and 2014 Improvement scale (MP - 2014) with no adjustments have been adopted from 2014, reflecting the mortality assumption most prevalent in the US.

## Notes to the consolidated financial statements continued

**25 Retirement benefit and other post-retirement obligations continued****Assumptions continued**

Using the above tables, the remaining average life expectancy in years of a pensioner retiring at age 65 on the balance sheet date for the UK Group plan and US plans is as follows

All figures in years	UK		US	
	2015	2014	2015	2014
Male	23.5	24.4	21.2	21.6
Female	25.6	24.5	23.2	23.8

The remaining average life expectancy in years of a pensioner retiring at age 65, 20 years after the balance sheet date, for the UK and US Group plans is as follows

All figures in years	UK		US	
	2015	2014	2015	2014
Male	25.5	26.6	22.9	23.3
Female	27.8	26.4	24.9	25.5

Although the Group anticipates that plan surpluses will be utilised during the life of the plan to address member benefits, the Group recognises its pension surplus in full in respect of the UK Group plan on the basis that it is management's judgement that there are no substantive restrictions on the return of residual plan assets in the event of a winding up of the plan after all member obligations have been met

**Financial statement information**

The amounts recognised in the income statement are as follows

All figures in £ millions	2015					Total
	UK Group plan	Defined benefit other	Sub-total	Defined contribution	PRMB	
Current service cost	20	2	22	74	-	96
Curtailments	(3)	-	(3)	-	-	(3)
Administration expenses	5	-	5	-	-	5
<b>Total operating expense</b>	<b>22</b>	<b>2</b>	<b>24</b>	<b>74</b>	<b>-</b>	<b>98</b>
Interest on plan assets	(98)	(5)	(103)	-	-	(103)
Interest on plan liabilities	90	7	97	-	2	99
<b>Net finance (income)/expense</b>	<b>(8)</b>	<b>2</b>	<b>(6)</b>	<b>-</b>	<b>2</b>	<b>(4)</b>
<b>Net income statement charge</b>	<b>14</b>	<b>4</b>	<b>18</b>	<b>74</b>	<b>2</b>	<b>94</b>

## 25 Retirement benefit and other post-retirement obligations continued

## Financial statement information continued

	2014					
All figures in £ millions	UK Group plan	Defined benefit other	Sub-total	Defined contribution	PRMB	Total
Current service cost	20	2	22	69	2	93
Curtailments	(5)	-	(5)	-	(13)	(18)
Administration expenses	4	-	4	-	-	4
<b>Total operating expense</b>	<b>19</b>	<b>2</b>	<b>21</b>	<b>69</b>	<b>(11)</b>	<b>79</b>
Interest on plan assets	(103)	(7)	(110)	-	-	(110)
Interest on plan liabilities	98	8	106	-	3	109
<b>Net finance (income)/expense</b>	<b>(5)</b>	<b>1</b>	<b>(4)</b>	<b>-</b>	<b>3</b>	<b>(1)</b>
<b>Net income statement charge/(income)</b>	<b>14</b>	<b>3</b>	<b>17</b>	<b>69</b>	<b>(8)</b>	<b>78</b>

Included within the 2015 results are discontinued operations consisting of a £5m charge (2014: £nil) relating to defined benefit schemes and a £8m charge (2014: £8m charge) relating to defined contribution schemes

The amounts recognised in the balance sheet are as follows

	2015				2014			
All figures in £ millions	UK Group plan	Other funded plans	Other unfunded plans	Total	UK Group plan	Other funded plans	Other unfunded plans	Total
Fair value of plan assets	2,803	135	-	2,938	2,714	164	-	2,878
Present value of defined benefit obligation	(2,466)	(157)	(18)	(2,641)	(2,524)	(196)	(23)	(2,743)
<b>Net pension asset/(liability)</b>	<b>337</b>	<b>(22)</b>	<b>(18)</b>	<b>297</b>	<b>190</b>	<b>(32)</b>	<b>(23)</b>	<b>135</b>
Other post-retirement medical benefit obligation				(76)				(81)
Other pension accruals				(23)				(27)
<b>Net retirement benefit asset</b>				<b>198</b>				<b>27</b>
<b>Analysed as:</b>								
Retirement benefit assets				<b>337</b>				<b>190</b>
Retirement benefit obligations				<b>(139)</b>				<b>(163)</b>

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## Notes to the consolidated financial statements continued

## 25 Retirement benefit and other post-retirement obligations continued

## Financial statement information continued

The following gains/(losses) have been recognised in other comprehensive income

All figures in £ millions	2015	2014
Amounts recognised for defined benefit plans	104	36
Amounts recognised for post-retirement medical benefit plans	6	(13)
<b>Total recognised in year</b>	<b>110</b>	<b>23</b>

The fair value of plan assets comprises the following

All figures in %	2015			2014		
	UK Group plan	Other funded plans	Total	UK Group plan	Other funded plans	Total
Equities	12	2	14	26	2	28
Bonds	8	2	10	42	3	45
Property	9	-	9	9	-	9
Qualifying investment fund	50	-	50	-	-	-
Other	17	-	17	17	1	18

The plan assets do not include any of the Group's own financial instruments, or any property occupied by the Group

The table below further disaggregates the UK Group plan assets into additional categories and those assets which have a quoted market price in an active market and those that do not

All figures in %	2015		2014	
	Quoted market price	No quoted market price	Quoted market price	No quoted market price
UK equities	-	1	5	1
Non-UK equities	11	2	20	2
Fixed-interest securities	6	-	19	-
Index-linked securities	4	-	26	-
Property	-	9	-	9
Qualifying investment fund	50	-	-	-
Other	-	17	-	18
<b>Total</b>	<b>71</b>	<b>29</b>	<b>70</b>	<b>30</b>

The liquidity profile of the UK Group plan assets is as follows

All figures in %	2015	2014
Liquid - call <1 month	73	72
Less liquid - call 1-3 months	2	2
Liquid - call >3 months	25	26

## 25 Retirement benefit and other post-retirement obligations continued

## Financial statement information continued

Changes in the values of plan assets and liabilities of the retirement benefit plans are as follows

All figures in £ millions	2015			2014		
	UK Group plan	Other plans	Total	UK Group plan	Other plans	Total
<b>Fair value of plan assets</b>						
Opening fair value of plan assets	2,714	164	2,878	2,353	156	2,509
Exchange differences	-	2	2	-	4	4
Interest on plan assets	98	5	103	103	7	110
Return on plans assets excluding interest	(8)	(4)	(12)	286	9	295
Contributions by employer	72	5	77	62	4	66
Contributions by employee	2	-	2	2	-	2
Benefits paid	(95)	(17)	(112)	(92)	(16)	(108)
Transfer	20	(20)	-	-	-	-
<b>Closing fair value of plan assets</b>	<b>2,803</b>	<b>135</b>	<b>2,938</b>	<b>2,714</b>	<b>164</b>	<b>2,878</b>
<b>Present value of defined benefit obligation</b>						
Opening defined benefit obligation	(2,524)	(219)	(2,743)	(2,267)	(191)	(2,458)
Exchange differences	-	(3)	(3)	-	(5)	(5)
Current service cost	(20)	(2)	(22)	(20)	(2)	(22)
Administration expenses	(5)	-	(5)	(4)	-	(4)
Curtailments	3	-	3	5	-	5
Interest cost	(90)	(7)	(97)	(98)	(8)	(106)
Actuarial gains/(losses) - experience	107	2	109	11	(1)	10
Actuarial gains/(losses) - demographic	(33)	1	(32)	-	(8)	(8)
Actuarial gains/(losses) - financial	33	6	39	(241)	(20)	(261)
Contributions by employee	(2)	-	(2)	(2)	-	(2)
Transfer	(30)	30	-	-	-	-
Benefits paid	95	17	112	92	16	108
<b>Closing defined benefit obligation</b>	<b>(2,466)</b>	<b>(175)</b>	<b>(2,641)</b>	<b>(2,524)</b>	<b>(219)</b>	<b>(2,743)</b>

The weighted average duration of the defined benefit obligation is 17.1 years for the UK and 8.7 years for the US

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## Notes to the consolidated financial statements continued

**25 Retirement benefit and other post-retirement obligations continued****Financial statement information continued**

Changes in the value of the US PRMB are as follows

All figures in £ millions	2015	2014
Opening defined benefit obligation	(81)	(77)
Exchange differences	(3)	(4)
Current service cost	-	(2)
Curtailments	-	13
Interest cost	(2)	(3)
Actuarial gains/(losses) – experience	2	-
Actuarial gains/(losses) – demographic	2	(7)
Actuarial gains/(losses) – financial	2	(6)
Benefits paid	4	5
<b>Closing defined benefit obligation</b>	<b>(76)</b>	<b>(81)</b>

**Funding**

The UK Group plan is self-administered with the plan's assets being held independently of the Group in trust. The trustee of the plan is required to act in the best interest of the plan's beneficiaries. The most recent triennial actuarial valuation for funding purposes was completed as at 1 January 2015 and this valuation revealed a technical provisions funding shortfall of £27m which was eliminated by contributions paid during 2015.

As a consequence of the disposal of the FT Group, an agreement has been made between Pearson and the Plan Trustee to accelerate the funding of the plan so that it becomes fully funded on a 'self-sufficiency' basis in the near future. This is a much higher level of funding than technical provisions. As a result the plan expects to be able to provide benefits (in accordance with the plan rules) with a very low level of reliance on future funding from Pearson. A commitment has also been made to maintain that level of funding in future years. In addition to a substantial company contribution following the Penguin Random House merger (to be paid before July 2017), an upfront contribution will be made to the plan following the disposal of the FT Group. This is expected to be approximately £90m and there will be further annual contributions to eliminate any remaining shortfall in the self-sufficiency funding.

At 31 December 2015, assets of the plan are divided into two elements: matching assets, which are assets that produce cash flows that can be expected to match the cash flows for a proportion of the membership, and include a Liability Driven Investment mandate (UK Bonds, interest rate/inflation swaps and other derivative instruments), inflation-linked property and infrastructure, and return seeking assets, which are assets invested with a longer-term horizon to generate the returns needed to provide the remaining expected cash flows for the beneficiaries, and include equities, property and alternative asset classes. During the fourth quarter of 2015 the plan's long-term investment strategy was updated to an allocation of 84.2% Matching Assets and 15.8% Return Seeking Assets as at 31 December 2015.

Regular contributions to the plan in respect of the defined benefit sections are estimated to be £8m for 2016.

The Group expects to contribute \$10m in 2016 and \$10m in 2017 to its US defined benefit pension plans.

## 25 Retirement benefit and other post-retirement obligations continued

### Sensitivities

The effect of a one percentage point increase and decrease in the discount rate on the defined benefit obligation and the total pension expense is as follows

All figures in £ millions	2015	
	1% increase	1% decrease
<b>Effect</b>		
(Decrease)/increase in defined benefit obligation – UK Group plan	(372)	495
(Decrease)/increase in defined benefit obligation – US plan	(16)	19

The effect of members living one year more or one year less on the defined benefit obligation is as follows

All figures in £ millions	2015	
	1 year increase	1 year decrease
<b>Effect</b>		
Increase/(decrease) in defined benefit obligation – UK Group plan	100	(96)
Increase/(decrease) in defined benefit obligation – US plan	7	(7)

The effect of a half percentage point increase and decrease in the inflation rate is as follows

All figures in £ millions	2015	
	0.5% increase	0.5% decrease
<b>Effect</b>		
Increase/(decrease) in defined benefit obligation – UK Group plan	113	(103)
Increase/(decrease) in defined benefit obligation – US plan	–	–

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant, although in practice this is unlikely to occur and changes in some assumptions may be correlated. When calculating these sensitivities the same method has been applied to calculate the defined benefit obligation as has been applied when calculating the liability recognised in the balance sheet. This methodology is the same as prior periods.

## 26 Share-based payments

The Group recognised the following charges in the income statement in respect of its equity-settled share-based payment plans

All figures in £ millions	2015	2014
Pearson plans	26	32

Share-based payment charges included in discontinued operations amounted to £3m (2014: £3m). The Group operates the following equity-settled employee option and share plans

**Worldwide Save for Shares Plan** Since 1994, the Group has operated a Save-As-You-Earn plan for UK employees. In 1998, the Group introduced a Worldwide Save for Shares Plan. Under these plans, employees can save a portion of their monthly salary over periods of three or five years. At the end of this period, the employee has the option to purchase ordinary shares with the accumulated funds at a purchase price equal to 80% of the market price prevailing at the time of the commencement of the employee's participation in the plan. Options that are not exercised within six months of the end of the savings period lapse unconditionally.



## Notes to the consolidated financial statements continued

**26 Share-based payments continued**

**Employee Stock Purchase Plan** In 2000, the Group established an Employee Stock Purchase Plan which allows all employees in the US to save a portion of their monthly salary over six-month periods. At the end of the period, the employee has the option to purchase ADRs with their accumulated funds at a purchase price equal to 85% of the lower of the market price prevailing at the beginning or end of the period.

**Long-Term Incentive Plan** This plan was first introduced in 2001, renewed in 2006 and again in 2011. The plan consists of restricted shares. The vesting of restricted shares is normally dependent on continuing service over a three to five-year period, and in the case of senior management upon the satisfaction of corporate performance targets over a three-year period. These targets may be based on market and/or non-market performance criteria. Restricted shares awarded to senior management in May 2014 and May 2015 vest dependent on relative total shareholder return, return on invested capital and earnings per share growth. Restricted shares awarded to senior management in November 2014 vest dependent on earnings per share growth. Other restricted shares awarded in 2014 and 2015 vest depending on continuing service over a three-year period.

The number and weighted average exercise prices of share options granted under the Group's plans are as follows:

	2015		2014	
	Number of share options 000s	Weighted average exercise price £	Number of share options 000s	Weighted average exercise price £
Outstanding at beginning of year	3,507	8.48	2,792	8.73
Granted during the year	1,024	11.49	1,985	8.11
Exercised during the year	(578)	8.78	(727)	8.24
Forfeited during the year	(696)	9.12	(538)	8.76
Expired during the year	(7)	8.85	(5)	7.43
Outstanding at end of year	3,250	9.24	3,507	8.48
Options exercisable at end of year	138	8.89	43	8.24

Options were exercised regularly throughout the year. The weighted average share price during the year was £11.86 (2014: £11.41). Early exercises arising from redundancy, retirement or death are treated as an acceleration of vesting and the Group therefore recognises in the income statement the amount that otherwise would have been recognised for services received over the remainder of the original vesting period.

The options outstanding at the end of the year have weighted average remaining contractual lives and exercise prices as follows:

Range of exercise prices £	2015		2014	
	Number of share options 000s	Weighted average contractual life Years	Number of share options 000s	Weighted average contractual life Years
0-5	-	-	-	-
5-10	2,361	2.08	3,507	2.68
>10	889	3.26	-	-
	3,250	2.40	3,507	2.68

In 2015 and 2014 options were granted under the Worldwide Save for Shares Plan. The weighted average estimated fair value for the options granted was calculated using a Black-Scholes option pricing model.

## 26 Share-based payments continued

The weighted average estimated fair values and the inputs into the Black-Scholes model are as follows

	2015 Weighted average	2014 Weighted average
Fair value	£1 99	£2 41
Weighted average share price	£13 37	£11 09
Weighted average exercise price	£11 49	£8 11
Expected volatility	23 00%	21 27%
Expected life	3 7 years	3 9 years
Risk-free rate	0 90%	1 3%
Expected dividend yield	4 44%	4 33%
Forfeiture rate	3 2%	3 4%

The expected volatility is based on the historical volatility of the company's share price over the previous three to seven years depending on the vesting term of the options

The following shares were granted under restricted share arrangements

	2015		2014	
	Number of shares 000s	Weighted average fair value £	Number of shares 000s	Weighted average fair value £
Long-Term Incentive Plan	1,942	12 27	5,875	11 44

The fair value of shares granted under the Long-Term Incentive Plan that vest unconditionally is determined using the share price at the date of grant. The number of shares expected to vest is adjusted, based on historical experience, to account for potential forfeitures. Restricted shares granted under the Annual Bonus Share Matching Plan are valued using the share price at the date of grant. Participants under both plans are entitled to dividends during the vesting period and therefore the share price is not discounted.

Restricted shares with a market performance condition were valued by an independent actuary using a Monte Carlo model. Restricted shares with a non-market performance condition were fair valued based on the share price at the date of grant. Non-market performance conditions are taken into consideration by adjusting the number of shares expected to vest based on the most likely outcome of the relevant performance criteria.

## Notes to the consolidated financial statements continued

**27 Share capital and share premium**

	Number of shares 000s	Ordinary shares £m	Share premium £m
At 1 January 2014	818,580	205	2,568
Issue of ordinary shares – share option schemes	1,303	–	11
At 31 December 2014	819,883	205	2,579
Issue of ordinary shares – share option schemes	1,185	–	11
At 31 December 2015	821,068	205	2,590

The ordinary shares have a par value of 25p per share (2014 25p per share) All issued shares are fully paid All shares have the same rights

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to shareholders through the optimisation of the debt and equity balance

The capital structure of the Group consists of debt (see note 18), cash and cash equivalents (see note 17) and equity attributable to equity holders of the parent, comprising issued capital, reserves and retained earnings

The Group reviews its capital structure on a regular basis and will balance its overall capital structure through payments of dividends, new share issues as well as the issue of new debt or the redemption of existing debt in line with the financial risk policies outlined in note 19

**28 Treasury shares**

	Pearson plc	
	Number of shares 000s	£m
At 1 January 2014	9,282	98
Purchase of treasury shares	907	9
Release of treasury shares	(2,997)	(32)
At 31 December 2014	7,192	75
Purchase of treasury shares	1,987	23
Release of treasury shares	(2,474)	(26)
At 31 December 2015	6,705	72

The Group holds Pearson plc shares in trust to satisfy its obligations under its restricted share plans (see note 26) These shares, representing 0.8% (2014 0.9%) of called-up share capital, are treated as treasury shares for accounting purposes and have a par value of 25p per share

The nominal value of Pearson plc treasury shares amounts to £1.7m (2014 £1.8m)

At 31 December 2015 the market value of Pearson plc treasury shares was £49.3m (2014 £85.6m)

## 29 Other comprehensive income

	2015				
All figures in £ millions	Attributable to equity holders of the company			Non controlling interest	Total
	Translation reserve	Retained earnings	Total		
Items that may be reclassified to the income statement					
Net exchange differences on translation of foreign operations – Group	(83)	–	(83)	(2)	(85)
Net exchange differences on translation of foreign operations – associate	16	–	16	–	16
Currency translation adjustment disposed – subsidiaries	(10)	–	(10)	–	(10)
Attributable tax	–	5	5	–	5
Items that are not reclassified to the income statement					
Remeasurement of retirement benefit obligations – Group	–	110	110	–	110
Remeasurement of retirement benefit obligations – associate	–	8	8	–	8
Attributable tax	–	(24)	(24)	–	(24)
Other comprehensive expense for the year	(77)	99	22	(2)	20

	2014				
All figures in £ millions	Attributable to equity holders of the company			Non controlling interest	Total
	Translation reserve	Retained earnings	Total		
Items that may be reclassified to the income statement					
Net exchange differences on translation of foreign operations – Group	150	–	150	–	150
Net exchange differences on translation of foreign operations – associate	25	–	25	–	25
Currency translation adjustment disposed – subsidiaries	(2)	–	(2)	–	(2)
Attributable tax	–	(6)	(6)	–	(6)
Items that are not reclassified to the income statement					
Remeasurement of retirement benefit obligations – Group	–	23	23	–	23
Remeasurement of retirement benefit obligations – associate	–	(15)	(15)	–	(15)
Attributable tax	–	(1)	(1)	–	(1)
Other comprehensive expense for the year	173	1	174	–	174

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**30 Business combinations**

There were no significant acquisitions in 2015. On 11 February 2014, the Group acquired 100% of Grupo Multi, the leading adult English language training company in Brazil. Fair values for the assets and liabilities arising from the Grupo Multi acquisition and other smaller acquisitions completed in the year are set out below.

Fair values for the assets and liabilities arising from acquisitions completed in the year are as follows:

All figures in £ millions	Notes	2015	2014
		Total fair value	Total fair value
Property, plant and equipment	10	-	2
Intangible assets	11	1	260
Intangible assets – pre-publication	20	-	1
Inventories		-	4
Trade and other receivables		-	36
Cash and cash equivalents (excluding overdrafts)		-	3
Financial liabilities – borrowings		-	(49)
Provisions for other liabilities and charges	23	-	(14)
Trade and other liabilities		-	(24)
Current income tax liabilities		-	(20)
<b>Net assets acquired at fair value</b>		<b>1</b>	<b>199</b>
Goodwill	11	-	238
<b>Total</b>		<b>1</b>	<b>437</b>
<b>Satisfied by</b>			
Cash		(1)	(437)
<b>Total consideration</b>		<b>(1)</b>	<b>(437)</b>

The goodwill arising on these acquisitions results from cost and revenue synergies and from assets and benefits that cannot be separately recognised.

There is no goodwill arising on 2015 acquisitions. Goodwill of £240m arising on 2014 acquisitions is expected to be deductible for tax purposes.

Intangible assets acquired in 2014 have the following useful economic lives: customer lists, contracts and relationships four years, trademarks and brands 20 years, and other acquired intangibles 12 years.

All figures in £ millions	2015	2014
<b>Cash flow on acquisitions</b>		
Cash – current year acquisitions	(1)	(437)
Deferred payments for prior year acquisitions and other items	(6)	(5)
Cash and cash equivalents acquired	-	3
Acquisition costs and other acquisition liabilities paid	(2)	(9)
<b>Net cash outflow</b>	<b>(9)</b>	<b>(448)</b>

## 31 Disposals including business closures

All figures in £ millions	2015				2014			
	FT Group	PowerSchool	Other	Total	Mergermarket	Penguin	Other	Total
<b>Disposal of subsidiaries</b>								
Property, plant and equipment	(15)	(2)	-	(17)	(2)	-	(1)	(3)
Intangible assets	(46)	(19)	(5)	(70)	(12)	-	-	(12)
Investments in joint ventures and associates	(8)	-	-	(8)	-	-	-	-
Intangible assets – pre-publication	-	(64)	-	(64)	-	-	-	-
Inventories	(1)	-	-	(1)	-	-	-	-
Trade and other receivables	(72)	(16)	(3)	(91)	(23)	-	(2)	(25)
Cash and cash equivalents (excluding overdrafts)	(29)	-	(4)	(33)	(19)	-	(11)	(30)
Net deferred income tax (assets)/liabilities	(2)	-	3	1	1	-	-	1
Retirement benefit obligations	7	-	-	7	-	-	-	-
Provisions for other liabilities and charges	2	-	-	2	4	-	-	4
Trade and other liabilities	109	35	6	150	69	-	12	81
Current income tax liabilities	1	-	-	1	6	-	-	6
Non-controlling interest	-	-	-	-	-	-	(2)	(2)
Attributable goodwill	(50)	(119)	(6)	(175)	(156)	-	(1)	(157)
Cumulative translation adjustment	4	6	-	10	2	-	-	2
<b>Net assets disposed</b>	<b>(100)</b>	<b>(179)</b>	<b>(9)</b>	<b>(288)</b>	<b>(130)</b>	<b>-</b>	<b>(5)</b>	<b>(135)</b>
Cash received	858	222	9	1,089	375	-	-	375
Deferred proceeds	-	-	-	-	-	-	6	6
Costs	(47)	(13)	(9)	(69)	(1)	29	(2)	26
<b>Gain/(loss) on disposal</b>	<b>711</b>	<b>30</b>	<b>(9)</b>	<b>732</b>	<b>244</b>	<b>29</b>	<b>(1)</b>	<b>272</b>

All figures in £ millions	2015	2014
<b>Cash flow from disposals</b>		
Cash – current year disposals	1,089	375
Cash and cash equivalents disposed	(33)	(30)
Costs and other disposal liabilities paid	(26)	(18)
<b>Net cash inflow</b>	<b>1,030</b>	<b>327</b>

Included in the gain on sale of PowerSchool is the write down of related software assets of £70m. The write down of the software assets reflects the reduced market opportunity for software which was to be integrated with PowerSchool and the recognition that adoption of such software in US schools is now unlikely to occur at the rate originally envisaged.

**Disposal of associates**

On 16 October 2015, the Group sold 39% of its 50% stake in The Economist resulting in a gain on disposal of £473m. The gain comprises proceeds of £377m, gain on revaluation of remaining 11% investment to fair value of £92m and liabilities disposed of £4m.

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**32 Cash generated from operations**

All figures in £ millions	Notes	2015	2014
Profit		823	470
<b>Adjustments for</b>			
Income tax		(24)	110
Depreciation	10	75	74
Amortisation and impairment of acquired intangibles and goodwill	11	1,051	264
Amortisation of software	11	74	63
Net finance costs		29	93
Share of results of joint ventures and associates	12	(68)	(51)
Profit on disposal of subsidiaries, associates, investments and fixed assets		(1,194)	(272)
Acquisition costs		-	6
Net foreign exchange adjustment from transactions		22	27
Share-based payment costs	26	26	32
Pre-publication		(57)	(52)
Inventories		10	6
Trade and other receivables		(99)	(69)
Trade and other liabilities		(80)	72
Retirement benefit obligations		(57)	(58)
Provisions for other liabilities and charges		(13)	(11)
<b>Net cash generated from operations</b>		<b>518</b>	<b>704</b>
Dividends from joint ventures and associates		162	120
Purchase of property, plant and equipment		(86)	(75)
Purchase of intangible assets		(161)	(107)
Proceeds from sale of property, plant and equipment		2	9
Proceeds from sale of intangible assets		1	2
Finance lease principal payments		(1)	(4)
<b>Operating cash flow</b>		<b>435</b>	<b>649</b>
Operating tax paid		(129)	(163)
Net operating finance costs paid		(51)	(73)
<b>Operating free cash flow</b>		<b>255</b>	<b>413</b>
Non operating tax paid		(103)	-
<b>Free cash flow</b>		<b>152</b>	<b>413</b>
Dividends paid (including to non-controlling interests)		(423)	(398)
<b>Net movement of funds from operations</b>		<b>(271)</b>	<b>15</b>
Acquisitions and disposals		1,395	(137)
Loans repaid/(advanced) (including to related parties)		7	(12)
Purchase of treasury shares	28	(23)	(9)
New equity		11	11
Other movements on financial instruments		(1)	15
<b>Net movement of funds</b>		<b>1,118</b>	<b>(117)</b>
Exchange movements on net debt		(133)	(143)
<b>Total movement in net debt</b>		<b>985</b>	<b>(260)</b>

### 32 Cash generated from operations continued

Net cash generated from operations is translated at an exchange rate approximating the rate at the date of cash flow. The difference between this rate and the average rate used to translate profit gives rise to a currency adjustment in the reconciliation between net profit and net cash generated from operations. This adjustment reflects the timing difference between recognition of profit and the related cash receipts or payments.

Operating cash flow, operating free cash flow and total free cash flow are non-GAAP measures and have been disclosed as they are part of Pearson's corporate and operating measures.

In the cash flow statement, proceeds from sale of property, plant and equipment comprise

All figures in £ millions	2015	2014
Net book amount	6	12
Loss on sale of property, plant and equipment	(4)	(3)
<b>Proceeds from sale of property, plant and equipment</b>	<b>2</b>	<b>9</b>

### 33 Contingencies

There are contingent Group liabilities that arise in the normal course of business in respect of indemnities, warranties and guarantees in relation to former subsidiaries and in respect of guarantees in relation to subsidiaries, joint ventures and associates. In addition there are contingent liabilities of the Group in respect of legal claims, contract disputes, royalties, copyright fees, permissions and other rights. None of these claims are expected to result in a material gain or loss to the Group.

### 34 Commitments

At the balance sheet date there were no commitments for capital expenditure contracted for but not yet incurred.

The Group leases various offices and warehouses under non-cancellable operating lease agreements. The leases have varying terms and renewal rights. The Group also leases various plant and equipment under operating lease agreements, also with varying terms. Lease expenditure charged to the income statement was £156m (2014: £157m).

The future aggregate minimum lease payments in respect of operating leases are as follows:

All figures in £ millions	2015	2014
Not later than one year	164	161
Later than one year and not later than two years	146	150
Later than two years and not later than three years	143	126
Later than three years and not later than four years	130	122
Later than four years and not later than five years	123	115
Later than five years	685	701
	<b>1,391</b>	<b>1,375</b>

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## Notes to the consolidated financial statements continued

**35 Related party transactions****Joint ventures and associates**

Amounts advanced to joint ventures and associates during the year and at the balance sheet date are set out in note 12. Apart from transactions with the Group's joint ventures and associates, there were no other material related party transactions.

**Key management personnel**

Key management personnel are deemed to be the members of the Pearson Executive (see page 7). It is this committee which had responsibility for planning, directing and controlling the activities of the Group in 2015. Key management personnel compensation is disclosed below.

All figures in £millions	2015	2014
Short-term employee benefits	7	10
Retirement benefits	1	1
Share-based payment costs	1	2
<b>Total</b>	<b>9</b>	<b>13</b>

There were no other material related party transactions. No guarantees have been provided to related parties.

**36 Events after the balance sheet date**

In January 2016, Pearson announced that it was embarking on a restructuring programme to simplify the business, reduce costs and position the company for growth in its major markets. The majority of the programme is expected to be complete by mid-year 2016 and will involve implementation costs in 2016 of approximately £320m.

### 37 Accounts and audit exemptions

The Pearson plc subsidiary companies listed below are exempt from the requirements of the Companies Act 2006 relating to the audit of individual accounts by virtue of section 479A

	Company number		Company number
Aldwych Finance Limited	04720439	Pearson Education Limited	00872828
ASET Limited	04231636	Pearson Funding Four plc	07970304
ASET Group Limited	03964551	Pearson Funding One plc	02911143
ASET Management Limited	03139404	Pearson Funding Two plc	07210654
Blue Wharf Limited	04344573	Pearson Heinemann Limited	03099304
Burmedia Investments Limited	03060487	Pearson in Practice ATA Limited	07679091
Edexcel Limited	04496750	Pearson in Practice Holdings Limited	06337129
Education Development International plc	03914767	Pearson in Practice Skills Based Learning Limited	03755464
Embankment Finance Limited	04460625	Pearson in Practice Technology Limited	03786989
EQL Assessment Limited	05224778	Pearson International Finance Limited	02496206
Green Wharf Limited	07009228	Pearson Loan Finance No 2 Unlimited	05632021
Icodeon Limited	05068195	Pearson Loan Finance No 3 Limited	05052661
Longman Group (Overseas Holdings) Limited	00690236	Pearson Loan Finance No 4 Limited	02635107
Midlands Educational Technology Limited	01448842	Pearson Loan Finance Unlimited	05144467
Pearson Affordable Learning Fund Limited	08038068	Pearson Management Services Limited	00096263
Pearson Amsterdam Finance Limited	03041245	Pearson Overseas Holdings Limited	00145205
Pearson Australia Finance Unlimited	05578463	Pearson PRH Holdings Limited	08561316
Pearson Books Limited	02512075	Pearson Services Limited	01341060
Pearson Brazil Finance Ltd	08848874	Pearson Shared Services Limited	04623186
Pearson Canada Finance Unlimited	05578491	Testchange Limited	02496240
Pearson Dollar Finance plc	05111013	The Coaching Space Limited	05333023
Pearson Dollar Finance Two plc	06507766	TQ Catalis Limited	07307943
Pearson Education Holdings Limited	00210859	TQ Clapham Limited	07307925
Pearson Education Investments Limited	08444933	TQ Global Limited	07802458

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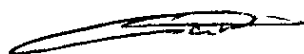
# Company balance sheet

As at 31 December 2015

All figures in £ millions	Notes	2015	2014
<b>Assets</b>			
<b>Non-current assets</b>			
Investments in subsidiaries	2	7,744	8,740
Amounts due from subsidiaries		3,953	27
Financial assets – derivative financial instruments	6	78	84
Other financial assets	7	92	-
		<b>11,867</b>	<b>8,851</b>
<b>Current assets</b>			
Amounts due from subsidiaries		446	5,220
Amounts due from related parties		47	54
Current income tax assets		-	28
Financial assets – derivative financial instruments	6	3	24
Cash and cash equivalents (excluding overdrafts)	4	1,168	13
Other assets		-	2
		<b>1,664</b>	<b>5,341</b>
<b>Total assets</b>		<b>13,531</b>	<b>14,192</b>
<b>Liabilities</b>			
<b>Non-current liabilities</b>			
Amounts due to subsidiaries		(3,760)	(2,346)
Financial liabilities – borrowings	5	(218)	(210)
Financial liabilities – derivative financial instruments	6	(136)	(73)
		<b>(4,114)</b>	<b>(2,629)</b>
<b>Current liabilities</b>			
Amounts due to subsidiaries		(1,431)	(4,414)
Current income tax liabilities		(108)	-
Financial liabilities – borrowings	5	(580)	(629)
Financial liabilities – derivative financial instruments	6	(29)	(1)
Other liabilities		(12)	(2)
		<b>(2,160)</b>	<b>(5,046)</b>
<b>Total liabilities</b>		<b>(6,274)</b>	<b>(7,675)</b>
<b>Net assets</b>		<b>7,257</b>	<b>6,517</b>
<b>Equity</b>			
Share capital	8	205	205
Share premium	8	2,590	2,579
Treasury shares	9	(27)	1
Special reserve		447	447
Retained earnings		4,042	3,285
<b>Total equity attributable to equity holders of the company</b>		<b>7,257</b>	<b>6,517</b>

These financial statements have been approved for issue by the board of directors on 4 March 2016 and signed on its behalf by

Coram Williams  
Chief financial officer



# Company statement of changes in equity

Year ended 31 December 2015

All figures in £ millions	Equity attributable to equity holders of the company					
	Share capital	Share premium	Treasury shares	Special reserve	Retained earnings	Total
At 1 January 2015	205	2,579	1	447	3,285	6,517
Profit for the year	-	-	-	-	1,206	1,206
Issue of ordinary shares under share option schemes*	-	11	-	-	-	11
Purchase of treasury shares	-	-	(23)	-	-	(23)
Contribution refund to subsidiaries	-	-	(31)	-	-	(31)
Release of treasury shares	-	-	26	-	(26)	-
Dividends	-	-	-	-	(423)	(423)
At 31 December 2015	205	2,590	(27)	447	4,042	7,257

All figures in £ millions	Equity attributable to equity holders of the company					
	Share capital	Share premium	Treasury shares	Special reserve	Retained earnings	Total
At 1 January 2014	205	2,568	(22)	447	2,447	5,645
Profit for the year	-	-	-	-	1,267	1,267
Issue of ordinary shares under share option schemes*	-	11	-	-	-	11
Purchase of treasury shares	-	-	(9)	-	-	(9)
Release of treasury shares	-	-	32	-	(32)	-
Dividends	-	-	-	-	(397)	(397)
At 31 December 2014	205	2,579	1	447	3,285	6,517

The special reserve represents the cumulative effect of cancellation of the company's share premium account included within retained earnings is an amount of £162m (2014 £131m) relating to profit on intra-Group disposals that is not distributable

\* Full details of the share-based payment plans are disclosed in note 26 to the consolidated financial statements

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# Company cash flow statement

Year ended 31 December 2015

All figures in £ millions	Notes	2015	2014
<b>Cash flows from operating activities</b>			
Net profit		1,206	1,267
<b>Adjustments for</b>			
Income tax		(154)	(9)
Net finance costs		68	24
Impairment charges		736	-
Profit on disposals		(279)	-
Amounts due to subsidiaries		(909)	(1,058)
<b>Net cash generated from operations</b>		668	224
Interest paid		(56)	(73)
Tax received		289	6
<b>Net cash generated from operating activities</b>		901	157
<b>Cash flows from investing activities</b>			
Disposal of subsidiaries, net of cash disposed		747	-
Loans repaid by/(advanced to) related parties		7	(10)
Interest received		11	15
<b>Net cash received from investing activities</b>		765	5
<b>Cash flows from financing activities</b>			
Proceeds from issue of ordinary shares	8	11	11
Net purchase of treasury shares		(53)	(9)
Proceeds from/(repayment of) borrowings		17	(250)
Dividends paid to company's shareholders		(423)	(397)
<b>Net cash used in financing activities</b>		(448)	(645)
Effects of exchange rate changes on cash and cash equivalents		(14)	(15)
<b>Net increase/(decrease) in cash and cash equivalents</b>		1,204	(498)
Cash and cash equivalents at beginning of year		(616)	(118)
<b>Cash and cash equivalents at end of year</b>	4	588	(616)

# Company balance sheet

As at 31 December 2015

All figures in £ millions	Notes	2015	2014
<b>Assets</b>			
<b>Non-current assets</b>			
Investments in subsidiaries	2	7,744	8,740
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		<b>(2,160)</b>	<b>(5,046)</b>
<b>Total liabilities</b>		<b>(6,274)</b>	<b>(7,675)</b>
<b>Net assets</b>		<b>7,257</b>	<b>6,517</b>
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Treasury shares	9	(27)	1
Special reserve		447	447
Retained earnings		4,042	3,285
<b>Total equity attributable to equity holders of the company</b>		<b>7,257</b>	<b>6,517</b>

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Coram Williams  
Chief financial officer

# Company statement of changes in equity

Year ended 31 December 2015

All figures in £ millions	Equity attributable to equity holders of the company					
	Share capital	Share premium	Treasury shares	Special reserve	Retained earnings	Total
At 1 January 2015	205	2,579	1	447	3,285	6,517
Profit for the year	-	-	-	-	1,206	1,206
Issue of ordinary shares under share option schemes*	-	11	-	-	-	11
Purchase of treasury shares	-	-	(23)	-	-	(23)
Contribution refund to subsidiaries	-	-	(31)	-	-	(31)
Release of treasury shares	-	-	26	-	(26)	-
Dividends	-	-	-	-	(423)	(423)
At 31 December 2015	205	2,590	(27)	447	4,042	7,257

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	Share capital	Share premium	Treasury shares	Special reserve	Retained earnings	Total
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Purchase of treasury shares	-	-	(9)	-	-	(9)
Release of treasury shares	-	-	32	-	(32)	-
Dividends	-	-	-	-	(397)	(397)
At 31 December 2014	205	2,579	1	447	3,285	6,517

The special reserve represents the cumulative effect of cancellation of the company's share premium account

Included within retained earnings is an amount of £162m (2014: £131m) relating to profit on intra-Group disposals that is not distributable

\* Full details of the share-based payment plans are disclosed in note 26 to the consolidated financial statements

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# Company cash flow statement

Year ended 31 December 2015

All figures in £ millions	Notes	2015	2014
<b>Cash flows from operating activities</b>			
Net profit		1,206	1,267
<b>Adjustments for</b>			
Income tax		(154)	(9)
Net finance costs		68	24
Impairment charges		736	-
Profit on disposals		(279)	-
Amounts due to subsidiaries		(909)	(1,058)
<b>Net cash generated from operations</b>		<b>668</b>	<b>224</b>
Interest paid		(56)	(73)
Tax received		289	6
<b>Net cash generated from operating activities</b>		<b>901</b>	<b>157</b>
<b>Cash flows from investing activities</b>			
Disposal of subsidiaries, net of cash disposed		747	-
Loans repaid by/(advanced to) related parties		7	(10)
Interest received		11	15
<b>Net cash received from investing activities</b>		<b>765</b>	<b>5</b>
<b>Cash flows from financing activities</b>			
Proceeds from issue of ordinary shares	8	11	11
Net purchase of treasury shares		(53)	(9)
Proceeds from/(repayment of) borrowings		17	(250)
Dividends paid to company's shareholders		(423)	(397)
<b>Net cash used in financing activities</b>		<b>(448)</b>	<b>(645)</b>
Effects of exchange rate changes on cash and cash equivalents		(14)	(15)
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>1,204</b>	<b>(498)</b>
Cash and cash equivalents at beginning of year		(616)	(118)
<b>Cash and cash equivalents at end of year</b>	<b>4</b>	<b>588</b>	<b>(616)</b>



## Five-year summary

All figures in £ millions	2011	2012	2013	2014	2015
<b>Sales By geography*</b>					
North America			3,008	2,906	2,940
Core			1,008	910	836
Growth			712	724	692
Continuing	4,390	4,615	4,728	4,540	4,468
Discontinued	1,472	1,497	962	343	312
<b>Total sales</b>	<b>5,862</b>	<b>6,112</b>	<b>5,690</b>	<b>4,883</b>	<b>4,780</b>

<b>Sales By line of business*</b>					
School			2,303	2,027	1,880
Higher Education			1,664	1,695	1,736
Professional			761	818	852
Continuing	4,390	4,615	4,728	4,540	4,468
Discontinued	1,472	1,497	962	343	312
<b>Total sales</b>	<b>5,862</b>	<b>6,112</b>	<b>5,690</b>	<b>4,883</b>	<b>4,780</b>

<b>Adjusted operating profit By geography*</b>					
North America			464	444	480
Core			103	122	114
Growth			35	32	(12)
Penguin Random House			50	69	90
Continuing	751	785	652	667	672
Discontinued	187	147	84	55	51
<b>Total adjusted operating profit</b>	<b>938</b>	<b>932</b>	<b>736</b>	<b>722</b>	<b>723</b>

<b>Adjusted operating profit: By line of business*</b>					
School			268	236	183
Higher Education			295	309	354
Professional			39	53	45
Penguin Random House	-	-	50	69	90
Continuing	751	785	652	667	672
Discontinued	187	147	84	55	51
<b>Total adjusted operating profit</b>	<b>938</b>	<b>932</b>	<b>736</b>	<b>722</b>	<b>723</b>

\* Periods prior to 2013 have not been restated to reflect the new organisation structure as there is no appropriate basis for restatement of those periods. 2011 onwards reflect the adoption of IAS 19 revised and have been restated as appropriate. Prior periods have not been restated.

<i>All figures in £ millions</i>	2011	2012	2013	2014	2015
<b>Operating margin – continuing</b>	<b>17.1%</b>	<b>17.0%</b>	<b>13.8%</b>	<b>14.7%</b>	<b>15.0%</b>
<b>Adjusted earnings</b>					
Total adjusted operating profit	938	932	736	722	723
Net finance costs	(55)	(65)	(72)	(64)	(46)
Income tax	(196)	(200)	(97)	(118)	(105)
Non-controlling interest	1	(3)	(1)	1	-
<b>Adjusted earnings</b>	<b>688</b>	<b>664</b>	<b>566</b>	<b>541</b>	<b>572</b>
Weighted average number of shares (millions)	800.2	804.3	807.8	810.9	813.3
<b>Adjusted earnings per share</b>	<b>86.0p</b>	<b>82.6p</b>	<b>70.1p</b>	<b>66.7p</b>	<b>70.3p</b>
<i>All figures in £ millions</i>	2011	2012	2013	2014	2015
<b>Cash flow</b>					
Operating cash flow	983	788	588	649	435
Operating cash conversion	105%	85%	80%	90%	60%
Operating free cash flow	772	657	324	413	255
Operating free cash flow per share	96.5p	81.7p	40.1p	50.9p	31.4p
Total free cash flow	772	657	269	413	152
Total free cash flow per share	96.5p	81.7p	33.3p	50.9p	18.7p
<b>Net assets</b>	<b>5,962</b>	<b>5,710</b>	<b>5,706</b>	<b>5,985</b>	<b>6,418</b>
<b>Net debt</b>	<b>499</b>	<b>918</b>	<b>1,379</b>	<b>1,639</b>	<b>654</b>
<b>Return on invested capital (gross basis)</b>					
Total adjusted operating profit	938	932	736	722	723
Cash tax paid	(151)	(65)	(191)	(163)	(129)
<b>Return</b>	<b>787</b>	<b>867</b>	<b>545</b>	<b>559</b>	<b>594</b>
Average invested capital	8,731	9,578	10,130	9,900	10,317
<b>Return on invested capital</b>	<b>9.0%</b>	<b>9.1%</b>	<b>5.4%</b>	<b>5.6%</b>	<b>5.8%</b>
<b>Dividend per share</b>	<b>42.0p</b>	<b>45.0p</b>	<b>48.0p</b>	<b>51.0p</b>	<b>52.0p</b>

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## Corporate and operating measures

### Sales – underlying and constant exchange rate movement

Underlying sales movements exclude the impact of acquisitions/disposals, movements in exchange rates and changes in revenue recognition policies

All figures in £ millions	2015
Underlying decrease	(80)
Portfolio changes	(129)
Exchange differences	137
<b>Total sales decrease</b>	<b>(72)</b>
Underlying decrease	(2)%
Constant exchange rate decrease	(5)%

### Adjusted income statement

Reconciliation of the consolidated income statement to the adjusted numbers presented as non-GAAP measures in the financial statements

All figures in £ millions	2015							
	Statutory income statement	Discontinued operations	Other net gains and losses	Acquisition costs	Intangible charges	Other net finance income/ costs	Tax amortisation benefit	Adjusted income statement
Operating (loss)/profit	(404)	51	(13)	-	1,089	-	-	723
Net finance costs	(29)	-	-	-	-	(17)	-	(46)
<b>(Loss)/profit before tax</b>	<b>(433)</b>	<b>51</b>	<b>(13)</b>	<b>-</b>	<b>1,089</b>	<b>(17)</b>	<b>-</b>	<b>677</b>
Income tax	81	(9)	40	-	(257)	7	33	(105)
<b>(Loss)/profit for the year from continuing operations</b>	<b>(352)</b>	<b>42</b>	<b>27</b>	<b>-</b>	<b>832</b>	<b>(10)</b>	<b>33</b>	<b>572</b>
Profit for the year from discontinued operations	1,175	(42)	(1,135)	-	2	-	-	-
<b>Profit for the year</b>	<b>823</b>	<b>-</b>	<b>(1,108)</b>	<b>-</b>	<b>834</b>	<b>(10)</b>	<b>33</b>	<b>572</b>
Non-controlling interest	-	-	-	-	-	-	-	-
<b>Earnings</b>	<b>823</b>	<b>-</b>	<b>(1,108)</b>	<b>-</b>	<b>834</b>	<b>(10)</b>	<b>33</b>	<b>572</b>

## Adjusted income statement continued

	2014							
All figures in £ millions	Statutory income statement	Discontinued operations	Other net gains and losses	Acquisition costs	Intangible charges	Other net finance income/ costs	Tax amortisation benefit	Adjusted income statement
Operating profit	398	2	(2)	6	318	-	-	722
Net finance costs	(93)	-	-	-	-	29	-	(64)
Profit before tax	305	2	(2)	6	318	29	-	658
Income tax	(63)	(1)	1	(1)	(73)	(5)	24	(118)
Profit for the year from continuing operations	242	1	(1)	5	245	24	24	540
Profit for the year from discontinued operations	228	(1)	(227)	-	-	-	-	-
Profit for the year	470	-	(228)	5	245	24	24	540
Non-controlling interest	1	-	-	-	-	-	-	1
Earnings	471	-	(228)	5	245	24	24	541

## Adjusted operating profit – underlying and constant exchange rate movement

Operating profit movement excluding the impact of acquisitions, disposals and movements in exchange rates

All figures in £ millions	2015
Underlying decrease	(12)
Portfolio changes	(9)
Exchange differences	22
Total adjusted operating profit increase	1
Underlying decrease	(2)%
Constant exchange rate decrease	(3)%

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## Corporate and operating measures continued

## Free cash flow per share

Operating cash flow for continuing and discontinued operations before tax and finance charges, divided by the weighted average number of shares in issue

All figures in £ millions	2015	2014
Adjusted operating profit	723	722
Cash conversion	60%	90%
Operating cash flow	435	649
Operating tax paid	(129)	(163)
Net operating finance costs paid	(51)	(73)
<b>Total operating free cash flow</b>	<b>255</b>	<b>413</b>
Non operating tax paid	(103)	–
<b>Total free cash flow</b>	<b>152</b>	<b>413</b>
Weighted average number of shares in issue (millions)	813.3	810.9
Operating free cash flow per share	31.4p	50.9p
<b>Total free cash flow per share</b>	<b>18.7p</b>	<b>50.9p</b>

## Return on invested capital

All figures in £ millions	Invested capital	
	2015	2014
Total adjusted operating profit	723	722
Operating tax paid	(129)	(163)
<b>Return</b>	<b>594</b>	<b>559</b>
Average goodwill and other intangibles	8,715	8,557
Average net operating assets	1,602	1,343
<b>Average invested capital</b>	<b>10,317</b>	<b>9,900</b>
<b>Return on invested capital</b>	<b>5.8%</b>	<b>5.6%</b>

Return on invested capital is calculated as total adjusted operating profit less operating cash tax paid expressed as a percentage of average invested capital. Invested capital includes the original unamortised goodwill and intangibles.

# Shareholder information

Pearson ordinary shares are listed on the London Stock Exchange and on the New York Stock Exchange in the form of American Depositary Receipts

## Corporate website

The investors' section of our corporate website [www.pearson.com/investors](http://www.pearson.com/investors) provides a wealth of information for shareholders. It is also possible to sign up to receive e-mail alerts for reports and press releases relating to Pearson at [www.pearson.com/news/newsletter-subscribe.html](http://www.pearson.com/news/newsletter-subscribe.html)

## Shareholder information online

Shareholder information can be found on our website [www.pearson.com/investors/investor-information.html](http://www.pearson.com/investors/investor-information.html)

Our registrar, Equiniti, also provides a range of shareholder information online. You can check your holding and find practical help on transferring shares or updating your details at [www.shareview.co.uk](http://www.shareview.co.uk). For more information, please contact our registrar, Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA. Telephone 0371 384 2233\* or, for those shareholders with hearing difficulties, telephone number 0371 384 2255\*

## Information about the Pearson share price

The company's share price can be found on our website at [www.pearson.com](http://www.pearson.com). It also appears in the financial columns of the national press.

## 2015 dividends

	Payment date	Amount per share
Interim	11 September 2015	18 pence
Final	6 May 2016	34 pence

## Payment of dividends to mandated accounts

Should you elect to have your dividends paid through BACS, this can be done directly into a bank or building society account, with the tax voucher sent to the shareholder's registered address. Equiniti can be contacted for information on 0371 384 2043\*

## Dividend reinvestment plan (DRIP)

The DRIP gives shareholders the right to buy the company's shares on the London stock market with their cash dividend. For further information, please contact Equiniti on 0371 384 2268\*

## Individual Savings Accounts (ISAs)

Equiniti offers ISAs in Pearson shares. For more information, please go to [www.shareview.co.uk/dealing](http://www.shareview.co.uk/dealing) or call customer services on 0345 300 0430\*

## Share dealing facilities

Equiniti offers telephone and internet services for dealing in Pearson shares. For further information, please contact their telephone dealing helpline on 03456 037 037\* or, for online dealing, log on to [www.shareview.co.uk/dealing](http://www.shareview.co.uk/dealing). You will need your shareholder reference number as shown on your share certificate.

A postal dealing service is also available through Equiniti. Please telephone 0371 384 2248\* for details or log on to [www.shareview.co.uk](http://www.shareview.co.uk) to download a form.

## ShareGift

Shareholders with small holdings of shares, whose value makes them uneconomic to sell, may wish to donate them to ShareGift, the share donation charity (registered charity number 1052686). Further information about ShareGift and the charities it has supported may be obtained from their website, [www.ShareGift.org](http://www.ShareGift.org) or by contacting them at ShareGift, PO Box 72253, London, SW1P 9LQ.

## American Depositary Receipts (ADRs)

Pearson's ADRs are listed on the New York Stock Exchange and traded under the symbol PSO. Each ADR represents one ordinary share. For enquiries regarding registered ADR holder accounts and dividends, please contact Bank of New York Mellon, Shareholder Correspondence (ADR), PO Box 30170, College Station, TX 77842-3170, telephone 1 (866) 259 2289 (toll free within the US) or 001 201 680 6825 (outside the US). Alternatively, you may e-mail [shrrelations@cpushareownerservices.com](mailto:shrrelations@cpushareownerservices.com)

Voting rights for registered ADR holders can be exercised through Bank of New York Mellon, and for beneficial ADR holders (and/or nominee accounts) through your US brokerage institution. Pearson will file with the Securities and Exchange Commission a Form 20-F.

\*Lines open 8.30am to 5.30pm Monday to Friday (excluding UK public holidays)

## Shareholder information continued

**Share register fraud protecting your investment**

Pearson does not contact its shareholders directly to provide recommendation advice and neither does it appoint third parties to do so. As required by law, our shareholder register is available for public inspection but we cannot control the use of information obtained by persons inspecting the register. Please treat any approaches purporting to originate from Pearson with caution.

For more information, please log on to our website at [www.pearson.com/investors/investor-information.html](http://www.pearson.com/investors/investor-information.html)

**Tips on protecting your shares**

- › Keep any documentation that contains your shareholder reference number in a safe place and shred any unwanted documentation
- › Inform our registrar, Equiniti, promptly when you change address
- › Be aware of dividend payment dates and contact the registrar if you do not receive your dividend cheque or better still, make arrangements to have the dividend paid directly into your bank account
- › Consider holding your shares electronically in a CREST account via a nominee

**2016 financial calendar**

Ex-dividend date	7 April
Record date	8 April
Last date for dividend reinvestment election	14 April
Annual General Meeting	29 April
Payment date for dividend and share purchase date for dividend reinvestment	6 May
Interim results	tbc*
Payment date for interim dividend	tbc*

\* to be announced during 2016

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#### Reliance on this document

The intention of this document is to provide information to shareholders and is not designed to be relied upon by any other party or for any other purpose

#### Forward-looking statements

Except for the historical information contained herein, the matters discussed in this document include forward-looking statements. In particular, all statements that express forecasts, expectations and projections with respect to future matters, including trends in results of operations, margins, growth rates, overall market trends, the impact of interest or exchange rates, the availability of financing, anticipated costs savings and synergies and the execution of Pearson's strategy, are forward-looking statements. By their nature, forward-looking statements involve risks and uncertainties because they relate to events and depend on circumstances that will occur in future. They are based on numerous

assumptions regarding Pearson's present and future business strategies and the environment in which it will operate in the future. There are a number of factors which could cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements, including a number of factors outside Pearson's control. These include international, national and local conditions, as well as competition. They also include other risks detailed from time to time in Pearson's publicly-filed documents and you are advised to read, in particular, the risk factors set out in this document. Any forward-looking statements speak only as of the date they are made, and Pearson gives no undertaking to update forward-looking statements to reflect any changes in its expectations with regard thereto or any changes to events, conditions or circumstances on which any such statement is based. No reliance should be placed on forward-looking statements.

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Illustrations  
Lauren Rolwing, [p17@laurenrolwing.com](mailto:p17@laurenrolwing.com)  
Kanae Sato, [p55@kanaes.com](mailto:p55@kanaes.com)  
Lucy Vigrass, [p69@lucyvigrass.co.uk](mailto:p69@lucyvigrass.co.uk)  
Tang Yau Hoong, [p125@tangyauhoong.com](mailto:p125@tangyauhoong.com)

Pearson has supported the planting of 137 square metres of new native woodland with the Woodland Trust, helping to remove 5.48 metric tonnes of carbon dioxide generated by the production of this report and associated documents

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## Principal offices

80 Strand,  
London WC2R 0RL, UK  
T +44 (0)20 7010 2000  
F +44 (0)20 7010 6060

330 Hudson Street,  
New York City,  
NY 10013, USA  
T +1 212 390 7100

firstname.lastname@pearson.com

**Pearson plc**  
Registered number 53723 (England)

[www.pearson.com](http://www.pearson.com)

[blog.pearson.com](http://blog.pearson.com)

@pearson