PEARSON

Always learning

Annual report and accounts 2009

Always learning

Pearson is a world-leading 'education' company, in the broadest sense of that word. We have a very simple goal: to help people get on in their lives through education. We aim to serve the citizens of our brain-based global economy wherever and whenever they are learning – old or young, at home or school or work, in any pursuit, anywhere.

Have you tried learning about Pearson online?

1 **Visit the all-new www.pearson.com**

2 **Browse, download or print our interactive online annual report at www.pearson.com/investor/ar2009**

3 **Take a virtual tour at www.pearson.com/pearsonville**

Notes

Reliance on this document

Our Business Review on pages 8 to 43 has been prepared in accordance with the Directors' Report Business Review Requirements of section 417 of the Companies Act 2006. It also incorporates much of the guidance set out in the Accounting Standards Board's Reporting Statement on the Operating and Financial Review.

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

This document contains forward-looking statements which are made by the directors in good faith based on information available to them at the time of approval of this report. 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 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. 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.

What's inside this report?

Directors' report

Business review

1 Introduction

A summary of who we are and what we do, including highlights of the operating and financial performance for the year.

2 Our strategy

An analysis of our business strategy and the key areas of investment and focus.

3 Our performance

An in-depth analysis of how we performed in 2009. Also looks at the outlook for 2010 and the principal risks and uncertainties affecting our businesses.

4 Our impact on society

Explains what corporate responsibility means at Pearson, giving a summary of our work in 2009 and our plans for 2010.

5 Governance

Provides details of the board, its policies and procedures and the report on directors' remuneration.

6 Financial statements

Detailed financial statements for both the Group and the parent company, including an analysis of the key measures used by the Group in its management of the business.

Pearson at a glance

Pearson is an international company with market-leading businesses in education, business information and consumer publishing. We are 37,000 people in more than 60 countries, helping children and adults to learn, business people to make informed decisions and readers of all ages to wind down or wise up with a good book.

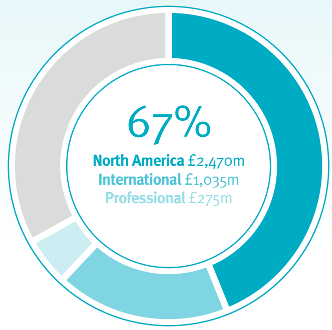
Overview | **People** | **Proportion of Pearson revenue**

Education

Pearson is the world's leading education company. We provide learning materials, technologies, assessments and services to teachers and students of all ages and in more than 60 countries.

PEARSON

27,000
US 16,400
UK 3,000
RoW 7,600

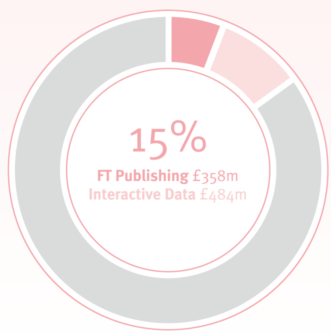


Business information

The FT Group provides news, data, comment and analysis to the international business community. It is known around the world for its independent and authoritative information.

FT

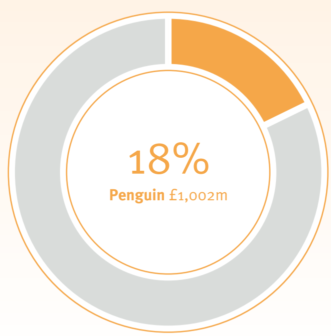
4,800
US 1,900
UK 2,000
RoW 900



Consumer publishing

Penguin publishes more than 4,000 fiction and non-fiction books each year – on paper, on screens and in audio formats – for readers of all ages. It is one of the world's leading consumer publishing businesses and an iconic global brand.

4,200
US 1,900
UK 800
RoW 1,500



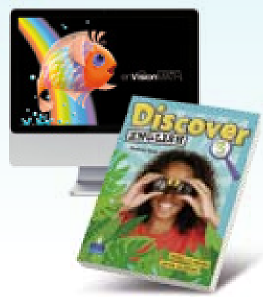
Learn more at **www.pearson.com/aboutus**

Businesses

Markets

We are a leading provider of educational material and learning technologies. We provide test development, processing and scoring services to educational institutions, corporations and professional bodies around the world. We publish across the curriculum under a range of respected imprints including: Scott Foresman, Prentice Hall, Addison-Wesley, Allyn and Bacon, Benjamin Cummings and Longman.

For some years, Pearson has been a leader in education, with leading positions in large developed markets and local publishing centres in more than 30 countries. More recently we have significantly accelerated our international expansion, investing in new education operations in countries including China, India, Southern Africa and Latin America.



See more on **page 16** and at **pearsoned.com**

FT Publishing includes: the *Financial Times* and FT.com; a range of specialist financial magazines and online services; and Mergermarket.

Interactive Data is Pearson's 61%-owned provider of specialist financial data to financial institutions and retail investors.

The FT Group also has a stake in a number of joint ventures, including those with FTSE International, Vedomosti in Russia, BDFM in South Africa and a 50% stake in The Economist Group.

The *Financial Times* has a network of approximately 600 journalists in 40 countries and a unique model of producing distinctive newspaper editions for Europe, the UK, the US, Asia and the Middle East. FT.com, with nine million unique users and 1.8 million registered users around the world, makes the FT even more widely available.

See more on **page 24** and at **ft.com**

Penguin operates around the world through a series of connected national publishing houses. It publishes under a number of well-known imprints including Putnam, Viking, Allen Lane, Hamish Hamilton, Berkley, the Penguin Press, Puffin and Dorling Kindersley.

Penguin combines a longstanding commitment to local publishing with a determination to benefit from its worldwide scale, a globally recognised brand and growing demand for books in emerging markets. Its largest businesses are in the US, the UK, Australia, Canada, Ireland, India, South Africa and New Zealand.

See more on **page 28** and at **penguin.com**

Financial highlights

In financial terms, Pearson's goal is to achieve sustainable growth on three key financial goals – earnings, cash and return on invested capital – and reliable cash returns to our investors through healthy and growing dividends. In 2009, we reported underlying growth in sales and operating profit, in spite of the exceptionally difficult macroeconomic environment and against record 2008 results. We achieved significant profit growth in education, helping us to grow even though our markets in US school publishing, financial advertising and consumer books were especially challenging.

	2009 £m	2008 £m	Headline growth	CER growth	Underlying growth
Business performance					
Sales	5,624	4,811	17%	4%	2%
Adjusted operating profit	858	762	13%	4%	2%
Adjusted profit before tax	761	674	13%		
Adjusted earnings per share	65.4p	57.7p	13%		
Operating cash flow	913	796	15%		
Total free cash flow	723	631	15%		
Total free cash flow per share	90.5p	79.2p	14%		
Return on invested capital	8.9%	9.2%	(0.3)%pts		
Net debt	1,092	1,460	25%		
Statutory results					
Operating profit	755	676	12%		
Profit before tax	660	585	13%		
Basic earnings per share – continuing	53.2p	47.9p	11%		
Cash generated from operations	1,012	894	13%		
Dividend per share	35.5p	33.8p	5%		

Note Throughout this document (unless otherwise stated), sales and adjusted operating profit growth rates are stated on a constant exchange rate (CER) basis. Where quoted, underlying growth rate exclude both currency movements and portfolio changes. The 'business performance' measures are non-GAAP measures and reconciliations to the equivalent statutory heading under IFRS are included in notes 2, 8 and 31 to the annual report. Adjusted operating profit is stated on a continuing basis.

2009 Sales

£5.6bn

+4%

2009 Adjusted operating profit

£858m

+4%

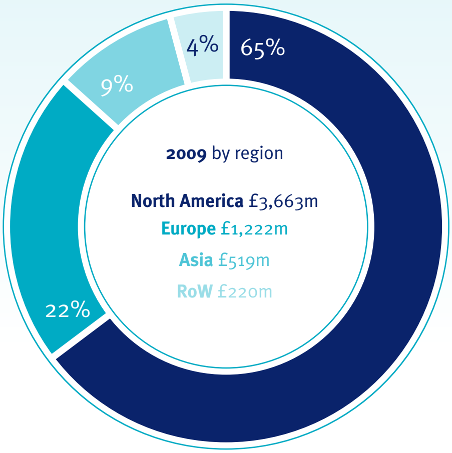
Our record
Average annual growth in headline terms
2004-2009

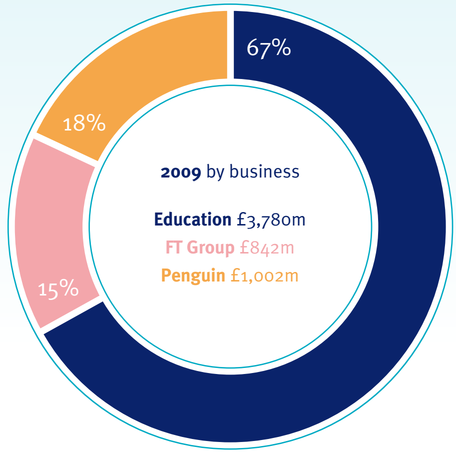
Sales

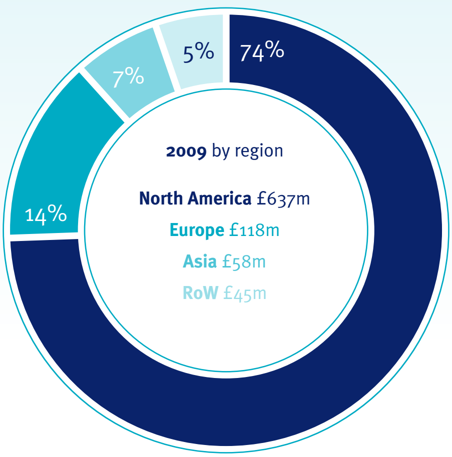
+11%

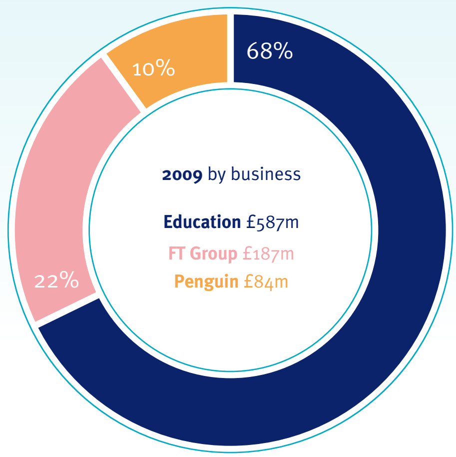
Adjusted operating profit

+19%

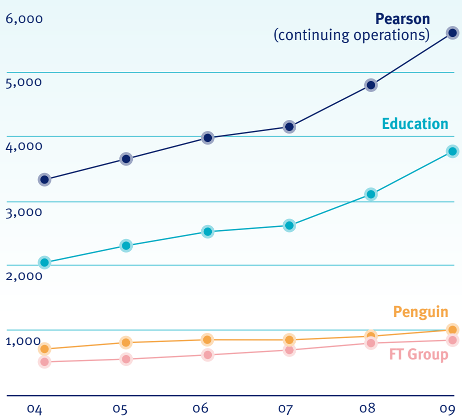




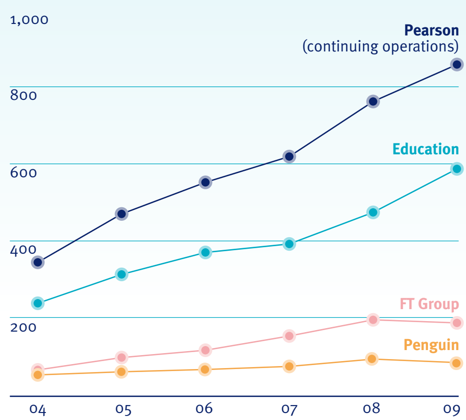




Sales £m



Adjusted operating profit £m



Chairman's statement

Glen Moreno Chairman

Twelve months ago I wrote to you with this very sober assessment:

"None of us is under any illusion: the short-term outlook is tough and 2009 will be a difficult year. All kinds of companies, including our own, will be affected."

In the event, economic conditions were every bit as bad as we feared. But in that challenging environment, **Pearson turned in an excellent performance by any measure.** I attribute this to two things:

Our people, who stayed close to their customers, anticipated significant changes in our markets and worked their socks off;

Our strategy, which we have patiently developed, implemented and invested in over a number of years.

It is worth recalling that, only a decade ago, Pearson was a completely different company. We were the publisher of general interest and sports newspapers in Spain; we were the TV production company behind *The Price is Right* and *Baywatch*; we were a part-owner of the Lazard banking houses. Marjorie and her colleagues had just begun the major move into the global education industry, but had barely articulated the strategy of investing in testing and technology to make learning more personal and more effective.

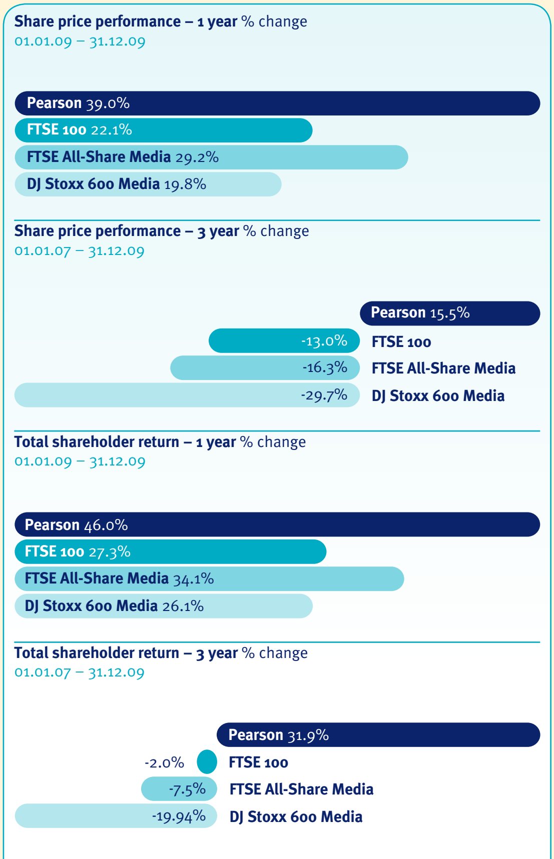
That year, a 'boom' period in the industry, our operating profits were £490m and our education revenues a little over £2bn; last year, in a deep recession, our operating profits were £858m and our education revenues approaching £4bn. The scale of our transformation is striking. It shows that sometimes it pays to take a long-term view.

But more important than our scale alone, we have once again demonstrated our credentials as both a *durable* company and a *growth* company. The financial results for 2009 that are set out elsewhere in this report paint a picture of remarkable performance and resilience in an extremely difficult economic environment.

There is evidence that those qualities were recognised by the market over the course of the past year, and that those who held their Pearson shares through a turbulent period were rewarded. Our shares began 2009 at 641p, and ended the year 39% higher, at close to nine pounds. That increase was well ahead of both the major market indices (the FTSE 100 was up 22%) and the media sector (FTSE All-Share Media index up 29% and DJ Stoxx 600 Media up 20%).

The second element of our return to shareholders – the dividend – was further increased in 2009. So our total shareholder return (which combines both the share price movement and dividends paid) was up 46%. Again, this was significantly ahead of the FTSE 100 (up 27%), the DJ Stoxx 600 Media (up 26%) and the FTSE media sector (up 34%).

Our decade-long transformation was partly the result of some extensive portfolio changes. Over those ten years, we made $4.1bn of disposals and $6.3bn of acquisitions. But underneath those very visible changes, there were some deeply held principles at work. Those are important to understand, because they tell you as much about our future as they do about our past.



Source: Datastream

First, every part of Pearson has **a relentless focus on the value we provide to our customers** – the learner, the teacher, the reader, the investor, the business person. We know that the ultimate measure of our performance is shareholder value; but we understand we can best deliver shareholder value through helping our customers make progress in their lives.

Second, one driver of our transformation has been to make Pearson **a reliable and resilient company**. Proud as we are of our performance in 2009, what's even more important to us is the long-term *consistency* of our growth. For each of the past six years, we have delivered growth in sales, earnings and cash, through both good markets and bad.

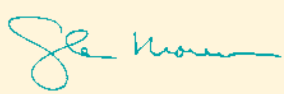
Third, companies can sometimes be defined by what they *don't* do: by **what they choose to avoid**. Because our strategy is about long-term value creation for customers and shareholders, Pearson did not engage in short-term financial engineering. During the credit bubble, we resisted calls to load up our balance sheet with cheap debt and reduce our equity capital. I believe you can attribute a good deal of our financial stability and competitive strength to our determination to stick to the fundamentals and to take a long-term view.

Fourth, that long-term view is accompanied by **a commitment to constant innovation and change**. As you'll read elsewhere in this report, Pearson has become a major innovator and investor in digital technologies – new reading experiences, new learning platforms, applications for new devices, new ways of communicating with and selling to our customers. This represents a profound and disruptive structural change in all our industries; we are encouraged by our progress so far but if we are to remain successful in this new world, we will need to continue to transform ourselves. And we will.

So, the story of 2009 is of a strong business, resolutely pursuing a successful strategy through tough markets and disruptive change.

My personal view is that the prospects for a sustained economic recovery remain fragile. We have to expect a prolonged period of severely restrained government and consumer spending. It's going to be a battle, but one we intend to keep fighting and winning. Pearson is prepared for it, and ready to help people carry on learning whatever the economic weather.

For that, I have to thank our people for their dedication and ingenuity; and our investors for their commitment to the company. As always, I look forward to seeing many of you at our annual meeting.



Glen Moreno Chairman

Pearson's strategy: Marjorie Scardino, chief executive

The Education of Pearson

"Anyone who stops learning is old, whether twenty or eighty."

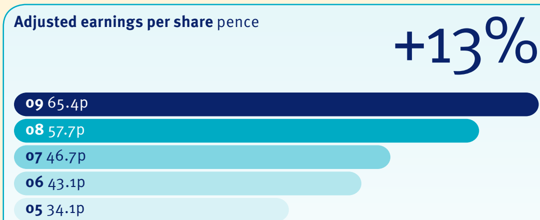
In that powerful sentence Henry Ford, one of the great innovators of the 20th century, captured perfectly our attitude to the 21st – we're trying to make sure we're **always learning**.

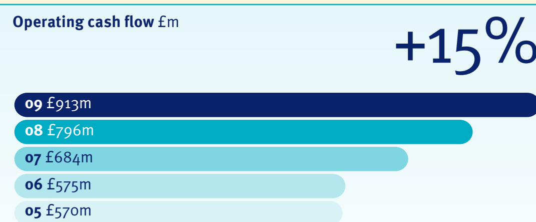
Marjorie Scardino Chief executive

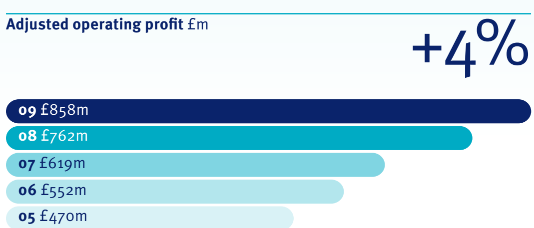
As a company, we learned a lot in 2009. We started the year facing a ragged array of challenges. The threat of a full financial meltdown looked less seismic, but the aftershocks of recession were rippling out to just about every one of our markets. At the same time, the gathering pace of disruptive technological change was testing the strategy and imagination of every media company.

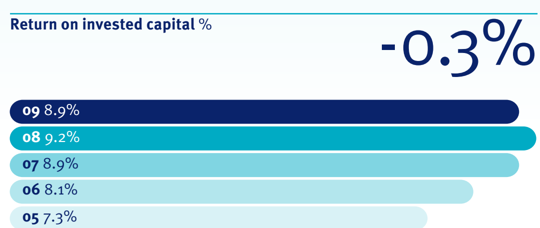
So we reviewed the lessons we'd learned in previous years – *keep our eyes on our goal; keep investing; keep people working; change, change, change*. And in spite of the challenges, we can now look back on 2009 as Pearson's best year yet.

To achieve that in any market would be a cause for modest pride. To achieve it in the most difficult trading conditions I've seen in my time at the company puts me in awe of my colleagues here. It's a testament to their talent, ingenuity and sheer bloody-minded grit, for which I'm grateful every day. And it's a just reward for our long-term shareholders who had confidence in our vision for Pearson when confidence was a scarce commodity. We thank you sincerely for your trust in us.









The 2009 lessons

Our approach to 2009 and the global economic downturn was aggressive. We saw an opportunity, not to ease off the gas but to accelerate, to invest both money and imagination in the fast-growing digital, services and international markets that have given us our impetus. We reckoned that in the short term we could pull further away from our competitors, and that in the long term we simply could not afford to pause for rest on the journey from publisher to digital services company that has been our goal for some years now.

I'm happy to say that, though we did not by any means get everything exactly right, that reckoning was true. **It showed up in our financial results**:

– Sales of £5.6bn, against £4.8bn in 2008, an increase of 4% at constant exchange rates;

– Profits of £858m, up 4% from £762m in 2008;

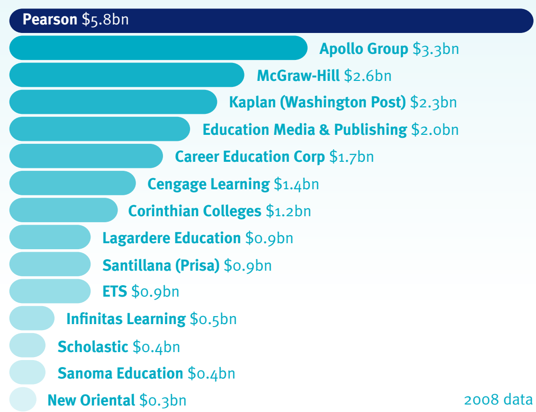
– Adjusted earnings per share of 65.4p, up from 57.7p in 2008 and well ahead of our expectations at the start of the year;

– A dividend increase of 5%, underlining our conviction that the dividend is both a reliable cash distribution to shareholders and a signal of the board's confidence and determination about the future.

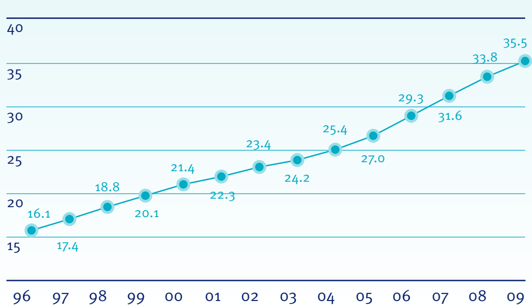
The lessons of our strategy also showed in some remarkably **strong competitive performances**:

In North America, we pulled further away from our traditional education competitors. In School and Higher Education we grew 5%, a full five percentage points faster than the industry. In testing, we won 60% of the state and national contracts that were up for bid during the year.

The world's leading education companies
Education revenues $bn



Dividend per share paid in fiscal year pence

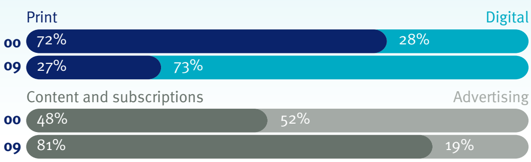


Pearson's strategy: Marjorie Scardino, chief executive continued

– In International education, we chalked up another year of good growth and at the same time built the foundations for faster progress in dynamic markets like China, India and Southern Africa.

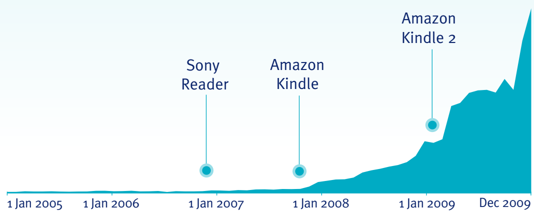
– At the FT Group, we produced healthy profits in spite of a precipitous fall in business advertising. This was possible because of our continued shift towards subscription and digital revenues.

Technology and services
FT Group revenue mix %



– And in Penguin we had another solid year of financial results and of great books while doing the things that will allow the publisher who invented the paperback to take its rightful place as a leader in the age of digital readers – both people and devices.

Trade publishing trends: digital
Penguin eBooks sold by month
2005 – 2009, US



(In some ways, those competitive performances are even more important than the financial results they make possible. They show that our customers are choosing Pearson's products and services – finding something more valuable or compelling or alluring in what we do. Those customers are the ultimate arbiters of whether our strategy is working.)

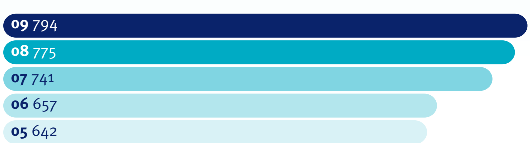
Our strategy

1

Long-term organic investment in content:

Over the past five years, **we have invested £2.3bn in content: new education programmes; new and established authors for Penguin; the FT's journalism.** In 2009, that investment reached an all-time high of £500m. We believe that this constant investment is critical to the quality and effectiveness of our products and services; and that it has helped us gain share in many of our markets.

Education and Penguin pre-publication expenditure and author's advances $m



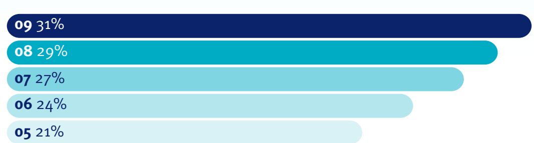
Our strategy

2

Digital and services businesses:

Our strategy centres on adding services to our content, usually enabled by technology, to make the content more useful, more personal, more valuable. These digital products and services give us access to new, bigger and faster growing sources of revenue to sustain our growth. In 2009, digital products accounted for £1.7bn in revenues – close to one-third of Pearson's total sales – and more than double the total five years ago.

Pearson's digital revenues
% of sales



Our world in 2010

Last year we faced down tougher markets – in some cases, much tougher. And we expect many to remain tough through this year. Some of our markets have 'cyclical challenges', and *all* our industries are going through a period of significant structural change.

So naturally, the question we've asked ourselves is: "Can we continue our record of performance in unpredictable markets and contracting economies?" To answer, we've had to stop and review our assumptions and revisit our plans. But our conclusion is a simple truth about demand: No matter what, people will still go to school; still need information about markets; still want to escape from their present into someone else's story. Those are the things we do.

And there is still much to do to further them. There are still 72 million children who don't go to school at all; still 30 million people who will enter university this year and not ever graduate; still a complex world of business, finance and politics to illuminate and explain; still buyers for some $70bn worth of books this year (and less than 2% of those are eBooks). So much to do.

Our approach to the task and our business is to stick with our strategy and to take a long-term view.

That may seem obvious, but don't take it as a 'business as usual' approach. We're making it ambitious and aggressive at every level.

Our *goal* is unchanged: *To help people make progress in their lives and to thrive in a brain-based economy through learning.* We're reaching for a wide definition of 'learning', though: one not constrained by age or circumstance or confined to a classroom. We think learning never stops: it's happening all the time, all around us. And we're setting out to prove it.

Our basic *strategy* to achieve that grand goal is pursued by all Pearson's businesses in some shape or form and has four fundamental parts:

1. To develop **high-quality, compelling, trustworthy content** that customers deem worth paying for;

2. To serve it up not just naked, but with **services, mostly delivered by technology**, to make it more useful, more valuable, more personal;

3. To work in **selected geographic markets** that are growing and have strong demand for our services;

4. To reap **cost savings and competitive advantages** from Pearson's global scale and the similarities of its businesses and processes **through efficiencies** in our central services.

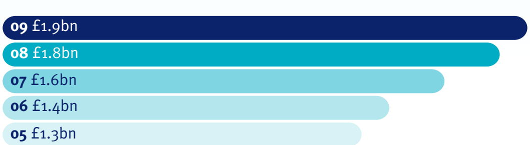
Our strategy

3

International expansion:

Pearson has market-leading positions in major developed economies – particularly the US, UK and Western Europe. We are already present in more than 60 countries and **we are investing to become a much larger global education company**, with particular emphasis on fast-growing markets in China, India, Africa and Latin America. Over the last five years, our international education business has grown headline sales at an average annual rate of 17%, becoming a £1bn business in 2009.

International revenues (outside USA and Canada) £bn



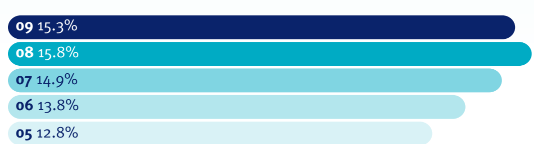
Our strategy

4

Efficiency:

Our investments in content, services and new geographic markets are fuelled by steady efficiency gains, often generated through Pearson's overall scale. Since 2005, our operating profit margins have increased from 12.8% to 15.3% and our ratio of average working capital to sales has improved from 27.4% to 25.1%. In 2009 our margins fell slightly compared to 2008 due to a decline in advertising, restructuring charges at Penguin and transactional exchange losses.

Pearson margins %



Pearson's strategy: Marjorie Scardino, chief executive continued

Who are we now?

Based on that goal and strategy, you should look out for many things that will continue to change in Pearson: our focus on consumers; our participation in more links of the chain of formal learning; our interest in training not only the minds of citizens, but also the skills of 21st-Century workers; our take-up of opportunities all over the world.

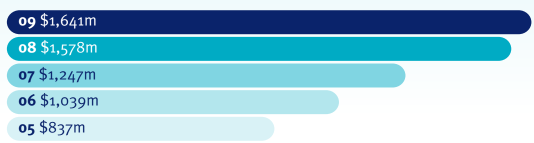
The 2009 results written up in this report are already just footnotes to history. Perhaps more important to you as you think about Pearson's future should be those things that are changing, because I believe Pearson today may not be *quite the company that you think we are.*

We're still a *publishing company* – and convinced that quality content is valuable. But today we're also *a digital services company,* and that change is responsible for our market share and efficiency as well as our growth opportunities.

In 2009, about a third of our sales came from digital products and services. Over the past five years, our digital revenues have grown at an average annual rate of 19%. Seven years ago, our testing and qualifications businesses (a good example of our providing education services, rather than 'products') had sales of less than £200m. This past year, they produced more than £1bn.

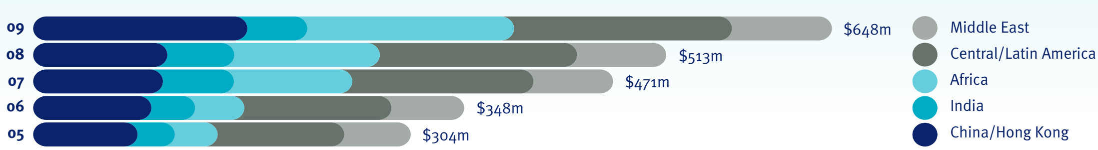
We're still proud to have strong roots in the UK, our historic 'home' market, and in North America, home to our largest concentration of business and people. But Pearson is becoming an ever more international company – in our mix of business and (maybe more importantly) in our attitude. Even though we've been growing well in the US, over the past five years Pearson's sales outside America have grown 11% per year on average and our profits outside America now amount to more than £250m, one-third of our operating profit.

Growth in services businesses
Pearson worldwide testing revenues $m



For some years now, our strategy has been yielding a virtuous circle of competitive advantage, strong financial results and heavy investment in new products. For now we believe that circle is spinning, but we can't count on its continuing. That's why we have to keep making changes of emphasis.

Rapid growth in emerging markets
Pearson revenues $m



We're certainly proud of 2009, but we're much more pleased about the foundations we've laid out for our next chapter. Our approach to that next chapter is based on a fundamental truth: We're always learning. But the experience of learning is different for every person. That's why we've been talking about and working on 'personalizing learning' long enough for it to become a buzz word.

So now we're trying to take it to a new level that still uses our strategy of content + services + internationalism + efficiency but is:

- more thoroughly involved in the whole process of education;
- more service-oriented than ever;
- more indifferent to medium;
- as interested in informal, consumer learning as in institutional learning and
- moving more deeply into the developing world.

We've made a good start on building the world's leading learning company. Our financial results say we're making progress. But we know that, to make more and faster progress, more and more of our customers have to see that we are also helping them make progress in their lives. That's our goal.

The road ahead

As we plunge out into 2010, we're clear that in macroeconomic terms the world is by no means a slick superhighway. We're expecting many of our markets to remain slow and subdued this year, and perhaps into the next one as well.

But *we're* anything but subdued. We have a successful strategy, one that's been producing consistent growth and high performance for some years now. We believe in it, and we're pushing ahead with it – with some bold changes.

Our strong performance – both financial and competitive – is largely the result of our having had the strategy and made the investment over the last decade to make Pearson a unified, digital, services-based, global education company. That strategy and investment will help us remain the innovator and the scale player in our industries, and remain both a durable company, and a long-term growth company, but not if we don't keep changing, keep learning.

That's why this 160-year-old company tries to be always learning. Like many students, we're finding that the learning itself can be as stimulating as the results. And all the time, that's making this company – one I hope you'd like to continue to call "your company" – stronger and stronger.

Marjorie Scardino Chief Executive

Our performance: 2009 financial overview

In 2009, Pearson's **sales increased 4%** at constant exchange rates to £5.6bn and **adjusted operating profit 4%** to £858m. Portfolio changes contributed 2% to sales and 2% to operating profit, largely in our education company. In underlying terms (ie, stripping out the benefit of both portfolio changes and currency movements), sales and operating profits increased by 2%.

Currency movements had a significant impact on reported results in 2009, adding £640m to sales and £69m to operating profit and contributing to headline sales and operating profit growth of 17% and 13% respectively. The currency impact was largely the result of the strengthening of the US dollar against sterling: we generated approximately 60% of our sales and profits in US dollars and the average exchange rate strengthened from £1:$1.85 in 2008 to £1:$1.57 in 2009.

Adjusted earnings per share were 65.4p, up 13% on a headline basis.

Operating cash flow increased by £117m to £913m (headline growth of 15%) and total free cash flow by £92m to £723m, or 90.5p per share (headline growth of 14%). **Cash conversion** was once again strong at 106% of operating profit and our ratio of average working capital to sales improved by a further 1.0% point. Our **tax rate** in 2009 was 25.5%, a little lower than in 2008.

Our **return on average invested capital** showed a headline reduction of 0.3% points to 8.9%, largely due to the impact of transaction foreign exchange on earnings. ROIC remains above our weighted average cost of capital.

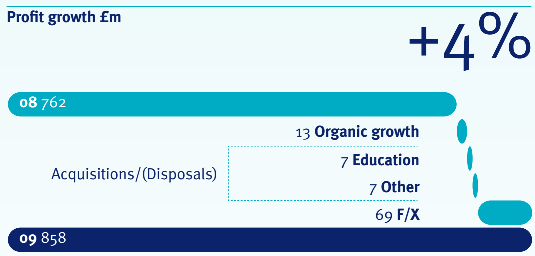
Statutory results show an increase of £79m in operating profit to £755m (£676m in 2008). **Basic earnings per share** for continuing businesses were 53.2p in 2009, up from 47.9p in 2008.

Net debt was £368m lower at £1,092m (£1,460m in 2008). Since 2000, Pearson's net debt/EBITDA ratio has fallen from 3.9x to 1.1x and our interest cover has increased from 3.1x to 8.8x.

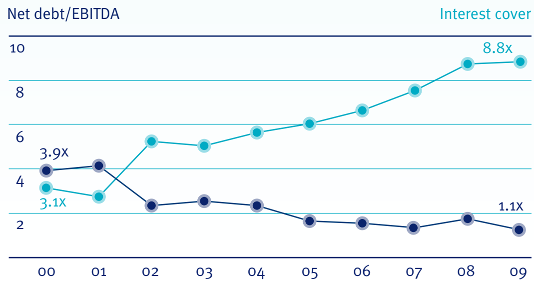
Dividend. The board is proposing a dividend increase of 5.0% to 35.5p, subject to shareholder approval. 2009 will be Pearson's 18th straight year of increasing our dividend above the rate of inflation. Over the past five years we have increased our dividend at a compound annual rate of 6%. Our dividend cover is now 1.8x.

Sales growth £m

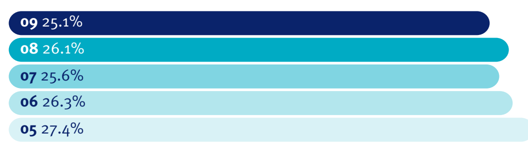
Profit growth £m



Balance sheet strength



Average working capital/sales %



Outlook: 2010

Pearson reported underlying growth in sales and operating profit in 2009, in spite of the exceptionally difficult macroeconomic environment and against record 2008 results. We achieved strong growth in education, helping us to make good financial progress even though our markets in US school publishing, financial advertising and consumer books were especially challenging.

Trading conditions in those tough markets began to ease towards the end of the year, but we are planning on the basis that some of our markets remain subdued throughout 2010. Even so, we expect Pearson to produce another year of underlying profit growth, helped by the overall resilience of our company and good growth prospects for our businesses in digital, services and emerging markets.

In **Education,** we believe that our sustained investment in content and our leadership position in learning services and technologies will enable us to build on our strong market positions. We expect to gain further share in the US School market which will benefit from a stronger adoption opportunity ($850m – $900m) and new federal funds, broadly offset by continued pressure on education funding at the state level. In Higher Education and International Education, we expect to produce further underlying growth and share gains.

At **FT Publishing,** we expect to sustain good renewal rates in our subscription businesses and healthy margins. Advertising revenues (which in 2009 accounted for less than 3% of total Pearson revenues) remain highly unpredictable but we expect to see some stabilisation after the sharp declines across the industry in 2009. **Interactive Data Corporation** expects 2010 revenues to range between $810m to $830m and healthy margins in the 25% to 26% range (guidance under US GAAP). As previously announced, the Board of Interactive Data Corporation is currently undertaking a preliminary review of strategic alternatives for the company.

We expect **Penguin** to post another good competitive performance in the context of a consumer books market that we expect to remain broadly level in 2010. Penguin will benefit from its leading position in the emerging market for eBooks and from the efficiency actions taken in 2009.

Interest and tax. In 2010, we expect our interest charge to adjusted earnings to be broadly level with 2009. We expect our P&L tax charge to be in the 25% to 27% range. We expect our cash tax rate to be around 15%.

Exchange rates. Pearson generates approximately 60% of its sales in the US. In 2009, a 5 cent move in the average £:$ exchange rate for the full year (which in 2009 was £1:$1.57) had an impact of approximately 1.3p on adjusted earnings per share.

North American Education

North American Education is **Pearson's largest business**, with 2009 sales of £2.5bn and operating profit of £403m. Over the past five years, it has increased both sales and profits at a compound annual growth rate of 8%. Building on our roots as a leading publisher of educational materials and provider of assessment services, we have made significant investments and change to transform Pearson into a world-leading provider of learning technologies for students and enterprise technologies for educational institutions.

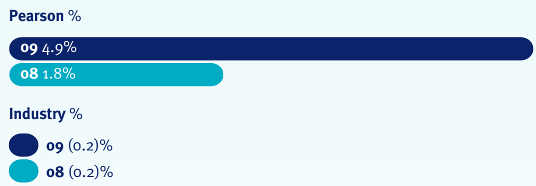
These technology services – including eCollege (3.5m student users in 2009), PowerSchool (8.5m), the MyLabs (6m) and Edustructures (8.1m) – are the backbone of our strategy to help educators raise student performance and institutions to become more effective. We are currently developing a new generation of powerful technologies to integrate student information, assessment, instruction and performance data into connected learning environments, for students and institutions at all levels of education.

In 2009, our combined US school curriculum and higher education businesses grew 5% on an underlying basis, once again outperforming the industry which was flat, according to the Association of American Publishers. We also achieved good margin improvement, benefiting from the growth of our higher education business and the successful integration of the Harcourt Assessment business acquired in 2008.

North American Education: Key performance indicators

£ millions	2009	2008	Headline growth	CER growth	Underlying growth
Sales	2,470	2,002	23%	5%	5%
Adjusted operating profit	403	303	33%	13%	13%

US combined school and college sales growth vs industry



Pearson's total year-on-year sales growth in school and college products in the US versus the year on year sales growth of the total US industry.

Adoption cycle win rates

Pearson's market share by value of new business in the US adoption states. Market share is quoted as a percentage of the total value of adoptions that we participated in.

State and national testing contract win rates

The lifetime value of US school testing contracts won by Pearson this year as a percentage of the total lifetime value of contracts bid for this year.

Online learning users

The number of registrations by students to access one of our US online learning programmes.

The education publishing industry is going through a period of significant structural change driven by the demand for high educational standards and accountability, the shift from print to digital products and a rapidly changing competitive environment.

Though the current economic climate has placed considerable pressure on state and local tax receipts – and therefore education funding – raising student achievement remains a key priority across the political spectrum in the US. In particular, the federal government's education reform proposals contain a range of measures designed to raise standards; use student data to improve classroom instruction; boost the quality of teachers and school leaders; and turn around the lowest-performing schools.

Higher Education Highlights in 2009 include:

The US Higher Education publishing market grew 11.5% in 2009, according to the Association of American Publishers. The industry benefited from strong enrolment growth and federal government action to support student funding.

Pearson grew faster than the industry and outperformed the market for the eleventh straight year, continuing to see strong demand for instructional materials enhanced by technology and customisation.

The MyLabs

Pearson's 'MyLab' digital learning, homework and assessment programmes again grew strongly. Our MyLab products saw **more than 6m student registrations globally, 39% higher than in 2008.** In North America, student registrations grew 37% to more than 5.6m. Evaluation studies show that the use of the MyLab programmes can significantly improve student test scores and institutional productivity.

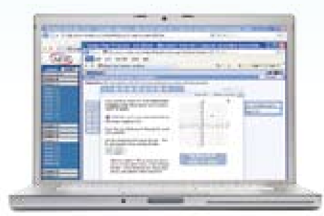
See more at **www.mymathlab.com**

Our sustained investment in content and technology continues to grow existing franchises and build new ones. In Engineering Mechanics, our market leading textbook Hibbeler's *Statics and Dynamics 12th Edition* gained an additional four percentage points of market share with the addition of our newly launched MasteringEngineering digital learning and assessment platform. Pearson became market leader in psychology supported by the recently launched textbook *Psychology 2nd Edition* by Cicarelli with MyPsychLab.

Custom Solutions grew strongly across both bespoke books and customised services including content creation, technology, curriculum, assessments and courseware. We partnered with the Kentucky Virtual Learning Initiative, for example, to deliver personalised mathematics instruction mapped to state college entry standards and have begun to extend this programme into transitional English and Reading.

eCollege

eCollege, our platform for fully-online distance learning in higher education, **increased online enrolments by 36% to 3.5m** and benefited from continued strong renewal rates of approximately 95% by value, new contract wins and strong growth in the usage of the platform, particularly by US for-profit colleges.



Thirteen Pearson higher education and school products in ten categories were nominated as America's best educational software products in the Software & Information Industry Association's 25th Annual CODiE Awards. They include MyMathLab, Miller & Levine Biology, PowerSchool, Prentice Hall Literature, myWorld Geography, MyWritingLab, CourseConnect and eCollege.

North American Education continued

Assessment and Information
Highlights in 2009 include:

Significant profit increase in Assessment and Information, benefiting from the successful integration of the Harcourt Assessment business acquired in 2008.

Our National Services assessment business renewed its contract with the College Board, worth $210m over 10 years, to process and score the SAT and contracts to support the College Board's new Readi-Step and ACCUPLACER diagnostics programmes.

Our State Services business won a number of significant new contracts including new programmes in Florida and Arizona. We continue to gain share, winning 60% of the contracts bid for by value, and to be a leader in online testing, delivering 9 million secure online assessments in 2009, up more than 100% on 2008.

Our Evaluation Systems teacher certification business secured contract extensions in California, Illinois, Arizona and Washington; won re-bids in Michigan and New York, each for five years; and added new contracts in California and Minnesota.

In Clinical Assessments, our AIMSWeb response-to-intervention data management and progress monitoring service for children who are having difficulty learning, continued to grow and now has more than 3 million students on the system.

Our Edustructures business, which provides interoperable systems to support data collection and reporting between school districts and state governments, doubled the number of students served to 8 million.

Our Student Information Systems (SIS) business continued to grow strongly, benefiting from strong demand for its services that help teachers automate and manage student attendance records, gradebooks, timetables and the like. It supports more than 12 million students – 8 million of them through its flagship PowerSchool product which is now available in more than 50 countries. In 2009 it won contracts for new school districts including Nova Scotia Department of Education (133,000 students), Newark, NJ (45,000 students), and the Hamilton County DOE, TN (40,000 students).

School Curriculum Highlights in 2009 include:

The US School publishing market declined 13.8% in 2009, according to the Association of American Publishers. State budget pressures and a slower new adoption year caused particular weakness in the basal publishing market.

US School publishing

Though Pearson's US School publishing sales declined, **we significantly outperformed the industry and took an estimated 37% of new adoptions competed for** (our highest market share for a decade) and 32% of the total new adoption market.

Pearson's enVisionMATH, an integrated print-and-digital programme, was the **top-selling basal programme in the US in 2009.** It helped Pearson to a market-leading 46% share of all maths adoptions and sold strongly across the open territories.

See more at **www.envisionmath.com**

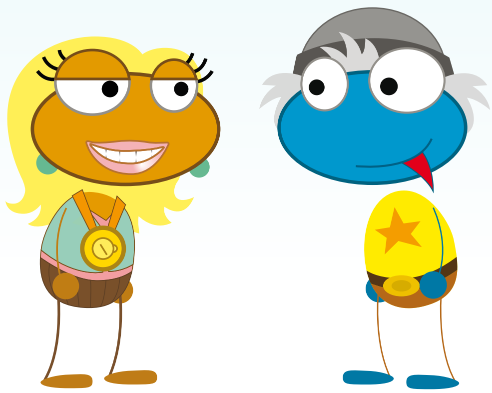
We successfully launched new blended digital curriculum programmes for the 2010 adoption campaign:

- Interactive Science **www.interactivescience.com**
- Prentice Hall Mathematics **www.poweralgebra.com/ www.powergeometry.com**
- Prentice Hall Literature **www.pearsonschool.com/live/ customer_central/microsite/connectedsampling/ overview/nat/lit/player.html**

Successnet, our online learning platform for teachers and students which supports Pearson's digital instruction, assessment and remedial programmes, grew strongly, achieving more than 4 million registrations in 2009.

Poptropica

Poptropica became one of the largest virtual worlds for young children in the US, with **unique visitors growing by more than 100%, to almost 70 million,** and the numbers of characters they have created approaching 200m, up 150% on 2008.



See more at **www.poptropica.com**

International Education

Pearson is the **world leader** in education publishing and related services outside North America. Over the past five years, this has been Pearson's fastest-growing business, increasing sales at a headline compound annual growth rate of 17% (from £559m in 2005 to £1,035m in 2009) and operating profit almost three-fold (from £51m in 2005 to £141m in 2009). The business has achieved strong organic growth and successfully integrated a number of acquisitions including Edexcel, Harcourt International and PBM. In 2009 we further extended our international scale, acquiring Wall Street English, a chain of premium English language training centres in China; and investing in vocational training and online learning in India.

Our 2009 results reflect good organic growth, continued investment in bolt-on acquisitions (Maskew Miller Longman, Longman Nigeria and Fronter announced in 2008 and Wall Street English in 2009) and currency movements. Our International Education business operates in 67 countries across the globe and has significant exposure to a wide range of currencies including the US dollar and the euro. In 2009, currency movements boosted revenues by £60m but reduced adjusted operating profits by £17m compared to 2008.

Looking ahead, we expect our International Education businesses to continue to benefit from a series of powerful growth trends: increasing public and private spending on education; growing participation rates in elementary, secondary and higher education; the demand for assessment to provide measures of achievement; the growing technology infrastructure in educational institutions; and the rise of English and other international languages.

International Education: Key performance indicators

£ millions	2009	2008	Headline growth	CER growth	Underlying growth
Sales	1,035	866	20%	13%	4%
Adjusted operating profit	141	135	4%	19%	14%

Online learning users

Registration no.

09	474,068
08	301,931

The number of registrations by students and professors to access one of our International Education online learning programmes.

Online results logins

Logins no.

09	79,751
08	55,244

Number of logins by users of International Education's online results service.

Global Highlights in 2009 include:

'MyLab' digital learning, homework and assessment programmes were used internationally by more than 470,000 students, up almost 60% on 2008, and are now sold in more than 200 countries worldwide.

Pearson Test of English

We launched the Pearson Test of English, our new test of Academic English which will be **delivered in up to 200 Pearson VUE testing centres in 37 countries.** Approximately 1,000 academic programmes worldwide now recognise, or are in the process of recognising, the Pearson Test of English.

Our eCollege learning management system is growing rapidly in international markets, winning new contracts in Australia, Brazil, Mexico, Colombia, Puerto Rico and Saudi Arabia.

Fronter

The Fronter learning management system continued to grow very strongly with **more than 6 million students** in more than 8,000 schools, colleges and Universities around the world.

Our new Pearson Learning Solutions business won its first contracts in the UK, the Gulf and Africa. It combines a broad range of products and services from across Pearson to deliver a systematic approach to improving student performance.

Africa and the Middle East Highlights in 2009 include:

Pearson successfully implemented the Abu Dhabi Education Council's External Measurement of Student Achievement programme covering English, Arabic, Maths and Science in April 2009 and was also contracted by the United Arab Emirates Ministry of Education to deliver the programme in the northern emirates.

In South Africa, Pearson launched Platinum, the first blended print and online course developed for the South African National Curriculum. 7,000 students registered for MyMathLab+, at the University of Witwatersrand, helping raise student pass rates in its initial phase from 31% in the first semester to 60% in the second semester.

Asia and Pacific Highlights in 2009 include:

English language teaching

We acquired Wall Street English, China's leading provider of premium English language training to adults, for $145m. **The combination of Longman Schools and Wall Street English gives Pearson a leading position in the English language teaching market in China,** serving students from elementary school to professional levels.

乐宁教育 Longman Schools

WALL STREET ENGLISH

We stepped up our presence in the Indian education market with two investments totalling $30m: a 50:50 joint-venture with Educomp, called IndiaCan, to offer vocational and skills training through 120 training centres across the country; and a 17.2% stake in TutorVista, which provides online tutoring for K-12 and college students.

International Education
continued

Continental Europe Highlights in 2009 include:

The launch of our digi libre (Content Plus) products helped us to gain share in the lower and upper secondary markets in Italy and positions us well for major curriculum reforms planned for 2010.

In Spain, our sales were down sharply with pressures on central and regional government spending and a worsening retail environment.

Our ELT sales continued to grow in Poland, and across central and Eastern Europe we saw good demand for our publishing and digital resources and our fledgling Language Learning Solutions activities.

Latin America Highlights in 2009 include:

New editions of the proven bestsellers, *BackPack* and *Pockets*, along with the successful launch of two new courses, *CornerStone* and *KeyStone*, helped to deliver strong growth in the sales of ELT materials across Latin America.

In Brazil, which has one of Latin America's largest and fastest-growing university populations, our virtual library now supports 30 post-secondary institutions.

And, in Panama, 75,000 high school students are now learning Biology and Chemistry, using Prentice Hall Virtual Labs.

United Kingdom Highlights in 2009 include:

We received over 3.7 million registrations for vocational assessment and general qualifications. We marked 4.5 million 'A'-level and GCSE scripts on-screen and successfully delivered the 2009 National Curriculum test series and were awarded the contract to administer the 2010 National Curriculum Tests at Key Stage 2.

Our qualifications

We made significant investments in supporting the new Diploma qualification for 14-19 year-olds; the IGCSE qualifications to meet the needs of International schools and colleges; and BTEC, our flagship vocational qualification. **BTEC registrations totalled more than 1 million** for the first time and were up almost 30% on 2008.

Our Higher Education business grew strongly, helped by the success of new first editions, the rapid take up of MyLabs adapted to meet local requirements, and the growing popularity of custom publishing. Sales of UK primary resources fell, on the back of minimal curriculum change and some signs of schools managing their budgets more tightly.

Professional Education

Our Professional Education business is focused on testing and certifying adults to become professionals; and on publishing and other learning programmes for professionals in business and technology. Over the past five years, we have increased sales in this division at a compound annual rate of 8% and operating profit from a profit of £2m in 2005 to a profit of £43m in 2009. Over that period, we significantly re-oriented our professional publishing businesses towards digital products and sales channels and built professional testing into a profitable industry leader. We expect these businesses to benefit from rising demand for work-related skills and qualifications in both developed and developing markets; and from close connections with professional content and customers in other parts of Pearson.

Professional testing and certification
Highlights in 2009 include:

In the UK, we extended our contract with the Driving Standards Agency to deliver the UK drivers theory test until 2014. With the Graduate Management Admissions Test and the recent contract extension for the NCLEX nursing examination, our three largest professional testing contracts now run to 2013 or after. More than seven million secure online tests were delivered in more than 4,000 test centres worldwide in 2009, an increase of 9% over 2008.

Registration volumes for the Graduate Management Admissions Council test rose 8% worldwide in 2009, including a 16% increase outside the US.

In the US, Pearson VUE won a number of new contracts with organisations including Oracle, Citrix, Novell, VMWare, and Adobe, the National Registry of Food Safety Professionals and the National Institute for Certification in Engineering Technologies.

Pearson VUE extended its international reach, signing an agreement with the Dubai Road and Transport Authority to deliver a new, high-tech Driver Testing System and launching the Law School Admission Test in India.

Professional Education: Key performance indicators

£ millions	2009	2008	Headline growth	CER growth	Underlying growth
Sales	275	244	13%	(1)%	(1)%
Adjusted operating profit	43	36	19%	8%	8%

Professional publishing Highlights in 2009 include:

Our Professional education business experienced tough trading conditions in the retail market but benefited from the increased breadth of its publishing and range of revenue streams, from online retail through digital subscriptions.

A best-selling product in 2009 was CCNA Network Simulator, which are digital networking labs designed, developed and published by Pearson, to help candidates successfully pass the Cisco CCNA certification exam.

Pearson launched new learning solutions for IT Professionals preparing for certification accreditation. Cert Flash Card applications were launched for students studying for Cisco CCNA, CompTIA and Microsoft certification exams and are accessible through web browsers and iPhone and iPod Touch devices.

FT Press launched a new e-publishing imprint, FT Press Delivers, providing essential insights from some of its leading business authors including Jim Champy, Brian Solis, Mark Zandi, Jon M. Huntsman, John Kao, Michael Abrashoff, and Seth Goldman.

FT Group

The FT Group is a **leading provider of essential information** in attractive niches of the global business information market. These include insight and analysis through the *Financial Times*, FT.com, Money-Media and *The Economist*, and intelligence, valuations and indices through Mergermarket, Interactive Data and FTSE.

In recent years, the FT Group has significantly shifted its business towards digital and subscription revenues. We have sold our largely print and advertising-based national media companies (Recoletos in Spain, Les Echos in France, FT Deutschland in Germany); acquired digital businesses with international opportunities (Mergermarket, Exec-Appointments.com, Money-Media, Mandate Wire and Medley Global Advisors); and invested steadily in our global and digital businesses including the *Financial Times*, FT.com and Interactive Data.

As a result of this strategy, in 2009 digital products and services accounted for 73% of FT Group revenues, up from 28% in 2000; and in 2009 advertising accounted for 19% of FT Group revenues, down from 52% in 2000. On a continuing business basis, FT Group sales have increased at a headline compound average growth rate of 11% (from £546m in 2005 to £842m in 2009) and profits by 18% (from £97m to £187m).

Looking ahead, we believe that the FT Group's premium and global positions, combined with our digital and subscription businesses, put us in a good position to weather tougher economic conditions.

FT Group: Key performance indicators

£ millions	2009	2008	Headline growth	CER growth	Underlying growth
Sales					
FT Publishing	358	390	(8)%	(12)%	(12)%
Interactive Data	484	406	19%	5%	2%
Total	**842**	**796**	**6%**	**(3)%**	**(5)%**
Adjusted operating profit					
FT Publishing	39	74	(47)%	(42)%	(42)%
Interactive Data	148	121	22%	7%	2%
Total	**187**	**195**	**(4)%**	**(12)%**	**(14)%**

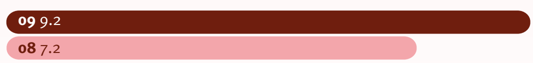
FT circulation revenue growth

Growth %

The FT Newspaper's year-on-year growth in circulation revenue.

The average monthly number of unique users of FT.com for the year

No. millions



The average monthly number of unique users of FT.com for the year.

Mergermarket renewal rates

Mergermarket %

Debtwire %

The current year value of sales to existing customers as a percentage of their spend in the previous year.

Interactive Data customer retention

Retention %

The number of customers renewing contracts as a percentage of total customer base.

FT Publishing Highlights in 2009 include:

FT Publishing's margins sustained at more than 10%, despite double digit revenue declines caused by tough market conditions for financial and corporate advertising. FT Publishing revenues declined 12% as the impact of advertising revenue declines was partly mitigated by growth in content revenues and the resilience of our subscription businesses.

A growing audience

We continued to see good demand for high-quality analysis of global business, finance, politics and economics resulting in:

A 15% increase in FT.com's paying online subscribers to more than 126,000, and 750 direct corporate licences.

Registered users on FT.com up 85% to 1.8m and up 12% to 1.4m on FTChinese.com.

While *Financial Times* worldwide circulation was 7% lower at 402,799 (for the July – December 2009 ABC period), subscription circulation grew modestly.

Digital publishing

We continued to invest in fast-growing digital formats. We launched a new luxury lifestyle website, to complement our existing *How To Spend It* magazine; a new iPhone application which has received more than 200,000 downloads; and, in association with Longman, Lexicon, an online glossary of economic, financial and business terms.

See more at **www.howtospendit.com**

FT Group
continued

Mergermarket faced challenging conditions in some of its markets with reduced Mergers and Acquisition activity impacting the merger arbitrage sector serviced by dealReporter whilst Debtwire benefited from an increased focus on distressed debt.

Mergermarket

Mergermarket continued to launch new products and expand globally. Our newest product, MergerID, launched in September 2009, provides **a secure online environment for principals and professionals to post and view M&A opportunities** globally and has secured over 1,500 active users in more than 450 companies across the globe.

The Economist, in which Pearson owns a 50% stake, increased global weekly circulation by 2.2% to 1.42m (for the July – December 2009 ABC period).

FTSE, our 50% owned joint-venture with the London Stock Exchange, increased revenues 17% and made a strong improvement in profits.

Interactive Data Highlights in 2009 include:

Interactive Data revenues up 5% and operating profit up 7% to £148m (£121m in 2008) driven by its Institutional Services segment, despite difficult market conditions in the financial services industry. In the fourth quarter we began to see continued signs of trading conditions easing in certain markets that were difficult earlier in the year, principally in our new sales.

Interactive Data continued to benefit from growth trends including: heightened scrutiny around the valuation of securities; increasing regulation and related investment in compliance and risk management processes; increasing adoption of low latency data for algorithmic trading; and continuing need to cost-effectively differentiate wealth management offerings with bespoke web-based client solutions.

Pricing and Reference Data (66% of Interactive Data revenues) continued to generate good growth in North America and Europe. Growth was primarily organic and also benefited from bolt-on acquisitions, most recently NDF, a leading provider of financial pricing and services in Japan, and Kler's Financial Data Service, a leading provider of reference data to the Italian financial industry.

Real-Time Services (19% of Interactive Data revenues) faced challenging market conditions as solid demand for web-based Managed Solutions was more than offset by higher cancellations of real-time market data services. In December 2009, we formed the Real-Time Market Data and Trading Solutions Group which combines the resources of our eSignal, Managed Solutions and Real-Time Services businesses into a single organisation. This initiative supports plans to integrate the company's suite of real-time market data and innovative, hosted technology services and solutions to more effectively capitalize on opportunities in the wealth management and electronic trading sectors. In addition, Interactive Data recently completed two acquisitions, 7ticks and the data and tools assets of Dow Jones' Online Financial Solutions business, that help further strengthen its real-time capabilities in the wealth management and electronic trading sectors.

Interactive Data continued to invest in expanding the breadth and depth of the data covered and products offered. Pricing and Reference Data added new information resources, transparency tools, and broader coverage of hard-to-value instruments. It also introduced new services such as the Business Entity Service and Options Volatility Service aimed at helping firms address risk management and compliance challenges. In Real-Time Services, investments were aimed at expanding market coverage to include a broader range of emerging markets, level 2 data for a variety of global exchanges, and multi-lateral trading facilities. New product launches in this business included PlusBook™, a new consolidated order book service for the European financial industry, and enhancements to the PrimePortal product, which are used to create customised Web solutions for wealth management and infomedia applications. eSignal introduced new services and enhanced existing offerings such as its Market-Q browser-based workstation, which has been well received in the North American wealth management market.

Interactive Data

Interactive Data made a number of bolt-on acquisitions in late 2009 and into early 2010 including: the data and tools assets of Dow Jones and Company's OFS business, which expands the growing web-based solutions business in North America; Dubai-based Telerate Systems Limited (completed on 14 January 2010), a long-time eSignal sales agent; and 7ticks (completed on 15 January 2010), an innovative provider of very fast electronic trading networks and managed services.

Interactive Data's full year earnings announcement and outlook for 2010 is available at: www.interactivedata-rts.com

On 15 January 2010, Pearson and Interactive Data announced that Interactive Data's Board of Directors is conducting a preliminary review of strategic alternatives for the Company. As previously stated, there can be no assurance on the potential outcome or timing of this review process.

Penguin

Penguin is **one of the most famous brands in book publishing**, known around the world for the quality of its publishing and its consistent record of innovation. Over the past five years, Penguin's sales have increased at an average rate of 2% and profits at 5% – the result of a plan to generate significant margin improvement.

That plan has four major parts:

1. Investing consistently and in a disciplined way in **author and product development**;

2. Developing a **globally co-ordinated publishing organisation**, benefiting from worldwide scale and rapid rates of growth in literacy, education and demand for books in emerging markets;

3. Innovating with **digital technologies** to provide new reading experiences, new ways to market, new sales channels, and more efficient means of production, storage and distribution of content;

4. **Becoming a more efficient organisation**, focusing on margin progression, working capital discipline and cash generation. In 2009, Penguin successfully implemented a series of organisational changes in the UK designed to strengthen its publishing, reduce costs and accelerate the transition to digital production, sales channels and formats, and to lower cost markets for design and production. Penguin's 2009 results include approximately £9m of charges relating to these organisational changes.

Penguin operates in 15 countries across the globe and has significant exposure to a wide range of currencies including the US and Australian dollars. In 2009, currency translation boosted revenues by £109m and adjusted operating profits by £13m compared to 2008. Adjusted operating profits were reduced by a transaction exchange loss of £6m.

Looking ahead, Penguin's strategy involves further investment in publishing in both established and emerging markets, in continued digital innovation and in efficiency improvements, as it seeks to build on its strong competitive position and accelerate sales growth.

Penguin Group: Key performance indicators

£ millions	2009	2008	Headline growth	CER growth	Underlying growth
Sales	1,002	903	11%	(1)%	(2)%
Adjusted operating profit	84	93	(10)%	(17)%	(19)%

US bestsellers

Bestsellers no.

The number of Penguin books entering the Top Ten bestseller lists in the US (New York Times).

UK bestsellers

Bestsellers no.

The number of Penguin books entering the Top Ten bestseller lists in the UK (Neilson BookScan Top Ten).

eBook sales

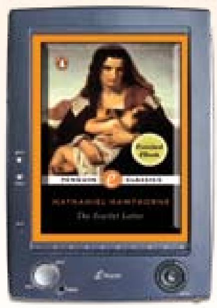
Sales %

Penguin global eBook sales as a percentage of Penguin Group net sales.

Penguin Highlights in 2009 include:

ebooks

eBook sales grew fourfold on the previous year. 14,000 eBook titles are now available. eBook sales are expected to grow rapidly in 2010, benefiting from the popularity of e-readers such as Amazon's Kindle, the Sony Reader and Barnes and Noble's nook as well as new devices such as Apple's iPad.



2009 bestsellers

In the US, Penguin had 30 #1 New York Times bestsellers, Penguin's most ever, and placed 243 bestsellers on New York Times lists. Bestsellers included debut novels such as Kathryn Stockett's *The Help* and Janice Y.K. Lee's *The Piano Teacher,* along with books by established authors such as Charlaine Harris and Nora Roberts.

In the UK, top-selling titles included Marian Keyes' *This Charming Man*, Malcolm Gladwell's *Outliers*, Ant and Dec's *Ooh! What a Lovely Pair* and Antony Beevor's *D-Day*. Penguin Children's list had a very strong year with standout performances from brands such as *The Very Hungry Caterpillar* (which celebrated its 40th anniversary) and *Peppa Pig*. Through an iPhone app, consumers were offered a try-before-you-buy model of Paul Hoffman's *The Left Hand of God*, providing free downloads of the first three chapters.

In Australia, Penguin was named Publisher of the Year for the second year running at the Australian Book Industry Awards. #1 bestselling authors included Bryce Courtenay, Tom Winton, Clive Cussler and Richelle Mead.

In Canada, top-selling local authors included Joseph Boyden and Alice Munro, who was awarded the International Man Booker prize, and our international authors Greg Mortenson and Elizabeth Gilbert led the paperback non-fiction category.

In India, Penguin is the largest English language trade publisher, with bestselling authors in 2009 including Narayana Murthy and Nandan Nilekani.

In South Africa, top-selling Penguin authors included John van de Ruit and Justin Bonello.

2010 highlights

In 2010, Penguin will publish major books including *Our Kind of Traitor* by John le Carre, two books from chef Jamie Oliver (*Jamie Does* and *20 Minute Meals*), *A Passion for Design* by Barbra Streisand, *The Weekend That Changed Wall Street* by CNBC's Maria Bartiromo, and a new series of paperbacks entitled Penguin Decades as part of Penguin's 75th birthday celebration. Penguin China's English language publishing programme will launch in 2010, with books including *Shanghai: A History in Photographs 1842 – Today.*

Other financial information

Net finance costs

£ millions	2009	2008
Net interest payable	(85)	(89)
Net foreign exchange losses reflected in adjusted earnings	–	(7)
Finance (costs)/income in respect of employee benefit plans	(12)	8
Net finance costs reflected in adjusted earnings	(97)	(88)
Other net finance income/(costs)	2	(3)
Total net finance costs	(95)	(91)

Net finance costs reported in our adjusted earnings comprise net interest payable, net finance costs relating to employee benefit plans and certain foreign exchange gains and losses.

Net interest payable in 2009 was £85m, down from £89m in 2008. Although our fixed rate policy reduces the impact of changes in market interest rates, we were still able to benefit from a fall in average US dollar and sterling interest rates during the year. Year-on-year, average three month LIBOR (weighted for the Group's net borrowings in US dollars and sterling at each year end) fell by 2.4% to 0.7%. This reduction in floating market interest rates was partially offset by higher fixed bond coupons prevailing at the time of our 2009 bond issue. The overall result was a decrease in the Group's average net interest rate payable by 0.6% to 5.3%. The Group's average net debt rose by £90m, reflecting the impact of acquisitions and disposals and the weakening of average year-on-year sterling exchange rates relative to the US dollar, in which the majority of our debt is denominated.

Finance charges relating to post-retirement plans were £12m in 2009 compared to an income of £8m in 2008 as a result of lower returns on plan assets. Exchange losses reported in adjusted earnings in 2008 of £7m related to retranslation of foreign currency bank overdrafts. There were no equivalent exchange gains or losses in 2009.

Also included in the statutory definition of net finance costs are foreign exchange and other gains and losses. These are excluded from adjusted earnings as they represent short-term fluctuations in market value and are subject to significant volatility. These 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 2009 the total of these items excluded from adjusted earnings was a profit of £2m compared to a loss of £3m in 2008.

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.

Net debt

£ millions	2009	2008
Cash and cash equivalents	750	685
Marketable securities	63	54
Net derivative assets	103	164
Bonds	(1,923)	(2,128)
Bank loans and overdrafts	(70)	(228)
Finance leases	(15)	(7)
Net debt	**(1,092)**	**(1,460)**

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 2009 (from $1.44 to $1.61:£1) is a significant contributor to the decrease in our reported net debt.

The Group's credit ratings remained unchanged during the year. The long-term ratings are Baa1 from Moody's and BBB+ from Standard & Poor's, and the short-term ratings are P2 and A2 respectively. The Group's policy is to strive to maintain a rating of Baa1/BBB+ over the long term.

In March 2009, the Group accessed the capital markets, raising £300m through the sale of notes maturing in 2015 and bearing interest at 6%. Of the £300m issued, £200m was swapped into US dollars for the life of the bond to conform with the policy described in note 19. The proceeds were used to repay floating rate amounts outstanding under our revolving credit facility, as described below.

The Group has in place a $1,750m committed revolving credit facility, of which $92m matures in May 2011 and the balance of $1,658m matures in May 2012. At 31 December 2009 the facility was undrawn.

The facility is intended to be 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 2009, 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 2009 was 25.5% which compares to an effective rate of 26.4% for 2008. Our overseas profits, which arise mainly in the US are largely subject to tax at higher rates than the UK corporation tax rate (an effective rate of 28% in 2009 compared to 28.5% in 2008). Higher tax rates were more than offset by amortisation-related tax deductions and releases from provisions reflecting continuing progress in agreeing our tax affairs with the authorities.

The reported tax charge on a statutory basis was £198m (30.0%) compared to a charge of £172m (29.4%) in 2008. The tax charge relating to the sale of the Data Management business in February 2008 is included in the loss on discontinued businesses. A charge arose on this disposal as although there is a book loss there is a gain for tax purposes. Tax paid in 2009 was £103m compared to £89m in 2008.

Discontinued operations

Discontinued operations in 2008 relates to Data Management business that were sold on 22 February 2008.

Minority interests

Minority interests comprise mainly the 39% share of Interactive Data Corporation, a US listed business.

Other comprehensive income

Included in other comprehensive income are the net exchange differences on translation of foreign operations. The loss on translation of £388m in 2009 compares to a gain in 2008 of £1,125m 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 2008 from an opening rate of £1:$1.99 to a closing rate at the end of that year of £1:$1.44. At the end of 2009 the US dollar had weakened in comparison to the opening rate moving from £1:$1.44 to £1:$1.61.

Dividends

The dividend accounted for in our 2009 financial statements totalling £273m represents the final dividend in respect of 2008 (22.0p) and the interim dividend for 2009 (12.2p). We are proposing a final dividend for 2009 of 23.3p, bringing the total paid and payable in respect of 2009 to 35.5p, a 5.0% increase on 2008. This final 2009 dividend was approved by the board in February 2010, is subject to approval at the forthcoming AGM and will be charged against 2010 profits. For 2009 the dividend is covered 1.8 times by adjusted earnings.

We seek to maintain a balance between the requirements of our shareholders for a rising stream of dividend income and the reinvestment opportunities which we identify around the Group. The board expects to raise the dividend more in line with earnings growth, above inflation while building our dividend cover towards two times earnings.

Pensions

Pearson operates a variety of pension plans. Our UK Group 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.

The income statement expense for defined benefit plans is determined using annually derived assumptions as to discount rates, investment returns and salary inflation, based on prevailing conditions at the start of the year. The assumptions for 2009 are disclosed in note 25 to our accounts, along with the year end surpluses and deficits in our defined benefit plans.

Other financial information continued

The charge to profit in respect of worldwide pensions and post-retirement benefits amounted to £94m in 2009 (2008: £76m) of which a charge of £82m (2008: £84m) was reported in operating profit and the net finance cost of £12m (2008 benefit: £8m) was reported against net finance costs.

The overall surplus on the UK Group plan of £49m at the end of 2008 has become a deficit of £189m at 31 December 2009. This is mainly due to an increase in liabilities as a result of an increase in the expected rate of future inflation, strengthening of mortality assumptions and a decrease in the discount rate used to value the liabilities.

Acquisitions

On 15 April 2009 the Group acquired Wall Street English, China's leading provider of premium English language training to adults. On 15 July 2009 the Group completed the purchase of an additional stake in Maskew Miller Longman, its South African publishing business.

Net cash consideration for all acquisitions made in the year ended 31 December 2009 was £201m and provisional goodwill recognised was £205m.

In total, acquisitions completed in the year contributed an additional £88m of sales and £10m of operating profit.

Return on invested capital (ROIC)

Our ROIC is calculated as adjusted operating profit less cash tax, expressed as a percentage of average gross invested capital. ROIC declined by 0.3% from 9.2% in 2008 to 8.9% in 2009. Transactional exchange gains, reported in adjusted operating profit and caused by the relative weakness of sterling in 2008, helped our ROIC by 0.2% in that year. In 2009 these transactional exchange gains became losses, as sterling strengthened for much of the year, negatively impacting our ROIC by 0.1%. The majority of transactional exchange gains and losses are in our International Education business and to a lesser extent it also impacts Penguin and the FT Group. The movements predominantly arise in trading companies that have significant revenues in multiple currencies. In 2009 transactional exchange recorded in operating profit was £27m lower than in 2008.

Capital expenditure

Net capital expenditure in the year on property, plant equipment and software amounted to £126m. The analysis of capital expenditure and details of capital commitments are shown in notes 10, 11 and 33 of the financial statements.

Transactions with related parties

Transactions with related parties are shown in note 34 of the financial statements.

Post balance sheet events

During January 2010, the Group announced that Interactive Data was undertaking a preliminary review of strategic alternatives for its business. At the date of this report, the outcome of the review is still uncertain.

On 3 February 2010 the FT Publishing business announced the acquisition of Medley Global Advisors LLC a premier provider of macro policy intelligence to the world's top investment banks, hedge funds and asset managers for $15.5m.

Supplier payment policy

Operating companies are responsible for agreeing the terms and conditions under which business transactions with their suppliers are conducted. These supplier payment terms vary by operating company reflecting the different industries and countries in which they operate. It is company policy that suppliers are aware of such terms of payment and that payments to them are made in accordance with these, provided that the supplier is also complying with all the relevant terms and conditions. Group trade creditors at 31 December 2009 were equivalent to 32 days of purchases during the year ended on that date. The company does not have any significant trade creditors and therefore is unable to disclose average supplier payment terms.

Principal risks and uncertainties: Group

We conduct regular risk reviews to identify risk factors which may affect our business and financial performance. Our Group internal audit function facilitates risk reviews with each business, shared service operations and corporate functions, identifying measures and controls to mitigate these risks. Management is responsible for considering and executing the appropriate action to mitigate these risks 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

As the current economic environment remains dynamic and challenging, the risk of weak trading conditions continues in 2010 which could adversely impact the company's financial performance. The outlook for the company for 2010 is set out on page 15. The effect of a continued deterioration in the global economy will vary across our businesses and will depend on the depth, length and severity of any economic downturn.

Our principal risks and uncertainties are outlined below.

Risk	Mitigating factors
Principal risks and uncertainties	
A significant deterioration in Group profitability and/or cash flow caused by a severe economic depression could reduce our liquidity and/or impair our financial ratios, and trigger a need to raise additional funds from the capital markets and/or renegotiate our banking covenants.	The Group's approach to funding is described on page 30 and the Group's approach to the management of financial risks is set out in note 19 to the financial statements.
Our US educational solutions and assessment businesses may be adversely affected by changes in state and local educational funding resulting from either general economic conditions, changes in government educational funding, programme and legislation (both at the federal and state level), and/or changes in the state procurement process.	Our customer relationship teams have detailed knowledge of each state market. We are investing in new and innovative ways to expand and combine our product and services to provide a superior customer offering when compared to our competitors, thereby reducing our reliance on any particular funding stream in the US market.
We generate a substantial proportion of our revenue in foreign currencies particularly the US dollar, and foreign exchange rate fluctuations could adversely affect our earnings and the strength of our balance sheet.	The Group's policy on managing foreign currency risk is described in note 19 to the financial statements.
Our intellectual property and proprietary rights may not be adequately protected under current laws in some jurisdictions and that may adversely affect our results and our ability to grow.	We seek to mitigate this type of risk through general vigilance, co-operation with other publishers and trade associations, advances in technology, as well as recourse to law as necessary. We take steps to challenge illegal distribution sources.
Our reported earnings and cash flows may be adversely affected by changes in our pension costs and funding requirements.	We review our funding arrangements every three years and will take steps to ensure pension funding plans are sufficient to meet future liabilities without unduly affecting the development of the company.
We operate in a highly competitive environment that is subject to rapid change and we must continue to invest and adapt to remain competitive.	To remain competitive we continue to invest in our authors, products, services, technology and people to take advantage of these opportunities. There is no guarantee that these investments will generate the anticipated returns or protect us from being placed at a competitive disadvantage with respect to scale, resources and our ability to develop and exploit opportunities.

Principal risks and uncertainties: Group continued

Risk	Mitigating factors
Principal risks and uncertainties (continued)	
A major data privacy breach may cause reputational damage to our brands and financial loss.	Through our global security office under the direction of our Chief Security Officer, we have established various data privacy and security programmes. We constantly 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 comply with relevant legislation and contractual requirements.
Other risks and uncertainties	
At Penguin, changes in product distribution channel and/or customer bankruptcy may restrict our ability to grow and affect our profitability.	We develop new distribution channels by adapting our product offering and investing in new formats. The application of strict credit control policies is used to monitor customer debt and we work with industry groups to minimise exposures (e.g. through retention of title claims) in the event of default.
Reductions in advertising revenues and/or circulation will adversely affect the profitability of our newspaper business.	The diversification of the FT Group into other business models and revenue streams, e.g. subscription based businesses, digital revenues, business to business products, conferences, in addition to its global reach, offsets reliance on newspaper print advertising and circulation revenue streams.
Operational disruption to our business caused by a major disaster and/or external threats could restrict our ability to supply products and services to our customers.	We have developed business continuity arrangements, including IT disaster recovery plans and back-up delivery systems, to minimise any business disruption in the event of a major disaster. The governance structure, overseen by a global coordinator, provides the capability to centrally monitor all related activities. A concerted effort was undertaken to facilitate creation of pandemic plans throughout Pearson. Insurance coverage may minimise any losses in certain circumstances.
A control breakdown or service failure in our school assessment businesses could result in financial loss and reputational damage.	We seek to minimise the risk of a breakdown in our student marking with the use of robust testing procedures and controls, combined with our investment in technology, project management and skills development of our people.
Failure to generate anticipated revenue growth, synergies and/or cost savings from acquisitions could lead to goodwill and intangible asset impairments.	We perform pre-acquisition due diligence and closely monitor the post-integration performance to ensure we are meeting 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 acquisition performance.

Risk	Mitigating factors
Other risks and uncertainties (continued)	
Changes in our tax position can significantly affect our reported earnings and cash flows.	We employ internal tax professionals in the UK and the US who review all significant arrangements around the world and respond to changes in tax legislation. They work closely with local management and external tax advisors.
Our professional services and school assessment businesses involve complex contractual relationships with both government agencies and commercial customers for the provision of various testing services. Our financial results, growth prospects and/or reputation may be adversely affected if these contracts and relationships are poorly managed.	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 associated risks. We also look to diversify our portfolio to minimise reliance on any single contract.
We operate in markets which are dependent on Information Technology (IT) systems and technological change.	We mitigate these IT risks by establishing strong IT policies and operational controls, employing project management techniques to manage new software developments and/or system implementations and have implemented an array of security measures to protect our IT assets from attacks or failures that could impact the confidentiality, availability or integrity of our systems.
Investment returns outside our traditional core US and UK markets may be lower than anticipated.	We draw on our experience of developing businesses outside our core markets and our existing international infrastructure to manage specific country risks. We have strengthened our financial control and managerial resources in these markets to mange expansion. The diversification of our international portfolio, and relative size of 'emerging markets' in relation to the Group, further minimises the effect any one territory could have on the overall Group results.
Social, environmental and ethical risk	We consider social, environmental and ethical (SEE) risks no differently to the way we manage any other business risk. Our 2009 risk assessment did not identify any significant under-managed SEE risks, nor have any of our most important SEE risks, many concerned with reputational risks, changed year-on-year. These are: journalistic/author integrity, ethical business behaviour, intellectual copyright protection, compliance with UN Global Compact standards, environmental impact, people and data privacy. For more information, see the Pearson corporate responsibility report Always learning: Our impact on society. The web link is available at www.pearson.com/responsibility/cr_report2009

Our impact on society

At the end of 2009, Sir David Bell retired as Pearson's director for people and also as the board director with oversight of corporate responsibility. In his 39 years at the company David did a huge amount to define what corporate responsibility means for Pearson and I am very pleased to take on the role and to try to continue David's work in this field. It has always struck me that the idea of being a responsible business – one that makes a positive contribution to society through effective learning, great books and powerful journalism – is in many ways the essence of Pearson.

Robin Freestone

It starts with being a values-based organisation (in our words, one that is 'brave, imaginative and decent'). It is not about what we say but about how we behave across our large, complex and diverse organisation. The kinds of businesses that we're in and the products that we make depend on our earning (and constantly re-earning) the trust of our readers, teachers and students for quality, accuracy and independence. We are proud of Pearson's long history as a responsible business, but we always feel that there is much more for us to do.

Pearson will continue to be that values-led company, placing enormous importance on the impact we have on the world through our products and services. We are as determined to enhance the learning experiences of our students (of all ages and walks of life) as we are to reduce our impact on the environment. Our goal remains simple: to be a socially responsible company that has a positive impact on society. We focus on our impact in four key areas:

Our strategy: Four key areas

1 Product quality and impact
2 Valuing our people
3 Sustainable business practice
4 Active citizenship

We report each year in conjunction with our annual financial results, so that our people and our other stakeholders can review our activity across the company and all over the world. You'll find a table of last year's targets and the new ones for 2010 at the end of this section and a fuller overview of our work over last year in our Always learning: Our impact on society 2009 report. Our corporate website will also be updated throughout the year if you'd like to read more about our work and projects in detail, and our Facebook page is regularly refreshed with examples of our CR and sustainability work from our businesses all over the world.

Please feel free to share any comments and suggestions with me at **robin.freestone@pearson.com**

Robin Freestone Chief financial officer

Board member responsible for corporate responsibility

Our strategy

1 Product quality and impact

Across Pearson, our brands have a hard-won reputation for quality: whether that is the FT for accurate, insightful and independent business journalism; Penguin for high-quality books of fiction and non-fiction; or our education company for effective learning materials.

We are a major investor in new content, new services, new technologies: in 2009, we invested approximately $800m in product development. We adhere to external codes like those upheld by the Press Complaints Commission, supplemented by our own internal standards, and our editors and journalists have freedom to make their own content choices within those frameworks. We partner with independent research agencies to measure the effectiveness of our educational products in raising student performance and institutional productivity, and we have a range of processes for engaging with our customers and other stakeholders to gain their insights into how we can serve them better.

At the same time, we want to ensure that people can access our books, newspapers and services in whatever way suits them best and we work hard to make that happen. For example, we have become a major provider of technology services, with digital revenues of £1.7bn in 2009. That transformation has made our content and technology much more widely available and accessible – for example through the 1.8m registered users of FT.com; the millions of buyers of Penguin eBooks; the 8.5m college students using our online homework programmes.

2009 highlights include:

Education:

– We have been working to connect our products and services to provide integrated learning platforms, systems that make teaching more efficient and learning more personal. In the US, our recently-launched Project Tapestry is allowing teachers to 'connect the dots' between student data, analytics, content and curriculum. Educators can view up-to-the-minute snapshots and in-depth analysis of each student's progress. This is the first connected learning environment built specifically for the US school market, the product of Pearson's collaboration with over 500 key education partners.

– In response to the alarming school drop-out problem in the US, we also launched Prevent, a software programme which aggregates the most relevant and predictive student information data to pinpoint which students are most likely to drop out of school. This early warning system helps teachers determine where best to prioritise their time to prevent students leaving school without a qualification.

– We are continuing to take highly effective learning programmes and apply them around the world. Our online homework and assessment services for college students, the MyLabs, are now used by 6 million college students in America and close to 500,000 in more than 60 countries. In South Africa, for example, our longitudinal study to determine the impact of MyMathLab at the University of Witwatersrand showed that the Lab has improved results of 7,000 students from an average score of 35% in the first semester to 65% in the second. Pearson Southern Africa's Maskew Miller Longman Foundation is also working with the Ministry of Education in four provinces, identifying ten of the poorest schools in the country to support intensively over the next three years with textbook provision and teacher coaching.

Business information: The *Financial Times* newspaper and FT.com continue to adhere to high standards of ethical and professional journalism. The FT's code of practice for financial and business journalism goes beyond the standards set by Britain's Press Complaint Commission, and compliance with the code is an obligation for all FT staff. This year, the FT has sought to further embrace the shift to digital rather than paper-based media, now used by many of our readers across the globe. In 2000, around two-thirds of the FT Group businesses were print-focused. In 2009, digital businesses represented over 73%. Since launching on Amazon's Kindle, the FT has seen steady growth in subscriptions and remains one of the top selling newspapers on the mobile device. The FT Facebook page has also gone from strength to strength, with 'Fans' of the page numbering well over 21,000 across all continents.

Consumer publishing: Penguin's long and proud history of championing free speech runs from our 1960's publication of *Lady Chatterley's Lover* right through to our more recent publication of Professor Deborah Lipstadt's *Denying the Holocaust.* In 2009, continuing this tradition, Penguin became a Silver PEN partner in the UK and was the proud sponsor of the 2009 PEN World Voices festival in New York, the world's oldest international literary and human rights organisation. We adhere to high standards of publishing around the world, taking care to protect the efforts of our authors and our copyright and trademarks. Penguin Group continues to support authors and publish books that raise awareness of environmental themes and global crises. One important book this year was *Rough Guide's Clean Breaks: 500 new ways to see the world* by Richard Hammond, (founder of greentraveller.co.uk) and Jeremy Smith (former editor of *The Ecologist*), winner of Planeta.com's Book of the Year award 2009. This book is the result of over a decade of travel, researching holidays that have less of an impact on the environment and genuinely give something back to the destination, through conservation and/or supporting local economies.

Introduction
Our strategy
Our performance
Our impact on society
Governance
Financial statements

Our impact on society
continued

2 Valuing our people

We work hard to attract and retain the most talented, diverse workforce we can in all parts of Pearson.

Our people are the source of many of our best ideas and we're getting better at enabling the cross-fertilisation of ideas across our business groups and departments via social media and other means.

Our People departments have focused particularly on the professional development, health and wellbeing of Pearson people this year, with several businesses highlighting Pearson-subsidised promotions and opportunities available to staff. We have a Group level health and safety policy, with numerous awareness days and other good practice examples at work across our offices. We have also paid particular attention to developing emerging leaders in our developing markets, running more training and leadership events and courses in Asia and India in 2009, including our new Emerging Leaders Programme this year. We are further developing our communications programme to include greater interactivity and collaboration between our global staff through online meetings and webinars, to add to the suite of large-scale presentations from senior managers to staff around the world and informal talks and seminars from colleagues around the business.

The following table shows for 2009 and 2008 the average number of people employed in each of our operating divisions.

Average number employed	2009	2008
Pearson Education North America	15,606	15,412
Pearson Education International	8,899	5,718
Professional	2,662	2,641
FT Group	4,787	4,792
Penguin	4,163	4,112
Corporate	1,047	909
Continuing businesses	37,164	33,584
Discontinued businesses	0	96
Total	**37,164**	**33,680**

2009 highlights include:

Diversity and inclusion: We try hard to reflect the societies in which we operate and while we don't set specific targets, we strive to have as diverse a pool of applicants for our jobs and suppliers as we can. We will always seek the best candidates for a role without regard for race, gender, age, physical ability, religion or sexual orientation, and have targets for tracking our progress on specific elements of that aim. We will make reasonable adjustment to premises or employment arrangements if these substantially disadvantage a disabled current or prospective member of staff, and make every effort to locate a suitable alternative role and/or training for people unable to continue in their existing role due to disability. Our diversity and inclusion teams on both sides of the Atlantic continue to develop our internship programmes for minority groups, winning the Gold Standard in the 2009 Race for Opportunity Benchmarking survey on race equality in UK organisations. We continue to improve on our recruitment and promotion of executives from minority backgrounds to middle and senior management levels, and feel that we still have much to achieve in this area.

Health and wellbeing: Our company can only be as healthy as our people, and we encourage our people to stay fit, eat well and balance their professional and personal lives. Pearson Benefits in the US sponsored National Employee Health and Fitness Day in May 2009. All US facilities with 50 or more people participated in on-site biometric screenings. The results were available immediately and over 2,300 staff had an opportunity to participate and discuss their numbers with onsite nurse educators. At Pearson in the UK, additional benefits will be in place for 2010 including a Weightwatchers programme in the workplace, health assessments and two online health management programmes to help anyone seeking to reduce high blood pressure, combat raised cholesterol or manage their health more effectively.

People for the future: We have a lot of talented people at every level of our company and we strive to identify, nurture and promote them in a number of ways. Our annual Forum brings together more than 100 of our newest and brightest managers from all over the world for a three-day session with the Pearson Management Committee and other senior managers, working on product innovation and better integration of the content and assets across the company. We launched our Emerging Leaders Programme in 2009, bringing together people from different businesses within one region to address organisational and team challenges. 72 Pearson people completed this programme in London, New York, Hong Kong and Minnesota and in total, we ran 589 personal days of leadership development in 2009.

3 Sustainable business practice

Pearson undertook in 2007 to become a climate neutral company by the end of 2009. We have reached our target through a series of direct actions, including: energy purchase and usage, investment in our buildings, communications and transport, and in the purchase of offset activity related to trees, the main raw material for our books and newspapers.

We continue to work on our supply chain to find the most environmentally-friendly way of producing the books and newspapers we print, actively seeking an FSC chain of custody for our paper supplies in the US for next year. We have been included in FTSE4Good indices since their inception and place great importance on not compromising our standards of quality or causing harm to our suppliers and their workers, wherever they may be in the world. We are committed to complying with the laws and regulations in all countries in which we operate, and work hard to build local partnerships as an active corporate citizen in emerging markets.

In this year's global analysis of corporate sustainability leadership by investment company SAM, Pearson was rated as the lead company of the Media supersector for the third year running as part of the Dow Jones Sustainability World Index. We were also classified as one of 100 Brand Emissions Leaders out of 600 brands surveyed by *Environmental Data Services* magazine, citing our ambitious carbon reduction targets and strong disclosure. Our chief financial officer now has board responsibility for matters relating to corporate responsibility.

2009 highlights include:

Reducing our impact: In 2009, Pearson signed up to the Copenhagen Communiqué[1], pledging to reduce our environmental impact while lobbying governments to create an effective international climate framework. Our formal environmental policy has been reviewed and updated a number of times since its launch in 1992, most recently in 2008, which you can read in full at www. pearson.com/environment. We completed the switch to the international environmental management standard ISO 14001 for all operating businesses in the UK, and our businesses in Australia aim to achieve certification in 2010. We committed to the Carbon Standard as part of our response to the Carbon Reduction Commitment, and have reduced our paper requirements at both Pearson North America and the FT. At Old Tappan, New Jersey – our first on-site renewable energy project for Pearson worldwide – the installation of solar panels is expected to reduce our electricity use at Old Tappan by 295,000 KwH each year, the equivalent of planting about 125,000 trees over the 25-year life of the panels.

Developing our emerging markets: By sharing best practice across Pearson, we can be more effective in our actions as a good corporate citizen in our developing markets. Penguin India has taken a number of freight initiatives which have saved a significant amount of fuel expenditure, increasing the number of books printed in India on behalf of Penguin UK, Penguin USA, Sterling and Bloomsbury to avoid the carbon emissions from moving 95 tonnes of books from the UK/USA to India. Penguin India is also forming an association with other companies in the community in Panchsheel to lobby government bodies to resolve issues such as poor parking facilities, faulty drainage and generators adding to the pollution and health and safety concerns in the area. The formation of Pearson Southern Africa – bringing together our education businesses in the region – means our company is now active in 12 developing countries in the region and employs, trains and develops local staff in each. By underpinning our educational and commercial imperative, with respect for the African environment, we can use our position as market leader to promote education in local cultures and languages to maintain a sustainable, socially responsible business.

Staff activity: Green Teams of volunteers are growing in size, structure and activity at various Pearson offices in India, the US, Australia, the UK, Canada and now South Africa. Several teams have also named specific Green Champions within their areas, tasking colleagues to help each other understand the small steps they can each take to make a big difference to reducing the environmental impact of their department or building. Planet Pearson – a cross-company environmental intranet site launched in 2008 as a pilot in the US – continues to expand in usage across our businesses in the US and Canada. The site serves as a communications hub where Pearson people can share ideas, resources and suggestions on the many eco-friendly initiatives taking place around the company. It has already helped significantly to raise awareness – Pearson North America's recent 'Go Green Survey' showed that 95% of respondents think it is important to work for a 'Green' employer, and 80% were aware of the company goal to be climate neutral by the end of 2009.

[1] The Copenhagen Communiqué was a short statement from the global business community to international governments, synthesising some of the key thinking that has come from business over the last two years.

Our impact on society continued

4 Active citizenship

Pearson's people are some of the most active citizens you will meet. We match their fundraising wherever we can and run a number of volunteer schemes for staff to give some of their working day to community programmes. Everything the Pearson Foundation, our charitable arm, does promotes literacy and education on a global scale, working with partner organisations to help level the playing field for those without ready access to education. In 2009, Pearson's charitable giving totalled £10.5m (2008: £7.7m). We give in a variety of ways, including provision of in-kind support such as books, website hosting, digital solutions and publishing expertise, as well as providing opportunities for staff to support their personal choice of charity through payroll giving schemes.

2009 highlights include:

The Pearson Foundation: Our Foundation allows us to promote education on an international level, partnering with other leading businesses and not-for-profit organisations to extend educational opportunity. We bring together experts to share good practice, to foster innovation and try to find workable solutions to the educational disadvantage facing millions of young people and adults across the globe.

In 2009, we continued our sponsorship of the annual Citi-FT Financial Education Summit, held in Singapore this year, and we organised the second Pearson International Education Summit in Helsinki, in conjunction with the US Council of Chief State School Officers. Our US flagship literacy campaign, Jumpstart's[2] Read for the Record continued to expand in 2009, as Pearson people around the world helped once again break our own record for the world's largest shared reading experience and raise funds for early education in low-income communities. More than two million participants read Eric Carle's classic *The Very Hungry Caterpillar* at organised events across the US, Brazil, and Europe, with Pearson donating over 275,000 Penguin books to children in need, and raising more than $1.5m to support Jumpstart's work.

Pearson people power: Our staff are passionate about volunteering, with many taking part in the organised reading schemes and other community programmes we offer at company level, in partnership with local organisations. This year, more than 200 Pearson UK people volunteered in schools local to our offices, reading with primary school children once a week as part of Booktime[3]. In 2008/09, our Booktime volunteers gave over 4,000 hours of their time to help children enjoy reading. We held our Pearson Community Awards under the chairmanship of our new director for people, Robin Baliszewski, and learned of the hundreds of people across our company taking on charitable endeavours in their spare time. The variety of activities included running winter clothing drives for the homeless, delivering emergency veterinary care for abandoned animals, performing as a clown in public hospitals and teaching at a community project for young refugees and migrants. We celebrated seven of those volunteers through our annual awards, making a donation of $2,000 to their chosen charity and giving certificates of Special Commendation to three other volunteer groups.

Corporate engagement: Each operating company has a number of different initiatives they're involved in, each promoting literacy in one way or another. We support local schools and colleges, promote or sponsor conferences, and form partnerships with other organisations with similar aims. In partnership with UK charity Booktrust and the Department for Children, Schools and Families, Pearson gave out 750,000 free Booktime book packs to every child starting school in England, Scotland and Northern Ireland this year, each containing Ed Vere's *Mr Big*. Children in England also received a copy of the *Booktime Book of Fantastic First Poems,* edited by June Crebbin. Building on the success of last year's UK event, the Penguin Group staged its first global Penguin Walk, involving over 1,000 staff members around the world to raise funds for the UN Environmental Programme's 'Plant a Billion Trees' campaign and develop our 96-acre Penguin Wood in the UK. The FT launched its annual seasonal appeal to support Room to Read, which works with local communities in the developing world to provide schools, libraries and educational scholarships for girls. By the end of 2010, it aims to provide over 11,000 communities access to their first library and has a long-term goal of reaching 10 million children in the developing world by 2020. Running from November to January each year, the FT's annual appeal includes editorial reports about the charity, and print and online marketing that encourages readers to donate. In the previous three years, the seasonal appeal has raised nearly £2.4m for WaterAid and Camfed International.

[2] Jumpstart for Young Children is a national non-profit based out of Boston, Massachusetts after being founded in Yale University in 1993 to help prepare pre-school children to succeed in their primary education.

[3] Booktime was launched by Pearson in association with independent charity Booktrust, to promote the pleasure of reading and encourage parents and carers to read aloud with their children.

Our impact on society: Progress and plans

1 Product quality and impact

Target 2009	Progress	Plan 2010
Continue and expand the Pearson Foundation/Council of Chief State School Officers (CCSSO) Educational Summit to include a focus on teacher quality and training, one of the key learnings of the Singapore convening.	**Achieved.** In September 2009, CCSSO and the Pearson Foundation welcomed more than 40 international education leaders to the second annual Pearson Foundation/CCSSO International Conference on Education in Helsinki, Finland. The aim was for the international delegation to learn from Finland's own success in preparing its K-12 and university educators to meet the demands of an increasingly inter-connected and technologically advanced workforce.	Continue the summit at an event in London in 2010 to include a focus on ICT in education, a key concern for educators in the classroom and for administrators hoping to improve academic systems, assessments and reporting.
Extend the Pearson Professional Development Program for African educators to involve education leaders in a cross-country dialogue addressing key education needs and solutions.	**Achieved.** This programme has now run for the second year, spearheaded by the Pearson Foundation and Pearson Southern Africa teams. The 2009 programme included training teachers in Literacy and Numeracy, ECD and Technology in Botswana, South Africa, Zambia, Namibia and Tanzania.	Continue to provide professional development for educators and administrators in Southern Africa and to integrate this programming with educational programming that is based on the Bridgeit model first introduced in Tanzania in 2009.

2 Valuing our people

Target 2009	Progress	Plan 2010
Focus our international moves to develop our rising stars and create assignments that even more closely match our corporate priorities.	**Ongoing.** The NewDirections team has now aligned the initiative with our annual talent review process and worked hard to create greater synergy between NewDirections placements and the business needs of Pearson in each of the regions.	Continue to develop our emerging leaders through international experience and support Pearson's needs in our developing markets.
Show evidence of progress in retention of people with diverse backgrounds for both entry level and management positions by tracking the success of women, people from minority ethnic backgrounds and those with a disability within Pearson. Develop more programmes and relationships to attract talented people from the above groups into our business.	**Achieved.** We have maintained the segment of our UK workforce from a minority ethnic background (14%) and minority representation in the US workforce now stands at 20.6%, up from 19.9% in 2008. Minority managers still make up 12% of the US management team. About 60% of Pearson UK staff are female (compared with 51% of the UK population) and 62% of Pearson UK's managers are female. Pearson wide, 27% of Pearson top 100 managers are female. In the UK, Pearson was awarded Gold Standard in the 2009 Race for Opportunity Benchmarking survey on race equality in UK organisations, and our UK diversity summer internship programme was shortlisted for the Race for Opportunity Widening the Talent Pool Award for work to increase the diversity of our workforce.	Continue to show evidence of progress in retention of people with diverse backgrounds for both entry level and management positions by tracking the success of women, people from minority ethnic backgrounds and those with a disability within Pearson. Continue to develop programmes and relationships to attract talented people from the above groups into our business.

Target ongoing
Target achieved
New target for 2010

Our impact on society: Progress and plans continued

2 Valuing our people continued

Target 2009	Progress	Plan 2010
Increase our capacity to combine training opportunities for our staff with opportunities to partner with schools, colleges and not-for-profits.	**Ongoing.** Edexcel staff in London have partnered with a nearby school to provide career coaching and mentoring to students. Students in the UK now benefit from a Pearson Student Advisory Board, mirroring the established PSAB in the US to provide student feedback and input to Pearson, while offering mentoring and internship opportunities to talented students.	Continue to develop our capacity to combine training opportunities for our staff with opportunities to partner with schools, colleges and not-for-profits.

3 Sustainable business practice

Target 2009	Progress	Plan 2010
Continue to expand our network of environmental teams across our businesses. Directly involving many more of our people.	**Ongoing.** Our Green Teams are now flourishing in Pearson facilities across the UK, the US, Canada, Australia, India and Southern Africa.	Continue to expand and consolidate our network of environmental teams across our businesses.
Hold training refresher seminars with key Pearson production departments on labour standards and environmental issues.	**Achieved.** We are working with relevant production staff at the Financial Times to review processes and environmental concerns.	
Continue the process of becoming a climate neutral company	**Achieved.** Pearson reached climate neutrality at the end of 2009 following a two-year programme of investment and offset activity.	Having completed our 2007 commitment, we are considering our next steps and will communicate our longer term environmental commitment later this year.

Programmes of activity include:	Highlights include:	Programmes of activity will include:
Extend Planet Pearson, a new website designed by Pearson staff in the US, to be available internationally.	International roll-out of Planet Pearson is ongoing, but the site is now available to staff in Canada and at many locations in the US.	Further development of the Planet Pearson website by Pearson staff.
Continue programme to ensure our key buildings are energy efficient.	Carried out substantial investment in server virtualisation across US, Australia and the UK. Completed the ISO 14001 environmental management system for businesses in the UK.	Continuation of our programme to make our key buildings energy efficient.
FT newspaper to assess feasibility of setting up its own offset programme.	FT newspaper successfully set up its own offset programme by developing the FT Rainforest in Costa Rica.	Completing the ISO 14001 environmental management system for our business in Australia.
Purchase 'green' energy where available and affordable.	Shifting to purchase green electricity wherever possible in the UK and US, equivalent to 100,000 metric tonnes of CO_2.	
	Generating renewable electricity via the solar panels on the roof of our Old Tappan site in New Jersey, US.	
Continue to work with industry partners to establish a methodology to assess the carbon footprint of a book.	**Ongoing.** Penguin UK has now measured the carbon footprint of a medium size paperback book, and this is in progress at Pearson Education.	Continue to work with industry partners to establish a methodology to assess the carbon footprint of a textbook.

3 Sustainable business practice continued

Target 2009	Progress	Plan 2010
Maintain our position in the key indices of social responsibility.	**Achieved.** Pearson retained its position as Global Leader for the Media Sector in the Dow Jones Sustainability Indices and its Platinum rating in the Business in the Community Responsibility Index.	Maintain our position in the key indices of social responsibility.
		New target Establish a total carbon footprint identification initiative for our company. **New target** Establish FSC chain of custody certification for our paper use in our North American businesses.

4 Active citizenship

Target 2009	Progress	Plan 2010
Increase the number of children reached through these campaigns, expanding Booktime once again and rolling out Jumpstart's Read for the Record programme internationally.  	**Achieved.** Booktime: 750,000 book packs donated to children in schools across England, Scotland and Northern Ireland. Read for the Record: Pearson people around the world again helped set a new world record for the largest 'shared reading experience' for Jumpstart's 2009 campaign. Shared more than two million books and raised \$1.5m for Jumpstart's year-round operations, helping to draw national attention to the US early education crisis.	Increase the impact on children and adults reached through these campaigns, focusing Booktime funds more strategically and rolling out Jumpstart's Read for the Record programme further internationally.
Increase the number of interventions we make to facilitate constructive debate on key contemporary issues	**Achieved.** The FT held its first conference on corporate responsibility and investing in March 2009 – the FT Sustainable Business and Responsible Investing Conference in New York. Plans are underway for a live panel debate at Pearson's London head office on the responsibility priorities for a 21st century media organisation, to be streamed in real-time via an interactive social media platform.	Increase the number of interventions we make to facilitate constructive debate on key contemporary issues 
		New target Launch the Pearson Prize in the US, identifying students currently in a two- or four-year college/university who are working on specific projects that support their institution and/or local communities, and providing a package of financial and in-kind support to help these students finish their college careers.

Target ongoing
Target achieved
New target for 2010

For a more in-depth look back over our activity as a corporate citizen in 2009, please go to our Always learning: Our impact on society 2009 report **www.pearson.com/responsibility/cr_report2009**

Board of directors

Chairman

Glen Moreno, †• chairman, aged 66, was appointed chairman of Pearson on 1 October 2005 and is chairman of the nomination committee. He is a director of Fidelity International Limited and effective 1 March 2010, was appointed a non-executive director of Lloyds Banking Group plc and became their senior independent director. He was previously senior independent director of Man Group plc and acting chairman of UK Financial Investments Limited, the company set up by HM Treasury to manage the government's shareholdings in UK banks.

Executive directors

Marjorie Scardino, • chief executive, aged 63, joined the Pearson board in January 1997. She trained and practised as a lawyer, and was chief executive of The Economist Group from 1993 until joining Pearson. She is also vice chairman of Nokia Corporation and on the boards of several charitable organisations.

Will Ethridge, chief executive, Pearson North American Education, aged 58, joined the Pearson board in May 2008, having held a number of senior positions within Pearson Education, including CEO of the International and Higher Education divisions. He is chairman of CourseSmart, a publishers' digital retail consortium and chairman of the Association of American Publishers.

Non-executive directors

David Arculus,*†• aged 63, is a non-executive director of Telefónica SA and was appointed chairman of Numis Corporation plc in May 2009. His previous roles include chairman of O2 plc, Severn Trent plc and IPC Group, chief operating officer of United Business Media plc and group managing director of EMAP plc. He became a non-executive director of Pearson in February 2006 and is chairman of the personnel committee.

Terry Burns,†• aged 65, is chairman of Santander UK and Glas Cymru Limited and is a non-executive director of Banco Santander SA. He was recently appointed chairman of the Channel 4 Television Corporation. He was previously chairman of Marks and Spencer Group plc. He was the UK government's chief economic adviser from 1980 until 1991 and Permanent Secretary of HM Treasury from 1991 until 1998. He was appointed a non-executive director of Pearson in May 1999 and senior independent director in February 2004.

Patrick Cescau,*• aged 61, is a non-executive director of Tesco plc and joined the board of directors of INSEAD, the Business School for the World, in June 2009. He was previously group chief executive of Unilever. He became a non-executive director of Pearson in April 2002.

Rona Fairhead, chairman and chief executive of The Financial Times Group, aged 48, joined the Pearson board in June 2002 as chief financial officer. She was appointed chief executive of The Financial Times Group in June 2006 and became responsible for Pearson VUE in March 2008. From 1996 until 2001, she served as executive vice president, group control and strategy at ICI. She is also chairman of Interactive Data, a non-executive director of HSBC Holdings plc and chairs the HSBC audit committee.

Robin Freestone, chief financial officer, aged 51, joined Pearson in 2004 as deputy chief financial officer and became chief financial officer in June 2006, when he also joined the Pearson board. He was previously group financial controller of Amersham plc (now part of GE). He qualified as a chartered accountant with Touche Ross (now Deloitte). He is also a non-executive director and founder shareholder of eChem Limited.

John Makinson, chairman and chief executive of The Penguin Group, aged 55, joined the Pearson board in March 1996 and was finance director until June 2002. He was appointed chairman of The Penguin Group in May 2001. He is also chairman of the Institute for Public Policy Research, director of The Royal National Theatre and trustee of The International Rescue Committee (UK).

* A member of the audit committee.
† A member of the personnel committee.
• A member of the nomination committee.

Susan Fuhrman,*• aged 65, is president of Teachers College at Columbia University, America's oldest and largest graduate school of education and president of the National Academy of Education. She was previously dean of the Graduate School of Education at the University of Pennsylvania and on the board of trustees of the Carnegie Foundation for the Advancement of Teaching. She became a non-executive director of Pearson in July 2004.

Ken Hydon,*†• aged 65, is a non-executive director of Reckitt Benckiser Group plc, Royal Berkshire NHS Foundation Trust and Tesco plc. He was previously financial director of Vodafone Group plc and of subsidiaries of Racal Electronics. He became a non-executive director of Pearson in February 2006 and is chairman of the audit committee.

CK Prahalad, • aged 68, is a distinguished university professor of corporate strategy and international business at The University of Michigan Business School. He is a non-executive director of NCR Corporation and Hindustan Unilever Corporation and director of the World Resources Institute and The Indus Entrepreneurs. He became a non-executive director of Pearson in May 2008.

Board governance

Directors

The present members of the board, together with their biographical details, are shown on pages 44 and 45. The chairman was appointed to the board of Lloyds Banking Group plc, effective 1 March 2010. Given his retirement from two major boards in 2009, both the chairman and the Pearson board are confident that he can carry out his new role without diluting his time commitment to Pearson.

Details of directors' remuneration, interests and dealings in ordinary shares and options of the company are contained in the report on directors' remuneration on pages 56 to 78.

In accordance with good corporate governance, the board has resolved that all directors should offer themselves for re-election on an annual basis at the company's Annual General Meeting (AGM). Accordingly, all eligible directors will offer themselves for re-election at the forthcoming AGM on 30 April 2010.

Details of directors' service agreements can be found on pages 66 and 67.

Corporate governance

Introduction

The board believes that the company is in full compliance with Section 1 of the Combined Code 2008 (The Code). A detailed account of the provisions of the Code can be found on the company website at **www.pearson.com/investors/shareholder-information/governance**

Composition of the board

The board consists of the chairman, Glen Moreno, five executive directors including the chief executive, Marjorie Scardino, and six independent non-executive directors. Terry Burns, Pearson's senior independent director, will be retiring at the forthcoming AGM and will not offer himself for re-election. The nomination committee is currently recruiting an independent non-executive director to replace Terry.

Senior independent director

Terry Burns was appointed senior independent director in 2004. His role includes being available to shareholders if they should have concerns that have not been addressed through the normal channels, and attending meetings with shareholders in order to gain a balanced understanding of any concerns that they might have. The senior independent director also meets with the non-executive directors at least once a year in order to appraise the performance of the chairman, and would be expected to chair the nomination committee in the event that it was considering succession to the role of chairman of the board. Following Terry's retirement, Patrick Cescau will be appointed senior independent director.

Independence of directors

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.

Although Terry Burns has served on the board for more than nine years, the board believes that due to his experience, knowledge and objectivity, he continued to be a highly effective non-executive director throughout the year.

All of the other non-executive directors, including the chairman, were considered by the board to be independent for the purposes of the Code during the year ended 31 December 2009.

Conflicts of interest

From October 2008, directors have had a statutory duty under the Companies Act 2006 (the Act) to avoid conflicts of interest with the company. As permitted by the Act, the company adopted new Articles of Association at its AGM in 2008 to 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 companies which are not part of the Pearson Group and which could give rise to actual or potential conflicts of interest. Such conflicts are then considered for approval by the board. The potential conflicted director cannot vote on an authorisation resolution or be counted in the quorum. The board reviews on an annual basis any authorisations granted.

Board meetings

The board meets six times a year and at other times as appropriate. The following table sets out the attendance of the company's directors at board and committee meetings during 2009:

	Board meetings (maximum 6)	Audit committee meetings (maximum 4)	Personnel committee meetings (maximum 4)	Nomination committee meetings (maximum 2)
Chairman				
Glen Moreno	6/6	–	4/4	2/2
Executive directors				
Marjorie Scardino	6/6	–	–	2/2
David Bell•	2/2	–	–	–
Will Ethridge	6/6	–	–	–
Rona Fairhead	6/6	–	–	–
Robin Freestone	6/6	–	–	–
John Makinson	5/6	–	–	–
Non-executive directors				
David Arculus	6/6	4/4	4/4	2/2
Terry Burns	6/6	–	4/4	2/2
Patrick Cescau	6/6	4/4	–	2/2
Susan Fuhrman	5/6	3/4	–	2/2
Ken Hydon	6/6	4/4	4/4	2/2
CK Prahalad	5/6	–	–	2/2

• Resigned from the board on 1 May 2009.

The role and business of the board

The formal matters reserved for the board's decision and approval include:

- The company's strategy and review of performance against it;
- Major changes to the company's corporate structure;
- Approval of all shareholder documents;
- Acquisitions, disposals and capital expenditure projects above certain thresholds;
- All guarantees over £10m;
- Treasury policies;
- The interim and final dividends and the financial statements;
- Borrowing powers;
- Ensuring adequate succession planning for the board and senior management;
- Appointments to the board; and
- The appointment and removal of the company secretary.

The board receives timely, regular and necessary financial, management and other information to fulfil its duties. 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.

We endeavour to give non-executive directors access to the senior managers of the business via involvement at both formal and informal meetings. In this way we hope that the experience and expertise of the non-executive directors can be utilised for the benefit of the company. At the same time, this practice enables the non-executive directors to develop an understanding of the abilities of senior management which will help them judge the company's prospects and plans for succession.

Board evaluation

For the review of 2008, conducted early in 2009, the chairman asked the directors to complete an evaluation questionnaire which was targeted specifically around issues of strategy and risk management. Responses to this questionnaire and from face-to-face meetings with the chairman were gathered and communicated to the board at the May 2009 board meeting.

Board governance continued

This process reinforced the view that strategy remained a key focus for the board in 2009. As a direct result of these discussions, strategic reviews of International Education and Education Technology were held in June and October respectively and the Pearson strategic plan was reviewed and updated in December.

The evaluation of 2009 is currently underway. The chairman is conducting detailed interviews with all directors to ensure the board is effectively focused on its agreed priorities: governance; strategy; business performance and people. The outcome of this review will be discussed at the April 2010 board meeting. The board anticipates using an external advisor for its 2010 review.

In addition, during the course of the year the executive directors were evaluated by the chief executive on their performance against personal objectives under the company's standard appraisal mechanism. The chairman leads the assessment of the chief executive and the senior independent director conducts a review of the chairman's performance.

Directors' training

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 includes a series of meetings with members of the board, presentations regarding the business from senior executives and a briefing on Pearson's investor relations programme. We supplement the existing directors' training programme through continuing presentations at board meetings about the company's operations, by holding board meetings at overseas locations and by encouraging the directors to visit operating companies and local management as and when their schedule allows. Externally run courses are also made available should directors wish to make use of them.

Directors' indemnities

In accordance with section 232 of the Companies Act 2006 (the Act), the company grants an indemnity to all of its directors. The indemnity relates to costs incurred by them in defending any civil or criminal proceedings and in connection with an application for relief under sections 661(3) and (4) or sections 1157(1)-(3) of the Act, so long as it is repaid not later than when the outcome becomes final if: (i) they are convicted in the proceedings; (ii) judgment is given against them; or (iii) the court refuses to grant the relief sought.

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.

Dialogue with institutional shareholders

There is an extensive programme for the chairman, CEO, executive directors and senior managers to meet with institutional shareholders. The non-executive directors meet informally with shareholders both before and after the AGM, and respond to shareholder queries and requests. The chairman and senior independent director make themselves available to meet any significant shareholder as required. Makinson Cowell and the company's investor relations department report to the board on the results of a comprehensive survey on major shareholders' views.

Furthermore, reports on changes in shareholder positions and views are given to the directors at every board meeting.

Board committees

The board has established three committees: the audit committee, the personnel committee and the nomination committee. 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 requisite committee chairman.

Audit committee report

Ken Hydon audit committee chairman

Members **Ken Hydon, David Arculus, Patrick Cescau and Susan Fuhrman**

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 held in other listed or publicly traded companies and/or similar public organisations. Ken Hydon, chairman of the committee, is the company's designated financial expert. He is a fellow of the Chartered Institute of Management Accountants, the Association of Chartered Certified Accountants and the Association of Corporate Treasurers. He also serves as audit committee chairman for Tesco plc, Reckitt Benckiser Group plc and Royal Berkshire NHS Foundation Trust.

The qualifications and experience of the other committee members are detailed on pages 44 and 45.

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/investors/shareholder-information/governance**

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 audits of the financial statements of the company.

The committee is 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. The Group's internal and external auditors have direct access to the committee to raise any matter of concern and to report on the results of work directed by the committee. The committee reports to the full board on a regular basis but no less frequently than at every board meeting immediately following a committee meeting. It also reviews the independence of the external auditors, including services supplied, and ensures that there is an appropriate audit relationship. Based on management's recommendations, the committee reviews the proposal to reappoint the external auditors. The committee evaluated the performance of the external auditors during the year and remains satisfied with their effectiveness. 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 Group audit every five years. The current lead audit partner has been in place for two years.

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

The committee met four times during the year with the chief financial officer, head of Group internal audit, members of the senior management team and the external auditors in attendance. The committee also met regularly in private with the external auditors and the head of Group internal audit. Some members of the committee attended site visits to a number of overseas locations in order to better understand how Group policies are embedded in operations.

At every meeting, the committee considered reports on the activities of the internal audit function, 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 and considered any significant legal claims and regulatory issues in the context of their impact on financial reporting.

Specifically, the committee considered the following matters during the course of the year:

- The annual report and accounts: preliminary announcement and trading update;
- The Group accounting policies;
- Compliance with the Combined Code;
- The Form 20-F and related disclosures including the annual Sarbanes-Oxley Act 404 attestation of financial reporting internal controls;
- Receipt of external auditor report on Form 20-F and on the year end audit;
- Assessment of the effectiveness of the company's internal control environment;
- Reappointment of external auditor;
- Appointment of new head of Group internal audit function;
- Review of the interim management statement;
- Review of the effectiveness of the audit committee and a review of both the internal and external auditors;
- Annual approval of the internal audit mandate;
- Compliance with SEC & NYSE requirements including Sarbanes Oxley;
- Review of interim financial statements and announcement;
- Approval of external audit engagement, scope and fees;
- Approval of external audit policy;
- Review of committee's terms of reference;
- Review of link between Pearson and IDC's audit committees;
- Annual internal audit plan including resourcing of the internal audit function;
- Review of company risk returns including Social, Ethical and Environmental (SEE) risks; and
- Annual review of treasury policy.

Board governance continued

Personnel committee report

David Arculus personnel committee chairman

Members **David Arculus, Terry Burns, Ken Hydon and Glen Moreno**

The personnel committee has responsibility for determining the remuneration and benefits packages of the executive directors, the chief executives of the principal operating companies and other members of the management committee, as well as recommending the chairman's remuneration to the board for its decision.

The committee takes independent advice from consultants when required. No director takes part in any discussion or decision concerning their own remuneration. The committee reports to the full board and its report on directors' remuneration, which has been considered and adopted by the board, is set out on pages 56 to 78.

The committee met three times during the year, and has written terms of reference which clearly set out its authority and duties. These can be found on the company website at ⓘ **www.pearson.com/investors/shareholder-information/governance**

On Terry Burns' retirement from the board, Patrick Cescau will join the personnel committee.

Nomination committee report

Glen Moreno nomination committee chairman

Members **Glen Moreno, Marjorie Scardino, David Arculus, Terry Burns, Patrick Cescau, Susan Fuhrman, Ken Hydon and CK Prahalad**

The nomination committee meets as and when required. 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.

When considering the appointment of a new director the committee reviews the current balance of skills and experience of the board.

Whilst the chairman of the board chairs this committee, he is not permitted to chair meetings when the appointment of his successor is being considered or during a discussion regarding his performance.

During 2009 the committee met to review succession planning for non-executive and executive board positions, as well as board committee assignments.

The committee has written terms of reference which clearly set out its authority and duties. These can be found on the company website at ⓘ **www.pearson.com/investors/shareholder-information/governance**

Internal control

The board of directors has overall responsibility for Pearson's system of internal control, which is designed to manage the risks facing the Group, safeguard assets and provide reasonable, but not absolute, assurance against material financial misstatement or loss.

In accordance with the provisions of the Code, the directors confirm that they have reviewed the effectiveness of the Group's internal control system.

They also confirm that there is an ongoing process allowing for the identification, evaluation and management of significant business risks. This ongoing process accords with the revised Turnbull guidance and has been in place throughout 2009 and up to the date of approval of this annual report.

The Group's internal control framework covers financial, operational and compliance risks. Its main features are described below:

i. Board

The board of directors exercises its control through an organisational structure with clearly defined levels of responsibility and authority and appropriate reporting procedures. To maintain effective control over strategic, financial, operational and compliance matters the board meets regularly, and has a formal schedule of matters that is brought to it, or its duly authorised committees, for attention. Responsibility for monitoring financial management and reporting, internal control and risk management 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 of the Group.

ii. Operating company controls

The identification and mitigation of major business risks is the responsibility of operating company management. Each operating company, including the corporate centre, maintains internal controls and procedures appropriate to its structure and business environment, whilst complying with Group policies, standards and guidelines. 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.

iii. Financial 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 and indebtedness, is reported against the corresponding figures for the plan and prior years, with corrective action outlined by operating company executives as appropriate. Group senior management meet, on a quarterly basis, with operating company management to review their business and financial performance against plan and forecast. Major business risks relevant to each operating company as well as performance against the stated strategic objectives are reviewed in these meetings.

In addition, the chief executive prepares a report for the board, 11 times a year, on key developments, performance and issues in the business.

iv. Risk management

Operating companies undertake formal, semi-annual risk reviews to identify new or potentially under-managed risks. Throughout the year, risk sessions facilitated by the head of Group internal audit are held with operating company management to identify key risks, assess the probability and impact of those risks and document the actions being taken to manage those risks. The Pearson Management Committee reviews the output of these sessions, focusing on the significant risks facing the business. Management has the responsibility to consider and execute appropriate action to mitigate these risks whenever possible. The results of these reviews are summarised by Group internal audit for evaluation and onward reporting to the board, in summary, and in more detail via the audit committee.

v. Group internal audit

The Group internal audit function is responsible for providing independent assurance to management on the effectiveness of internal controls. The annual internal audit plan, derived from a risk model, is approved by the audit committee. Recommendations to improve internal controls and to mitigate risks, or both, are agreed with operating company management after each audit. Formal follow-up procedures allow Group internal audit to monitor operating companies' progress in implementing its recommendations and to resolve any control deficiencies. The Group internal audit function also has a remit to monitor significant Group projects, in conjunction with the central project management office, to provide assurance that appropriate project governance and risk management strategies are in place. Regular reports on the work of Group internal audit are provided to executive management and, via the audit committee, to the board.

The head of Group internal audit is jointly responsible with the Group legal counsel for monitoring compliance with our Code of Conduct, and investigating any reported incidents including fraud allegations.

vi. Treasury management

The treasury department operates within policies approved by the board and its procedures are reviewed regularly by the audit committee. 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.

vii. Insurance

Insurance is provided through Pearson's insurance subsidiary or externally, depending on the scale of the risk and the availability of cover in the external market, with the objective of achieving the most cost-effective balance between insured and uninsured risks.

Going concern

Having reviewed the Group's liquid resources and borrowing facilities and the Group's 2010 and 2011 cash flow forecasts, the directors believe that the Group has adequate resources to continue as a going concern. For this reason, the financial statements have, as usual, been prepared on that basis.

Shareholder communication

Pearson has an extensive programme of communication with all of its shareholders – large and small, institutional and private. We also make a particular effort to communicate regularly with our employees, a large majority of whom are shareholders in the company. We post all company announcements on our website, ⓘ **www.pearson.com**, as soon as they are released, and major 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.

We have an established programme of educational seminars for our institutional shareholders focusing on individual parts of Pearson. These seminars are available to all shareholders via webcast on ⓘ **www.pearson.com**

Board governance continued

Our AGM – which will be held on 30 April this year – is an opportunity to meet the company's managers, hear presentations about Pearson's businesses and the previous year's results as well as to conduct general AGM business.

Share capital

Details of share issues are given in note 27 to the accounts on page 140. 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 2009, 810,799,351 ordinary shares were in issue. At the AGM held on 1 May 2009, the company was authorised, subject to certain conditions, to acquire up to 80 million of its ordinary shares by market purchase. Shareholders will be asked to renew this authority at the AGM on 30 April 2010.

As at 26 February 2010, the company had been notified of the following substantial shareholdings in the capital of the company.

	Number of shares	Percentage
Legal & General Group plc	32,300,784	3.98%

Annual General Meeting (AGM)

The notice convening the AGM to be held at 12 noon on Friday, 30 April 2010 at The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE, is contained in a circular to shareholders to be dated 25 March 2010.

Registered auditors

In accordance with section 489 of the Companies Act 2006 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.

Auditor independence

In line with best practice, our relationship with PwC is governed by our external auditor 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 due diligence services up to £100,000 per transaction;

Tax compliance and related activities up to the greater of £1,000,000 per annum or 50% of the external audit fee; and

For forward-looking tax planning services we use the most appropriate advisor, usually after a tender process. Where we decide to use our independent auditor, 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 awarding work to the auditor.

In 2007, Interactive Data appointed Ernst & Young LLP (Ernst & Young) as its independent auditor. To maintain Ernst & Young's independence we have restricted the services that Ernst & Young can provide to Pearson and its subsidiaries, similar to those restrictions which we place on PwC.

The audit committee receives regular reports summarising the amount of fees paid to the auditor.

A full statement of the fees for audit and services is provided in note 4 to the accounts on page 99.

Statement of directors' responsibilities

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 judgments and accounting estimates that are reasonable and prudent;

State that the financial statements comply with IFRSs as adopted by the European Union or disclose and explain any material departures; and

Prepare the financial statements on a going concern basis, unless it is inappropriate to presume that the company and/or the Group 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. This enables them to ensure that the financial statements and the report on directors' remuneration comply with the Companies Act 2006 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 United Kingdom 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 pages 44 and 45, confirm that to the best of their knowledge and belief:

The Group financial statements, prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group and company; and

The directors' report contained in the annual report includes a fair review of the development and performance of the business and the position of the company and Group, together with a description of the principal risks and uncertainties that they face.

The directors also confirm that, for all directors in office at the date of this report:

a) so far as the directors are aware, there is no relevant audit information of which the company's auditors are unaware; and

b) 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.

Approved by the board on 10 March 2010 and signed on its behalf by

Philip Hoffman Secretary

Board governance continued

Additional information for shareholders

Amendment to Articles of Association

Any amendments to the Articles of Association (the Articles) of the company may be made in accordance with the provisions of the Companies Act 2006 (the Act) by way of a special resolution.

Rights attaching to shares

The rights attaching to the ordinary shares are defined in the company's 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 for every ordinary share of which they are the registered holder. 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 be conducted on a poll.

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, provided the distributable profits of the company justify such payment. 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 members or different classes of members. The liquidator can also transfer the whole or any part of the assets to trustees upon any trusts for the benefit of the members.

Voting at general meetings

Any form of proxy sent by the company to shareholders in relation to any general meeting must be delivered to the company, 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.

No shareholder is, unless the board decides otherwise, 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.

Pearson operates two employee benefit trusts to hold shares, pending employees becoming entitled to them under the company's employee share plans. There were 9,664,922 shares so held as at 31 December 2009. Each 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 these trusts.

Pearson also operates a nominee shareholding arrangement known as Sharestore which holds shares on behalf of employees. There were 2,747,925 shares so held as at 31 December 2009. The trustees holding these shares seek voting instructions from the employee as beneficial owner, and voting rights are not exercised if no instructions are given.

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 class; or

(ii) with the sanction of a special resolution passed at a separate general meeting of the holders of the shares of the class.

Without guidance 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

Directors shall number no less than two. 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.

At every AGM of the company, 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.

However, although not required by the Articles, the board has resolved that for this year, and in future years, all directors offer themselves for re-election annually, in accordance with good corporate governance.

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 July 2004 (as amended) of which $92,000,000 matures in May 2011 and the balance of $1,658,000,000 matures in May 2012 between, amongst others, the company, HSBC Bank plc (as facility agent) and the banks and financial institutions named therein as lenders (together, the Credit Facilities), the facility agent must, upon a change of control, cancel the total commitments of the lenders under such Credit Facilities and declare all outstanding advances, together with accrued interest and any other amounts payable in respect of such Credit Facilities, to be immediately due and payable. 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 840 of the Income and Corporation Taxes Act 1988) 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.

Introduction
Our strategy
Our performance
Our impact on society
Governance
Financial statements

Report on directors' remuneration

The board presents its report on directors' remuneration to shareholders. This report complies with Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 and was approved by the board of directors on 10 March 2010.

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

We will put a resolution to shareholders at the Annual General Meeting (AGM) on 30 April 2010 inviting them to consider and approve this report.

The personnel committee

David Arculus chaired the personnel committee for the year 2009; the other members were Terry Burns, Ken Hydon and Glen Moreno. David Arculus, Terry Burns and Ken Hydon are independent non-executive directors. Glen Moreno, chairman of the board, is a member of the committee as permitted under the Combined Code.

Marjorie Scardino, chief executive, David Bell, director for people, Robin Baliszewski (who replaced David Bell as director for people on 1 September 2009), Robert Head, compensation and benefits director, and Stephen Jones, deputy company secretary, provided material assistance to the committee during the year. They attended meetings of the committee, although no director was involved in any decisions relating to his or her own remuneration.

To ensure that it receives independent advice, the committee has appointed Towers Perrin (now Towers Watson) to supply survey data and to advise on market trends, long-term incentives and other general remuneration matters. Towers Perrin also advised the company on health and welfare benefits in the US and provided consulting advice directly to certain Pearson operating companies.

The committee's principal duty is to determine and regularly review, having regard to the Combined Code and on the advice of the chief executive, the remuneration policy and the remuneration and benefits packages of the executive directors, the chief executives of the principal operating companies and other members of the Pearson Management Committee who report directly to the chief executive. This includes base salary, annual and long-term incentive entitlements and awards, and pension arrangements.

The committee's terms of reference are available on the company's website.

The committee met four times during 2009. The matters discussed and actions taken were as follows:

20 and 27 February 2009
Reviewed and approved 2008 annual incentive plan payouts
Reviewed and approved 2006 long-term incentive plan payouts
Approved vesting of 2004 and 2006 annual bonus share matching awards
Reviewed and approved 2009 Pearson and operating company annual incentive plan targets
Reviewed and approved 2009 individual annual incentive opportunities for Pearson Management Committee
Reviewed and approved 2009 long-term incentive awards and associated performance conditions for Pearson Management Committee
Reviewed and approved 2008 report on directors' remuneration
Reviewed strategy on 2009 long-term incentive awards for executives and managers
Noted company's use of equity for employee share plans
Reviewed and approved treatment of David Bell's outstanding share awards on his retirement from the company on 31 December 2009

23 July 2009
Approved 2009 long-term incentive awards for executives and managers
Reviewed committee's charter and terms of reference

11 December 2009
Reviewed status of outstanding long-term incentive awards
Considered return on invested capital targets for long-term incentive plan
Reviewed 2010 annual incentive plan metrics
Considered Towers Perrin's report on remuneration for Pearson Management Committee for 2010

Summary of policy changes in 2009

There were no changes to remuneration policy that took effect during 2009.

Remuneration policy

This report sets out the company's policy on directors' remuneration that applies to executive directors for 2010 and, so far as practicable, for subsequent years. The committee considers that a successful remuneration policy needs to be sufficiently flexible to take account of future changes in the company's business environment and in remuneration practice. Future reports, which will continue to be subject to shareholder approval, will describe any changes in this policy.

Pearson's goal remains unchanged: to help people make progress in their lives and thrive in a brain-based economy through learning. The basic strategy to achieve that goal is pursued by all Pearson's businesses in some shape or form and has four fundamental parts: long-term organic growth investment in content; adding services to our content; international expansion; and efficiency.

One of the most important measures of our strategy is, of course, financial performance. Here, our goal is to produce consistent growth in three key financial measures – adjusted earnings per share, cash flow and return on invested capital. We believe those are, in concert, good indicators that we are building the long-term value of Pearson. So those measures (or others that contribute to them, such as operating margins and working capital) form the basis of our annual budgets and plans, and the basis for bonuses and long-term incentives.

The performance conditions that we select for the company's various performance-related annual or long-term incentive plans are therefore linked to the company's strategic objectives set out above and aligned with the interests of shareholders. We determine whether or not targets have been met under the company's various performance-related annual or long-term incentive plans based on relevant internal information and input from external advisers.

In light of the prevailing economic conditions and the impact of these on the company's objectives and strategy, we continue to keep our remuneration policy under review particularly with regard to its approach to annual and long-term incentives.

Our starting point continues to be that total remuneration (base compensation plus annual and long-term incentives) should reward both short- and long-term results, delivering competitive rewards for target performance, but outstanding rewards for exceptional company performance.

Generally speaking, we have concluded that no fundamental changes are required to the performance measures used in the company's annual and long-term incentive plans.

We will however continue to give careful consideration to the selection and weighting of these measures and the targets that apply taking into account the company's short- and longer term strategy and risk and the impact on the sustainability and future development of the company.

Report on directors' remuneration continued

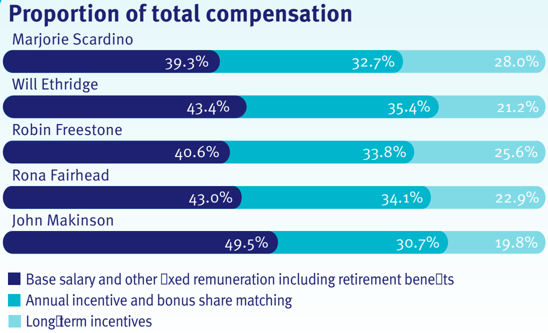
Main elements of remuneration

Total remuneration is made up of fixed and performance-linked elements, with each element supporting different objectives.

Element	Objective	Performance period	Performance conditions
Base salary (see page 59)	Reflects competitive market level, role and individual contribution	Not applicable	Normally reviewed annually taking into account the remuneration of directors and executives in similar positions in comparable companies, individual performance and the approach to pay across the company as a whole
Annual incentives (see page 59)	Motivates achievement of annual strategic goals	One year	Subject to achievement of targets for sales, earnings per share or profit, working capital and cash
Bonus share matching (see page 61)	Encourages executive directors and other senior executives to acquire and hold Pearson shares. Aligns executives' and shareholders' interests	Three years	Subject to achievement of target for earnings per share growth
Long-term incentives (see page 62)	Drives long-term earnings and share price growth and value creation. Aligns executives' and shareholders' interests	Three years	Subject to achievement of targets for relative total shareholder return, return on invested capital and earnings per share growth

Consistent with its policy, the committee places considerable emphasis on the performance-linked elements i.e. annual incentives, bonus share matching and long-term incentives. Our assessment of the relative importance of fixed and performance-related remuneration for each of the directors based on our policy and the data set out in this report is as follows:

Proportion of total compensation



Note The method for valuing the different elements of remuneration is summarised in the table on page 59.

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

Benchmarking

The committee wants our executive directors' remuneration to be competitive with those of directors and executives in similar positions in comparable companies.

The policy is that target total direct compensation (base salary plus annual and long-term incentives) should be set by reference to the UK and US mid-market depending on the relevant market or markets for particular jobs.

We use a range of UK companies in different sectors including the media sector. Some are of a similar size to Pearson, while others are larger, but the method which our independent advisers use to make comparisons on remuneration takes this into account. All have very substantial overseas operations. We also use selected media companies in North America.

We use these companies because they represent the wider executive talent pool from which we might expect to recruit externally and the pay market to which we might be vulnerable if our remuneration was not competitive.

Market assessments against the two groups take account of those factors which Towers Perrin's research shows differentiate remuneration for jobs of a similar nature, such as sales, board membership, reporting relationships and international activities.

For benchmarking purposes, the main elements of remuneration are valued as follows:

Element of remuneration	Valuation
Base salary	Actual base salary
Annual incentive	Target level of annual incentive
Bonus share matching	Expected value of matching award based on 50% of target level of annual incentive
Long-term incentive	Expected value of long-term incentive award
Pension and benefits	Cost to company of providing pension and other benefits
Total remuneration	Sum of all elements of remuneration

Expected value means the net present value of awards taking into account the vesting schedule, risk of forfeiture and the probability that any performance target will be met.

Base salary

The committee's normal policy is to review salaries annually taking into account the remuneration arrangements and the level of increases applicable to employees across the rest of the company as a whole.

For 2010, the company is reviewing salaries for employees taking into account the location and economic conditions of each business. For executive directors, and other members of the Pearson Management Committee, we have reviewed base salaries in line with the general level of increases elsewhere. Full details of the executive directors' remuneration for 2010 will be set out in the report on directors' remuneration for 2010.

The committee reviewed executive directors' base salaries for 2009 at the end of 2008. In light of the then prevailing economic conditions and consistent with the action taken across the company to control costs and minimise job losses, there were no increases in base salary for the executive directors and other members of the Pearson Management Committee for 2009. Full details of the executive directors' 2009 remuneration are set out in table 1 on page 71.

Allowances and benefits

The company's policy is that benefit programmes should be competitive in the context of the local labour market, but as an international company we require executives to operate worldwide and recognise that recruitment also operates worldwide.

Annual incentives

The committee establishes the annual incentive plans for the executive directors and the chief executives of the company's principal operating companies, including performance measures and targets. These plans then become the basis of the annual incentive plans below the level of the principal operating companies, particularly with regard to the performance measures used and the relationship between the incentive plan targets and the relevant business unit operating plans.

We will continue to review the annual incentive plans each year and to revise the performance measures, targets and individual incentive opportunities in light of current conditions. We will continue to disclose details of the operation of the annual incentive plans in the report on directors' remuneration each year.

Annual incentive payments do not form part of pensionable earnings.

Performance measures

The financial performance measures relate to the company's main drivers of business performance at both the corporate, operating company and business unit level. Performance is measured separately for each item. For each performance measure, the committee establishes threshold, target and maximum levels of performance for different levels of payout.

A proportion (which for 2010 may be up to 30%) of the total annual incentive opportunity for the executive directors and other members of the Pearson Management Committee is based on performance against personal objectives as agreed with the chief executive (or, in the case of the chief executive, the chairman). These comprise functional, operational, strategic and non-financial objectives relevant to the executives' specific areas of responsibility and *inter alia* may include objectives relating to environmental, social and governance issues.

For 2010, the principal financial performance measures are: sales; operating profit (for the operating companies) and growth in underlying earnings per share for continuing operations at constant exchange rates (for Pearson plc); average working capital as a ratio to sales; and operating cash flow. The selection and weighting of performance measures takes into account the strategic objectives and the business priorities relevant to each operating company and to Pearson overall each year.

Incentive opportunities

In each year's report on directors' remuneration, we describe any changes to target and maximum incentive opportunities for the chief executive and the other executive directors for the year ahead.

Report on directors' remuneration continued

For 2010, there is no change to the target annual incentive opportunity for the chief executive which remains at 100% of base salary. We reviewed the chief executive's maximum opportunity in light of competitive market data and practice elsewhere in the company and have increased it to 180% of base salary (150% in 2009).

For the other members of the Pearson Management Committee, we have reviewed individual incentive opportunities taking into account their membership of that committee and the contribution of their respective businesses or role to Pearson's overall financial goals. In the case of the executive directors, the target individual incentive opportunity is in a range up to 87.5% of base salary. The maximum opportunity remains at twice target (as in 2009).

The annual incentive plans are discretionary and the committee reserves the right to make adjustments to payouts up or down if it believes exceptional factors warrant doing so. The committee may also award individual discretionary incentive payments although no such payments were awarded in respect of 2009.

For 2009, total annual incentive opportunities were based on Pearson plc and operating company financial performance and performance against personal objectives as follows:

Name	Pearson plc	Operating company/ companies	Personal objectives
Marjorie Scardino	100%	–	–
David Bell	75%	–	25%
Will Ethridge	30%	60%	10%
Rona Fairhead	30%	60%	10%
Robin Freestone	90%	–	10%
John Makinson	30%	60%	10%

2009 performance

Performance in 2009 against the relevant incentive plans was as follows:

		Performance against incentive plan			
Incentive plan	Performance measure	Below threshold	Between threshold and target	Between target and maximum	Above maximum
Pearson plc	Sales			✓	
	Underlying growth in adjusted earnings per share at constant exchange rates			✓	
	Average working capital to sales ratio				✓
	Operating cash flow				✓
Pearson Education North America	Sales			✓	
	Operating profit				✓
	Average working capital to sales ratio				✓
	Operating cash flow				✓
FT Publishing	Sales	✓			
	Operating profit				✓
	Operating cash flow				✓
Pearson VUE	Sales		✓		
	Operating profit			✓	
	Average working capital to sales ratio				✓
	Operating cash flow			✓	
Penguin Group	Sales			✓	
	Operating profit			✓	
	Operating margin			✓	
	Average working capital to sales ratio			✓	
	Operating cash flow				✓

Details of actual payouts for 2009 are set out in table 1 on page 71.

Bonus share matching

In 2008, shareholders approved the renewal of the annual bonus share matching plan first approved by shareholders in 1998.

Invested and matching shares

The plan permits executive directors and senior executives around the company to invest up to 50% of any after-tax annual bonus in Pearson shares.

If the participant's invested shares are held, they are matched subject to earnings per share growth over the three-year performance period on a gross basis i.e. the maximum number of matching shares is equal to the number of shares that could have been acquired with the amount of the pre-tax annual bonus taken in invested shares.

50% of the maximum matching award is released if the company's adjusted earnings per share increase in real terms by 3% per annum compound over the three-year performance period. 100% of the maximum matching award is released if the company's adjusted earnings per share increase in real terms by 5% per annum compound over the same period.

For real growth in adjusted earnings per share of between 3% and 5% per annum compound, the rate at which the matching award is released is calculated according to a straight-line sliding scale.

Real earnings per share growth per annum	Proportion of maximum matching award released
Less than 3%	0%
3%	50%
Between 3% and 5%	Sliding scale between 50% and 100%
5% or more	100%

Performance condition

Earnings per share growth is calculated using the point-to-point method. This method compares the adjusted earnings per share in the company's accounts for the financial year ended prior to the grant date with the adjusted earnings per share for the financial year ending three years later and calculates the implicit compound annual growth rate over the period.

Real growth is calculated by reference to the UK Government's Retail Prices Index (All Items). We choose to test our earnings per share growth against UK inflation over three years to measure the company's financial progress over the period to which the entitlement to matching shares relates.

Dividend shares

Where matching shares vest in accordance with the plan, a participant also receives 'dividend' shares representing the gross value of dividends that would have been paid on the matching shares during the holding period and reinvested.

Report on directors' remuneration continued

Outstanding awards

Details of awards made, outstanding, held or released under the annual bonus share matching plan are as follows (subject to audit):

Date of award	Share price on date of award	Vesting	Status of award
16 April 2009	670.0p	16 April 2012	Outstanding subject to 2008 to 2011 performance
4 June 2008	670.7p	4 June 2011	Outstanding subject to 2007 to 2010 performance
22 May 2007	899.9p	50% on 22 May 2010	Performance condition met. Real compound annual growth in earnings per share for 2006 to 2009 of 12.2% against target of 3.0%
		100% on 22 May 2012	Outstanding subject to participants not electing to call for 50% of shares that vest on 22 May 2010 and subject to 2006 to 2011 performance
12 April 2006	776.2p	50% on 12 April 2009	Target met as reported in report on directors' remuneration for 2008. Shares held pending release on 12 April 2011
		100% on 12 April 2011	Outstanding subject to 2005 to 2010 performance
15 April 2005	631.0p	100% on 2 March 2010	Performance condition met. Increase in adjusted earnings per share for 2004 to 2009 of 137.8% against target of 29.8%. Shares held pending release on 2 March 2010
16 April 2004	652.0p	100% on 16 April 2009	Target met as reported in report on directors' remuneration for 2008. Shares released on 16 April 2009

Note For awards made prior to 2008, the annual bonus share matching plan operated on the basis of a 50% match after three years and 100% match after five years, subject to the earnings per share growth targets being met over the relevant performance periods.

All of the executive directors hold or held awards under this plan in 2009. Details are set out in table 4 on pages 74 to 76 and itemised as a or a*.

Long-term incentives

At the Annual General Meeting in April 2006, shareholders approved the renewal of the long-term incentive plan first introduced in 2001.

Executive directors, senior executives and other managers can participate in this plan which can deliver restricted stock and/or stock options. Approximately 6% of the company's employees currently hold awards under this plan.

The aim is to give the committee a range of tools with which to link corporate performance to management's long-term reward in a flexible way. It is not the committee's intention to grant stock options in 2010.

Restricted stock granted to executive directors vests only when stretching corporate performance targets over a specified period have been met. Awards vest on a sliding scale based on performance over the period. There is no retesting.

Performance measures

The committee determines the performance measures and targets governing an award of restricted stock prior to grant.

The performance measures that have applied since 2006 and that will apply for 2010 and subsequent awards for the executive directors are focused on delivering and improving returns to shareholders. These are relative total shareholder return (TSR), return on invested capital (ROIC) and earnings per share (EPS) growth.

Total shareholder return is the return to shareholders from any growth in Pearson's share price and reinvested dividends over the performance period. For long-term incentive awards, TSR is measured relative to the constituents of the FTSE World Media Index over a three-year period. Companies that drop out of the index are normally excluded i.e. only companies in the index for the entire period are counted.

Share price is averaged over 20 days at the start and end of the performance period, commencing on the date of Pearson's results announcement in the year of grant and the year of vesting. Dividends are treated as reinvested on the ex-dividend date, in line with the Datastream methodology.

The vesting of shares based on relative TSR is subject to the committee satisfying itself that the recorded TSR is a genuine reflection of the underlying financial performance of the business.

The committee chose TSR relative to the constituents of the FTSE World Media Index because, in line with many of our shareholders, it felt that part of executive directors' rewards should be linked to performance relative to the company's peers.

Return on invested capital is adjusted operating profit less cash tax expressed as a percentage of gross invested capital (net operating assets plus gross goodwill).

We chose ROIC because, over the past few years, the transformation of Pearson has significantly increased the capital invested in the business (mostly in the form of goodwill associated with acquisitions) and required substantial cash investment to integrate those acquisitions.

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 any ordinary shares purchased by the company and held as treasury shares (note 8 of the financial statements).

For 2008 and subsequent awards, EPS growth is calculated using the point-to-point method. This method compares the adjusted EPS in the company's accounts for the financial year ended prior to the grant date with the adjusted EPS for the financial year ending three years later and calculates the implicit compound annual growth rate over the period.

We chose EPS growth because strong bottom-line growth is imperative if we are to improve our TSR and our ROIC.

Pearson's reported financial results for the relevant periods are used to measure performance.

The committee has discretion to make adjustments taking into account exceptional factors that distort underlying business performance. In exercising such discretion, the committee is guided by the principle of aligning shareholder and management interests.

Restricted stock may be granted without performance conditions to satisfy recruitment and retention objectives. Restricted stock awards that are not subject to performance conditions will not be granted to any of the current executive directors.

Performance targets
We will set stretching targets for the 2010 awards that are consistent with the company's strategic objectives over the period to 2012. Full details of the targets and individual awards will be set out in the report on directors' remuneration for 2010.

Value of awards
Our independent advisers verify each year the expected value of awards i.e. their net present value after taking into account the vesting schedule, risk of forfeiture and the probability that any performance targets will be met.

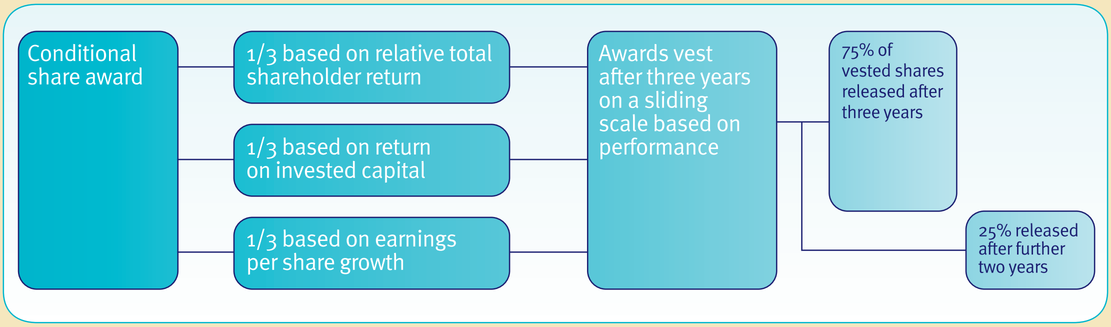
The level of individual awards takes into account three factors: their expected values; the assessments by our independent advisers of market practice for comparable companies and of directors' total remuneration relative to the market; and the face value of individual awards and their potential value should the performance targets be met in full.

Dividends
Where shares vest, participants receive additional shares representing the gross value of dividends that would have been paid on these shares during the performance period and reinvested. The expected value of awards made on this basis takes this into account.

Retention period
We encourage executives and managers to build up a long-term holding of shares so as to demonstrate their commitment to the company.

To achieve this, for awards of restricted stock that are subject to performance conditions over a three-year period, 75% of the award vests at the end of the three-year period. The remaining 25% of the award only vests if the participant retains the after-tax number of shares that vest at year three for a further two years.

Report on directors' remuneration continued



Outstanding awards

Details of awards made, outstanding, vested and held or released under the long-term incentive plan are as follows (subject to audit):

Date of award	Share price on date of award	Vesting date	Performance measures (award split equally across three measures)	Performance period	Payout at threshold	Payout at maximum	Actual performance	% of award vested	Status of award
03/03/09	654.0p	03/03/12	Relative TSR	2009 to 2012	30% at median	100% at upper quartile	–	–	Outstanding
			ROIC	2011	25% for ROIC of 8.5%	100% for ROIC of 10.5%	–	–	Outstanding
			EPS growth	2011 compared to 2008	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%	–	–	Outstanding
04/03/08	649.5p	04/03/11	Relative TSR	2008 to 2011	30% at median	100% at upper quartile	–	–	Outstanding
			ROIC	2010	25% for ROIC of 8.5%	100% for ROIC of 10.5%	–	–	Outstanding
			EPS growth	2010 compared to 2007	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%	–	–	Outstanding
30/07/07	778.0p	02/03/10	Relative TSR	2007 to 2010	30% at median	100% at upper quartile	94th percentile (6th out of 85 companies)	100%	Vested and remain held pending release
			ROIC	2009	25% for ROIC of 8.5%	100% for ROIC of 10.5%	8.9%	40%	Vested and remain held pending release
			EPS growth	2007 to 2009 compared to 2006 (see note 2)	30% for EPS growth of 6.0%	100% for EPS growth of 12.0%	14.3%	100%	Vested and remain held pending release

Date of award	Share price on date of award	Vesting date	Performance measures (award split equally across three measures)	Performance period	Payout at threshold	Payout at maximum	Actual performance	% of award vested	Status of award
13/10/06	767.5p	13/10/09	Relative TSR	2006 to 2009	30% at median	100% at upper quartile	90th percentile (10th out of 95 companies)	100%	83.3% of shares vested. Three-quarters released on 13 October 2009. If after tax number of shares are retained for a further two years, the remaining quarter will be released on 13 October 2011
			ROIC	2008	25% for ROIC of 8.0%	100% for ROIC of 10.0%	9.2%	50% (see note 1)	
			EPS growth	2006 to 2008 compared to 2005 (see note 2)	30% for EPS growth of 5.0%	100% for EPS growth of 12.0%	18.3%	100%	

Note 1 In relation to the award made on 13 October 2006, the committee noted the change in the calculation of return in invested capital and the resulting figure of 9.2% for 2008. The committee agreed with the rationale for the change but considered that, given that the new basis of calculation differed from that used at the time the award was made, it would not be appropriate simply to use this basis for the purposes of determining payout on this element. The payout of 50% of shares originally awarded reflects the committee's judgement on this point.

Note 2 For awards prior to 2008, EPS growth is calculated using the aggregate method that sums the results for each year and calculates the compound aggregate average annual growth assuming a constant increase on the base year throughout the period.

All of the executive directors hold awards under the long-term incentive plan. Details are set out in table 4 on pages 74 to 76 and itemised as b or b*.

All-employee share plans

Executive directors can participate in the company's all-employee share plans on the same terms as other employees.

These plans comprise savings-related share acquisition programmes in the UK and the US.

These plans operate within specific tax legislation (including a requirement to finance acquisition of shares using the proceeds of a monthly savings contract) and the acquisition of shares under these plans is not subject to the satisfaction of a performance target.

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 stock 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 2009, stock awards to be satisfied by new-issue equity granted in the last ten years under all employee share plans amounted to 3.6% of the company's issued share capital and under executive or discretionary plans amounted to 2.0%.

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 2009 amounted to 1.7% of the company's issued share capital.

The headroom available for all employee plans, executive or discretionary plans and shares held in trust is as follows:

Headroom	2009	2008	2007
All employee plans	6.4%	6.2%	6.0%
Executive or discretionary plans	3.0%	2.8%	2.3%
Shares held in trust	3.3%	3.3%	3.4%

Report on directors' remuneration continued

Shareholding of executive directors

The committee expects executive directors to build up a substantial shareholding in the company in line with the policy of encouraging widespread employee ownership and describes separately here both the number of shares that the executive directors hold and the value expressed as a percentage of base salary.

The current value of the executive directors' own shares based on the middle market value of Pearson shares of 912.0p on 26 February 2010 (which is the latest practicable date before the results announcement) against annual base salaries in 2009 is as follows:

Own shares	Number of shares	Value (% of base salary)
Marjorie Scardino	824,124	791%
Will Ethridge	262,988	375%
Rona Fairhead	270,982	488%
Robin Freestone	118,996	241%
John Makinson	474,581	824%

In addition, the executive directors have prospective holdings as a result of restricted shares that have vested and are held pending release. The current value of these shares before any withholdings is as follows:

Restricted shares	Number of shares	Value (% of base salary)
Marjorie Scardino	640,590	615%
Will Ethridge	183,938	263%
Rona Fairhead	233,298	420%
Robin Freestone	130,113	264%
John Makinson	181,169	315%

The size of these holdings, the volatility of the stock market and the share retention features that already exist in our long-term incentive plans means that we do not prescribe a particular relationship of shareholding to salary.

No executive director sold shares during the year other than to satisfy income tax liability on the release of restricted shares.

Service agreements

In accordance with long established policy, all continuing executive directors have rolling service agreements under which, other than by termination in accordance with the terms of these agreements, employment continues until retirement.

The committee reviewed the policy on executive employment agreements in 2008 and again in 2010. Our policy is that for future executive directors service agreements should provide that the company may terminate these agreements by giving no more than 12 months' notice. As an alternative, the company may at its discretion pay in lieu of that notice. Payment in lieu of notice may be made in instalments and may be subject to mitigation.

We will keep the application of the policy on executive employment agreements, including provisions for payment in lieu of notice, under review, particularly with regard to the arrangements for any new executive directors.

In the case of the longer serving directors with legacy employment agreements, the compensation payable in circumstances where the company terminates the agreements without notice or cause takes the form of liquidated damages.

There are no special provisions for notice, pay in lieu of notice or liquidated damages in the event of termination of employment in the event of a change of control of Pearson.

On termination of employment, executive directors' entitlements to any vested or unvested awards under Pearson's discretionary share plans are treated in accordance with the terms of the relevant plan.

We summarise the service agreements that applied during 2009 and that continue to apply for 2010 as follows:

Name	Date of agreement	Notice periods	Compensation on termination by the company without notice or cause
Glen Moreno	29 July 2005	12 months from the director; 12 months from the company	100% of annual fees at the date of termination
Marjorie Scardino	27 February 2004	Six months from the director; 12 months from the company	100% of annual salary at the date of termination, the annual cost of pension and all other benefits and 50% of potential annual incentive
David Bell (stepped down on 1 May 2009) (see note)	15 March 1996	Six months from the director; 12 months from the company	100% of annual salary at the date of termination, the annual cost of pension and all other benefits and 50% of potential annual incentive
Will Ethridge	26 February 2009	Six months from the director; 12 months from the company	100% of annual salary at the date of termination, the annual cost of pension and all other benefits and target annual incentive
Rona Fairhead	24 January 2003	Six months from the director; 12 months from the company	100% of annual salary at the date of termination, the annual cost of pension and all other benefits and 50% of potential annual incentive
Robin Freestone	5 June 2006	Six months from the director; 12 months from the company	No contractual provisions
John Makinson	24 January 2003	Six months from the director; 12 months from the company	100% of annual salary at the date of termination, the annual cost of pension and all other benefits and 50% of potential annual incentive

Note No compensation was paid to David Bell when he retired from the company on 31 December 2009.

Retirement benefits

We describe the retirement benefits for each of the executive directors. Details of directors' pension arrangements are set out in table 2 on page 72 of this report.

Executive directors participate in the pension arrangements set up for Pearson employees.

Marjorie Scardino, Will Ethridge, John Makinson, Rona Fairhead and Robin Freestone will also have other retirement arrangements because of the cap on the amount of benefits that can be provided from the pension arrangements in the US and the UK.

The differences in the arrangements for the current executive directors reflect the different arrangements in the UK and the US and the changes in pension arrangements generally over the periods of their employment.

The pension arrangements for all the executive directors include life insurance cover while in employment, and entitlement to a pension in the event of ill-health or disability. A pension for their spouse and/or dependants is also available on death.

In the US, the defined benefit arrangement is the Pearson Inc. Pension Plan. This plan provides a lump sum convertible to a pension on retirement. The lump sum accrued at 6% of capped compensation until 31 December 2001 when further benefit accruals ceased for most employees. Employees who satisfied criteria of age and service at that time continued to accrue benefits under the plan. Will Ethridge is included in this group and continues to accrue benefits under this plan. Marjorie Scardino is not and her benefit accruals under this plan ceased at the end of 2001.

Report on directors' remuneration continued

The defined contribution arrangement in the US is a 401(k) plan. At retirement, the account balances will be used to provide benefits. In the event of death before retirement, the account balances will be used to provide benefits for dependants.

In the UK, the pension plan is the Pearson Group Pension Plan and executive directors participate in either the Final Pay or the Money Purchase 2003 section. Normal retirement age is 62, but, subject to company consent, retirement is currently possible after age 50 (age 55 from April 2010). In the Final Pay section, the accrued pension is reduced on retirement prior to age 60. Pensions in payment are guaranteed to increase each year at 5% or the increase in the Index of Retail Prices, if lower. Pensions for a member's spouse, dependant children and/or nominated financial dependant are payable in the event of death. In the Money Purchase 2003 section the account balances are used to provide benefits at retirement. In the event of death before retirement pensions for a member's spouse, dependant children and/or nominated financial dependant are payable.

Members of the Pearson Group Pension Plan who joined after May 1989 are subject to an upper limit of earnings that can be used for pension purposes, known as the earnings cap. This limit, £108,600 as at 6 April 2006, was abolished by the Finance Act 2004. However the Pearson Group Pension Plan has retained its own 'cap', which will increase annually in line with the UK Government's Index of Retail Prices (All Items). The cap was £123,600 as at 6 April 2009.

As a result of the UK Government's A-Day changes effective from April 2006, UK executive directors and other members of the Pearson Group Pension Plan who are, or become, affected by the lifetime allowance are provided with a cash supplement as an alternative to further accrual of pension benefits on a basis that is broadly cost neutral to the company. In 2009, the only executive director to whom this was applicable was David Bell. He was offered the allowance alternative but declined and continued as an active member of the plan. With his retirement there are no executive directors who received the offer of an allowance alternative.

Marjorie Scardino

Marjorie Scardino participates in the Pearson Inc. Pension Plan and the approved 401(k) plan.

Additional pension benefits are provided through an unfunded unapproved defined contribution plan. Notional annual contributions to this plan are based on a percentage of salary and a fixed cash amount index-linked to inflation and the notional cash balance of this plan increases annually by a specified notional interest rate. The unfunded plan also provides the opportunity to convert a proportion of this notional cash account into a notional share account reflecting the value of a number of Pearson ordinary shares. The number of shares in the notional share account is determined by reference to the market value of Pearson shares at the date of conversion. Part of the unfunded plan is replaced by a funded defined contribution plan approved by HM Revenue and Customs as a corresponding plan.

David Bell

David Bell is drawing his pension from the Pearson Group Pension Plan. He began to receive his pension effective 30 September 2008 on attainment of Normal Retirement Age.

Will Ethridge

Will Ethridge is a member of the Pearson Inc. Pension Plan and the approved 401(k) plan. He also participates in an unfunded, unapproved Supplemental Executive Retirement Plan (SERP) that provides an annual accrual of 2% of final average earnings, less benefits accrued in the Pearson Inc. Pension Plan and US Social Security. Additional defined contribution benefits are provided through a funded, unapproved 401(k) excess plan.

Rona Fairhead

Rona Fairhead is a member of the Pearson Group Pension Plan. Her pension accrual rate is 1/30th of pensionable salary per annum, restricted to the plan earnings cap.

Until April 2006, the company also contributed to a Funded Unapproved Retirement Benefits Scheme (FURBS) on her behalf. Since April 2006, she has received a taxable and non-pensionable cash supplement in replacement of the FURBS.

Robin Freestone

Robin Freestone is a member of the Money Purchase 2003 section of the Pearson Group Pension Plan. Company contributions are 16% of pensionable salary per annum, restricted to the plan earnings cap.

Until April 2006, the company also contributed to a Funded Unapproved Retirement Benefits Scheme (FURBS) on his behalf. Since April 2006, he has received a taxable and non-pensionable cash supplement in replacement of the FURBS.

John Makinson

John Makinson is a member of the Pearson Group Pension Plan under which his pensionable salary is restricted to the plan earnings cap. The company ceased contributions on 31 December 2001 to his FURBS arrangement. During 2002 it set up an Unfunded Unapproved Retirement Benefits Scheme (UURBS) for him. The UURBS tops up the pension payable from the Pearson Group Pension Plan and the closed FURBS to target a pension of two-thirds of a revalued base salary on retirement at age 62. The revalued base salary is defined as £450,000 effective at 1 June 2002, increased at 1 January each year by reference to the increase in the UK Government's Index of Retail Prices (All Items). In the event of his death a pension from the Pearson Group Pension Plan, the FURBS and the UURBS will be paid to his spouse or nominated financial dependant. Early retirement is possible from age 50 (age 55 from April 2010), with company consent.

The pension is reduced to reflect the shorter service, and before age 60, further reduced for early payment.

Executive directors' non-executive directorships

The committee's policy is that executive directors may, by agreement with the board, serve as non-executives of other companies and retain any fees payable for their services.

The following executive directors served as non-executive directors elsewhere and received fees or other benefits for the period covered by this report as follows:

	Company	Fees/benefits
Marjorie Scardino	Nokia Corporation	€150,000
	MacArthur Foundation	$24,000
Rona Fairhead	HSBC Holdings plc	£135,000
	Spencer Stuart Advisory Board	£10,000

Other executive directors served as non-executive directors elsewhere but did not receive fees.

Chairman's remuneration

The committee's policy is that the chairman's pay should be set at a level that is competitive with those of chairmen in similar positions in comparable companies. He is not entitled to any annual or long-term incentive, retirement or other benefits.

There were no changes in the chairman's remuneration in 2009. With effect from 1 January 2007, his remuneration was £450,000 per year.

Non-executive directors

Fees for non-executive directors are determined by the full board having regard to market practice and within the restrictions contained in the company's Articles of Association. Non-executive directors receive no other pay or benefits (other than reimbursement for expenses incurred in connection with their directorship of the company) and do not participate in the company's equity-based incentive plans.

There were no changes in the structure and level of non-executive directors' fees in 2009. With effect from 1 July 2007, these were as follows:

	Fees payable from 1 July 2007
Non-executive director	£60,000
Chairmanship of audit committee	£20,000
Chairmanship of personnel committee	£15,000
Membership of audit committee	£10,000
Membership of personnel committee	£5,000
Senior independent director	£15,000

A minimum of 25% of the basic fee is paid in Pearson shares that the non-executive directors have committed to retain for the period of their directorships.

Terry Burns also receives a fee in respect of his non-executive directorship of Edexcel which is included in the figure shown in table 1 on page 71.

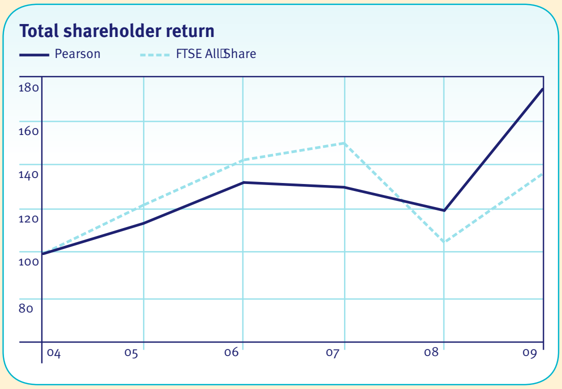
Non-executive directors serve Pearson under letters of appointment and do not have service contracts. There is no entitlement to compensation on the termination of their directorships.

Report on directors' remuneration continued

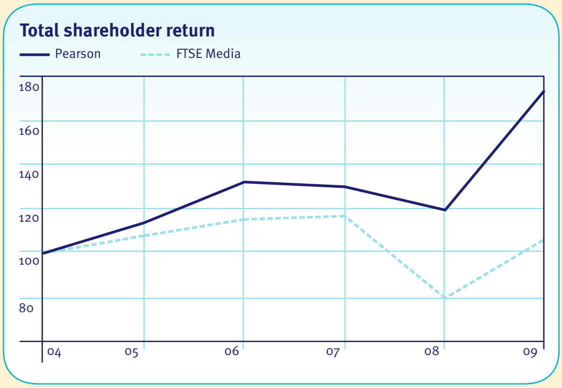
Total shareholder return performance

Below we set out Pearson's total shareholder return on three bases. Pearson is a constituent of all the indices shown.

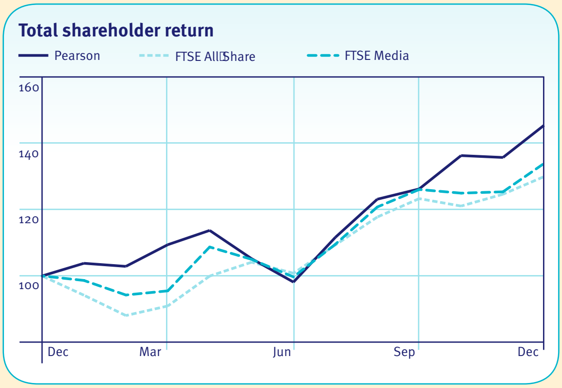
First, we set out Pearson's total shareholder return performance relative to the FTSE All-Share index on an annual basis over the five-year period 2004 to 2009. We have chosen this index, and used it consistently in each report on directors' remuneration since 2002, on the basis that it is a recognisable reference point and an appropriate comparator for the majority of our investors.



Secondly, to illustrate performance against our sector, we show Pearson's total shareholder return relative to the FTSE Media index over the same five-year period.



And thirdly, we show Pearson's total shareholder return relative to the FTSE All-Share and Media indices on a monthly basis over 2009, the period to which this report relates.



Items subject to audit

The following tables form the auditable part of the remuneration report.

Table 1: Remuneration of the directors

Excluding contributions to pension funds and related benefits set out in table 2, directors' remuneration was as follows:

	2009					2008
All figures in £000s	Salaries/fees	Annual incentive	Allowances	Benefits	Total	Total
Chairman						
Glen Moreno	450	–	–	–	450	450
Executive directors						
Marjorie Scardino	950	1,301	56	21	2,328	2,057
David Bell (stepped down 1 May 2009)	154	207	–	6	367	983
Will Ethridge	639	874	–	–	1,513	1,171
Rona Fairhead	506	570	–	28	1,104	1,036
Robin Freestone	450	639	–	13	1,102	957
John Makinson	525	655	216	29	1,425	1,240
Non-executive directors						
David Arculus	85	–	–	–	85	85
Terry Burns	83	–	–	–	83	83
Patrick Cescau	70	–	–	–	70	70
Susan Fuhrman	70	–	–	–	70	70
Ken Hydon	85	–	–	–	85	81
CK Prahalad	60	–	–	–	60	40
Total	4,127	4,246	272	97	8,742	8,323

Note 1 Allowances for Marjorie Scardino include £44,870 in respect of housing costs and a US payroll supplement of £10,961. John Makinson is entitled to a location and market premium in relation to the management of the business of the Penguin Group in the US and received £215,594 for 2009.

Note 2 Benefits include company car, car allowance and UK health care premiums. US health and welfare benefits for Marjorie Scardino and Will Ethridge are self-insured and the company cost, after employee contributions, is tax free to employees. For Marjorie Scardino, benefits include £5,317 for pension planning and financial advice. Marjorie Scardino, Rona Fairhead, David Bell and John Makinson have the use of a chauffeur.

Note 3 There were no increases in base salary for the executive directors for 2009.

Note 4 No amounts as compensation for loss of office and no expense allowances chargeable to UK income tax were paid during the year.

Note 5 David Bell stepped down from the board on 1 May 2009. He continued to be entitled to the same base salary and other benefits in accordance with his service agreement with the company until his retirement from the company on 31 December 2009.

Report on directors' remuneration continued

Table 2: Directors' pensions and other pension-related items

Directors' pensions	Age at 31 Dec 09	Accrued pension at 31 Dec 09 £000[1]	Increase in accrued pension over the period £000[2]	Transfer value at 31 Dec 08 £000[3]	Transfer value at 31 Dec 09 £000[4]	Increase in transfer value* over the period £000	Increase/ (decrease) in accrued pension† over the period £000	Transfer value* of the increase/ (decrease) in accrued pension† at 31 Dec 09 £000	Other pension costs to the company over the period £000[5]	Other allowances in lieu of pension £000[6]	Other pension related benefit costs £000[7]
Marjorie Scardino	62	4.5	(0.5)	47.5	44.1	(3.4)	(0.5)	(4.9)	623.7	–	54.5
David Bell (stepped down 1 May 2009)	63	236.0	(76.7)	6,045.5	5456.4	(589.1)	(76.7)	(1,773.3)	–	–	–
Will Ethridge	57	127.0	(1.2)	853.7	1037.2	183.5	(1.2)	(9.8)	44.4	–	2.1
Rona Fairhead	48	32.3	5.0	294.6	466.0	165.5	5.0	66.2	–	128.2	3.4
Robin Freestone	51	–	–	–	–	–	–	–	18.8	112.1	4.9
John Makinson	55	254.8	18.4	3,532.2	4,897.6	1,359.4	18.4	347.8	–	–	12.4

* Less directors' contributions.

† Net of inflation. An inflation rate of 0% has been used.

Note 1 The accrued pension at 31 December 2009 is that which would become payable from normal retirement age if the member left service at 31 December 2009. For Marjorie Scardino it relates only to the pension from the US Plan. For David Bell this is the pension in payment as at 31 December 2009. For Will Ethridge it relates to his pension from the US Plan and US SERP. For Rona Fairhead it relates to the pension payable from the UK Plan. For John Makinson it relates to the pension from the UK Plan, the FURBS and the UURBS in aggregate.

Note 2 For Marjorie Scardino and Will Ethridge, the increase in accrued pension figure is negative due to movements in exchange rates over the year.

Note 3 For David Bell, this is the value of his pre-commutation pension at his Normal Retirement Date based on market conditions at 31 December 2008.

Note 4 The UK transfer values at 31 December 2009 are calculated using the assumptions for cash equivalents payable from the UK Plan and are based on the accrued pension at that date. For David Bell the transfer value has been calculated as the value of the pension in payment at 31 December 2009. For the US SERP, transfer values are calculated using a discount rate equivalent to current US long-term bond yields. The US Plan is a lump sum plan and the accrued balance is shown.

Note 5 For UK benefits, this column comprises employer contributions to the Money Purchase 2003 section of the Pearson Group Pension Plan. For US benefits, it includes company contributions to funded defined contribution plans and notional contributions to unfunded defined contribution plans.

Note 6 This column comprises cash allowances paid in lieu of pension benefits above the plan earnings cap.

Note 7 This column comprises life cover and long-term disability insurance not covered by the retirement plans.

Note 8 David Bell did not receive any cash in lieu of pension benefits in 2009.

Table 3: Interests of directors

	Ordinary shares at 1 Jan 09	Ordinary shares at 31 Dec 09
Glen Moreno	210,000	210,000
Marjorie Scardino	632,755	824,124
David Arculus	11,740	13,044
David Bell (stepped down 1 May 2009)	250,348	253,050
Terry Burns	10,290	12,008
Patrick Cescau	4,144	5,356
Will Ethridge	128,758	262,988
Rona Fairhead	209,259	270,982
Robin Freestone	44,379	118,996
Susan Fuhrman	7,365	9,384
Ken Hydon	8,559	9,774
John Makinson	397,733	474,581
CK Prahalad	969	2,197

Note 1 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 2 No director sold shares during the year other than to satisfy income tax liability on the release of restricted shares.

Note 3 At 31 December 2009, John Makinson held 1,000 shares in Interactive Data Corporation.

Note 4 From 2004, Marjorie Scardino is also deemed to be interested in a further number of shares under her unfunded pension arrangement described in this report, which provides the opportunity to convert a proportion of her notional cash account into a notional share account reflecting the value of a number of Pearson shares.

Note 5 The register of directors' interests (which is open to inspection during normal office hours) contains full details of directors' shareholdings and options to subscribe for shares. The market price on 31 December 2009 was 891.0p per share and the range during the year was 578.0p to 892.5p.

Note 6 At 31 December 2009, Patrick Cescau held 168,000 Pearson bonds.

Note 7 There were no movements in ordinary shares between 1 January 2010 and a month prior to the sign-off of this report.

Introduction
Our strategy
Our performance
Our impact on society
Governance
Financial statements

Report on directors' remuneration continued

Table 4: Movements in directors' interests in restricted shares

Restricted shares designated as: a annual bonus share matching plan; b long-term incentive plan; * where shares at 31 December 2009 have vested and are held pending release; and ** where dividend-equivalent shares were added to the released shares.

Date of award		1 Jan 09	Awarded	Released	Lapsed	31 Dec 09	Market value at date of award	Earliest release date	Date of release	Market value at date of release
Marjorie Scardino										
a*	22/5/07	30,143				30,143	899.9p	22/5/10		
a	22/5/07	30,144				30,144	899.9p	22/5/12		
a	4/6/08	99,977				99,977	670.7p	4/6/11		
b	16/12/02	301,700			301,700	0	638.5p	28/6/05		
b	26/9/03	120,200				120,200	582.0p	29/9/06		
b*	21/12/04	83,197				83,197	613.0p	21/12/09		
b*	23/9/05	97,500				97,500	655.0p	2/3/10		
b*	13/10/06	225,000		168,750		56,250	767.5p	13/10/09	13/10/09	791.5p
b*	13/10/06	150,000		112,500		37,500	767.5p	13/10/09	13/10/09	791.5p
b**	13/10/09	0	37,688	37,688		0	791.5p	13/10/09	13/10/09	791.5p
b*	30/7/07	420,000			84,000	336,000	778.0p	2/3/10		
b	4/3/08	400,000				400,000	649.5p	4/3/11		
b	3/3/09	0	450,000			450,000	654.0p	3/3/12		
Total		1,957,861	487,688	318,938	385,700	1,740,911				
David Bell										
a*	16/4/04	4,503		4,503		0	652.0p	16/4/09	16/4/09	670.0p
b	16/12/02	133,065			133,065	0	638.5p	28/6/05		
b	26/9/03	82,400				82,400	582.0p	29/9/06		
b*	21/12/04	33,002				33,002	613.0p	21/12/09		
b*	23/9/05	36,833				36,833	655.0p	2/3/10		
b*	13/10/06	62,500		46,875		15,625	767.5p	13/10/09	13/10/09	791.5p
b*	13/10/06	41,667		31,250		10,417	767.5p	13/10/09	13/10/09	791.5p
b**	13/10/09	0	10,469	10,469		0	791.5p	13/10/09	13/10/09	791.5p
b*	30/7/07	100,000			20,000	80,000	778.0p	2/3/10		
b	4/3/08	100,000				100,000	649.5p	4/3/11		
Total		593,970	10,469	93,097	153,065	358,277				

Table 4: Movements in directors' interests in restricted shares continued

Restricted shares designated as: a annual bonus share matching plan; b long-term incentive plan; * where shares at 31 December 2009 have vested and are held pending release; and ** where dividend-equivalent shares were added to the released shares.

Date of award	1 Jan 09	Awarded	Released	Lapsed	31 Dec 09	Market value at date of award	Earliest release date	Date of release	Market value at date of release
Will Ethridge									
a* 22/5/07	1,254				1,254	899.9p	22/5/10		
a 22/5/07	1,254				1,254	899.9p	22/5/12		
a 16/4/09	0	112,515			112,515	670.0p	16/4/12		
b* 23/9/05	21,017				21,017	655.0p	23/9/08		
b* 13/10/06	100,000		75,000		25,000	767.5p	13/10/09	13/10/09	791.5p
b* 13/10/06	66,667		50,000		16,667	767.5p	13/10/09	13/10/09	791.5p
b** 13/10/09	0	16,750	16,750		0	791.5p	13/10/09	13/10/09	791.5p
b* 30/7/07	150,000			30,000	120,000	778.0p	2/3/10		
b 4/3/08	150,000				150,000	649.5p	4/3/11		
b 3/3/09	0	175,000			175,000	654.0p	3/3/12		
Total	490,192	304,265	141,750	30,000	622,707				
Rona Fairhead									
a* 16/4/04	5,146		5,146		0	652.0p	16/4/09	16/4/09	670.0p
a* 15/4/05	19,746				19,746	631.0p	2/3/10		
a* 12/4/06	8,050				8,050	776.2p	12/4/11		
a 12/4/06	8,051				8,051	776.2p	12/4/11		
b 16/12/02	133,065			133,065	0	638.5p	28/6/05		
b 26/9/03	82,400				82,400	582.0p	26/9/06		
b* 21/12/04	33,002				33,002	613.0p	21/12/09		
b* 23/9/05	43,333				43,333	655.0p	2/3/10		
b* 13/10/06	70,000		52,500		17,500	767.5p	13/10/09	13/10/09	791.5p
b* 13/10/06	46,667		35,000		11,667	767.5p	13/10/09	13/10/09	791.5p
b** 13/10/09	0	11,725	11,725		0	791.5p	13/10/09	13/10/09	791.5p
b* 30/7/07	125,000			25,000	100,000	778.0p	2/3/10		
b 4/3/08	125,000				125,000	649.5p	4/3/11		
b 3/3/09	0	150,000			150,000	654.0p	3/3/12		
Total	699,460	161,725	104,371	158,065	598,749				

Report on directors' remuneration continued

Table 4: Movements in directors' interests in restricted shares continued

Restricted shares designated as: a annual bonus share matching plan; b long-term incentive plan; * where shares at 31 December 2009 have vested and are held pending release; and ** where dividend-equivalent shares were added to the released shares.

Date of award	1 Jan 09	Awarded	Released	Lapsed	31 Dec 09	Market value at date of award	Earliest release date	Date of release	Market value at date of release
Robin Freestone									
a* 12/4/06	1,717				1,717	776.2p	12/4/11		
a 12/4/06	1,718				1,718	776.2p	12/4/11		
a* 22/5/07	2,354				2,354	899.9p	22/5/10		
a 22/5/07	2,354				2,354	899.9p	22/5/12		
a 4/6/08	37,906				37,906	670.7p	4/6/11		
a 16/4/09	0	35,446			35,446	670.0p	16/4/12		
b* 13/10/06	62,500		46,875		15,625	767.5p	13/10/09	13/10/09	791.5p
b* 13/10/06	41,667		31,250		10,417	767.5p	13/10/09	13/10/09	791.5p
b** 13/10/09	0	10,469	10,469		0	791.5p	13/10/09	13/10/09	791.5p
b* 30/7/07	125,000			25,000	100,000	778.0p	2/3/10		
b 4/3/08	125,000				125,000	649.5p	4/3/11		
B 3/3/09	0	150,000			150,000	654.0p	3/3/12		
Total	400,216	195,915	88,594	25,000	482,537				
John Makinson									
b 16/12/02	172,400			172,400	0	638.5p	28/6/05		
b 26/9/03	82,400				82,400	582.0p	26/9/06		
b* 21/12/04	33,002				33,002	613.0p	21/12/09		
b* 23/9/05	39,000				39,000	655.0p	2/3/10		
b* 13/10/06	70,000		52,500		17,500	767.5p	13/10/09	13/10/09	791.5p
b* 13/10/06	46,667		35,000		11,667	767.5p	13/10/09	13/10/09	791.5p
b** 13/10/09	0	11,725	11,725		0	791.5p	13/10/09	13/10/09	791.5p
b* 30/7/07	100,000			20,000	80,000	778.0p	2/3/10		
b 4/3/08	125,000				125,000	649.5p	4/3/11		
b 3/3/09	0	150,000			150,000	654.0p	3/3/12		
Total	668,469	161,725	99,225	192,400	538,569				
Total	4,810,168	1,321,787	845,975	944,230	4,341,750				

Note 1 The number of shares shown represents the maximum number of shares that may vest, subject to any performance conditions being met.

Note 2 No variations to the terms and conditions of plan interests were made during the year.

Note 3 The performance and other conditions that apply to outstanding awards under the annual bonus share matching plan and the long-term incentive plan and that have yet to be met were set out in the reports on directors' remuneration for the years in which they were granted.

Note 4 In the case of the long-term incentive plan awards made on 13 October 2006, we detail separately the part of the award based on ROIC and EPS growth (two-thirds of total award) and that part based on relative TSR (one-third of total award), because vesting of that part of the awards based on TSR was not known at the date of the 2008 report.

Note 5 For long-term incentive awards made prior to 2004 the performance condition was the Pearson share price. The award made on 16 December 2002 lapsed as the Pearson share price failed to meet the required hurdle prior to 28 June 2009.

Table 5: Movements in directors' interests in share options

Shares under option are designated as: a executive; b worldwide save for shares; c premium priced; d long-term incentive; and * where options are exercisable.

Date of grant	1 Jan 09	Granted	Exercised	Lapsed	31 Dec 09	Option price	Earliest exercise date	Expiry date	Date of exercise	Price on exercise	Gain on exercise
Marjorie Scardino											
c 8/6/99	37,583			37,583	0	1372.4p	8/6/02	8/6/09			
c 8/6/99	37,583			37,583	0	1647.5p	8/6/02	8/6/09			
d* 9/5/01	41,550				41,550	1421.0p	9/5/02	9/5/11			
d* 9/5/01	41,550				41,550	1421.0p	9/5/03	9/5/11			
d* 9/5/01	41,550				41,550	1421.0p	9/5/04	9/5/11			
d* 9/5/01	41,550				41,550	1421.0p	9/5/05	9/5/11			
Total	241,366	0	0	75,166	166,200						£0
David Bell											
b 5/5/06	297			297	0	629.6p	1/8/09	1/2/10	5/8/09	704.0p	£221
b 4/5/07	821				821	690.4p	1/8/10	1/2/11			
c 8/6/99	18,705			18,705	0	1372.4p	8/6/02	8/6/09			
c 8/6/99	18,705			18,705	0	1647.5p	8/6/02	8/6/09			
d* 9/5/01	16,350				16,350	1421.0p	9/5/02	9/5/11			
d* 9/5/01	16,350				16,350	1421.0p	9/5/03	9/5/11			
d* 9/5/01	16,350				16,350	1421.0p	9/5/04	9/5/11			
d* 9/5/01	16,350				16,350	1421.0p	9/5/05	9/5/11			
Total	103,928	0	0	37,707	66,221						£221
Will Ethridge											
c 8/6/99	10,802			10,802	0	1372.4p	8/6/02	8/6/09			
c 8/6/99	10,802			10,802	0	1647.5p	8/6/02	8/6/09			
d* 9/5/01	11,010				11,010	$21.00	9/5/02	9/5/11			
d* 9/5/01	11,010				11,010	$21.00	9/5/03	9/5/11			
d* 9/5/01	11,010				11,010	$21.00	9/5/04	9/5/11			
d* 9/5/01	11,010				11,010	$21.00	9/5/05	9/5/11			
d* 1/11/01	14,680				14,680	$11.97	1/11/02	1/11/11			
d* 1/11/01	14,680				14,680	$11.97	1/11/03	1/11/11			
d* 1/11/01	14,680				14,680	$11.97	1/11/04	1/11/11			
Total	109,684	0	0	21,604	88,080						£0
Rona Fairhead											
b 4/5/07	2,371				2,371	690.4p	1/8/12	1/2/13			
d* 1/11/01	20,000				20,000	822.0p	1/11/02	1/11/11			
d* 1/11/01	20,000				20,000	822.0p	1/11/03	1/11/11			
d* 1/11/01	20,000				20,000	822.0p	1/11/04	1/11/11			
Total	62,371	0	0	0	62,371						£0

Introduction
Our strategy
Our performance
Our impact on society
Governance
Financial statements

Report on directors' remuneration continued

Table 5: Movements in directors' interests in share options continued

Shares under option are designated as: a executive; b worldwide save for shares; c premium priced; d long-term incentive; and * where options are exercisable.

Date of grant	1 Jan 09	Granted	Exercised	Lapsed	31 Dec 09	Option price	Earliest exercise date	Expiry date	Date of exercise	Price on exercise	Gain on exercise
Robin Freestone											
b 9/5/08	1,757				1,757	534.8p	1/8/11	1/2/12			
Total	1,757				1,757						£0
John Makinson											
b 9/5/03	4,178				4,178	424.8p	1/8/10	1/2/11			
c 8/6/99	21,477			21,477	0	1372.4p	8/6/02	8/6/09			
c 8/6/99	21,477			21,477	0	1647.5p	8/6/02	8/6/09			
d* 9/5/01	19,785				19,785	1421.0p	9/5/02	9/5/11			
d* 9/5/01	19,785				19,785	1421.0p	9/5/03	9/5/11			
d* 9/5/01	19,785				19,785	1421.0p	9/5/04	9/5/11			
d* 9/5/01	19,785				19,785	1421.0p	9/5/05	9/5/11			
Total	126,272	0	0	42,954	83,318						£0
Total	645,378	0	0	177,431	467,947						£221

Note 1 No variations to the terms and conditions of share options were made during the year.

Note 2 Each plan is described below.

a Executive – The plans under which these options were granted were replaced with the introduction of the long-term incentive plan in 2001. No executive options have been granted to the directors since 1998.

All options have now lapsed, having been unexercised at the tenth anniversary of the date of grant.

b Worldwide save for shares – The acquisition of shares under the worldwide save for shares plan is not subject to the satisfaction of a performance target.

David Bell, Rona Fairhead, Robin Freestone and John Makinson hold options under this plan. Details of these holdings are itemised as b.

c Premium priced – The plan under which these options were granted was replaced with the introduction of the long-term incentive plan in 2001. No Premium Priced Options (PPOs) have been granted to the directors since 1999.

The share price targets for the three-year and five-year tranches of PPOs granted in 1999 have already been met prior to 2009. The share price target for the seven-year tranche of PPOs granted in 2000 was not met in 2009 and the options lapsed. The secondary real growth in earnings per share target for any PPOs to become exercisable has already been met prior to 2009.

All PPOs that remain outstanding lapse if they remain unexercised at the tenth anniversary of the date of grant.

Marjorie Scardino, David Bell, Will Ethridge and John Makinson hold PPOs under this plan. Details of these awards are itemised as c.

d Long-term incentive – All options that remain outstanding are exercisable and lapse if they remain unexercised at the tenth anniversary of the date of grant.

Details of the option grants under this plan for Marjorie Scardino, David Bell, Will Ethridge, Rona Fairhead and John Makinson are itemised as d.

Note 3 In addition, Marjorie Scardino contributes US$1,000 per month (the maximum allowed) to the US employee stock purchase plan. The terms of this plan allow participants to make monthly contributions for one year and to acquire shares at the end of that period at a price that is the lower of the market price at the beginning or the end of the period, both less 15%.

Note 4 The market price on 31 December 2009 was 891.0p per share and the range during the year was 578.0p to 892.5p.

Approved by the board and signed on its behalf by

David Arculus Director
10 March 2010

Consolidated income statement
Year ended 31 December 2009

All figures in £ millions	Notes	2009	2008
Continuing operations			
Sales	2	5,624	4,811
Cost of goods sold	4	(2,539)	(2,174)
Gross profit		3,085	2,637
Operating expenses	4	(2,360)	(1,986)
Share of results of joint ventures and associates	12	30	25
Operating profit	2	755	676
Finance costs	6	(122)	(136)
Finance income	6	27	45
Profit before tax		660	585
Income tax	7	(198)	(172)
Profit for the year from continuing operations		462	413
Loss for the year from discontinued operations	3	–	(90)
Profit for the year		462	323
Attributable to:			
Equity holders of the company		425	292
Minority interest		37	31
Earnings per share for profit from continuing and discontinued operations attributable to the equity holders of the company during the year (expressed in pence per share)			
– basic	8	53.2p	36.6p
– diluted	8	53.1p	36.6p
Earnings per share for profit from continuing operations attributable to the equity holders of the company during the year (expressed in pence per share)			
– basic	8	53.2p	47.9p
– diluted	8	53.1p	47.9p

Consolidated statement of comprehensive income
Year ended 31 December 2009

All figures in £ millions	Notes	2009	2008
Profit for the year		462	323
Net exchange differences on translation of foreign operations		(388)	1,125
Currency translation adjustment disposed – subsidiaries		–	49
Currency translation adjustment disposed – joint venture		–	1
Actuarial losses on retirement benefit obligations – Group	25	(299)	(71)
Actuarial losses on retirement benefit obligations – associate	12	(3)	(3)
Net increase in fair values of proportionate holding arising on stepped acquisition		18	–
Taxation on items recognised in other comprehensive income	7	91	9
Other comprehensive (expense)/income for the year		(581)	1,110
Total comprehensive (expense)/income for the year		(119)	1,433
Attributable to:			
Equity holders of the company		(127)	1,327
Minority interest		8	106

Consolidated statement of changes in equity
Year ended 31 December 2009

All figures in £millions	Share capital	Share premium	Treasury shares	Translation reserve	Retained earnings	Total	Minority interest	Total equity
	Equity attributable to the equity holders of the company							
At 1 January 2009	202	2,505	(222)	586	1,679	4,750	274	5,024
Total comprehensive (expense)/income	–	–	–	(359)	232	(127)	8	(119)
Equity-settled transactions	–	–	–	–	37	37	–	37
Taxation on equity-settled transactions	–	–	–	–	6	6	–	6
Issue of ordinary shares under share option schemes	1	7	–	–	–	8	–	8
Purchase of treasury shares	–	–	(33)	–	–	(33)	–	(33)
Release of treasury shares	–	–	29	–	(29)	–	–	–
Put option over minority interest	–	–	–	–	(23)	(23)	–	(23)
Changes in minority shareholding	–	–	–	–	–	–	24	24
Dividends	–	–	–	–	(273)	(273)	(15)	(288)
At 31 December 2009	203	2,512	(226)	227	1,629	4,345	291	4,636

All figures in £millions	Share capital	Share premium	Treasury shares	Translation reserve	Retained earnings	Total	Minority interest	Total equity
	Equity attributable to the equity holders of the company							
At 1 January 2008	202	2,499	(216)	(514)	1,724	3,695	179	3,874
Total comprehensive income	–	–	–	1,100	227	1,327	106	1,433
Equity-settled transactions	–	–	–	–	33	33	–	33
Taxation on equity-settled transactions	–	–	–	–	(7)	(7)	–	(7)
Issue of ordinary shares under share option schemes	–	6	–	–	–	6	–	6
Purchase of treasury shares	–	–	(47)	–	–	(47)	–	(47)
Release of treasury shares	–	–	41	–	(41)	–	–	–
Changes in minority shareholding	–	–	–	–	–	–	6	6
Dividends	–	–	–	–	(257)	(257)	(17)	(274)
At 31 December 2008	202	2,505	(222)	586	1,679	4,750	274	5,024

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.

Consolidated balance sheet
As at 31 December 2009

All figures in £ millions	Notes	2009	2008
Assets			
Non-current assets			
Property, plant and equipment	10	388	423
Intangible assets	11	5,129	5,353
Investments in joint ventures and associates	12	30	23
Deferred income tax assets	13	387	372
Financial assets – Derivative financial instruments	16	112	181
Retirement benefit assets	25	–	49
Other financial assets	15	62	63
Other receivables	22	112	152
		6,220	6,616
Current assets			
Intangible assets – Pre-publication	20	650	695
Inventories	21	445	501
Trade and other receivables	22	1,284	1,342
Financial assets – Derivative financial instruments	16	–	3
Financial assets – Marketable securities	14	63	54
Cash and cash equivalents (excluding overdrafts)	17	750	685
		3,192	3,280
Total assets		9,412	9,896
Liabilities			
Non-current liabilities			
Financial liabilities – Borrowings	18	(1,934)	(2,019)
Financial liabilities – Derivative financial instruments	16	(2)	(15)
Deferred income tax liabilities	13	(473)	(447)
Retirement benefit obligations	25	(339)	(167)
Provisions for other liabilities and charges	23	(50)	(33)
Other liabilities	24	(253)	(221)
		(3,051)	(2,902)
Current liabilities			
Trade and other liabilities	24	(1,467)	(1,429)
Financial liabilities – Borrowings	18	(74)	(344)
Financial liabilities – Derivative financial instruments	16	(7)	(5)
Current income tax liabilities		(159)	(136)
Provisions for other liabilities and charges	23	(18)	(56)
		(1,725)	(1,970)
Total liabilities		(4,776)	(4,872)
Net assets		4,636	5,024

Consolidated balance sheet continued

All figures in £ millions	Notes	2009	2008
Equity			
Share capital	27	203	202
Share premium	27	2,512	2,505
Treasury shares	28	(226)	(222)
Translation reserve		227	586
Retained earnings		1,629	1,679
Total equity attributable to equity holders of the company		4,345	4,750
Minority interest		291	274
Total equity		4,636	5,024

These financial statements have been approved for issue by the board of directors on 10 March 2010 and signed on its behalf by

Robin Freestone Chief financial officer

Consolidated cash flow statement
Year ended 31 December 2009

All figures in £ millions	Notes	2009	2008
Cash flows from operating activities			
Net cash generated from operations	31	1,012	894
Interest paid		(90)	(87)
Tax paid		(103)	(89)
Net cash generated from operating activities		819	718
Cash flows from investing activities			
Acquisition of subsidiaries, net of cash acquired	29	(208)	(395)
Acquisition of joint ventures and associates		(14)	(5)
Purchase of investments		(10)	(1)
Purchase of property, plant and equipment (PPE)		(62)	(75)
Proceeds from sale of investments		–	5
Proceeds from sale of PPE	31	1	2
Purchase of intangible assets		(58)	(45)
Disposal of subsidiaries, net of cash disposed	30	14	111
Interest received		3	11
Dividends received from joint ventures and associates		22	23
Net cash used in investing activities		(312)	(369)
Cash flows from financing activities			
Proceeds from issue of ordinary shares	27	8	6
Purchase of treasury shares		(33)	(47)
Proceeds from borrowings		296	455
Liquid resources acquired		(13)	–
Repayment of borrowings		(343)	(275)
Finance lease principal payments		(2)	(3)
Dividends paid to company's shareholders	9	(273)	(257)
Dividends paid to minority interest		(20)	(28)
Net cash used in financing activities		(380)	(149)
Effects of exchange rate changes on cash and cash equivalents		(36)	(103)
Net increase in cash and cash equivalents		91	97
Cash and cash equivalents at beginning of year		589	492
Cash and cash equivalents at end of year	17	680	589

Independent auditors' report to the members of Pearson plc

We have audited the consolidated and company financial statements (together the 'financial statements') of Pearson plc for the year ended 31 December 2009. The consolidated financial statements comprise the consolidated income statement, the consolidated balance sheet, the consolidated statement of comprehensive income, the consolidated statement of changes in equity, the consolidated cash flow statement and the related notes to the consolidated financial statements. The company financial statements comprise the company statement of comprehensive income, the company statement of changes in equity, the company balance sheet, the company cash flow statement and the related notes to the company financial statements. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRS) 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.

Respective responsibilities of directors and auditors

As explained more fully in the statement of directors' responsibilities set out in the Governance section of the directors' report, 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 the financial statements in accordance with applicable law and International Standards on Auditing (UK and 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.

Scope of the audit of the financial statements

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.

Opinion on statements

In our opinion:

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 2009 and of the Group's profit and Group's and company's cash flows for the year then ended;

The consolidated financial statements have been properly prepared in accordance with IFRS as adopted by the European Union;

The company financial statements have been properly prepared in accordance with IFRS 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.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

The part of the report on directors' remuneration to be audited has been properly prepared in accordance with the Companies Act 2006;

The information given in the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and

The information given in the corporate governance statement set out in the Governance section of the directors' report with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

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

Adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or

The company financial statements and the information in the report on directors' remuneration that is described as having been audited are not in agreement with the accounting records and returns; or

Certain disclosures of directors' remuneration specified by law are not made; or

We have not received all the information and explanations we require for our audit; or

A corporate governance statement has not been prepared by the company.

Under the Listing Rules we are required to review:

The directors' statement set out in the Governance section of the directors' report in relation to going concern; and

The parts of the corporate governance statement relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review.

Ranjan Sriskandan (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
10 March 2010

Notes to the consolidated financial statements

General information

Pearson plc (the company) and its subsidiaries (together the Group) are international media businesses covering education, business information and consumer publishing.

The company is a limited liability 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 but is also listed on the New York Stock Exchange.

These consolidated financial statements were approved for issue by the board of directors on 10 March 2010.

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 in accordance with International Financial Reporting Standards (IFRS) and International Financial Reporting Interpretations Committee (IFRIC) interpretations as adopted by the European Union (EU) and with those parts of the Companies Act 1985 and/or the Companies Act 2006 (as applicable) applicable to companies reporting under IFRS. These consolidated financial statements are also prepared in accordance with IFRS as issued by the International Accounting Standards Board (IASB). In respect of the accounting standards applicable to the Group there is no difference between EU-adopted and IASB-adopted IFRS. The Group transitioned from UK GAAP to IFRS on 1 January 2003.

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.

1. Interpretations and amendments to published standards effective in 2009

IAS 1 (Revised) 'Presentation of Financial Statements', effective for annual reporting periods beginning on or after 1 January 2009. The amendments require a number of presentational changes including the requirement to present a statement of changes in equity as a primary statement and the introduction of the statement of comprehensive income, which presents all items of recognised income and expense, either in one statement or in two linked statements. Management have elected to present two statements.

Amendments to IAS 23 'Borrowing Costs', effective for annual reporting periods beginning on or after 1 January 2009. The amendment requires capitalisation of borrowing costs that relate to qualifying assets (ones that take a substantial amount of time to get ready for use or sale, with the exception of assets measured at fair value or inventories manufactured in large quantities or on a repetitive basis). Management have assessed that this amendment has no impact on the Group's financial statements as there are currently no material qualifying assets.

Amendments to IFRS 7 'Financial Instruments: Disclosures', effective for annual reporting periods beginning on or after 1 January 2009. The amendments require additional disclosures about fair value measurement and liquidity risk. For financial instruments measured at fair value in the balance sheet disclosure is required, based on observability of inputs, into a three level fair value hierarchy. In addition, a reconciliation between the opening and closing balance for level 3 fair value measurements must be presented, along with significant transfers between the levels of the hierarchy. The amendments also clarify the scope of liquidity risk disclosures. Fair value measurement and liquidity risk disclosures are detailed in note 19.

Amendments to IFRS 2 'Share-based Payment', effective for annual reporting periods beginning on or after 1 January 2009. The amendment clarifies that only service and performance conditions are vesting conditions and that all cancellations, whether Group or counterparty, should be accounted for the same way. Management have determined that this does not have any impact on the financial statements for the Group.

1. Accounting policies continued

a. Basis of preparation continued

1. Interpretations and amendments to published standards effective in 2009 – continued

Amendments to IAS 32 'Financial Instruments: Presentation' and IAS 1 'Presentation of Financial Statements' – Puttable Financial Instruments and Obligations Arising on Liquidation, effective for annual reporting periods beginning on or after 1 January 2009. The amendments require puttable financial instruments or investments that impose on the entity an obligation to another party in respect of a share of net assets only on liquidation to be classified as equity. Management have determined that this has no impact on the financial statements of the Group.

Amendments to IFRIC 9 'Reassessment of Embedded Derivatives' and IAS 39 'Financial Instruments: Recognition and Measurement', effective for annual reporting periods ending on or after 30 June 2009. The amendments clarify the position on embedded derivatives following the earlier amendments to IAS 39 regarding reclassification. The amendment to IFRIC 9 requires an entity to assess whether an embedded derivative must be separated from a host contract when the entity reclassifies a hybrid financial asset out of the fair value through profit or loss category. IAS 39 now states that if an embedded derivative cannot be reliably measured, the entire hybrid instrument must remain classified as at fair value through profit and loss. Management have determined this has no impact on the financial statements of the Group.

'Improvements to Financial Reporting Standards 2008', mostly effective for annual reporting periods beginning on or after 1 January 2009. This is the first standard published under the IASB's annual improvements process which is designed to deal with non-urgent minor amendments to standards. Of the 35 amendments issued, the adoption of the following amendment resulted in a change to accounting policy but did not have any significant impact on the Group's financial position or performance.

Amendments to IAS 38 'Intangible Assets' require expenditure on advertising and promotional activities to be recognised as an expense when the Group either has the right to access the goods or has received the service, rather than when the Group uses the goods or service.

Other amendments did not have any impact on the accounting policies or financial statements of the Group.

In the 2008 accounts the Group early adopted IFRS 8 'Operating Segments', effective for annual reporting periods beginning on or after 1 January 2009.

The standard requires a management approach to reporting segmental information and six reporting segments have been identified under IFRS 8 as detailed in note 2.

IFRIC 13 'Customer Loyalty Programmes', effective for annual reporting periods beginning on or after 1 July 2008. IFRIC 13 explains how entities that grant loyalty award credit to customers should account for their obligations to provide free or discounted goods or services to customers who redeem award credits. As no Group entities operate a customer loyalty programme management have assessed that IFRIC 13 is not relevant to the Group.

IFRIC 15 'Agreements for the Construction of Real Estate', effective for annual reporting periods beginning on or after 1 January 2009. IFRIC 15 addresses the accounting by entities that undertake the construction of real estate with guidance on determining whether an agreement for the construction of real estate falls within the scope of IAS 11 'Construction Contracts' or IAS 18 'Revenue'. As no Group entities undertake the construction of real estate management have assessed that IFRIC 15 is not relevant to the Group.

IFRIC 16 'Hedges of a Net Investment in Foreign Operations', effective for annual reporting periods beginning on or after 1 October 2008. IFRIC 16 provides guidance on net investment hedging including which foreign currency risks within the Group qualify for hedging and where the hedging investments can be held within the Group. Management have assessed that this has no impact on the Group's financial statements.

Notes to the consolidated financial statements continued

1. Accounting policies continued

a. Basis of preparation continued

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 3 (Revised) 'Business Combinations' and amendments to IAS 27 'Consolidated and Separate Financial Statements', effective for annual reporting periods beginning on or after 1 July 2009. The amendments affect the accounting for business combinations, including the requirement to re-measure the fair value of previously held interests in step acquisitions with any gain or loss arising being recognised in the income statement, the requirement to expense acquisition costs and the requirement to recognise adjustments to contingent consideration in the income statement.

Amendments to IAS 39 'Financial Instruments: Recognition and Measurement', effective for annual reporting periods beginning on or after 1 July 2009. These amendments clarify that inflation may only be hedged where changes in inflation are a specified portion of cash flows of a financial instrument, and also clarify hedging with options.

Amendments to IAS 24 'Related Parties', effective for annual reporting periods beginning on or after 1 January 2011. The amendments simplify disclosure for government related entities and clarify the definition of a related party.

Amendments to IFRS 2 'Share-based Payment': Group cash-settled share-based payment transactions, effective for annual reporting periods beginning on or after 1 January 2010. This amendment clarifies the scope and accounting for group cash-settled share-based payment transactions.

Amendments to IAS 32 'Financial Instruments: Presentation' – Classification of Rights, effective for annual reporting periods beginning on or after 1 February 2010. The amendment clarifies that rights, options or warrants issued to a acquire a fixed number of an entity's own non-derivative equity instruments for a fixed amount in any currency are classified as equity instruments provided the offer is made pro-rata to all existing owners of the same class of the entity's own non-derivative equity instruments.

IFRS 9 'Financial Instruments', effective for annual reporting periods beginning on or after 1 January 2013. The new standard details the requirements for the classification and measurement of financial assets.

'Improvements to IFRSs – 2009' effective dates vary upon the amendment. This is the second set of amendments published under the IASB's annual improvements process and incorporates minor amendments to 12 standards and interpretations.

IFRIC 18 'Transfers of Assets from Customers' effective for transfers of assets from customers received on or after 1 July 2009. IFRIC 18 states that when an item of property, plant and equipment is received from a customer and it meets the definition of an asset from the perspective of the recipient, the recipient should recognise the asset at its fair value at the date of transfer and recognise the credit in accordance with IAS 18 'Revenue'.

IFRIC 19 'Extinguishing Financial Liabilities with Equity Instruments', effective for annual reporting periods beginning on or after 1 July 2010. IFRIC 19 clarifies accounting by entities issuing equity instruments to extinguish all or part of a financial liability.

Amendments to IFRIC 14 'Prepayments of a Minimum Funding Requirement,' effective for annual reporting periods beginning on or after 1 January 2011. This amendment remedies a consequence of IFRIC 14 where, in certain circumstances, an entity was not permitted to recognise prepayments of a minimum funding requirement as an asset.

Management are currently assessing the impact of these new standards, interpretations and amendments on the Group's financial statements.

In addition, management has assessed the relevance of the following interpretation with respect to the Group's operations:

1. Accounting policies continued

a. Basis of preparation continued

2. Standards, interpretations and amendments to published standards that are not yet effective – continued

IFRIC 17 'Distributions of Non-cash Assets to Owners', effective for annual reporting periods beginning on or after 1 July 2009. IFRIC 17 provides guidance on the appropriate accounting treatment when an entity distributes assets other than cash as dividends, including recognition upon authorisation and measurement at fair value of assets distributed, with any difference between fair value and carrying value of these assets being recognised in the income statement when an entity settles the dividend payable. This does not apply to distributions of non-cash assets under common control. This interpretation will have no impact on the Group's financial statements as the Group does not currently distribute non-cash assets.

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:

Intangible assets:	Goodwill
Intangible assets:	Pre-publication assets
Royalty advances	
Taxation	
Employee benefits:	Pension obligations
Revenue recognition	

b. Consolidation

1. Business combinations The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Where the settlement of consideration payable is deferred, or contingent on future events, the fair value of the deferred component is determined by discounting the amount payable or probable to be paid to its present value using an appropriate discount rate.

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. For material acquisitions, the fair value of the acquired intangible assets is determined by an external, independent valuer. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. See note 1e(1) for the accounting policy on goodwill.

2. Subsidiaries Subsidiaries are entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group and are de-consolidated from the date that control ceases.

3. Transactions with minority interests Transactions with minority interests are treated as transactions with shareholders. Any surplus or deficit arising from disposals to a minority interest is recorded in equity. For purchases from a minority 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 which are jointly controlled, with one or more other venturers, under a contractual arrangement. 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 cost.

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. 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.

Notes to the consolidated financial statements continued

1. Accounting policies continued

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.

At the date of transition to IFRS the cumulative translation differences in respect of foreign operations have been deemed to be zero.

Any gains and losses on disposals of foreign operations will exclude translation differences that arose prior to the transition date.

The principal overseas currency for the Group is the US dollar. The average rate for the year against sterling was $1.57 (2008: $1.85) and the year end rate was $1.61 (2008: $1.44).

d. Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation. 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 Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary, associate or joint venture at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisitions of associates and joint ventures is included in investments in associates and joint ventures.

Goodwill is tested 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 to sell 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 cash-generating units for the purpose of impairment testing. The allocation is made to those 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.

1. Accounting policies continued

e. Intangible assets continued

1. Goodwill – continued

IFRS 3 'Business Combinations' has not been applied retrospectively to business combinations before the date of transition to IFRS. Subject to the transition adjustments to IFRS required by IFRS 1, the accounting for business combinations before the date of transition has been grandfathered.

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 and relationships, trademarks and brands, publishing rights, content and technology. 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 a depreciation 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 31).

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.

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.

Notes to the consolidated financial statements continued

1. Accounting policies continued

i. Newspaper development costs
Investment in the development of newspaper titles consists of measures to increase the volume and geographical spread of circulation. The measures include additional and enhanced editorial content, extended distribution and remote printing. These costs are expensed as incurred as they do not meet the criteria under IAS 38 'Intangible Assets' to be capitalised as intangible assets.

j. Cash and cash equivalents
Cash and cash equivalents in the cash flow statement include cash in hand, deposits held at 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 as these amounts are used to offset the borrowings of the Group.

k. 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.

l. 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.

m. Derivative financial instruments
Derivatives are recognised at fair value and re-measured 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.

n. 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.

1. Accounting policies continued

n. Taxation continued

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.

o. Employee benefits

1. Pension obligations 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.

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, longevity and expected return on scheme assets.

Actuarial gains and losses arising from differences between actual and expected returns on plan assets, experience adjustments on liabilities and changes in actuarial assumptions are recognised immediately in other comprehensive income.

The service cost, representing benefits accruing over the year, is included in the income statement as an operating cost. The unwinding of the discount rate on the scheme liabilities and the expected return on scheme assets are 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 healthcare 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 material other post-retirement obligations are assessed annually by independent qualified actuaries.

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. The Group has applied IFRS 2 'Share-based Payment' retrospectively to all options granted but not fully vested at the date of transition to IFRS.

p. 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 when the payment of the deferred consideration is probable.

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.

Notes to the consolidated financial statements continued

1. Accounting policies continued

q. Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services net of value-added tax and other 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.

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.

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 with textbooks, revenue is recognised for each element as if it were an individual contractual arrangement.

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 in 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. 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 by the contract.

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.

r. 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.

s. Dividends

Dividends are recorded in the Group's financial statements in the period in which they are approved by the company's shareholders. Interim dividends are recorded in the period in which they are approved and paid.

t. Non-current 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 intended to recover their carrying amount 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 1q).

2. Segment information

The Group is organised into six business segments:

North American Education Educational publishing, assessment and testing for the school and higher education market within the USA and Canada;

International Education Educational publishing, assessment and testing for the school and higher education market outside of North America;

Professional Business and technology publishing and testing and certification for professional bodies;

FT Publishing Publisher of the *Financial Times*, business magazines and specialist information;

Interactive Data Provider of financial and business information to financial institutions and retail investors;

Penguin Publisher with brand imprints such as Penguin, Putnam, Berkley, Viking and Dorling Kindersley.

For more detail on the services and products included in each business segment refer to the business review.

All figures in £ millions	Notes	North American Education	International Education	Professional	FT Publishing	Interactive Data	Penguin	Corporate	Group 2009
Continuing operations									
Sales (external)		2,470	1,035	275	358	484	1,002	–	5,624
Sales (inter-segment)		–	–	7	–	–	24	–	31
Adjusted operating profit		403	141	43	39	148	84	–	858
Amortisation of acquired intangibles		(49)	(32)	(1)	(8)	(12)	(1)	–	(103)
Operating profit		354	109	42	31	136	83	–	755
Finance costs	6								(122)
Finance income	6								27
Profit before tax									660
Income tax	7								(198)
Profit for the year from continuing operations									462
Segment assets		4,382	1,635	377	420	471	1,173	924	9,382
Joint ventures	12	13	–	1	1	–	3	–	18
Associates	12	–	5	–	7	–	–	–	12
Total assets		4,395	1,640	378	428	471	1,176	924	9,412
Other segment items									
Share of results of joint ventures and associates	12	(2)	6	1	25	–	–	–	30
Capital expenditure	10, 11, 20	258	80	20	15	29	46	–	448
Depreciation	10	24	16	10	5	21	9	–	85
Amortisation	11, 20	274	89	13	20	16	42	–	454

Notes to the consolidated financial statements continued

2. Segment information continued

All figures in £ millions	Notes	North American Education	International Education	Professional	FT Publishing	Interactive Data	Penguin	Corporate	Group
									2008
Continuing operations									
Sales (external)		2,002	866	244	390	406	903	–	4,811
Sales (inter-segment)		–	–	4	–	–	22	–	26
Adjusted operating profit		303	135	36	74	121	93	–	762
Amortisation of acquired intangibles		(45)	(22)	(1)	(7)	(9)	(2)	–	(86)
Operating profit		258	113	35	67	112	91	–	676
Finance costs	6								(136)
Finance income	6								45
Profit before tax									585
Income tax	7								(172)
Profit for the year from continuing operations									413
Segment assets		4,952	1,358	423	482	524	1,211	923	9,873
Joint ventures	12	–	8	–	2	–	3	–	13
Associates	12	–	4	–	6	–	–	–	10
Total assets		4,952	1,370	423	490	524	1,214	923	9,896
Other segment items									
Share of results of joint ventures and associates	12	–	5	–	19	–	1	–	25
Capital expenditure	10, 11, 20	224	82	22	17	25	51	–	421
Depreciation	10	25	12	8	13	13	9	–	80
Amortisation	11, 20	219	69	12	12	12	36	–	360

In 2009, sales from the provision of goods were £3,947m (2008: £3,411m) and sales from the provision of services were £1,677m (2008: £1,400m). Sales from the Group's educational publishing, consumer publishing and newspaper business are classified as being from the provision of goods and sales from its assessment and testing, market pricing and other service businesses are classified as being from the provision of services.

2. Segment information continued

Corporate costs are allocated to business segments on an appropriate basis depending on the nature of the cost and therefore the segment result is equal to the Group operating profit. Inter-segment pricing is determined on an arm's-length basis. Segment assets consist of property, plant and equipment, intangible assets, inventories, receivables, retirement benefit assets and deferred taxation 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 intangible assets, including pre-publication but excluding goodwill (see notes 10, 11 and 20).

Property, plant and equipment and intangible assets acquired through business combination were £153m (2008: £253m) (see note 29). Capital expenditure, depreciation and amortisation include amounts relating to discontinued operations. Discontinued operations in 2008 relate to the Data Management business (see note 3).

The Group operates in the following main geographic areas:

	Sales		Non-current assets	
All figures in £ millions	2009	2008	2009	2008
Continuing operations				
UK	748	754	941	701
Other European countries	474	463	242	224
USA	3,462	2,861	3,811	4,624
Canada	201	167	204	209
Asia Pacific	519	415	340	179
Other countries	220	151	121	14
Total continuing	5,624	4,811	5,659	5,951
Discontinued operations				
UK	–	–	–	–
Other European countries	–	–	–	–
USA	–	8	–	–
Canada	–	–	–	–
Asia Pacific	–	–	–	–
Other countries	–	–	–	–
Total discontinued	–	8	–	–
Total	5,624	4,819	5,659	5,951

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. Non-current assets are 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 other receivables.

Notes to the consolidated financial statements continued

3. Discontinued operations

There are no discontinued operations in 2009. Discontinued operations in 2008 relate to the Group's interest in the Data Management business (sold on 22 February 2008).

An analysis of the results and cash flows of the discontinued operation is as follows:

All figures in £ millions	2008 Data Management
Sales	8
Operating profit	–
Profit before tax	–
Attributable tax expense	–
Profit after tax	–
Loss on disposal of discontinued operations before tax	(53)
Attributable tax expense	(37)
Loss for the year from discontinued operations	(90)
Operating cash flows	–
Investing cash flows	–
Financing cash flows	–
Total cash flows	–

4. Operating expenses

All figures in £ millions	2009	2008
By function:		
Cost of goods sold	2,539	2,174
Operating expenses		
Distribution costs	274	235
Administrative and other expenses	2,206	1,853
Other income	(120)	(102)
Total operating expenses	2,360	1,986
Total	4,899	4,160

4. Operating expenses continued

All figures in £ millions	Notes	2009	2008
By nature:			
Utilisation of inventory	21	843	832
Depreciation of property, plant and equipment	10	85	80
Amortisation of intangible assets – Pre-publication	20	307	244
Amortisation of intangible assets – Other	11	147	116
Employee benefit expense	5	1,903	1,553
Operating lease rentals		171	168
Other property costs		87	116
Royalties expensed		497	415
Advertising, promotion and marketing		297	244
Information technology costs		96	76
Other costs		586	418
Other income		(120)	(102)
Total		4,899	4,160

During the year the Group obtained the following services from the Group's auditor:

All figures in £ millions	2009	2008
Fees payable to the company's auditor for the audit of parent company and consolidated financial statements	4	3
The audit of the company's subsidiaries pursuant to legislation	2	2
Tax services	2	2
Other services	1	1
Total	9	8

Reconciliation between audit and non-audit service fees is shown below:

All figures in £ millions	2009	2008
Group audit fees including fees for attestation under section 404 of the Sarbanes-Oxley Act	6	5
Non-audit fees	3	3
Total	9	8

Fees for attestation under section 404 of the Sarbanes-Oxley Act are allocated between fees payable for the audits of consolidated and subsidiary accounts.

Tax services include services related to tax planning and various other tax advisory matters. Other services include due diligence on acquisitions.

Notes to the consolidated financial statements continued

5. Employee information

All figures in £ millions	Notes	2009	2008
Employee benefit expense			
Wages and salaries (including termination benefits and restructuring costs)		1,632	1,317
Social security costs		152	119
Share-based payment costs	26	37	33
Retirement benefits – defined contribution plans	25	62	41
Retirement benefits – defined benefit plans	25	18	37
Other post-retirement benefits	25	2	6
		1,903	1,553

The details of the emoluments of the directors of Pearson plc are shown in the report on directors' remuneration.

Average number employed	2009	2008
Employee numbers		
North American Education	15,606	15,412
International Education	8,899	5,718
Professional	2,662	2,641
FT Publishing	2,328	2,379
Interactive Data	2,459	2,413
Penguin	4,163	4,112
Other	1,047	909
Continuing operations	37,164	33,584
Discontinued operations	–	96
	37,164	33,680

6. Net finance costs

All figures in £ millions	Notes	2009	2008
Interest payable		(92)	(106)
Finance costs in respect of retirement benefits	25	(12)	–
Net foreign exchange losses		(7)	(11)
Other losses on financial instruments in a hedging relationship:			
– fair value hedges		(1)	(7)
Other losses on financial instruments not in a hedging relationship:			
– derivatives		(10)	(12)
Finance costs		(122)	(136)
Interest receivable		7	17
Finance income in respect of retirement benefits	25	–	8
Other gains on financial instruments in a hedging relationship:			
– fair value hedges		4	2
– net investment hedges		–	1
Other gains on financial instruments not in a hedging relationship:			
– amortisation of transitional adjustment on bonds		3	1
– derivatives		13	16
Finance income		27	45
Net finance costs		(95)	(91)
Analysed as:			
Net interest payable		(85)	(89)
Net foreign exchange losses reflected in adjusted earnings		–	(7)
Finance (costs)/income in respect of retirement benefits	25	(12)	8
Net finance costs reflected in adjusted earnings		(97)	(88)
Other net finance income/(costs)		2	(3)
Total net finance costs		(95)	(91)

The £3m net gain (2008: £5m net loss) on fair value hedges comprises a £96m gain (2008: £156m loss) on the underlying bonds offset by a £93m loss (2008: £151m gain) on the related derivative financial instruments.

7. Income tax

All figures in £ millions	Notes	2009	2008
Current tax			
Charge in respect of current year		(156)	(89)
Other adjustments in respect of prior years		9	10
Total current tax charge		(147)	(79)
Deferred tax			
In respect of temporary differences		(55)	(97)
Other adjustments in respect of prior years		4	4
Total deferred tax charge	13	(51)	(93)
Total tax charge		(198)	(172)

Notes to the consolidated financial statements continued

7. Income tax continued

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the UK tax rate as follows:

All figures in £ millions	2009	2008
Profit before tax	660	585
Tax calculated at UK rate (2009: 28%, 2008: 28.5%)	(185)	(167)
Effect of overseas tax rates	(40)	(23)
Joint venture and associate income reported net of tax	8	7
Net income/(expense) not subject to tax	5	(7)
Utilisation of previously unrecognised tax losses	2	4
Unutilised tax losses	(1)	–
Prior year adjustments	13	14
Total tax charge	(198)	(172)
UK	(43)	(53)
Overseas	(155)	(119)
Total tax charge	(198)	(172)
Tax rate reflected in earnings	30.0%	29.4%

The tax rate reflected in adjusted earnings is calculated as follows:

All figures in £ millions	2009	2008
Profit before tax	660	585
Adjustments:		
Amortisation of acquired intangibles	103	86
Other net finance (income)/costs	(2)	3
Adjusted profit before tax – continuing operations	761	674
Adjusted profit before tax – discontinued operations	–	–
Total adjusted profit before tax	761	674
Total tax charge	(198)	(172)
Adjustments:		
Tax benefit on other net gains and losses	–	(7)
Tax benefit on amortisation of acquired intangibles	(37)	(31)
Tax charge/(benefit) on other finance income	1	(1)
Tax amortisation benefit on goodwill and intangibles	40	33
Adjusted income tax charge – continuing operations	(194)	(178)
Adjusted income tax charge – discontinued operations	–	–
Total adjusted income tax charge	(194)	(178)
Tax rate reflected in adjusted earnings	25.5%	26.4%

The tax benefit/(charge) recognised in other comprehensive income is as follows:

All figures in £ millions	2009	2008
Pension contributions and actuarial gains and losses	79	10
Net investment hedges and other foreign exchange gains and losses	12	(1)
	91	9

A tax benefit of £6m (2008: tax charge £7m) 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	2009	2008
Profit for the year from continuing operations		462	413
Minority interest		(37)	(31)
Earnings from continuing operations		425	382
Loss for the year from discontinued operations	3	–	(90)
Earnings		425	292
Weighted average number of shares (millions)		799.3	797.0
Effect of dilutive share options (millions)		0.8	0.5
Weighted average number of shares (millions) for diluted earnings		800.1	797.5
Earnings per share from continuing and discontinued operations			
Basic		53.2p	36.6p
Diluted		53.1p	36.6p
Earnings per share from continuing operations			
Basic		53.2p	47.9p
Diluted		53.1p	47.9p
Earnings per share from discontinued operations			
Basic		–	(11.3p)

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.

The following items are excluded in the calculation of adjusted earnings:

Other net gains and losses represent profits and losses on the sale 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 of acquired intangibles is the amortisation of intangible assets acquired through business combinations. The amortisation charge is not considered to be fully reflective of the underlying performance of the Group.

Notes to the consolidated financial statements continued

8. Earnings per share continued

Other net finance income/costs are foreign exchange and other gains and losses that represent short-term fluctuations in market value and foreign exchange movements on transactions and balances that are no longer in a hedge relationship. These gains and losses are subject to significant volatility and may not be realised in due course as it is normally the intention to hold these 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. The Group also adds the benefit of tax amortisation of goodwill and intangibles as this benefit more accurately aligns the adjusted tax charge with the expected medium-term rate of cash tax payments.

Minority interest for the above items is excluded from adjusted earnings.

The following tables reconcile statutory earnings to adjusted earnings.

						2009
All figures in £ millions	Statutory income statement	Other net gains and losses	Amortisation of acquired intangibles	Other net finance income/costs	Tax amortisation benefit	Adjusted income statement
Operating profit	755	–	103	–	–	858
Net finance costs	(95)	–	–	(2)	–	(97)
Profit before tax	660	–	103	(2)	–	761
Income tax	(198)	–	(37)	1	40	(194)
Profit for the year from continuing operations	462	–	66	(1)	40	567
Profit for the year from discontinued operations	–	–	–	–	–	–
Profit for the year	462	–	66	(1)	40	567
Minority interest	(37)	–	(5)	–	(2)	(44)
Earnings	425	–	61	(1)	38	523
Weighted average number of shares (millions)						799.3
Adjusted earnings per share						65.4p

8. Earnings per share continued

All figures in £ millions	Statutory income statement	Other net gains and losses	Amortisation of acquired intangibles	Other net finance income/costs	Tax amortisation benefit	Adjusted income statement
						2008
Operating profit	676	–	86	–	–	762
Net finance costs	(91)	–	–	3	–	(88)
Profit before tax	585	–	86	3	–	674
Income tax	(172)	(7)	(31)	(1)	33	(178)
Profit for the year from continuing operations	413	(7)	55	2	33	496
Loss for the year from discontinued operations	(90)	90	–	–	–	–
Profit for the year	323	83	55	2	33	496
Minority interest	(31)	–	(3)	–	(2)	(36)
Earnings	292	83	52	2	31	460
Weighted average number of shares (millions)						797.0
Adjusted earnings per share						57.7p

9. Dividends

All figures in £ millions	2009	2008
Final paid in respect of prior year 22.0p (2008: 20.5p)	176	163
Interim paid in respect of current year 12.2p (2008: 11.8p)	97	94
	273	257

The directors are proposing a final dividend in respect of the financial year ended 31 December 2009 of 23.3p per share which will absorb an estimated £187m of shareholders' funds. It will be paid on 7 May 2010 to shareholders who are on the register of members on 9 April 2010. These financial statements do not reflect this dividend.

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
Cost				
At 1 January 2008	298	622	16	936
Exchange differences	54	138	6	198
Additions	6	67	6	79
Disposals	(7)	(38)	–	(45)
Acquisition through business combination	2	29	2	33
Reclassifications	2	21	(23)	–
At 31 December 2008	355	839	7	1,201
Exchange differences	(21)	(55)	(1)	(77)
Additions	14	46	7	67
Disposals	(2)	(41)	–	(43)
Acquisition through business combination	1	17	–	18
Reclassifications	1	5	(6)	–
At 31 December 2009	348	811	7	1,166

All figures in £ millions	Land and buildings	Plant and equipment	Assets in course of construction	Total
Depreciation				
At 1 January 2008	(126)	(455)	–	(581)
Exchange differences	(30)	(102)	–	(132)
Charge for the year	(19)	(61)	–	(80)
Disposals	6	36	–	42
Acquisition through business combination	(1)	(26)	–	(27)
At 31 December 2008	(170)	(608)	–	(778)
Exchange differences	11	42	–	53
Charge for the year	(17)	(68)	–	(85)
Disposals	2	39	–	41
Acquisition through business combination	–	(9)	–	(9)
At 31 December 2009	(174)	(604)	–	(778)
Carrying amounts				
At 1 January 2008	172	167	16	355
At 31 December 2008	185	231	7	423
At 31 December 2009	174	207	7	388

Depreciation expense of £12m (2008: £12m) has been included in the income statement in cost of goods sold, £7m (2008: £6m) in distribution expenses and £66m (2008: £61m) in administrative and other expenses. 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 £15m (2008: £7m).

11. Intangible assets

All figures in £ millions	Goodwill	Software	Acquired customer lists and relationships	Acquired trademarks and brands	Acquired publishing rights	Other intangibles acquired	Total
Cost							
At 1 January 2008	3,343	217	187	62	136	99	4,044
Exchange differences	1,082	71	77	24	31	62	1,347
Additions – internal development	–	29	–	–	–	–	29
Additions – purchased	–	16	–	–	–	–	16
Disposals	(8)	(27)	–	–	–	–	(35)
Acquisition through business combination	153	17	77	42	–	97	386
Disposal through business disposal	–	(1)	–	–	(2)	–	(3)
Transfer to Pre-publication	–	(12)	–	–	–	–	(12)
At 31 December 2008	4,570	310	341	128	165	258	5,772
Exchange differences	(420)	(25)	(32)	(9)	(5)	(22)	(513)
Additions – internal development	–	35	–	–	–	–	35
Additions – purchased	–	24	–	–	–	–	24
Disposals	(9)	(5)	–	–	–	–	(14)
Acquisition through business combination	205	–	38	24	55	25	347
At 31 December 2009	4,346	339	347	143	215	261	5,651

Notes to the consolidated financial statements continued

11. Intangible assets continued

All figures in £ millions	Goodwill	Software	Acquired customer lists and relationships	Acquired trademarks and brands	Acquired publishing rights	Other intangibles acquired	Total
Amortisation							
At 1 January 2008	–	(142)	(28)	(4)	(32)	(24)	(230)
Exchange differences	–	(50)	(15)	(3)	(13)	(12)	(93)
Charge for the year	–	(30)	(24)	(10)	(25)	(27)	(116)
Disposals	–	27	–	–	–	–	27
Acquisition through business combination	–	(13)	–	–	–	–	(13)
Disposal through business disposal	–	1	–	–	1	–	2
Transfer to Pre-publication	–	4	–	–	–	–	4
At 31 December 2008	–	(203)	(67)	(17)	(69)	(63)	(419)
Exchange differences	–	19	6	1	6	8	40
Charge for the year	–	(44)	(35)	(11)	(22)	(35)	(147)
Disposals	–	4	–	–	–	–	4
At 31 December 2009	–	(224)	(96)	(27)	(85)	(90)	(522)
Carrying amounts							
At 1 January 2008	3,343	75	159	58	104	75	3,814
At 31 December 2008	4,570	107	274	111	96	195	5,353
At 31 December 2009	4,346	115	251	116	130	171	5,129

Goodwill

The goodwill carrying value of £4,346m 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. £3,127m of the carrying value relates to acquisitions completed between 1 January 1998 and 31 December 2002 and £1,219m relates to acquisitions completed after 1 January 2003 (the date of transition to IFRS).

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, with only the remaining difference between the purchase price and the fair value of net assets acquired being allocated to goodwill.

Other intangible assets

Other intangibles acquired include content, technology and software rights. Amortisation of £5m (2008: £5m) is included in the income statement in cost of goods sold and £142m (2008: £111m) in administrative and other expenses.

11. Intangible assets continued

Impairment tests for cash-generating units containing goodwill

Impairment tests have been carried out where appropriate as described below. The recoverable amount for each unit tested exceeds its carrying value.

Goodwill is allocated to 14 cash-generating units (CGUs) within the business segments as follows:

All figures in £ millions	2009	2008
US School Curriculum	812	937
US School Assessment and Information	652	722
US Higher Education	1,064	1,164
Canada	181	173
International Education Publishing	468	315
International Education Assessment and Testing	222	241
Professional Publishing	13	15
Professional Assessment and Testing	226	254
Pearson Education total	3,638	3,821
Financial Times	43	46
Mergermarket	125	130
Interactive Data	184	208
FT Group total	352	384
Penguin US	190	216
Penguin UK	103	95
Pearson Australia	63	54
Penguin total	356	365
Total goodwill	4,346	4,570

As highlighted in the 2008 business review, integration of the US School and Higher Education businesses began in 2008. This integration continued throughout 2009 and has now advanced to a point where, from 1 January 2010, these companies will be combined into one CGU for impairment review purposes.

The recoverable amount of each CGU is based on value in use calculations. Goodwill is tested for impairment annually. 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.

Key assumptions

The value in use calculations use cash flow projections based on financial budgets approved by management covering a five-year period. The key assumptions used by management in the value in use calculations were:

Discount rate 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 pre-tax discount rates used are in the range of 10.9% to 11.8% for the Pearson Education businesses (2008: 10.2% to 11.7%), 12.7% to 18.1% for the FT Group businesses (2008: 10.8% to 20.5%) and 9.5% to 11.4% for the Penguin businesses (2008: 8.8% to 10.4%).

Perpetuity growth rates The cash flows subsequent to the approved budget period are based upon the long-term historic growth rates of the underlying territories in which the CGU operates and reflect the long-term growth prospects of the sectors in which the CGU operates. A perpetuity growth rate of 2.0% was used for all CGUs in 2009 (2008: 2.0%). The perpetuity growth rates are consistent with appropriate external sources for the relevant markets.

Notes to the consolidated financial statements continued

11. Intangible assets continued

Cash flow growth rates The cash flow growth rates are derived from management's latest forecast of sales taking into consideration past experience of operating margins achieved in the CGU. Historically, such forecasts have been reasonably accurate.

Sensitivities

The Group's impairment review is sensitive to a change in assumptions used, most notably the discount rates, the perpetuity growth rates and expected future cash flows. Based on the Group's sensitivity analysis, a reasonably possible change in the discount rate or perpetuity growth rate could cause an impairment in the US School Curriculum CGU. Following a restructuring during 2009, the Penguin UK CGU is no longer considered sensitive to impairment.

The fair value of US School Curriculum is 6%, or approximately £59m, above its carrying value, but an increase of 0.4 percentage points in the discount rate or a reduction of 0.5 percentage points in the perpetuity growth rate would have caused the value in use to fall below the carrying value.

12. Investments in joint ventures and associates

Joint ventures

All figures in £ millions	2009	2008
At beginning of year	13	11
Exchange differences	–	(4)
Share of profit after tax	4	6
Dividends	(3)	(5)
Loan repayment	(3)	–
Additions and further investment	13	5
Transfer to subsidiary	(6)	–
At end of year	18	13

Investments in joint ventures are accounted for using the equity method of accounting and are initially recognised at cost. Investments at 31 December 2009 include goodwill of £11m (2008: £nil).

The aggregate of the Group's share of its joint ventures' assets (including goodwill) and liabilities, none of which are individually significant, are as follows:

All figures in £ millions	2009	2008
Assets		
Non-current assets	15	6
Current assets	11	21
Liabilities		
Current liabilities	(8)	(14)
Net assets	18	13
Income	12	36
Expenses	(8)	(30)
Profit after income tax	4	6

12. Investments in joint ventures and associates continued

Associates

All figures in £ millions	2009	2008
At beginning of year	10	9
Exchange differences	4	(5)
Share of profit after tax	26	19
Dividends	(19)	(16)
Additions	1	–
(Reversal of distribution)/Distribution from associate in excess of carrying value	(7)	6
Actuarial losses on retirement benefit obligations	(3)	(3)
At end of year	12	10

Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost. There is no acquisition goodwill relating to the Group's investments in associates.

The Group's interests in its principal associates, all of which are unlisted, are as follows:

2009 All figures in £ millions	Country of incorporation	% interest held	Assets	Liabilities	Revenues	Profit
The Economist Newspaper Ltd	England	50	116	(116)	161	22
Other			42	(30)	50	4
Total			158	(146)	211	26

2008 All figures in £ millions	Country of incorporation	% interest held	Assets	Liabilities	Revenues	Profit
The Economist Newspaper Ltd	England	50	86	(86)	149	16
Other			35	(25)	42	3
Total			121	(111)	191	19

The interests held in associates are equivalent to voting rights.

Notes to the consolidated financial statements continued

13. Deferred income tax

All figures in £ millions	2009	2008
Deferred income tax assets		
Deferred income tax assets to be recovered after more than 12 months	374	341
Deferred income tax assets to be recovered within 12 months	13	31
	387	372
Deferred income tax liabilities		
Deferred income tax liabilities to be settled after more than 12 months	(473)	(447)
Deferred income tax liabilities to be settled within 12 months	–	–
	(473)	(447)
Net deferred income tax	(86)	(75)

Deferred income tax assets to be recovered within 12 months relate to the utilisation of losses in the US.

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. The Group has unrecognised deferred income tax assets at 31 December 2009 in respect of UK losses of £20m (2008: £28m). None of these unrecognised deferred income tax assets have expiry dates associated with them.

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	2009	2008
At beginning of year		(75)	41
Exchange differences		10	(12)
Income statement charge	7	(51)	(93)
Acquisition through business combination	29	(45)	(4)
Tax benefit/(charge) to other comprehensive income or equity		75	(7)
At end of year		(86)	(75)

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	Goodwill and intangibles	Returns provisions	Retirement benefit obligations	Other	Total
Deferred income tax assets						
At 1 January 2008	87	20	79	10	132	328
Exchange differences	19	6	28	2	38	93
Acquisition through business combination	2	–	–	–	–	2
Income statement (charge)/benefit	(35)	(6)	(1)	(8)	5	(45)
Tax benefit/(charge) to other comprehensive income or equity	–	–	–	3	(9)	(6)
At 31 December 2008	73	20	106	7	166	372
Exchange differences	(5)	(2)	(10)	(1)	(17)	(35)
Acquisition through business combination	–	–	–	–	–	–
Income statement (charge)/benefit	(46)	(7)	(4)	(6)	42	(21)
Tax benefit to other comprehensive income or equity	–	–	–	68	3	71
At 31 December 2009	22	11	92	68	194	387

Other deferred income tax assets include temporary differences on share-based payments, inventory and other provisions.

All figures in £ millions	Goodwill and intangibles	Other	Total
Deferred income tax liabilities			
At 1 January 2008	(214)	(73)	(287)
Exchange differences	(73)	(32)	(105)
Acquisition through business combination	(5)	(1)	(6)
Income statement charge	(26)	(22)	(48)
Tax charge to other comprehensive income or equity	–	(1)	(1)
At 31 December 2008	(318)	(129)	(447)
Exchange differences	30	15	45
Acquisition through business combination	(41)	(4)	(45)
Income statement (charge)/benefit	10	(40)	(30)
Tax benefit to other comprehensive income or equity	–	4	4
At 31 December 2009	(319)	(154)	(473)

Other deferred income tax liabilities include temporary differences in respect of depreciation and royalty advances.

Notes to the consolidated financial statements continued

14. Classification of financial instruments

The accounting classification of each class of the Group's financial assets and financial liabilities, together with their fair values, is as follows:

		2009							
		Fair value				Amortised cost			
All figures in £ millions	Notes	Available for sale	Derivatives deemed held for trading	Derivatives in hedging relationships	Other liabilities	Loans and receivables	Other liabilities	Total carrying value	Total market value
Investments in unlisted securities	15	62	–	–	–	–	–	62	62
Cash and cash equivalents	17	–	–	–	–	750	–	750	750
Marketable securities		63	–	–	–	–	–	63	63
Derivative financial instruments	16	–	42	70	–	–	–	112	112
Trade receivables	22	–	–	–	–	989	–	989	989
Total financial assets		125	42	70	–	1,739	–	1,976	1,976
Derivative financial instruments	16	–	(9)	–	–	–	–	(9)	(9)
Trade payables	24	–	–	–	–	–	(461)	(461)	(461)
Other financial liabilities – put option over minority interest	24	–	–	–	(23)	–	–	(23)	(23)
Bank loans and overdrafts	18	–	–	–	–	–	(70)	(70)	(70)
Borrowings due within one year	18	–	–	–	–	–	(4)	(4)	(4)
Borrowings due after more than one year	18	–	–	–	–	–	(1,934)	(1,934)	(1,969)
Total financial liabilities		–	(9)	–	(23)	–	(2,469)	(2,501)	(2,536)

14. Classification of financial instruments continued

All figures in £ millions	Notes	Fair value: Available for sale	Fair value: Derivatives deemed held for trading	Fair value: Derivatives in hedging relationships	Amortised cost: Loans and receivables	Amortised cost: Other liabilities	Total carrying value	Total market value
								2008
Investments in unlisted securities	15	63	–	–	–	–	63	63
Cash and cash equivalents	17	–	–	–	685	–	685	685
Marketable securities		54	–	–	–		54	54
Derivative financial instruments	16	–	23	161	–	–	184	184
Trade receivables	22	–	–	–	1,030	–	1,030	1,030
Total financial assets		117	23	161	1,715	–	2,016	2,016
Derivative financial instruments	16	–	(20)	–	–	–	(20)	(20)
Trade payables	24	–	–	–	–	(450)	(450)	(450)
Bank loans and overdrafts	18	–	–	–	–	(228)	(228)	(228)
Borrowings due within one year	18	–	–	–	–	(248)	(248)	(247)
Borrowings due after more than one year	18	–	–	–	–	(1,887)	(1,887)	(1,620)
Total financial liabilities		–	(20)	–	–	(2,813)	(2,833)	(2,565)

Certain of the Group's derivative financial instruments are deemed to be held for trading either as they do not meet the hedge accounting criteria specified in IAS 39 'Financial Instruments: Recognition and Measurement' or the Group has chosen not to seek hedge accounting for these instruments. None of these derivatives are held for speculative trading purposes. Transactions in derivative financial instruments are only undertaken to manage risks arising from underlying business activity, in accordance with the Group's treasury policy as described in note 19.

The Group designates certain qualifying derivative financial instruments as hedges of the fair value of its bonds (fair value hedges). Changes in the fair value of these derivative financial instruments are recorded in the income statement, together with any change in the fair value of the hedged liability attributable to the hedged risk.

The Group also designates certain of its borrowings and derivative financial instruments as hedges of its investments in foreign operations (net investment hedges). Movements in the fair value of these financial instruments (to the extent they are effective) are recognised in other comprehensive income.

None of the Group's financial assets or liabilities are designated at fair value through the income statement upon initial recognition.

More detail on the Group's accounting for financial instruments is included in the Group's accounting policies. The Group's approach to managing risks in relation to financial instruments is described in note 19.

Notes to the consolidated financial statements continued

15. Other financial assets

All figures in £ millions	2009	2008
At beginning of year	63	52
Exchange differences	(6)	18
Acquisition of investments	10	1
Disposal of investments	(5)	(8)
At end of year	62	63

Other financial assets comprise non-current unlisted securities.

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:

	2009			2008		
All figures in £ millions	Gross notional amounts	Assets	Liabilities	Gross notional amounts	Assets	Liabilities
Interest rate derivatives – in a fair value hedge relationship	1,103	70	–	1,232	161	–
Interest rate derivatives – not in a hedge relationship	486	13	(7)	1,033	23	(20)
Cross currency rate derivatives – in a net investment hedge relationship	220	29	(2)	–	–	–
Total	1,809	112	(9)	2,265	184	(20)
Analysed as expiring:						
In less than one year	238	–	(7)	487	3	(5)
Later than one year and not later than five years	844	60	(2)	859	47	(15)
Later than five years	727	52	–	919	134	–
Total	1,809	112	(9)	2,265	184	(20)

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 2009, 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 £(127)m, sterling £252m and South African rand £(22)m (2008: US dollar £161m, sterling £3m and South African rand £nil).

The fixed interest rates on outstanding rate derivative contracts at the end of 2009 range from 3.65% to 9.28% (2008: 4.45% to 7.00%) and the floating rates are based on LIBOR in US dollar 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.

16. Derivative financial instruments continued

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	2009	2008
Cash at bank and in hand	580	528
Short-term bank deposits	170	157
	750	685

Short-term bank deposits are invested with banks and earn interest at the prevailing short-term deposit rates.

At the end of 2009 the currency split of cash and cash equivalents was US dollar 35% (2008: 36%), sterling 22% (2008: 22%), euro 18% (2008: 20%) and other 25% (2008: 22%).

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	2009	2008
Cash and cash equivalents	750	685
Bank overdrafts	(70)	(96)
	680	589

Notes to the consolidated financial statements continued

18. Financial liabilities – Borrowings

The Group's current and non-current borrowings are as follows:

All figures in £ millions	2009	2008
Non-current		
Bank loans and overdrafts	–	132
7.0% Global Dollar Bonds 2011 (nominal amount $500m)	322	368
5.5% Global Dollar Bonds 2013 (nominal amount $350m)	226	258
5.7% US Dollar Bonds 2014 (nominal amount $400m)	274	322
7.0% Sterling Bonds 2014 (nominal amount £250m)	254	254
6.0% Sterling Bonds 2015 (nominal amount £300m)	297	–
6.25% Global Dollar Bonds 2018 (nominal amount $550m)	359	445
4.625% US Dollar notes 2018 (nominal amount $300m)	191	237
Finance lease liabilities	11	3
	1,934	2,019
Current		
Due within one year or on demand:		
Bank loans and overdrafts	70	96
4.7% US Dollar Bonds 2009 (nominal amount $350m)	–	244
Finance lease liabilities	4	4
	74	344
Total borrowings	2,008	2,363

Included in the non-current borrowings above is £12m of accrued interest (2008: £12m). Included in the current borrowings above is £nil of accrued interest (2008: £1m).

The maturity of the Group's non-current borrowing is as follows:

All figures in £ millions	2009	2008
Between one and two years	327	2
Between two and five years	760	759
Over five years	847	1,258
	1,934	2,019

18. Financial liabilities – Borrowings continued

The carrying amounts and market values of borrowings are as follows:

All figures in £ millions	Effective interest rate	2009 Carrying value	2009 Market value	2008 Carrying value	2008 Market value
Bank loans and overdrafts	n/a	70	70	228	228
4.7% US Dollar Bonds 2009	4.86%	–	–	244	243
7.0% Global Dollar Bonds 2011	7.16%	322	331	368	349
5.5% Global Dollar Bonds 2013	5.76%	226	232	258	227
5.7% US Dollar Bonds 2014	5.88%	274	266	322	262
7.0% Sterling Bonds 2014	7.20%	254	276	254	258
6.0% Sterling Bonds 2015	6.27%	297	317	–	–
6.25% Global Dollar Bonds 2018	6.46%	359	360	445	352
4.625% US Dollar notes 2018	4.69%	191	176	237	169
Finance lease liabilities	n/a	15	15	7	7
		2,008	2,043	2,363	2,095

The market values 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	2009	2008
US dollar	1,457	2,081
Sterling	551	277
Euro	–	5
	2,008	2,363

The Group has the following undrawn capacity on its committed borrowing facilities as at 31 December:

All figures in £ millions	2009	2008
Floating rate		
– expiring within one year	–	–
– expiring beyond one year	1,084	1,085
	1,084	1,085

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.

Notes to the consolidated financial statements continued

18. Financial liabilities – Borrowings continued

The maturity of the Group's finance lease obligations is as follows:

All figures in £ millions	2009	2008
Finance lease liabilities – minimum lease payments		
Not later than one year	4	4
Later than one year and not later than two years	5	2
Later than two years and not later than three years	3	1
Later than three years and not later than four years	3	–
Later than four years and not later than five years	–	–
Later than five years	–	–
Future finance charges on finance leases	–	–
Present value of finance lease liabilities	15	7

The present value of finance lease liabilities is as follows:

All figures in £ millions	2009	2008
Not later than one year	4	4
Later than one year and not later than five years	11	3
Later than five years	–	–
	15	7

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 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 and sterling, at both floating and fixed rates of interest, using derivative financial instruments ('derivatives), where appropriate, to generate the desired effective 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 below. All the treasury policies remained unchanged throughout 2009, apart from a revision to the Group's bank counterparty limits policy and a minor change applicable to the authorisation of treasury policy waivers.

The audit committee receives 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.

19. Financial risk management continued

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'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 'Financial Instruments: Recognition and Measurement') 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 2009 the fixed to floating hedging ratio, on the above basis, was approximately 71%. This above-policy level was a result of better than forecast cash collections in December 2009, resulting in lower than expected net debt. A simultaneous 1% change on 1 January 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.

Use of interest rate derivatives

The policy described in the section above creates a group of derivatives, under which the Group is a payer of fixed rates and a receiver of floating rates. 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 second group of derivatives, under which the Group is a receiver of fixed rates and a payer of floating rates. The Group's accounting objective in 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 sharply 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.

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 has been that 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) should be between three and ten years. At the end of 2009 the average maturity of gross borrowings was 5.1 years of which bonds represented 96% of these borrowings (up from 5.0 years and up from 90% respectively at the beginning of the year).

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. All of the Group's credit ratings remained unchanged during the year. The long-term ratings are Baa1 from Moody's and BBB+ from Standard & Poor's, and the short-term ratings are P2 and A2 respectively. The Group's policy is to strive to maintain a rating of Baa1/BBB+ over the long term. The Group will also continue to use internally a range of ratios to monitor and manage its finances. 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 2009 the committed facilities amounted to £1,084m and their weighted average maturity was 2.4 years.

Notes to the consolidated financial statements continued

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	2009	2008
Cash and cash equivalents	750	685
Marketable securities	63	54
Derivative financial instruments	103	164
Bank loans, overdrafts and loan notes	(70)	(228)
Bonds	(1,923)	(2,128)
Finance lease liabilities	(15)	(7)
Net debt	(1,092)	(1,460)

The split of net debt between fixed and floating rate, stated after the impact of rate derivatives, is as follows:

All figures in £ millions	2009	2008
Fixed rate	772	781
Floating rate	320	679
Total	1,092	1,460

Gross borrowings, after the impact of cross-currency rate derivatives, analysed by currency are as follows:

All figures in £ millions	2009	2008
US dollar	1,656	2,081
Sterling	330	277
Other	22	5
Total	2,008	2,363

As at 31 December 2009 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	74	1,087	847	2,008
Effect of rate derivatives	1,289	(762)	(527)	–
Total	1,363	325	320	2,008

19. Financial risk management continued

The maturity of contracted cash flows on the Group's borrowings and all of its derivative financial instruments are as follows:

				2009
All figures in £ millions	USD	GBP	Other	Total
Not later than one year	42	21	2	65
Later than one year and not later than five years	878	313	30	1,221
Later than five years	739	106	–	845
Total	1,659	440	32	2,131
Analysed as:				
Revolving credit facilities and commercial paper	–	–	–	–
Bonds	1,692	745	–	2,437
Rate derivatives – inflows	(386)	(313)	–	(699)
Rate derivatives – outflows	353	8	32	393
Total	1,659	440	32	2,131

				2008
All figures in £ millions	USD	GBP	Other	Total
Not later than one year	311	17	–	328
Later than one year and not later than five years	884	65	–	949
Later than five years	954	266	–	1,220
Total	2,149	348	–	2,497
Analysed as:				
Revolving credit facilities and commercial paper	141	–	–	141
Bonds	2,237	355	–	2,592
Rate derivatives – inflows	(392)	(21)	–	(413)
Rate derivatives – outflows	163	14	–	177
Total	2,149	348	–	2,497

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.

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.

Financial counterparty risk management

Counterparty credit limits, which take published credit rating and other factors into account, are set to cover our 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.

Notes to the consolidated financial statements continued

19. Financial risk management continued

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 dampen 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. Our 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 £1,314m, sterling £168m and South African rand £9m.

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.

Financial instruments – fair value measurement

The following table provides an analysis of those financial instruments that are measured subsequent 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).

				2009
All figures in £ millions	Level 1	Level 2	Level 3	Total
Financial assets at fair value				
Derivative financial assets	–	112	–	112
Marketable securities	–	63	–	63
Available for sale financial assets				
Investments in unlisted securities	–	–	62	62
Financial liabilities at fair value				
Derivative financial liabilities	–	(9)	–	(9)
Other financial liabilities – put option over minority interest	–	–	(23)	(23)
Total	–	166	39	205

19. Financial risk management continued

The following table analyses the movements in level 3 fair value measurements:

	2009	
All figures in £ millions	Investments in unlisted securities	Other financial liabilities
At beginning of year	63	–
Exchange differences	(6)	–
Additions	10	(23)
Disposals	(5)	–
At end of year	62	(23)

The fair value of the 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. The fair value of other financial liabilities represents the present value of the estimated future liability.

Financial instruments – sensitivity analysis

As at 31 December 2009 the sensitivity 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 unlisted securities	62	–	–	(2)	3
Cash and cash equivalents	750	–	–	(47)	58
Marketable securities	63	–	–	(5)	7
Derivative financial instruments	103	(59)	66	14	(17)
Bonds	(1,923)	54	(61)	118	(144)
Other borrowings	(85)	–	–	8	(9)
Put option over minority interest	(23)	–	–	3	(3)
Other net financial assets	528	–	–	(42)	52
Total financial instruments	(525)	(5)	5	47	(53)

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 assets less trade liabilities.

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, depending on the location and functional currency of the entity 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.

Notes to the consolidated financial statements continued

20. Intangible assets – Pre-publication

All figures in £ millions	2009	2008
Cost		
At beginning of year	1,800	1,264
Exchange differences	(160)	494
Additions	322	297
Disposals	(230)	(345)
Acquisition through business combination	(1)	78
Transfer from software	–	12
Transfer to inventories	(4)	–
At end of year	1,727	1,800
Amortisation		
At beginning of year	(1,105)	(814)
Exchange differences	102	(337)
Charge for the year	(307)	(244)
Disposals	230	345
Acquisition through business combination	3	(51)
Transfer from software	–	(4)
At end of year	(1,077)	(1,105)
Carrying amounts		
At end of year	650	695

Included in the above are pre-publication assets amounting to £398m (2008: £462m) which will be realised in more than 12 months.

Amortisation is included in the income statement in cost of goods sold.

21. Inventories

All figures in £ millions	2009	2008
Raw materials	32	31
Work in progress	23	29
Finished goods	390	441
	445	501

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 £843m (2008: £832m). In 2009 £75m (2008: £56m) of inventory provisions was charged in the income statement. None of the inventory is pledged as security.

22. Trade and other receivables

All figures in £ millions	2009	2008
Current		
Trade receivables	989	1,030
Royalty advances	99	111
Prepayments and accrued income	75	62
Other receivables	121	135
Receivables from related parties	–	4
	1,284	1,342
Non-current		
Royalty advances	86	102
Prepayments and accrued income	24	3
Other receivables	2	47
	112	152

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	2009	2008
At beginning of year	(72)	(52)
Exchange differences	5	(18)
Income statement movements	(26)	(27)
Utilised	20	27
Acquisition through business combination	(3)	(2)
At end of year	(76)	(72)

Concentrations of credit risk with respect to trade receivables are limited due to the Group's large number of customers, who are internationally dispersed.

Notes to the consolidated financial statements continued

22. Trade and other receivables continued

The ageing of the Group's trade receivables is as follows:

All figures in £ millions	2009	2008
Within due date	1,096	1,110
Up to three months past due date	228	248
Three to six months past due date	51	60
Six to nine months past due date	20	21
Nine to 12 months past due date	4	15
More than 12 months past due date	20	20
Total trade receivables	1,419	1,474
Less: provision for bad and doubtful debts	(76)	(72)
Less: provision for sales returns	(354)	(372)
Net trade receivables	989	1,030

The Group reviews its bad debt provision at least twice a year following a detailed review of receivable balances and historic payment profiles. Management believe all the remaining receivable balances are fully recoverable.

23. Provisions for other liabilities and charges

All figures in £ millions	Deferred consideration	Leases	Other	Total
At 1 January 2009	43	8	38	89
Exchange differences	(2)	–	(3)	(5)
Charged to income statement	3	3	2	8
Released to income statement	–	–	(3)	(3)
Acquisition through business combination – current year	27	–	–	27
Acquisition through business combination – prior year adjustments	(4)	–	–	(4)
Utilised	(29)	(2)	(13)	(44)
At 31 December 2009	38	9	21	68

All figures in £ millions	2009	2008
Analysis of provisions		
Non-current	50	33
Current	18	56
	68	89

Deferred consideration primarily relates to the acquisition of Fronter in 2009.

24. Trade and other liabilities

All figures in £ millions	2009	2008
Trade payables	461	450
Social security and other taxes	30	35
Accruals	504	501
Deferred income	487	444
Interest payable	10	10
Dividends payable to minority interest	–	5
Put option over minority interest	23	–
Other liabilities	205	205
	1,720	1,650
Less: non-current portion		
Accruals	23	42
Deferred income	116	87
Interest payable	–	1
Put option over minority interest	23	–
Other liabilities	91	91
	253	221
Current portion	1,467	1,429

The carrying value of the Group's payables approximates its fair value.

The deferred income balances comprise:

multi-year obligations to deliver workbooks to adoption customers in school businesses;
advance payments in assessment and testing businesses;
subscription income in school, newspaper and market pricing businesses;
advertising income relating to future publishing days in newspaper businesses; and
obligations to deliver digital content in future periods.

The put option over minority interest is the fair value of an option held by the minority interest in our Pearson South Africa business. The option enables the minority interest to sell their 15% share of Pearson South Africa to Pearson from 1 January 2012 at a price determined by the future performance of that business.

Notes to the consolidated financial statements continued

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. For the defined benefit plans, benefits are based on employees' length of service and final pensionable pay. Defined contribution benefits are based on the amount of contributions paid in respect of an individual member, the investment returns earned and the amount of pension this money will buy when a member retires.

The largest plan is the Pearson Group Pension Plan ('UK Group plan') with both defined benefit and defined contribution sections. From 1 November 2006, all sections of the UK Group plan were closed to new members with the exception of a defined contribution section that was opened in 2003. This section is available to all new employees of participating companies. The other major defined benefit plans are based in the US.

Other defined contribution plans are operated principally overseas with the largest plan being in the US. The specific features of these plans vary in accordance with the regulations of the country in which employees are located.

Pearson 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.

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.

	2009			2008		
%	UK Group plan	Other plans	PRMB	UK Group plan	Other plans	PRMB
Inflation	3.50	2.50	2.50	2.80	2.80	2.80
Rate used to discount plan liabilities	5.70	5.25	5.50	6.40	6.25	6.25
Expected return on assets	6.03	6.75	–	6.33	7.60	–
Expected rate of increase in salaries	5.00	4.00	–	4.30	4.50	–
Expected rate of increase for pensions in payment and deferred pensions	2.60 to 4.40	–	–	2.30 to 4.20	–	–
Initial rate of increase in healthcare rate	–	–	8.50	–	–	9.00
Ultimate rate of increase in healthcare rate	–	–	5.00	–	–	5.00

The UK discount rate is based on the annualised yield on the iBoxx over 15-year AA-rated corporate bond index, adjusted to reflect the duration of our liabilities. The US discount rate is set by reference to a US bond portfolio matching model. The expected return on assets is based on market expectations of long-term asset returns for the defined portfolio at the end of the year.

The expected rates of return on categories of plan assets are determined by reference to relevant indices. The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the plan's investment portfolio.

The expected rate of increase in salaries has been set at 5.0% for 2009 with a short-term assumption of 3.0% for three years.

In 2008 the UK mortality assumptions were derived by adjusting standard mortality tables (PMFA 92 tables projected forward with medium cohort improvement factors). In 2009 the Group changed its mortality assumptions in the UK. 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 medium cohort improvement factors. In 2008 a 1% improvement floor on the medium cohort was applied. In 2009 this was changed to 1.5% for males and 1.25% for females, with tapering.

For the US plans, the assumptions used were based on standard US mortality tables. In 2008 a switch from GAM94 to RP2000 was made, to reflect the mortality assumption now more prevalent in the US.

25. Retirement benefit and other post-retirement obligations 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 and US Group plans is as follows:

	UK		US	
	2009	2008	2009	2008
Male	22.7	21.5	17.6	17.6
Female	23.5	21.8	20.2	20.2

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:

	UK		US	
	2009	2008	2009	2008
Male	25.3	23.3	17.6	17.6
Female	25.6	23.8	20.2	20.2

Financial statement information

The amounts recognised in the income statement are as follows:

						2009
All figures in £ millions	UK Group plan	Defined benefit other	Sub-total	Defined contribution	PRMB	Total
Current service cost	14	3	17	62	2	81
Past service cost	–	1	1	–	–	1
Total operating expense	14	4	18	62	2	82
Expected return on plan assets	(83)	(5)	(88)	–	–	(88)
Interest on plan liabilities	89	8	97	–	3	100
Net finance expense	6	3	9	–	3	12
Net income statement charge	20	7	27	62	5	94
Actual return on plan assets	136	8	144	–	–	144

						2008
All figures in £ millions	UK Group plan	Defined benefit other	Sub-total	Defined contribution	PRMB	Total
Current service cost	33	3	36	41	1	78
Past service cost	–	1	1	–	5	6
Total operating expense	33	4	37	41	6	84
Expected return on plan assets	(104)	(7)	(111)	–	–	(111)
Interest on plan liabilities	93	7	100	–	3	103
Net finance (income)/expense	(11)	–	(11)	–	3	(8)
Net income statement charge	22	4	26	41	9	76
Actual loss on plan assets	(130)	(27)	(157)	–	–	(157)

The total operating charge is included in administrative and other expenses. In 2008 the UK Group plan current service cost included £14m relating to defined contribution sections. In 2009 the defined contribution section of the UK Group plan is recorded within the defined contribution expense.

Notes to the consolidated financial statements continued

25. Retirement benefit and other post-retirement obligations continued

The amounts recognised in the balance sheet are as follows:

All figures in £ millions	2009 UK Group plan	2009 Other funded plans	2009 Other unfunded plans	2009 Total	2008 UK Group plan	2008 Other funded plans	2008 Other unfunded plans	2008 Total
Fair value of plan assets	1,609	118	–	1,727	1,478	100	–	1,578
Present value of defined benefit obligation	(1,798)	(151)	(18)	(1,967)	(1,429)	(149)	(16)	(1,594)
Net pension (liability)/asset	(189)	(33)	(18)	(240)	49	(49)	(16)	(16)
Other post-retirement medical benefit obligation				(65)				(68)
Other pension accruals				(34)				(34)
Net retirement benefit obligations				(339)				(118)
Analysed as:								
Retirement benefit assets				–				49
Retirement benefit obligations				(339)				(167)

The following (losses)/gains have been recognised in other comprehensive income:

All figures in £ millions	2009	2008
Amounts recognised for defined benefit plans	(295)	(74)
Amounts recognised for post-retirement medical benefit plans	(4)	3
Total recognised in year	(299)	(71)
Cumulative amounts recognised	(246)	53

The fair value of plan assets comprises the following:

%	2009 UK Group plan	2009 Other funded plans	2009 Total	2008 UK Group plan	2008 Other funded plans	2008 Total
Equities	27.4	2.4	29.8	28.0	3.1	31.1
Bonds	47.2	2.1	49.3	40.8	2.2	43.0
Properties	9.4	0.0	9.4	7.4	0.1	7.5
Other	10.4	1.1	11.5	17.5	0.9	18.4

The plan assets do not include any of the Group’s own financial instruments, or any property occupied by the Group.

25. Retirement benefit and other post-retirement obligations continued

Changes in the values of plan assets and liabilities of the retirement benefit plans are as follows:

All figures in £ millions	2009 UK Group plan	2009 Other plans	2009 Total	2008 UK Group plan	2008 Other plans	2008 Total
Fair value of plan assets						
Opening fair value of plan assets	1,478	100	1,578	1,744	109	1,853
Exchange differences	–	(6)	(6)	–	23	23
Expected return on plan assets	83	5	88	104	7	111
Actuarial gains and (losses)	53	3	56	(234)	(34)	(268)
Contributions by employer	64	26	90	54	3	57
Contributions by employee	3	–	3	9	–	9
Benefits paid	(72)	(10)	(82)	(72)	(8)	(80)
Other movements	–	–	–	(127)	–	(127)
Closing fair value of plan assets	1,609	118	1,727	1,478	100	1,578
Present value of defined benefit obligation						
Opening defined benefit obligation	(1,429)	(165)	(1,594)	(1,682)	(129)	(1,811)
Exchange differences	–	14	14	–	(38)	(38)
Current service cost	(14)	(3)	(17)	(33)	(3)	(36)
Past service cost	–	(1)	(1)	–	(1)	(1)
Interest cost	(89)	(8)	(97)	(93)	(7)	(100)
Actuarial gains and (losses)	(335)	(16)	(351)	189	5	194
Contributions by employee	(3)	–	(3)	(9)	–	(9)
Benefits paid	72	10	82	72	8	80
Other movements	–	–	–	127	–	127
Closing defined benefit obligation	(1,798)	(169)	(1,967)	(1,429)	(165)	(1,594)

During 2008 changes made to the administration of the plan assets enabled assets relating to the defined contribution sections of the UK Group plan to be identified separately from those of the defined benefit section, for accounting purposes. Defined contribution assets are no longer disclosed as part of the UK Group plan assets. The other movements in both the change in value of plan assets and liabilities in 2008 represent the separation out of these defined contribution assets.

Notes to the consolidated financial statements continued

25. Retirement benefit and other post-retirement obligations continued

Changes in the value of the US PRMB are as follows:

All figures in £ millions	2009	2008
Opening defined benefit obligation	(68)	(47)
Exchange differences	8	(19)
Current service cost	(2)	(1)
Past service cost	–	(5)
Interest cost	(3)	(3)
Actuarial gains and (losses)	(4)	3
Benefits paid	4	4
Closing defined benefit obligation	(65)	(68)

The history of the defined benefit plans is as follows:

All figures in £ millions	2009	2008	2007	2006	2005
Fair value of plan assets	1,727	1,578	1,853	1,633	1,500
Present value of defined benefit obligation	(1,967)	(1,594)	(1,811)	(1,810)	(1,803)
Net pension (liability)/asset	(240)	(16)	42	(177)	(303)
Experience adjustments on plan assets	56	(268)	29	74	140
Experience adjustments on plan liabilities	(351)	194	50	28	(119)

Funding

The UK Group plan is self-administered with the plan's assets being held independently of the Group. The trustees of the plan are required to act in the best interest of the plan's beneficiaries. The plan trustees and the company are currently finalising the latest triennial valuation for funding purposes as at 1 January 2009. At this point, the Group has contributed an additional £20m to the plan in 2009. In total the Group contributed £42m (2008: £21m) towards the funding shortfall and expects to contribute a similar amount in 2010. Regular contributions to the plan are estimated to be £23m for 2010.

The Group expects to contribute $83m in 2010 and $126m in 2011 to its US pension plans.

25. Retirement benefit and other post-retirement obligations continued

Sensitivities

The net retirement benefit obligations are calculated using a number of assumptions, the most significant being the discount rate used to calculate the defined benefit obligation. 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:

	2009	
All figures in £ millions	1% increase	1% decrease
Effect on:		
(Decrease)/increase in defined benefit obligation – UK Group plan	(260.2)	325.4
(Decrease)/increase of aggregate of service cost and interest cost – UK Group plan	(4.5)	3.9
(Decrease)/increase in defined benefit obligation – US plan	(12.4)	14.7

The effect of members living one year more or one year less on the defined benefit obligation and the total pension expense is as follows:

	2009	
All figures in £ millions	1 year increase	1 year decrease
Effect on:		
Increase/(decrease) in defined benefit obligation – UK Group plan	50.7	(49.3)
Increase/(decrease) in defined benefit obligation – US plan	1.3	(1.7)

The effect of a one percentage point increase and decrease in the assumed medical cost trend rates is as follows:

	2009	
All figures in £ millions	1% increase	1% decrease
Effect on:		
Increase/(decrease) in post-retirement medical benefit obligation	3.1	(2.7)
Increase/(decrease) of aggregate of service cost and interest cost	0.2	(0.2)

Notes to the consolidated financial statements continued

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	2009	2008
Pearson plans	27	25
Interactive Data plans	10	8
Total share-based payment costs	37	33

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, five or seven 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.

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 introduced in 2001 and renewed in 2006 and consists of two parts: share options and/or restricted shares.

Options were last granted under this plan in 2001 based on a pre-grant earnings per share growth test and are not subject to further performance conditions on exercise. The options became exercisable in tranches and lapse if they remain unexercised at the tenth anniversary of the date of grant.

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 March 2008 and March 2009 vest dependent on relative shareholder return, return on invested capital and earnings per share growth. The award was split equally across all three measures. Other restricted shares awarded in 2008 and 2009 vest depending on continuing service over a three-year period.

Annual Bonus Share Matching Plan This plan permits executive directors and senior executives around the Group to invest up to 50% of any after tax annual bonus in Pearson shares. If these shares are held and the Group meets an earnings per share growth target, the company will match them on a gross basis i.e. the maximum number of matching shares is equal to the number of shares that could have been acquired with the amount of the pre-tax annual bonus taken in invested shares.

In addition to the above, share options remain outstanding under Executive Share Option, Reward and Special Share Option Plans. These are legacy plans which were replaced with the introduction of the Long-Term Incentive Plan in 2001.

26. Share-based payments continued

The number and weighted average exercise prices of share options granted under the Group's plans are as follows:

	2009		2008	
	Number of share options 000s	Weighted average exercise price £	Number of share options 000s	Weighted average exercise price £
Outstanding at beginning of year	14,379	13.14	16,781	13.15
Granted during the year	1,320	5.47	1,437	5.35
Exercised during the year	(656)	5.91	(683)	4.85
Forfeited during the year	(2,488)	13.02	(3,082)	11.56
Expired during the year	(68)	5.20	(74)	6.06
Outstanding at end of year	12,487	12.78	14,379	13.14
Options exercisable at end of year	9,264	15.28	11,527	14.97

Options were exercised regularly throughout the year. The weighted average share price during the year was £7.15 (2008: £6.44). 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:

	2009		2008	
Range of exercise prices £	Number of share options 000s	Weighted average contractual life Years	Number of share options 000s	Weighted average contractual life Years
0 – 5	172	1.07	453	1.23
5 – 10	5,523	2.37	5,113	2.84
10 – 15	4,225	1.36	5,481	1.97
15 – 20	270	0.75	908	0.84
20 – 25	344	0.19	350	1.19
>25	1,953	0.19	2,074	1.19
	12,487	1.57	14,379	2.05

In 2009 and 2008 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.

Notes to the consolidated financial statements continued

26. Share-based payments continued

The weighted average estimated fair values and the inputs into the Black-Scholes model are as follows:

	2009 Weighted average	2008 Weighted average
Fair value	£1.69	£1.67
Weighted average share price	£7.13	£6.96
Weighted average exercise price	£5.47	£5.35
Expected volatility	27.32%	21.41%
Expected life	4.0 years	4.1 years
Risk free rate	2.45%	4.28%
Expected dividend yield	4.74%	4.54%
Forfeiture rate	3.5%	3.6%

The expected volatility is based on the historic 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:

	2009		2008	
	Number of shares 000s	Weighted average fair value £	Number of shares 000s	Weighted average fair value £
Long-Term Incentive Plan	4,519	5.77	4,152	5.78
Annual Bonus Share Matching Plan	271	6.70	253	6.73

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. Participants of the Long-Term Incentive Plan are entitled to dividends during the vesting period. The number of shares to vest has been adjusted, based on historical experience, to account for any potential forfeitures. Restricted shares granted under the Annual Bonus Share Matching Plan are valued using the share price at the date of grant. Shares granted include the entitlement 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 were considered by adjusting the number of shares expected to vest based on the most likely outcome of the relevant performance criteria.

Subsidiary share option plans

Interactive Data, a 61% subsidiary of the Group, operates the following share-based payment plans:

2001 Employee Stock Purchase Plan The 2001 Employee Stock Purchase Plan allows all eligible employees worldwide to purchase stock at a discounted price at specific times.

26. Share-based payments continued

2000 Long-Term Incentive Plan Under this plan, the Compensation Committee of the Board of Directors can grant share-based awards representing up to 20% of the total number of shares of common stock outstanding at the date of grant. The plan provides for the discretionary issuance of share-based awards to directors, officers and employees of Interactive Data, as well as persons who provide consulting or other services to Interactive Data. The exercise price for all options granted to date has been equal to the market price of the underlying shares at the date of grant. Options expire ten years from the date of grant and generally vest over a three to four-year period without any performance criteria attached.

In addition, grants of restricted stock can be made to certain executives and members of the Board of Directors of Interactive Data. The awarded shares are available for distribution, at no cost, at the end of a three-year vesting period. No performance criteria are attached to shares granted under this plan.

Interactive Data employees purchased 234,956 shares (2008: 183,318) under the 2001 Employee Stock Purchase Plan at an average share price of $19.47 (£12.06) (2008: $22.95; £15.96). The weighted average fair value at the date of grant was $5.82 (£3.60) (2008: $6.59; £4.58).

The number and weighted average exercise prices of share options granted under the 2000 Long-Term Incentive Plan are as follows:

	2009			2008		
	Number of share options 000s	Weighted average exercise price $	Weighted average exercise price £	Number of share options 000s	Weighted average exercise price $	Weighted average exercise price £
Outstanding at beginning of year	10,264	19.38	13.48	9,827	18.21	9.15
Granted during the year	1,224	23.25	14.40	1,449	24.95	17.35
Exercised during the year	(1,493)	14.20	8.79	(895)	15.37	10.69
Forfeited during the year	(159)	24.44	15.13	(99)	22.05	15.34
Expired during the year	(64)	25.93	16.06	(18)	12.17	8.46
Outstanding at end of year	9,772	20.53	12.71	10,264	19.38	13.48
Options exercisable at end of year	6,839	18.92	11.72	6,865	16.89	11.75

The options outstanding at the end of the year have a weighted average remaining contractual life and exercise price as follows:

	2009		2008	
Range of exercise prices $	Number of share options 000s	Weighted average contractual life Years	Number of share options 000s	Weighted average contractual life Years
0 – 4.4	–	–	–	–
4.4 – 7.5	20	0.3	47	1.3
7.5 – 12	909	1.5	1,502	2.4
12 – 20	2,339	3.6	2,987	4.6
› 20	6,504	7.5	5,728	8.0
	9,772	6.0	10,264	6.2

Notes to the consolidated financial statements continued

26. Share-based payments continued

The fair value of the options granted under the 2000 Long-Term Incentive Plan and of the shares awarded under the 2001 Employee Stock Purchase Plan was estimated using a Black-Scholes option pricing model. The weighted average estimated fair values and the inputs into the Black-Scholes model are as follows:

	Long-Term Incentive Plan		Employee Stock Purchase Plan	
	2009	2008	2009	2008
	Weighted average	Weighted average	Weighted average	Weighted average
Fair value	$4.92	$5.58	$5.82	$6.59
Weighted average share price	$23.25	$24.95	$19.47	$22.95
Weighted average exercise price	$23.25	$24.95	$19.47	$22.95
Expected volatility	29.70%	24.20%	48.40%	33.70%
Expected life	5.9 years	5.7 years	0.5 years	0.5 years
Risk free rate	2.4% to 2.6%	1.5% to 3.5%	0.3% to 0.4%	2.0% to 2.4%
Expected dividend yield	3.6%	2.2%	3.6%	2.1%
Forfeiture rate	0.0%	0.0%	0.0%	0.0%

The expected volatility is based on the historic volatility of Interactive Data's share price over the vesting term of the options.

During the year Interactive Data granted the following shares under restricted share arrangements:

	2009			2008		
	Number of shares 000s	Weighted average fair value $	Weighted average fair value £	Number of shares 000s	Weighted average fair value $	Weighted average fair value £
2000 Long-Term Incentive Plan	415	22.92	14.19	194	25.43	17.69

Shares awarded under the 2000 Long-Term Incentive Plan were valued based on the share price prevailing at the date of grant.

27. Share capital and share premium

	Number of shares 000s	Ordinary shares £m	Share premium £m
At 1 January 2008	808,028	202	2,499
Issue of ordinary shares – share option schemes	1,248	–	6
At 31 December 2008	809,276	202	2,505
Issue of ordinary shares – share option schemes	1,523	1	7
At 31 December 2009	810,799	203	2,512

The ordinary shares have a par value of 25p per share (2008: 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.

27. Share capital and share premium continued

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		Interactive Data		Total
	Number of shares 000s	£m	Number of shares 000s	£m	£m
At 1 January 2008	11,761	141	7,229	75	216
Purchase of treasury shares	2,028	12	1,976	35	47
Release of treasury shares	(3,341)	(41)	–	–	(41)
At 31 December 2008	10,448	112	9,205	110	222
Purchase of treasury shares	2,200	13	1,280	20	33
Release of treasury shares	(2,983)	(29)	–	–	(29)
At 31 December 2009	9,665	96	10,485	130	226

The Group holds Pearson plc shares in trust to satisfy its obligations under its restricted share plans (see note 26). These shares, representing 1.2% (2008: 1.3%) of called-up share capital, are treated as treasury shares for accounting purposes and have a par value of 25p per share.

Interactive Data hold their own shares in respect of share buy-back programmes. These shares are held as treasury shares and have a par value of $0.01.

The nominal value of Pearson plc treasury shares amounts to £2.4m (2008: £2.6m). The nominal value of Interactive Data treasury shares amounts to £0.07m (2008: £0.06m).

At 31 December 2009 the market value of Pearson plc treasury shares was £86.1m (2008: £67.0m) and the market value of Interactive Data treasury shares was £164.3m (2008: £157.9m).

Notes to the consolidated financial statements continued

29. Business combinations

On 15 April 2009 the Group acquired Wall Street English (WSE), China's leading provider of premium English language training to adults. On 15 July 2009 the Group completed the purchase of an additional stake in Maskew Miller Longman (MML), its South African publishing business. Provisional values for the assets and liabilities arising from these and other acquisitions completed in the year together with adjustments to prior year acquisitions are as follows:

					2009	2008
All figures in £ millions	Notes	Wall Street English Fair value	MML Fair value	Other Fair value	Total Fair value	Total Fair value
Property, plant and equipment	10	6	1	2	9	6
Intangible assets	11	40	47	55	142	220
Intangible assets – Pre-publication	20	–	–	2	2	27
Inventories		1	12	1	14	7
Trade and other receivables		8	7	8	23	54
Cash and cash equivalents		3	9	17	29	16
Trade and other liabilities		(56)	(16)	(19)	(91)	(52)
Current income tax liabilities		–	(2)	(2)	(4)	(3)
Net deferred income tax liabilities	13	(9)	(12)	(24)	(45)	(4)
Provisions for other liabilities and charges		–	–	–	–	(26)
Retirement benefit obligations		–	–	(1)	(1)	–
Minority interest		–	(7)	(9)	(16)	(2)
Assets held for sale		–	–	–	–	3
Net assets/(liabilities) acquired at fair value		(7)	39	30	62	246
Goodwill	11	108	38	59	205	153
Increase in fair values of proportionate holding arising on stepped acquisition		–	(23)	–	(23)	–
Total		101	54	89	244	399
Satisfied by:						
Cash		(101)	(49)	(51)	(201)	(394)
Other consideration		–	(5)	–	(5)	–
Deferred consideration		–	–	(27)	(27)	–
Net prior year adjustments		–	–	(11)	(11)	(5)
Total consideration		(101)	(54)	(89)	(244)	(399)

Carrying value of net (liabilities)/assets acquired		(22)	5	2	(15)	78
Fair value adjustments		15	34	28	77	168
Fair value		(7)	39	30	62	246

The goodwill arising on these acquisitions results from substantial cost and revenue synergies and from benefits that cannot be separately recognised, such as the assembled workforce.

29. Business combinations continued

Wall Street English

All figures in £ millions	Carrying value	Fair value adjustments	Fair value
Property, plant and equipment	6	–	6
Intangible assets	16	24	40
Inventories	1	–	1
Trade and other receivables	8	–	8
Cash and cash equivalents	3	–	3
Trade and other liabilities	(56)	–	(56)
Net deferred income tax liabilities	–	(9)	(9)
Net liabilities acquired	(22)	15	(7)
Goodwill			108
Total			101

MML

All figures in £ millions	Carrying value	Fair value adjustments	Fair value
Property, plant and equipment	1	–	1
Intangible assets	–	47	47
Inventories	12	–	12
Trade and other receivables	7	–	7
Cash and cash equivalents	9	–	9
Trade and other liabilities	(16)	–	(16)
Current income tax liabilities	(2)	–	(2)
Net deferred income tax liabilities	1	(13)	(12)
Minority interest	(7)	–	(7)
Net assets acquired	5	34	39
Goodwill			38
Increase in fair values of proportionate holding arising on stepped acquisition			(23)
Total			54

Net cash outflow on acquisition:

All figures in £ millions	2009	2008
Cash – Current year acquisitions	(201)	(394)
Cash – Acquisitions yet to complete	(4)	(12)
Deferred payments for prior year acquisitions and other items	(32)	(5)
Cash and cash equivalents acquired	29	16
Cash outflow on acquisition	(208)	(395)

Wall Street English contributed £29m of sales and £nil to the Group's profit before tax between the date of acquisition and the balance sheet date. MML contributed £22m of sales and £4m to the Group's profit before tax between the date of acquisition and the balance sheet date. Other businesses acquired contributed £37m to the Group's sales and £6m to the Group's profit before tax between the date of acquisition and the balance sheet date.

If the acquisitions had been completed on 1 January 2009, the Group estimates that sales for the period would have been £5,658m and profit before tax would have been £662m.

Notes to the consolidated financial statements continued

30. Disposals

All figures in £ millions	2009 Total	2008 Total
Disposal of subsidiaries		
Property, plant and equipment	–	(7)
Intangible assets	–	(1)
Intangible assets – Pre-publication	–	(2)
Inventories	–	(7)
Trade and other receivables	–	(8)
Trade and other liabilities	–	9
Minority interest	–	–
Attributable goodwill	–	(99)
Cumulative translation adjustment	–	(49)
Net assets disposed	–	(164)
Cash received	–	114
Deferred receipts	–	2
Costs	–	(5)
Loss on sale	–	(53)

	2009	2008
Cash flow from disposals		
Cash – Current year disposals	–	114
Cash – Transactions with minorities	14	12
Costs paid	–	(15)
Net cash inflow	14	111

Further details of the Data Management business disposal in 2008 are shown in note 3.

31. Cash generated from operations

All figures in £ millions	Notes	2009	2008
Net profit		462	323
Adjustments for:			
Income tax		198	209
Depreciation	10	85	80
Amortisation of purchased intangible assets	11	103	86
Amortisation of other intangible assets	11	44	30
Loss on sale of property, plant and equipment		2	1
Net finance costs	6	95	91
Share of results of joint ventures and associates	12	(30)	(25)
Loss on sale of discontinued operations	3	–	53
Net foreign exchange adjustment from transactions		(14)	105
Share-based payment costs	26	37	33
Pre-publication		(16)	(58)
Inventories		32	(12)
Trade and other receivables		(14)	(81)
Trade and other liabilities		103	82
Retirement benefit obligations		(72)	(14)
Provisions for other liabilities and charges		(3)	(9)
Net cash generated from operations		1,012	894
Dividends from joint ventures and associates		22	23
Purchase of property, plant and equipment		(62)	(75)
Purchase of intangible assets		(58)	(45)
Finance lease principal payments		(2)	(3)
Proceeds from sale of property, plant and equipment		1	2
Operating cash flow		913	796
Operating tax paid		(103)	(89)
Net operating finance costs paid		(87)	(76)
Total operating and free cash flow		723	631
Dividends paid (including to minorities)		(293)	(285)
Net movement of funds from operations		430	346
Acquisitions and disposals		(218)	(285)
Purchase of treasury shares		(33)	(47)
New equity		8	6
Other movements on financial instruments		3	8
Net movement of funds		190	28
Exchange movements on net debt		178	(515)
Total movement in net debt		368	(487)

Notes to the consolidated financial statements continued

31. Cash generated from operations continued

Net cash generated from operations is translated at an exchange rate approximating to 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	2009	2008
Net book amount	3	3
Loss on sale of property, plant and equipment	(2)	(1)
Proceeds from sale of property, plant and equipment	1	2

The principal other non-cash transactions are movements in finance lease obligations of £8m (2008: £2m).

32. 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 and associates. In addition there are contingent liabilities of the Group in respect of legal claims. None of these claims are expected to result in a material gain or loss to the Group.

33. Commitments

There were no commitments for capital expenditure contracted for at the balance sheet date 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. The lease expenditure charged to the income statement during the year is disclosed in note 4.

The future aggregate minimum lease payments in respect of operating leases are as follows:

All figures in £ millions	2009	2008
Not later than one year	153	149
Later than one year and not later than two years	144	138
Later than two years and not later than three years	129	129
Later than three years and not later than four years	114	118
Later than four years and not later than five years	99	108
Later than five years	848	970
	1,487	1,612

34. 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. Amounts falling due from joint ventures and associates are set out in note 22.

Key management personnel

Key management personnel are deemed to be the members of the board of directors of Pearson plc. It is this board which has responsibility for planning, directing and controlling the activities of the Group. Key management personnel compensation is disclosed in the directors' remuneration report.

There were no other material related party transactions.

No guarantees have been provided to related parties.

35. Events after the balance sheet date

During January 2010, the Group announced that Interactive Data was undertaking a preliminary review of strategic alternatives for its business. At the date of this report, the outcome of the review is still uncertain.

On 3 February 2010 the FT Publishing business announced the acquisition of Medley Global Advisors LLC, a premier provider of macro policy intelligence to the world's top investment banks, hedge funds and asset managers for $15.5m.

Company statement of comprehensive income
Year ended 31 December 2009

All figures in £ millions	2009	2008
Profit for the year	233	526
Currency translation differences on fair value hedges	–	(6)
Total comprehensive income for the year	233	520

Company statement of changes in equity
Year ended 31 December 2009

	Equity attributable to equity holders of the company					
All figures in £millions	Share capital	Share premium	Treasury shares	Special reserve	Retained earnings	Total
At 1 January 2009	202	2,505	(63)	447	835	3,926
Total comprehensive income	–	–	–	–	233	233
Issue of ordinary shares under share option schemes	1	7	–	–	–	8
Purchase of treasury shares	–	–	(13)	–	–	(13)
Release of treasury shares	–	–	29	–	(29)	–
Dividends	–	–	–	–	(273)	(273)
At 31 December 2009	203	2,512	(47)	447	766	3,881

	Equity attributable to equity holders of the company					
All figures in £millions	Share capital	Share premium	Treasury shares	Special reserve	Retained earnings	Total
At 1 January 2008	202	2,499	(82)	447	603	3,669
Total comprehensive income	–	–	–	–	520	520
Issue of ordinary shares under share option schemes	–	6	–	–	–	6
Purchase of treasury shares	–	–	(12)	–	–	(12)
Release of treasury shares	–	–	41	–	(31)	10
Prior year contribution applied to release of shares	–	–	(10)	–	–	(10)
Dividends	–	–	–	–	(257)	(257)
At 31 December 2008	202	2,505	(63)	447	835	3,926

The special reserve represents the cumulative effect of cancellation of the company's share premium account.

Included within retained earnings is an amount of £131m (2008: £131m) relating to profit on intra-group disposals that is not distributable.

Company balance sheet
As at 31 December 2009

All figures in £ millions	Notes	2009	2008
Assets			
Non-current assets			
Investments in subsidiaries	2	8,547	6,912
Amounts due from subsidiaries		464	322
Financial assets – Derivative financial instruments	6	112	181
Other financial assets		–	6
		9,123	7,421
Current assets			
Amounts due from subsidiaries		2,151	2,953
Current income tax assets		21	30
Cash and cash equivalents (excluding overdrafts)	4	124	57
Financial assets – Derivative financial instruments	6	–	3
Total assets		11,419	10,464
Liabilities			
Non-current liabilities			
Financial liabilities – Borrowings	5	(767)	(991)
Financial liabilities – Derivative financial instruments	6	(2)	(15)
Amounts due to subsidiaries		(3,808)	(1,840)
		(4,577)	(2,846)
Current liabilities			
Current income tax liabilities		–	(2)
Financial liabilities – Borrowings	5	(419)	(352)
Financial liabilities – Derivative financial instruments	6	(7)	(5)
Amounts due to subsidiaries		(2,535)	(3,333)
Total liabilities		(7,538)	(6,538)
Net assets		3,881	3,926
Equity			
Share capital	7	203	202
Share premium	7	2,512	2,505
Treasury shares	8	(47)	(63)
Special reserve		447	447
Retained earnings		766	835
Total equity attributable to equity holders of the company		3,881	3,926

These financial statements have been approved for issue by the board of directors on 10 March 2010 and signed on its behalf by

Robin Freestone Chief financial officer

Company cash flow statement
Year ended 31 December 2009

All figures in £ millions	Notes	2009	2008
Cash flows from operating activities			
Net profit		233	526
Adjustments for:			
Income tax		(57)	(37)
Net finance costs		169	98
Other receivables		–	2
Amounts due from subsidiaries		115	193
Net cash generated from operations		460	782
Interest paid		(130)	(209)
Tax received		65	52
Net cash generated from operating activities		395	625
Cash flows from investing activities			
Acquisition of subsidiaries, net of cash acquired		(1)	–
Interest received		–	2
Net cash (used in)/generated from investing activities		(1)	2
Cash flows from financing activities			
Proceeds from issue of ordinary shares	7	8	6
Net purchase of treasury shares		(13)	(12)
Proceeds from borrowings		–	152
Repayment of borrowings		(131)	(584)
Dividends paid to company's shareholders		(273)	(257)
Net cash used in financing activities		(409)	(695)
Effects of exchange rate changes on cash and cash equivalents		15	(7)
Net decrease in cash and cash equivalents		–	(75)
Cash and cash equivalents at beginning of year		(295)	(220)
Cash and cash equivalents at end of year	4	(295)	(295)

Notes to the company financial statements

1. Accounting policies

a. Basis of preparation

The financial statements on pages 148 to 156 comprise the separate financial statements of Pearson plc. As permitted by section 408 of the Companies Act 2006, only the Group's income statement has been presented.

The company has no employees.

b. Group accounting policies

The accounting policies applied in the preparation of these company financial statements are the same as those set out in note 1 to the Group financial statements with the addition of the following:

Investments

Investments in subsidiaries are stated at cost less provision for impairment, with the exception of certain hedged investments that are held in a foreign currency and revalued at each balance sheet date.

2. Investments in subsidiaries

All figures in £ millions	2009	2008
At beginning of year	6,912	6,650
Subscription for share capital in subsidiaries	1,658	152
External disposal	(1)	–
Currency revaluations	(22)	110
At end of year	8,547	6,912

3. Financial risk management

The company's financial instruments comprise amounts due to/from subsidiary undertakings, cash and cash equivalents, derivative financial instruments and current and non-current borrowings. Derivative financial instruments are held at fair value, with all other financial instruments held at amortised cost. The company's approach to the management of financial risks is consistent with the Group's treasury policy, as discussed in note 19 to the Group's financial statements. The company believes the value of its financial assets to be fully recoverable.

The company designates certain of its qualifying derivative financial instruments as hedges of the fair value of its bonds (fair value hedges). Changes in the fair value of these derivative financial instruments are recorded in the income statement, together with any change in the fair value of the hedged liability attributable to the hedged risk.

The carrying value of the company's financial instruments is exposed to movements in interest rates and foreign currency exchange rates (primarily US dollars). The company estimates that a 1% increase in interest rates would result in a £36m decrease in the carrying value of its financial instruments, with a 1% decrease in interest rates resulting in a £40m increase in their carrying value. The company also estimates that a 10% strengthening in sterling would decrease the carrying value of its financial instruments by £110m, while a 10% decrease in the value of sterling would increase the carrying value by £137m. These increases and decreases in carrying value would be recorded through the income statement. Sensitivities are calculated using 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%.

Notes to the company financial statements continued

3. Financial risk management continued

The maturity of contracted cash flows on the company's borrowings and all of its derivative financial instruments are as follows:

All figures in £ millions	USD	GBP	Other	Total
				2009
Not later than one year	(5)	3	2	–
Later than one year and not later than five years	249	241	30	520
Later than five years	324	(212)	–	112
Total	568	32	32	632
Analysed as:				
Bonds	601	337	–	938
Rate derivatives – inflows	(386)	(313)	–	(699)
Rate derivatives – outflows	353	8	32	393
Total	568	32	32	632

All figures in £ millions	USD	GBP	Other	Total
				2008
Not later than one year	8	17	–	25
Later than one year and not later than five years	435	65	–	500
Later than five years	178	266	–	444
Total	621	348	–	969
Analysed as:				
Revolving credit facility and commercial paper	141	–	–	141
Bonds	709	355	–	1,064
Rate derivatives – inflows	(392)	(21)	–	(413)
Rate derivatives – outflows	163	14	–	177
Total	621	348	–	969

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 company net settles these amounts wherever possible.

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.

4. Cash and cash equivalents (excluding overdrafts)

All figures in £ millions	2009	2008
Cash at bank and in hand	2	2
Short-term bank deposits	122	55
	124	57

Short-term bank deposits are invested with banks and earn interest at the prevailing short-term deposit rates.

At the end of 2009 the currency split of cash and cash equivalents was US dollar 26% (2008: nil), sterling 72% (2008: 95%) and euro 2% (2008: 5%).

Cash and cash equivalents have fair values that approximate to their carrying amounts 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	2009	2008
Cash and cash equivalents	124	57
Bank overdrafts	(419)	(352)
	(295)	(295)

5. Financial liabilities – Borrowings

All figures in £ millions	2009	2008
Non-current		
Bank loans and overdrafts	–	132
7.0% Global Dollar Bonds 2011 (nominal amount $500m)	322	368
7.0% Sterling Bonds 2014 (nominal amount £250m)	254	254
4.625% US Dollar notes 2018 (nominal amount $300m)	191	237
	767	991
Current		
Due within one year or on demand:		
Bank loans and overdrafts	419	352
	419	352
Total borrowings	1,186	1,343

Included in the non-current borrowings above is £4m of accrued interest (2008: £5m).

Included in the current borrowings above is £nil of accrued interest (2008: £nil).

Notes to the company financial statements continued

5. Financial liabilities – Borrowings continued

The maturity of the company's non-current borrowings is as follows:

All figures in £ millions	2009	2008
Between one and two years	322	–
Between two and five years	254	500
Over five years	191	491
	767	991

As at 31 December 2009 the exposure to interest rate changes of the borrowings and amounts due to subsidiaries when the borrowings re-price is as follows:

All figures in £ millions	One year	One to five years	More than five years	Total
Re-pricing profile of borrowings	419	576	191	1,186
Amounts due to subsidiaries	5,159	517	527	6,203
Effect of rate derivatives	1,288	(762)	(526)	–
	6,866	331	192	7,389

The carrying amounts and market values of borrowings are as follows:

		2009		2008	
All figures in £ millions	Effective interest rate	Carrying amount	Market value	Carrying amount	Market value
Bank loans and overdrafts	n/a	419	419	484	484
7.0% Global Dollar Bonds 2011	7.16%	322	331	368	349
7.0% Sterling Bonds 2014	7.20%	254	276	254	258
4.625% US Dollar notes 2018	4.69%	191	176	237	169
		1,186	1,202	1,343	1,260

The market values 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 company's borrowings are denominated in the following currencies:

All figures in £ millions	2009	2008
US dollar	523	1,089
Sterling	648	254
Euro	15	–
	1,186	1,343

6. Derivative financial instruments

The company's outstanding derivative financial instruments are as follows:

All figures in £ millions	Gross notional amounts 2009	Assets 2009	Liabilities 2009	Gross notional amounts 2008	Assets 2008	Liabilities 2008
Interest rate derivatives – in a fair value hedge relationship	360	17	–	398	44	–
Interest rate derivatives – not in a hedge relationship	1,229	66	(7)	1,867	140	(20)
Cross currency rate derivatives	220	29	(2)	–	–	–
Total	1,809	112	(9)	2,265	184	(20)
Analysed as expiring:						
In less than one year	238	–	(7)	487	3	(5)
Later than one year and not later than five years	844	60	(2)	859	47	(15)
Later than five years	727	52	–	919	134	–
Total	1,809	112	(9)	2,265	184	(20)

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.

7. Share capital and share premium

	Number of shares 000s	Ordinary shares £m	Share premium £m
At 1 January 2008	808,028	202	2,499
Issue of shares – share option schemes	1,248	–	6
At 31 December 2008	809,276	202	2,505
Issue of shares – share option schemes	1,523	1	7
At 31 December 2009	810,799	203	2,512

The ordinary shares have a par value of 25p per share (2008: 25p per share). All issued shares are fully paid. All shares have the same rights.

Notes to the company financial statements continued

8. Treasury shares

	Number of shares 000s	£m
At 1 January 2008	11,761	82
Purchase of treasury shares	2,028	12
Release of treasury shares	(3,341)	(41)
Prior year contributions applied to release of shares	–	10
At 31 December 2008	10,448	63
Purchase of treasury shares	2,200	13
Release of treasury shares	(2,983)	(29)
At 31 December 2009	9,665	47

The company holds its own shares in trust to satisfy its obligations under its restricted share plans. These shares are treated as treasury shares for accounting purposes and have a par value of 25p per share. The nominal value of the company's treasury shares amounts to £2.4m (2008: £2.6m). At 31 December 2009 the market value of the company's treasury shares was £86.1m (2007: £67.0m).

9. Contingencies

There are contingent 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. In addition there are contingent liabilities in respect of legal claims. None of these claims are expected to result in a material gain or loss to the company.

10. Audit fees

Statutory audit fees relating to the company were £35,000 (2008: £35,000). Audit-related regulatory reporting fees relating to the company were £nil (2008: £nil).

11. Related party transactions

Subsidiaries

The company transacts and has outstanding balances with its subsidiaries. Amounts due from subsidiaries and amounts due to subsidiaries are disclosed on the face of the company balance sheet.

These loans are generally unsecured and interest is calculated based on market rates. The company has interest payable to subsidiaries for the year of £232m (2008: £214m) and interest receivable from subsidiaries for the year of £147m (2008: £86m). Management fees payable to subsidiaries in respect of centrally provided services amounted to £37m (2008: £33m). Dividends received from subsidiaries were £383m (2008: £620m).

Key management personnel

Key management personnel are deemed to be the members of the board of directors of the company. It is this board which has responsibility for planning, directing and controlling the activities of the company. Key management personnel compensation is disclosed in the directors' remuneration report of the Group.

There were no other material related party transactions.

Principal subsidiaries

The principal operating subsidiaries at 31 December 2009 are listed below. They operate mainly in the countries of incorporation or registration, the investments are in equity share capital and they are all 100% owned unless stated otherwise.

	Country of incorporation or registration
Pearson Education	
Pearson Education Inc.	US
Pearson Education Ltd	England
Edexcel Ltd*	England
NCS Pearson Inc.	US
FT Group	
The Financial Times Ltd	England
Mergermarket Ltd	England
Interactive Data Corporation (61%)	US
The Penguin Group	
Penguin Group (USA) Inc.	US
The Penguin Publishing Co Ltd	England
Dorling Kindersley Holdings Ltd*	England

* Direct investment of Pearson plc.

Five year summary

All figures in £ millions	2005	2006	2007	2008	2009
Sales					
North American Education	1,576	1,679	1,667	2,002	2,470
International Education	559	640	735	866	1,035
Professional	177	211	226	244	275
Education	2,312	2,530	2,628	3,112	3,780
FT Publishing	249	280	344	390	358
Interactive Data	297	332	344	406	484
FT Group	546	612	688	796	842
Penguin	804	848	846	903	1,002
Continuing	3,662	3,990	4,162	4,811	5,624
Discontinued	461	433	167	8	–
Total sales	4,123	4,423	4,329	4,819	5,624
Adjusted operating profit					
North American Education	260	280	273	303	403
International Education	51	73	92	135	141
Professional	2	17	27	36	43
Education	313	370	392	474	587
FT Publishing	17	27	56	74	39
Interactive Data	80	89	97	121	148
FT Group	97	116	153	195	187
Penguin	60	66	74	93	84
Continuing	470	552	619	762	858
Discontinued	36	40	15	–	–
Total adjusted operating profit	506	592	634	762	858
Operating margin – continuing	12.8%	13.8%	14.9%	15.8%	15.3%
Adjusted earnings					
Total adjusted operating profit	506	592	634	762	858
Net finance costs	(84)	(90)	(85)	(88)	(97)
Income tax*	(128)	(130)	(145)	(178)	(194)
Minority interest	(22)	(28)	(32)	(36)	(44)
Adjusted earnings*	272	344	372	460	523
Weighted average number of shares (millions)	797.9	798.4	796.8	797.0	799.3
Adjusted earnings per share*	34.1p	43.1p	46.7p	57.7p	65.4p

* 2005 not restated for tax deductibility of goodwill and intangible amortisation.

All figures in £ millions	2005	2006	2007	2008	2009
Cash flow					
Operating cash flow	570	575	684	796	913
Operating cash conversion	113%	97%	108%	104%	106%
Operating free cash flow	440	434	533	631	723
Operating free cash flow per share	55.1p	54.4p	66.9p	79.2p	90.5p
Total free cash flow	431	433	407	631	723
Total free cash flow per share	54.0p	54.2p	51.1p	79.2p	90.5p
Net assets	3,733	3,644	3,874	5,024	4,636
Net debt	996	1,059	973	1,460	1,092
Return on invested capital (gross basis)					
Total adjusted operating profit	506	592	634	762	858
Cash tax paid	(65)	(59)	(61)	(89)	(103)
Return	441	533	573	673	755
Average invested capital	6,060	6,553	6,423	7,337	8,504
Return on invested capital	7.3%	8.1%	8.9%	9.2%	8.9%
Dividend per share	27.0p	29.3p	31.6p	33.8p	35.5p

Corporate and operating measures

Sales – underlying and constant exchange rate movement

Sales movement for continuing operations excluding the impact of acquisitions and disposals and movements in exchange rates.

All figures in £ millions	2009
Underlying increase	74
Portfolio changes	99
Exchange differences	640
Total sales increase	813
Underlying increase	2%
Constant exchange rate increase	4%

Adjusted income statement

Reconciliation of the consolidated income statement to the adjusted numbers presented as non-GAAP measures in the financial statements.

						2009
All figures in £ millions	Statutory income statement	Other net gains and losses	Amortisation of acquired intangibles	Other net finance income/costs	Tax amortisation benefit	Adjusted income statement
Operating profit	755	–	103	–	–	858
Net finance costs	(98)	–	–	(2)	–	(97)
Profit before tax	660	–	103	(2)	–	761
Income tax	(198)	–	(37)	1	40	(194)
Profit for the year from continuing operations	462	–	66	(1)	40	567
Profit for the year from discontinued operations	–	–	–	–	–	–
Profit for the year	462	–	66	(1)	40	567
Minority interest	(37)	–	(5)	–	(2)	(44)
Earnings	425	–	61	(1)	38	523

						2008
All figures in £ millions	Statutory income statement	Other net gains and losses	Amortisation of acquired intangibles	Other net finance income/costs	Tax amortisation benefit	Adjusted income statement
Operating profit	676	–	86	–	–	762
Net finance costs	(91)	–	–	3	–	(88)
Profit before tax	585	–	86	3	–	674
Income tax	(172)	(7)	(31)	(1)	33	(178)
Profit for the year from continuing operations	413	(7)	55	2	33	496
Profit for the year from discontinued operations	(90)	90	–	–	–	–
Profit for the year	323	83	55	2	33	496
Minority interest	(31)	–	(3)	–	(2)	(36)
Earnings	292	83	52	2	31	460

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	2009
Underlying increase	13
Portfolio changes	14
Exchange differences	69
Total adjusted operating profit increase	96
Underlying increase	2%
Constant exchange rate increase	4%

Total 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	2009	2008
Adjusted operating profit	858	762
Cash conversion	106%	104%
Operating cash flow	913	796
Operating tax paid	(103)	(89)
Net operating finance costs paid	(87)	(76)
Total operating and free cash flow	723	631
Weighted average number of shares in issue (millions)	799.3	797.0
Operating free cash flow per share	90.5p	79.2p
Total free cash flow per share	90.5p	79.2p

Return on invested capital

	Net invested capital		Gross invested capital	
All figures in £ millions	2009	2008	2009	2008
Total adjusted operating profit	858	762	858	762
Intangible amortisation	(103)	(86)	–	–
Cash tax paid	(103)	(89)	(103)	(89)
Return	652	587	755	673
Average goodwill and other intangibles	5,152	4,352	7,194	6,058
Average net operating assets	1,310	1,279	1,310	1,279
Average invested capital	6,462	5,631	8,504	7,337
Return on invested capital	10.1%	10.4%	8.9%	9.2%

Return on invested capital is calculated using two methods:

Gross basis – total adjusted operating profit less operating cash tax paid expressed as a percentage of average gross invested capital. Gross invested capital includes the original unamortised goodwill and intangibles.

Net basis – total adjusted operating profit less intangible amortisation and operating cash tax paid expressed as a percentage of average net invested capital. Net invested capital includes the carrying value (after amortisation) of goodwill and intangibles.

Index to the financial statements

Shareholder information

Payment of dividends to mandated accounts

Dividends are paid through BACS and can be paid directly into a bank or building society account, with the tax voucher sent to the shareholder's registered address. For more information, please contact our registrar, Equiniti, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA. Telephone 0871 384 2043* or, for those shareholders with hearing difficulties, textphone number 0871 384 2255*.

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 0871 384 2268*.

Individual Savings Accounts (ISAs)

Equiniti offers ISAs in Pearson shares. For more information, please call them on 0871 384 2244*.

Share dealing facilities

Equiniti offers telephone and internet services for dealing in Pearson shares. For further information, please contact them on 08456 037 037 (telephone dealing – weekdays only) or log on to **www.shareview.co.uk/dealing** (online dealing). You will need your shareholder reference number as shown on your share certificate.

A postal facility for dealing in Pearson shares is also available through JPMorgan Cazenove Limited, 20 Moorgate, London EC2R 6DA.
Telephone 020 7588 2828.
An alternative weekly postal dealing service is available through Equiniti.
Please telephone 0871 384 2248* for details.

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** or by contacting them at 17 Carlton House Terrace, London SW1Y 5AH.

Shareholder information online

Equiniti 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**. Equiniti can be contacted for information on 0871 384 2233*.

Information about the Pearson share price

The company's share price can be found on our website at **www.pearson.com**. It also appears in the financial columns of the national press.

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 BNY Mellon Shareowner Services, PO Box 358516, Pittsburgh, PA 15252-8516, telephone 1 866 259 2289 (toll free within the US) or 1 201 680 6825 (outside the US). Alternatively, you may e-mail **shrrelations@bnymellon.com**, or log on to **www.bnymellon.com/shareowner**. Voting rights for registered ADR holders can be exercised through The 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.

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.

*Calls to these numbers are charged at 8p per minute from a BT landline. Other provider costs may vary.

Shareholder information continued

Tips on protecting your shares

Keep any documentation that contains your shareholder reference number in a safe place and shred any unwanted documentation.

Inform the registrar 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.

For more information, please log on to our website at
www.pearson.com/shareholderfaqs

Advisers

Auditors PricewaterhouseCoopers LLP
Bankers HSBC Bank plc
Brokers JPMorgan Cazenove Limited and Citigroup
Financial advisers Goldman Sachs, JP Morgan Cazenove Limited and Citigroup
Solicitors Freshfields Bruckhaus Deringer, Herbert Smith and Morgan, Lewis & Bockius

2010 Financial calendar

Ex-dividend date – 7 April
Record date – 9 April
Last date for dividend reinvestment election – 15 April
Annual General Meeting – 30 April
Payment date for dividend and share purchase date for dividend reinvestment – 7 May
Interim results – 26 July
Payment date for interim dividend – 17 September

Principal offices worldwide

Pearson (UK)
80 Strand, London WC2R 0RL, UK
T +44 (0)20 7010 2000
F +44 (0)20 7010 6060
firstname.lastname@pearson.com
www.pearson.com

Pearson (US)
1330 Avenue of the Americas,
New York City, NY 10019, USA
T +1 212 641 2400
F +1 212 641 2500
firstname.lastname@pearson-inc.com
www.pearson.com

Pearson Education
One Lake Street,
Upper Saddle River,
NJ 07458, USA
T +1 201 236 7000
F +1 201 236 3222
firstname.lastname@pearsoned.com
www.pearsoned.com

Financial Times Group
Number One Southwark Bridge,
London SE1 9HL, UK
T +44 (0)20 7873 3000
F +44 (0)20 7873 3076
firstname.lastname@ft.com
www.ft.com

The Penguin Group (UK)
80 Strand, London WC2R 0RL, UK
T +44 (0)20 7010 2000
F +44 (0)20 7010 6060
firstname.lastname@uk.penguingroup.com
www.penguin.co.uk

The Penguin Group (US)
375 Hudson Street, New York City,
NY 10014, USA
T +1 212 366 2000
F +1 212 366 2666
firstname.lastname@us.penguingroup.com
us.penguingroup.com

Pearson plc
Registered number 53723 (England)

Recycled
Supporting responsible use of forest resources
www.fsc.org Cert no. SGS-COC-0620

Design and Production: Radley Yeldar (London) **ry.com**
Print: Beacon Press

Pearson has supported the planting of 1,750m² of new native woodland with the Woodland Trust, helping to capture and store 70 tonnes of carbon dioxide emissions generated by the production of this report.

The cover of this report has been printed on Cocoon Silk 100 which is FSC certified and contains 100% recycled de-inked waste paper. The text pages are printed on Cocoon Offset which is also made from 100% recycled fibres. This report was printed using vegetable oil based inks and 100% renewable energy by a CarbonNeutral® printer certified to ISO 14001 environmental management system and registered to EMAS the Eco Management Audit Scheme.